Joint Opinion Statement FC 8/2015

on strengthening controlled foreign company rules

(BEPS Action 3)

Prepared by AOTCA and CFE

Submitted to the OECD

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The AOTCA (The Asia-Oceania Tax Consultants´ Association) was founded in 1992 by 10 tax professionals' bodies located in the Asian and Oceanic regions. It has expanded to embrace 20 leading organizations from 16 countries/regions.

The CFE (Confédération Fiscale Européenne) is the umbrella organisation representing the tax profession in Europe. Its functions are to safeguard the professional interests of tax advisers, to assure the quality of tax services provided by tax advisers, to exchange information about national tax laws and professional law and to contribute to the coordination of tax law in Europe. The CFE is registered in the EU Transparency Register (no. 3543183647-05).

AOTCA and CFE unite almost 500,000 individual tax professionals in 37 countries (19 OECD member states).

Introduction

This is a joint Opinion Statement of the Asia-Oceania Tax Consultants´ Association (AOTCA) and the Confédération Fiscale Européenne (CFE), the European federation of tax advisers, responding to the OECD discussion draft on BEPS Action 3 (Strengthening CFC Rules) of 3 April 2015[1] (hereinafter: the Discussion Draft). If you should have any questions on the comments below or on AOTCA or CFE, please contact Rudolf Reibel, CFE Fiscal and Professional Affairs Officer: brusselsoffice@cfe-eutax.org.

This Opinion Statement supports the observations of the position paper of Valente Associati GEB Partners (link, see page 225) with which it should be read in conjunction.

General comments

1. All income derived by a controlled foreign company (CFC) such as operational income which does not raise profit shifting concerns and is thus meaningless from a BEPS point of view should be excluded as an available option in the final recommendations on Option 3.
2. There is no consideration of the CFC issues as they concern countries which tax on a receipts basis rather than a residency/citizenship basis. They appear to be irrelevant to the receipts based countries but the inter-reaction with jurisdictions that have CFC legislation needs analysis.
3. It is observed in the Discussion Draft that CFC rules provide a backstop to transfer pricing actions. However, the Discussion Draft does not provide any consideration about how transfer pricing disputes (which tend to be very lengthy) should interplay with the CFC rules and how they are to be resolved by competent authority negotiations.
4. We are concerned about the possible interaction of BEPS Action 4 (interest deductions and other financial payments) with Action 3 and the double taxation issues that can arise if on the one hand interest is considered not deductible with the paying company while on the other hand it is included in the CFC income of the shareholders in the CFC.
5. For jurisdictions such as Hong Kong, Malaysia and Singapore, CFC rules are not that relevant for the following reasons:
    a) They do not tax on worldwide income but impose tax based on the principal of territoriality;
    b) Hong Kong and Singapore are relatively low tax jurisdictions so profits being shifted away from these jurisdictions and kept in foreign controlled corporations are less likely an issue; and

[1] http://www.oecd.org/ctp/aggressive/discussion-draft-beps-action-3-strengthening-CFC-rules.pdf

c) even if profit shifting is an issue, there are other existing tax rules in in those jurisdictions which may be used to deal with shifting profits offshore e.g. the general anti-avoidance rules.

Comments relating to specific chapters of the Discussion Draft:

6. CFC rules as preventative measures (paras 16 and 17):
The claim is made at paragraph 16 and thereabouts that the existence of CFC rules has an impact on the erosion of profits from the source country (as compared with the ultimate recipient country). This appears to be based solely on the existence of CFC rules being a deterrent to engaging in deferral behaviour in respect of recipient countries. There is no evidence offered to support this proposition. The real focus of BEPS should be on the country which has a base erosion problem rather than a country which has a deferral issue. It is not at all clear that CFC legislation offers any substantive advantage to source countries suffering base erosion.

7. How CFC rules can accurately attribute income that raises BEPS concerns; interest and other financing income (paras 100 and 101):

   While the Discussion Draft mentions that CFC rules must be capable of dealing with, among other types of income, interest and other financing income, it does not deal in any great detail with attributing financing income of a CFC to its shareholders of controlling parties. While non-trading intra-group finance profits will almost always be fully attributable under a best practice CFC regime, an issue for consideration is whether a CFC that is not overcapitalised and has the substance to generate the finance income itself should be excluded from the CFC regime.

8. Question 16: What practical problems arise with applying the categorical approach and the excess profits approach?

   The excess profits calculation which the Discussion Draft notes may be able to better address some of the issues arising from transactions involving intellectual property. The risk of this approach is that it not only focused on shifted income and would need to be combined with a substance based exclusion.