

Country by Country Reporting (“CbCR)

- **A Guide to the Appropriate Use of Information Exchanged**

States of Guernsey Income Tax

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Introduction

International tax issues have been high on the political agenda in recent years.

The integration of national economies and markets has put a strain on the international tax framework, which was designed more than a century ago. These rules, generally accepted for many years, nevertheless contained weaknesses that created opportunities for Base Erosion and Profit Shifting (“BEPS”).

To help restore confidence in the international tax system, and ensure that profits are taxed where economic activities take place and value is created, in September 2013, G20 Leaders endorsed the ambitious and comprehensive Action Plan on BEPS.

A package of 13 reports was delivered by the OECD just 2 years later, including new or reinforced international standards as well as measures to help countries tackle BEPS.

One of these measures (Action 13) is standardised Country-by-Country Reporting (“CbCR”) which is intended to give tax administrations a global picture of where multinational enterprises (“MNEs”) derive their profits, pay tax and carry out economic activities.

Broadly, under CbCR, the ultimate parent entity (UPE) of a group with annual consolidated group revenue equal to or higher than EUR 750 million (or near equivalent in domestic currency as of January 2015) in the preceding fiscal year is required to file a CbC Report on behalf of the group with its local tax authority. The deadline for filing the CbC Report is by no later than 12 months after the last day of the group's reporting fiscal year. The tax authority with which the CbC Report is filed will exchange the CbC Report with the tax authority in other jurisdictions where the group has operations, under bilateral or multilateral tax treaties or tax information exchange agreements (TIEAs) that permit the automatic exchange of information. This is subject to conditions, including the jurisdictions having a legal framework for CbC Reporting in place and meeting conditions concerning confidentiality, consistency and the appropriate use of CbCR information.

CbCR will therefore give tax administrations the ability to use this information to assess transfer pricing and other BEPS risks, so they can focus audit resources where they will be most effective.

MNEs will report their revenues, pre-tax profits, income tax paid and accrued, number of employees, stated capital, retained earnings, and tangible assets in each jurisdiction where they operate.

Country-by-Country Reports are required to be filed for MNEs' fiscal years starting from 1 January 2016 (although some jurisdictions will need time to follow their particular domestic legislative process in order to make necessary adjustments to the law).

This Guidance covers Guernsey's approach to the requirement of CbCR that information exchanged is to be used by the recipient tax administration appropriately.

Legal Background to CbCR

Guernsey participates in CbCR through its general political commitment to meet international standards in tax transparency. Guernsey joined the BEPS Inclusive Framework, in 2016, thereby committing to implement the minimum standards of BEPS (which includes, amongst other things, CbCR).

Since 2014, Guernsey has been a participant in the Multilateral Convention on Mutual Administrative Assistance in Tax Matters ("the Convention"). The Convention provides the international framework for Guernsey to cooperate in tax matters with a significant number of other jurisdictions (at present there are 112 participants in the Convention, including Guernsey).

The Convention provides for assistance between participants by way of automatic exchange of information ("AEOI"). CbCR is a form of AEOI.

Guernsey has also signed the CbCR Multilateral Competent Authority Agreement ("CbCR MCAA"), which is the mechanism by which the relevant authorities who wish to participate in CbCR agree the practical application of reporting. There are currently 65 signatories to the CbCR MCAA. In addition, Guernsey has signed, and is planning to sign, a number of bilateral CbCR Competent Authority Agreements ("CbCR BCAAs") with jurisdictions committed to CbCR but for which the Convention and the CbCR MCAA cannot provide the necessary framework.

The CbCR MCAA and all of the signed/anticipated CbCR BCAAS contain/ will contain a clear obligation that the participants commit to appropriate use of information exchanged under CbCR.

Parties to these agreements are committed to disclose to each other breaches of appropriate use, and to promptly concede inappropriate adjustments in any competent

authority proceedings under CbCR. Significant non-compliance by a Party can also lead to temporary suspension of the CbCR regime by the other Party(ies).

The meaning of “appropriate use” for CbCR

Use of CbCR information is restricted to:

- high level transfer pricing risk assessment
- assessment of other BEPS related risks
- economic and statistical analysis, where appropriate.

The BEPS Action 13 Report clarifies what would **not** be considered appropriate use;

... the information in the Country-by-Country Report should not be used as a substitute for a detailed transfer pricing analysis of individual transactions and prices based on a full functional analysis and a full comparability analysis. The information in the Country-by-Country Report on its own does not constitute conclusive evidence that transfer prices are or are not appropriate. It should not be used by tax administrations to propose transfer pricing adjustments based on a global formulary apportionment of income. (Paragraph 25)...

...Jurisdictions should not propose adjustments to the income of any taxpayer on the basis of an income allocation formula based on the data from the Country-by-Country Report....This does not imply, however, that jurisdictions would be prevented from using the Country-by-Country Report data as a basis for making further enquiries into the MNE's transfer pricing arrangements or in to other tax matters in the course of a tax audit (Paragraph 59)

It is clear that information contained in CbC Reports may be used for high level transfer pricing risk assessment, but should not be used **by itself** as a basis for proposing changes to transfer prices or adjusting a taxpayer's income using a formulaic global apportionment.

This would not prevent a tax authority from using CbCR information in planning a tax audit/investigation or as the basis for making further enquiries, into the MNE's transfer pricing arrangements or other tax matters. There is no requirement that such enquiries must relate to potential risks identified through the use of CbCR information. CbCR information may be used as the basis for making enquiries into tax matters identified using other data sources or arising during the course of a tax audit/ investigation, if it is relevant for that purpose.

This raises the question of the meaning of “BEPS related risk” (see the second bullet point above).

The OECD February 2013 Report “*Addressing Base Erosion and Profit*”

Shifting” refers to the challenge faced by countries as “planning aimed at shifting profits in ways that erode the taxable base to locations where they are subject to a more favourable tax treatment”.

The report went on to state that;

“While the specific goals will vary among MNEs, in particular with respect to companies headquartered in different jurisdictions, broadly speaking BEPS focuses on moving profits to where they are taxed at lower rates and expenses to where they are relieved at higher rates. Specific strategies may also be put in place to make use of existing “tax attributes” such as tax credits, loss-carry forwards, etc. These generic goals are often achieved in a way that aligns with the overall management of the treasury operations of the group, e.g. in terms of cash management, management of foreign exchange risks and efficient repatriation strategies.”

The term assessment of “BEPS-related risk”, is understood, therefore, to refer to the high level assessment of tax risks that may result in the erosion of a country's tax base. CbC Reports may be used to identify indicators of possible tax risk, but it will usually only be possible to fully understand what gave rise to that risk once further enquiries have been conducted. CbCR information should be limited to use in risk assessment and as a basis for making further enquiries in the course of a tax audit/ investigation. CbCR information on its own does not constitute conclusive evidence that transfer prices that have been used are not appropriate. It also does not constitute conclusive evidence that an MNE is engaged in other forms of BEPS.

CbCR data may also be used for economic and statistical analysis, where appropriate. This is taken as meaning where its use is not otherwise prohibited for this purpose (as maybe the case, under the Convention if, for example, it would lead to the identification of a particular entity, as this would breach the confidentiality requirements).

Application of the above by the Director of Income Tax

The Director of Income Tax in Guernsey has statutory responsibility for the care and management of the income tax law. He is committed to application of the use of information received by him, under CbCR, from other jurisdictions in accordance with the principles set out in this document.

Officers in the Guernsey Income Tax Service are instructed to use CbCR information in accordance with this Guidance.

To ensure that CbC Reports are controlled and monitored for appropriate use, the Director of Income Tax has delegated initial responsibility for receiving and disseminating CbCR information to the nominated officers (“delegated officers”), who will consider the information at the point it is received and, if it is considered appropriate for enquiries to be instituted, will pass instructions on the use of the data to

the relevant Inspector. The delegated officers will also monitor the enquiries, until they are concluded, to ensure that this Guidance is correctly applied (and, in particular, to promptly concede any appeal or competent authority proceeding that involves a tax adjustment using an income allocation formula based solely on CbCR information).

The delegated officers will also ensure that the Director is promptly notified of any cases of non-compliance with the appropriate use condition, so that he may, in turn, make any notifications required under the relevant MCAA or BCAA.

The delegated officers will review this Guidance, and the procedures put in place to ensure appropriate use of CbCR data, on an ongoing basis, and will recommend to the Director any changes that are considered desirable.