The Brockman brief: Performance review: The OECD’s reputation

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The curtain is drawing to a close on the final OECD BEPS recommendations, while the OECD actors and supporting staff anxiously await reaction from the audience. This month’s Brockman brief runs the rule over the OECD’s BEPS work to date and looks ahead to see how developments are likely to impact the organisation’s reputation as the ‘go-to’ body for international tax matters.

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The OECD’s continuing role as a leader in the international tax arena is under critical review as the new guidelines emerge; will the Paris-based organisation’s reputation be enhanced, or diminished, by this ambitious project?

The BEPS Action Plans and development of new transfer pricing guidelines have placed reputational risk at the forefront of today’s news, and this extends to the OECD’s reputation going forward. However, what are the key performance indicators (KPIs) that will be useful to determine measurable results? Was the OECD’s game-plan an ‘all-or–nothing’ proposal, initiated by political and parliamentary advocates willing to push such efforts along the way?

The BEPS actions embraced several objectives, including the development of enhanced transfer pricing risk tools such as the country-by-country report (CbCR), procedural rules to mitigate treaty shopping and neutralisation of enhanced benefits for hybrid mismatch arrangements.

A secret ingredient for the successful formulation of the new guidelines and KPI measurement is the willingness of countries to wait for the final act and move in a coordinated manner, rather than deciding on an early exit to legislate BEPS ‘intent’. Several countries envision BEPS Actions as a timely incentive to increase fiscal revenues, while retaining sovereign rights and their ‘rogue’ roles on the global team; for example, adopting a stance of saying ‘we are members of the team’ on the arbitration front, but ‘we’re doing our own thing, too’. However, such countries are not outspoken as to how their efforts may endanger the OECD’s efforts (or undermine its reputation), thereby achieving quick wins while tainting global unity. The OECD has publicly expressed its annoyance and embarrassment over such unilateral measures, although it does not have the binding, rule-making capacity to limit such efforts.

Levels of engagement

The OECD should receive an outstanding rating for its efforts to unify developed and developing countries in a collaborative engagement designed to achieve global consistency while developing the objectives set forth. The engagement with developing countries represents a continuum as the OECD partners with the UN, IMF, World Bank and others to set forth tools by which transfer pricing risk processes, among others, are developed.

One possible misstep for KPI determination, resulting in a neutral rating, is the timing and content of the multilateral instrument that is subsequent to, rather than parallel with, the final guidelines. As a consequence, countries have not been willing to wait for the relevant treaty coordination of permanent establishment (PE) rules, among others. Instead, they have proactively developed creative, and inherently subjective, criteria to claim their ‘fair share of tax’ wherever income is derived.
The OECD's reputation may be closely aligned with preservation of the 'arms-length principle'. A wide chasm is potentially emerging between the time-honoured arm's-length principle and the assessment of taxes where economic activity occurs, thereby representing divergent views as to how such taxes are to be collected, and by whom. As the chasm grows larger (or dual guidelines emerge), the OECD may be proportionally losing its reputational status in the tax community as international tax principles are eroded.

There are several counter-measures by countries that may not be conducive with the OECD's heroic efforts. Economic indicators, including the CbCR, may be used by tax administrations as an impetus for tax assessments, ignoring domestic legislation and treaty precedents. The CbCR will be used as a quick win by several countries for fiscal stimulus, thereby resulting in silo approaches to tackling double taxation. Additionally, inherently subjective PE legislation and general anti-avoidance rules (GAAR) are being crafted by rule-making bodies in many countries, both within and outside of the boundaries of treaty protection.

The rating, and remedy, for providing effective dispute resolution to obtain certainty and avoid double taxation is neutral at this time. Winning arguments have met unilateral obstacles for agreement and adoption. Arguably, important precedents for mandatory arbitration and so on may not have been pushed to the limit in an attempt to repair the currently impaired system for competent authority assistance and timely resolution of issues. This is despite a late ‘push’ from the US, which appeared to be little more than lip service – it said it would be open to adoption if everybody subscribed to mandatory arbitration. However, there may be continuing peer pressure for future adoption of such measures, for which the OECD should receive credit.

The OECD's KPIs in relation to clarity of definitive approaches in developing final guidelines should be viewed as a neutral rating. The subjectivity and suggestiveness of various provisions have allowed countries to adopt rules within a wide range of parameters, offsetting global consistency objectives and simplicity. Such vagaries, perhaps prompted by a desire for collaboration, have weakened the tenets of international tax principles and promoted unilateral objectives that are dissimilar, complex and subject to additional tax appeals and controversy.

The focus to mitigate double taxation will result in a neutral rating for KPI measurement, as it was not on the forefront of discussions and ‘must-haves’ by the OECD and global forum of tax administrations (which focused predominantly on mitigating double non-taxation), notwithstanding its importance for multinational organisations. This lack of focus will weaken the international tax system if there are not corresponding, and timely, rules to address this dilemma.

The aspect of monitoring BEPS actions is an excellent idea, although not yet proven in practice. One may question why early unilateral country actions are not yet summarised in a central forum for reference to achieve further transparency. Will such unilateral actions be reversed, unilaterally or via the multilateral legal instrument, to achieve OECD consistency? Countries have not been outspoken on this topic to date, further challenging the efforts by the BEPS working parties to develop globally consistent international tax principles.

In summary, OECD's exemplary collaboration effects have been partially overshadowed by unilateral actions, sovereignty principles, lag time for a multilateral instrument, increased potential of double taxation, ineffective dispute resolution processes, and inherently subjective guidance that erode the arm’s-length principle.

The successful implementation of BEPS deliverables, or not, is likely to have a huge bearing on whether the OECD's reputation remains intact, or is diminished by factors largely outside of its control.

It is now time for the final curtain, as the actors courteously bow to an audience that appreciates, and recognises, their outstanding performance.

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