

In Confidence

Office of the Minister of Finance
Office of the Minister of Revenue

Economic Growth and Infrastructure Committee

TAX MEASURES TO PREVENT BASE EROSION AND PROFIT SHIFTING

Proposal

1. This paper provides an overview of three attached Cabinet papers seeking approval for measures to address base erosion and profit shifting in New Zealand. This paper also summarises the background to the attached papers, highlights the most important aspects of the proposals, and discusses matters common to all three papers (including application dates, publicity, and financial implications). The attached papers are:

- BEPS – strengthening our interest limitation rules;
- BEPS – transfer pricing and permanent establishment avoidance; and
- BEPS – addressing hybrid mismatch arrangements.

Background

2. Since late 2012, there has been significant global media and political concern about evidence suggesting that some multinationals pay little or no tax anywhere in the world. Initially matters surfaced in the context of Parliamentary and Senate inquiries in the UK, US and elsewhere into the tax avoidance strategies used by multinationals. In 2013 the issue formed part of the G20 agenda who asked the OECD to report back to it on global strategies to address countries' concerns.

3. The OECD reported back to the G20 in July 2013 highlighting the aggressive tax practices used by multinationals to exploit gaps and mismatches in countries' domestic tax rules to avoid tax, now known as "base erosion and profit shifting" (BEPS). They found that BEPS strategies distort investment decisions, allow multinationals to benefit from unintended competitive advantages over more compliant or domestic companies, and result in the loss of substantial corporate tax revenue. More fundamentally, the perceived unfairness resulting from BEPS jeopardises citizens' trust in the integrity of the tax system as a whole.

4. The end result was the adoption of a G20/OECD 15 point Action Plan recommending a combination of domestic reforms, tax treaty changes, and administrative measures that would allow countries to strengthen their laws in a consistent manner and work together in combatting BEPS. Recognising our own vulnerability to BEPS and the value of working cooperatively, New Zealand actively participated in the OECD/G20 project, which was finalised at the end of 2015.

New Zealand's response to BEPS

5. On the whole, New Zealand is fairly well placed when we assess our tax system against the OECD/G20 recommendations. However, while the majority of multinationals operating in New Zealand are compliant, there are some that adopt BEPS strategies to minimise or eliminate their New Zealand tax obligations. It is important to address these BEPS activities without reducing the general attractiveness of New Zealand as an investment destination.

6. In June last year the Government released its own programme to address BEPS issues in New Zealand (CAB-16-MIN-0218 refers). This programme presented a measured approach that prioritises the problems observed in relation to New Zealand's laws. At the same time, it is a coherent package of measures. Stripping the tax benefits from one type of arrangement is ineffective if multinationals can get the same benefit from switching to a different type of arrangement.

7. In summary the Government's package of New Zealand domestic law measures:

- prevent multinationals from using artificially high interest rates on loans from related parties (interest limitation);
- prevent multinationals from using artificial arrangements to avoid having a taxable presence (a permanent establishment) in New Zealand;
- prevent multinationals from using transfer pricing payments to shift profits to their offshore group members in a manner that does not reflect the actual economic activities undertaken in New Zealand and offshore; and
- remove the tax advantages of exploiting hybrid mismatches between different countries' tax rules.

8. New Zealand's response to BEPS is generally aligned with Australia's response. It is also broadly consistent with the OECD's BEPS Action Plan, although the specific proposals are tailored for the New Zealand environment. Appendix One provides a table that compares New Zealand's and Australia's response to the OECD's BEPS Action Plan.

9. The detail of the BEPS proposals was subsequently set out in three Government discussion documents, which were released for public consultation in September 2016 and March 2017:

- *BEPS – Strengthening our interest limitation rules;*
- *BEPS – Transfer pricing and permanent establishment avoidance;* and
- *Addressing hybrid mismatch arrangements.*

10. Our officials have since received a significant amount of feedback on the discussion documents. Most of the submissions were from tax advisors to the affected businesses and raised concerns about uncertainty and compliance costs. We consider that these additional costs will mostly be borne by those who the measures are designed to address (taxpayers engaging in BEPS activities) and that the overall benefits to New Zealand of addressing BEPS outweigh these costs. We have used this feedback to refine the measures, so they are more certain for taxpayers and better targeted. These refinements should not reduce the overall effectiveness of the proposed measures. We consider the measures will address the BEPS issues we are concerned about.

11. The following are what we consider to be the most important matters coming out of consultation. This is not an exhaustive list. The individual Cabinet papers accompanying this paper also discuss other significant issues raised by submitters.

12. Finally we note the progress in relation to the OECD's *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS* (also known as the multilateral instrument or MLI) signed by the Minister of Revenue on behalf of New Zealand in June. The MLI is intended to prevent our double tax agreements from being used to facilitate BEPS.

Main issues on BEPS – Strengthening our interest limitation rules

13. One of the easiest ways to shift profits out of New Zealand is for a foreign parent of a New Zealand subsidiary to fund the subsidiary with a loan rather than equity. This is because the interest paid to the parent is deductible to the subsidiary thereby reducing its taxable income. The specific problem we have identified is that transfer pricing rules are not effective in limiting the rate of interest that can be charged on that loan.

Proposal on pricing related-party debt

14. The discussion document proposed a hard rule to limit the interest rate on related-party debt to an amount close to the parent's cost of external borrowing - specifically an interest rate cap, based on the credit rating of the offshore parent plus a small margin. Submitters argued that this proposal could affect the interest rates of companies with only small amounts of debt (so not seen as a risk to the tax base) and could be difficult to apply if the parent has no credit rating. They were also concerned that it could produce results that were inconsistent with our tax treaties, leading to double taxation.

15. In light of these concerns we recommend using what we have termed a "restricted transfer pricing approach" for debt. We expect that this approach will generally result in the interest rate on related-party debt being in line with that facing the foreign parent. This is because the debt would be priced under a transfer pricing methodology but (i) be carried out with a rebuttable presumption that the borrower could be expected to be supported by its foreign parent; and (ii) disregard any commercially unattractive terms used to justify an excessive interest rate. We also intend that taxpayers be able to challenge the rate using the dispute resolution process in tax treaties. The Australian Taxation Office has recently released administrative guidelines which outline a similar approach for limiting related party interest rates (albeit Australia is implementing this approach as an operational policy, rather than a law change).

Proposal on allowable debt levels

16. The second interest limitation issue relates to allowable debt levels under our thin capitalisation rules. These rules limit the quantity of debt a foreign-owned subsidiary can have (generally to 60 percent of the subsidiary's assets). We propose to adjust what counts as "assets" by reducing them by "non-debt liabilities" (liabilities other than interest-bearing debt).

17. While there was some support for the broad proposal, submitters were very concerned about one aspect: that the proposed change would include what are known as "deferred tax liabilities." Accounting standards require deferred tax to be recognised in certain situations – broadly, where profits for tax and accounting purposes differ. This is a complicated issue, with some types of deferred tax liabilities having a stronger case for exclusion than others.

We recommend that officials consider this matter further as part of future consultation on the detailed design of the interest limitation proposals, with Cabinet delegating us the power to make a decision.

Main issues on BEPS – Transfer pricing and permanent establishment avoidance

18. The *BEPS – transfer pricing and permanent establishment avoidance* Cabinet paper contains measures to strengthen our transfer pricing rules, counter permanent establishment avoidance and help Inland Revenue deal with uncooperative multinationals.

Proposal on Transfer Pricing Time Bar

19. The discussion document proposed extending Inland Revenue's time bar for adjusting a taxpayer's transfer pricing position from four to seven years. Submitters opposed this extension on the basis that it increased uncertainty and was out of step with the general time bar, which applies to other areas of tax. However, we are continuing to recommend the seven year rule. Having a longer time bar for transfer pricing cases is consistent with both Australia and Canada (who also have shorter time bars for other tax disputes) and reflects the information asymmetry that exists in transfer pricing cases (especially where taxpayers may hold relevant information offshore).

Proposal on permanent establishment avoidance

20. This proposal is aimed at preventing taxpayers from structuring their affairs to avoid a taxable presence in New Zealand where one exists in substance. The OECD has updated their model tax treaty to address this issue and New Zealand is adopting this into our tax treaties by signing the OECD's multilateral instrument. In addition to this, like Australia and the UK, we are also introducing a permanent establishment avoidance rule into our domestic law. The domestic law change is necessary to cover cases where the relevant tax treaty does not yet include the OECD's new recommendation. Submitters were of the view that the proposed rule was too broad and would catch ordinary commercial arrangements that were not its intended target. We agree that any rule should be more narrowly targeted at avoidance arrangements and therefore recommend that officials consult further with submitters to achieve this result.

Main Issues on BEPS – Addressing hybrid mismatch arrangements

21. The *BEPS – addressing hybrid mismatch arrangements* Cabinet paper proposes measures to remove the tax advantages of hybrid mismatch arrangements. Hybrid mismatch arrangements arise when countries classify transactions and entities differently from each other under their domestic tax laws. For example, fixed rate shares may be treated as debt in one country and shares in another, thus allowing the payment of an amount that is deductible in the payer's country but non-assessable in the payee's. Australia, the UK and EU member countries are taking similar actions to address BEPS from hybrid mismatches.

Scope of the rules

22. The hybrids proposals in the discussion document covered the full suite of OECD recommendations in this area, even though there is limited evidence of some of the structures being used in New Zealand. Submitters therefore suggested that our rules should concentrate on the known mischief. On balance, we recommend a comprehensive adoption of the OECD recommendations on hybrid mismatch arrangements with suitable modifications for the New

Zealand context. Tackling only the known structures might leave a loophole to use those that are not covered, encouraging taxpayers to move into different tax-efficient hybrids rather than converting to more conventional funding structures. A partial response also ignores the fact that some of the other structures might actually be in use, but have not been picked up by Inland Revenue audit.

Foreign Trusts

23. Foreign trusts are, simply put, trusts that have a New Zealand trustee, but are set up by a non-resident (the settlor) and generally derive only foreign-sourced income. Under current settings, foreign trusts are not taxed in New Zealand, except on any New Zealand sourced income. This was confirmed as appropriate by the 2016 Government Inquiry into Foreign Trust Disclosure Rules (the Shewan Inquiry). However, the Shewan Inquiry's conclusion was based on the existing tax settings and the hybrids project has the potential to change these settings in certain circumstances.

24. From a tax policy perspective, foreign trusts are treated as transparent in New Zealand. New Zealand takes the view that, to the extent the income is not paid to beneficiaries more or less as earned, it should be taxed to the settlor in their home jurisdiction. By contrast, the jurisdiction of the settlor may see the trust as a separate entity and not tax the income on the mistaken assumption that the trustee is being taxed in New Zealand. When the income of the trust is not taxed anywhere in the world because of the different tax treatment the relevant countries place on the trust structure, we recommend the New Zealand trustee be subject to tax. This measure would not result in double taxation of current year trust income.

25. We anticipate this meaning that most foreign trusts will be taxed in New Zealand on their foreign sourced income. However, it is important to note that this does not mean that they all will be. The relevant enquiry is "would the income be included in the tax calculation of the settlor in their own country if they had earned that income directly?" If the answer is "no" (and there might be numerous reasons why this would be the case, such as if the settlor is tax exempt, or in a country that does not tax residents on their worldwide income) then no New Zealand tax would be imposed. If the answer is "yes" then New Zealand tax should be imposed unless the income is included in the tax calculation of any person in the same control group (for example, the settlor or a beneficiary) in their own country in the corresponding income year.

26. Finally, we note that taxing foreign trusts in this way was signalled when the hybrids consultation paper was released in September 2016. However, because this rule has the potential to apply to both foreign trusts and limited partnerships, and because the foreign trust industry has very recently incurred significant compliance costs associated with the recommendations of the Shewan Inquiry, we are recommending a delayed effective date to give these structures time to assess their options.

Application dates and transitional measures

27. The measures should generally apply from income years beginning on or after 1 July 2018. Cabinet has already noted that the reforms are expected to apply from this date (CAB-17-MIN-0164 refers). This is based on the expectation that the legislation will be progressed to enactment before this date.

28. The new administrative powers for Inland Revenue to deal with uncooperative multinationals should apply from the date the legislation is enacted. We also propose different

application dates for two of the specific hybrid mismatch proposals. We recommend the unstructured imported mismatch rule (explained more fully in the attached BEPS – addressing hybrid mismatch arrangements Cabinet paper) apply from 1 January 2020 and the reverse hybrid measures (generally expected to apply to limited partnerships and foreign trusts) apply for income years beginning on or after 1 April 2019.

29. We do not recommend any additional transitional relief from the measures, except:

- relief from the hybrids measures for certain hybrid financial instruments issued to the public before 6 September 2016 (the date on which the hybrids discussion document was released); and
- relief from the transfer pricing and interest limitation measures for arrangements subject to an advance pricing agreement entered into before 1 July 2018. (An advance pricing agreement is a binding ruling from Inland Revenue that confirms that the taxpayer’s planned transfer pricing positions are compliant with the transfer pricing rules for up to five years.)

Consultation

30. Officials consulted widely on the measures in the attached papers. Discussion documents were released for public feedback on the relevant topics (referred to in paragraph 8 above). For the hybrids proposals, given the earlier release of that discussion document, officials have undertaken a further round of consultation on the details of the proposals with interested stakeholders. Inland Revenue and Treasury officials have also consulted with the Ministry of Foreign Affairs and Trade and the Ministry of Business, Innovation and Employment. In addition, officials have discussed some of the measures with their counterparts in the Australian Taxation Office, the Australian Treasury and the OECD secretariat.

General feedback on measures

31. Submitters generally acknowledged the importance of addressing BEPS risks facing New Zealand and agreed in principle that change is needed to strengthen the current rules. However, they did raise issues with certain features of the proposed measures and made suggestions to make them more workable and better targeted. We have incorporated many of these suggestions into the measures on which we now seek Cabinet approval.

Feedback on economic impact

32. Some submitters argued that the proposals will have a detrimental effect on New Zealand being an attractive investment destination and should not be implemented. They also argued that the proposed measures were complex and onerous, and may induce foreign companies to remove their existing personnel from New Zealand.

33. It is true that there will be additional tax and compliance costs for some investors but these are necessary to address the issues. We have used consultation to refine the proposals, minimise unintended impacts and better target the BEPS concerns. This should reduce the additional compliance costs, although it will not eliminate them. The higher tax payments resulting from these measures will inevitably make New Zealand a less attractive investment location for multinationals engaged in BEPS arrangements. At the same time, these

multinationals should not be allowed to exploit weaknesses in our tax rules to achieve a competitive advantage over more compliant multinationals or domestic firms. Furthermore, arbitrary reductions in tax, depending upon the opportunism of taxpayers, are likely to distort the allocation of investment into New Zealand. New Zealand is also undertaking these BEPS measures in line with a number of like-minded partners throughout the OECD and the expected tax revenue increase is expected to be relatively small. Given this, we believe any impacts on foreign direct investment into New Zealand will not be material and implementing these measures remains in New Zealand's best economic interests.

Feedback on application date

34. The discussion documents did not indicate a likely application date. However, some submitters expected the Government to seek an early application date and argued that it would be better to allow taxpayers time to consider the proposals and rearrange their affairs if necessary.

35. We expect to receive more submissions on, and opposition to, the application date once affected parties become aware it is proposed to be 1 July 2018.

Further consultation

36. Following Cabinet decisions on these papers, we recommend Inland Revenue and Treasury officials engage in further targeted consultation on outstanding policy issues and technical design details relating to the measures. Due the timing constraints necessary for a 1 July 2018 application date, we are not proposing that submitters be consulted on an exposure draft of the entire bill before the bill is introduced to Parliament. However, we recommend targeted consultation of specific sections where additional consultation will provide the most value ahead of the bill's introduction.

Financial implications

37. Some of the revenue for these proposals has already been included in Budget 2017 forecasts. These are:

Vote Revenue	\$m – increase/(decrease)						
	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Foreign hybrid entity double deductions	-	-	25.000	50.000	50.000	50.000	50.000
BEPS taxation bill	-	-	25.000	50.000	50.000	50.000	50.000
Total Revenue effect	-	-	50.000	100.000	100.000	100.000	100.000

38. If our recommendations in these Cabinet papers are agreed and adopted by the Government, then the forecasts would be adjusted upward by these additional amounts:

Vote Revenue Minister of Revenue	\$m – increase/(decrease)					
	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Grand-parenting of certain hybrids issued to the public	-	19.000	19.000	19.000	14.000	-
Other BEPS measures	-	45.000	90.000	90.000	90.000	90.000
Total Revenue effect	-	64.000	109.000	109.000	104.000	90.000

39. The additional revenue from the hybrids measures results from our proposed grand-parenting approach for hybrid financial instruments issued to the public before 6 September 2016. This revenue is contingent on taxpayer behaviour after the implementation of the hybrid rules.

40. We are recommending that officials continue to consult on details of how deferred tax liabilities and assets should be dealt with under the interest limitation measures - specifically, the measure to eliminate assets funded by non-debt liabilities from a taxpayer's total assets for thin capitalisation purposes. The above fiscal impact assumes deferred tax liabilities are included in the non-debt liabilities adjustments (as per the proposal in the discussion document). If these assets and liabilities were excluded from the adjustments the revenue forecast would be \$10 million per year lower. In the attached paper on interest limitation we are asking Cabinet to delegate to us the authority to make a decision on this along with an authority to update the relevant revenue forecasts, if necessary.

41. The revenue in paragraph 37 was treated as a saving in Budget 2017. We propose the additional revenue in paragraph 38 be treated as a saving in Budget 2018.

Administrative impacts

42. The changes proposed in the BEPS discussion documents and recommended in these Cabinet papers are not expected to increase administrative costs or require any significant systems changes for Inland Revenue. This is because the reforms largely change the way some taxpayers self-assess the income and deductions that they report to Inland Revenue. Further, the administrative amendments we are recommending should make it easier for Inland Revenue to deal with uncooperative multinationals.

43. We note, however, that a common theme in submissions on all three discussion documents was that administration of the proposals would place a higher demand on Inland Revenue's audit and investigation functions. Our view is that any required increase in Inland Revenue's resourcing as a result of the BEPS package will be accommodated within existing baselines.

Human rights

44. There are no human rights implications arising from the measures.

Legislative implications

45. Legislative changes to the Income Tax Act 2007 and the Tax Administration Act 1994 will be required to implement the proposed measures. To achieve this, we intend to include the measures in a BEPS taxation bill introduced after the General Election. The BEPS bill will need to be introduced and have its first reading by 14 December 2017 in order to be enacted in time for the planned 1 July 2018 application date.

Impact Analysis Requirements

46. There are no regulatory implications arising directly from this Cabinet paper.

47. The regulatory impact analysis for each set of measures is set out in the Cabinet paper for those measures.

Publicity

48. We will arrange for an appropriate announcement of the policy decisions on these BEPS measures.

49. We also recommend that the Government proactively release the BEPS Cabinet papers, policy reports and submissions on the BEPS discussion documents and the issues paper on the multilateral instrument (including the pre-Budget 2017 policy report and Cabinet paper (T2017/949, IR2017/237)). This could be done when we announce the package. Given their inevitable release under the Official Information Act in any event, releasing these documents proactively will promote transparency around the policy process to the public, rather than just individual requestors. It would also be consistent with the approach taken for previous BEPS Cabinet papers.

Recommendations

50. We recommend that the Cabinet Economic Growth and Infrastructure Committee:

1. **Note** we have developed and consulted on a package of measures to counter certain base erosion and profit shifting (BEPS) activities we are concerned about in New Zealand. In summary, the measures in the package:
 - prevent multinationals from using artificially high interest rates on loans from related parties (interest limitation);
 - prevent multinationals from using artificial arrangements to avoid having a taxable presence (a permanent establishment) in New Zealand;
 - prevent multinationals from using transfer pricing payments to shift profits to their offshore group members in a manner that does not reflect the actual economic activities undertaken in New Zealand and offshore; and
 - remove the tax advantages of exploiting hybrid mismatches between different country's tax rules.

2. **Note** the attached three Cabinet papers seek Cabinet approval to introduce these BEPS measures.
3. **Agree** that work progresses along the indicative timeline, where we plan to introduce a BEPS taxation bill by the end of this year, and enact the bill by 1 July 2018.
4. **Agree** that the measures should apply from income years starting on or after 1 July 2018, apart from:
 - The new administrative powers for Inland Revenue to deal with uncooperative multinationals should apply from the date the legislation is enacted;
 - the hybrids unstructured imported mismatch measure, which should apply from 1 January 2020; and
 - the reverse hybrid measures (generally expected to apply in relation to limited partnerships and foreign trusts), which should apply for income years beginning on or after 1 April 2019.
5. **Agree** that there should be transitional relief from the measures:
 - in relation to the hybrid measures, relief for hybrid financial instruments issued to the public before 6 September 2016; and
 - in relation to the transfer pricing and interest limitation measures, relief for arrangements subject to an advance pricing agreement entered into before 1 July 2018.
6. **Note** the original BEPS revenue that was forecast in April:

Vote Revenue	\$m – increase/(decrease)						
	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Foreign hybrid entity double deductions	-	-	25.000	50.000	50.000	50.000	50.000
BEPS taxation bill	-	-	25.000	50.000	50.000	50.000	50.000
Total Revenue effect	-	-	50.000	100.000	100.000	100.000	100.000

7. **Note** the following changes as a result of the decisions in recommendations 1 to 5 above, with a corresponding impact on the operating balance:

Vote Revenue Minister of Revenue	\$m – increase/(decrease)					
	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Tax Revenue: BEPS taxation bill	-	64.000	109.000	109.000	104.000	90.000
Total Revenue effect	-	64.000	109.000	109.000	104.000	90.000

8. **Note** the attached paper on interest seeks delegated authority for the Minister of Finance and the Minister of Revenue to make a decision on the treatment of deferred tax liabilities which includes authority to reduce the revenue forecast by \$10 million per year.
9. **Note** that forecast BEPS revenue in recommendation 6 above was treated as savings in Budget 2017.
10. **Agree** that the additional revenue in recommendation 7 be treated as savings in Budget 2018 (total to be confirmed after the decision on the treatment of deferred tax liabilities which could reduce the revenue forecast by \$10 million per year).
11. **Agree** that Inland Revenue and the Treasury undertake further targeted consultation on outstanding policy issues, technical design details and selected parts of an exposure draft of the planned BEPS bill in relation to the measures.
12. **Agree** to proactively release the Cabinet papers, policy reports and submissions for the BEPS discussion documents and the issues paper for the multilateral instrument.

Authorised for lodgement

Hon Steven Joyce
Minister of Finance

Hon Judith Collins
Minister of Revenue

Appendix One: Comparison of Australia's and New Zealand's response to the OECD's BEPS Action Plan

Action Report	OECD recommendation	Current law	NZ response to OECD recommendations	Australian response to OECD recommendations
1 – Address the tax challenges of the digital economy	Report identified issues raised by the digital economy and possible actions to address them. Did not generally recommend fundamental changes to international tax framework.	Generally robust and consistent with current international tax norms.	New Zealand imposed GST on online services. <i>GST imposed on supplies occurring on or after 1 October 2016.</i>	Same response as New Zealand. Australia to impose GST on online services. <i>GST imposed on supplies occurring on or after 1 July 2017.</i>
2 – Neutralise the effects of hybrid mismatch arrangements	Recommended domestic hybrid mismatch rules. Changes to the OECD Model Tax Convention and multilateral instrument (MLI) to address hybrid entities.	Domestic law and Double Tax Agreements (DTAs) already contain some targeted anti-hybrid mismatch rules.	New Zealand proposing comprehensive domestic hybrid mismatch rules based on OECD recommendations. <i>Public consultation in 2016/17. Legislation for domestic rules to be introduced late 2017/early 2018.</i> NZ has adopted MLI hybrid provisions to strengthen DTAs. <i>Consulted on the MLI in March 2017. NZ signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>	Same response as New Zealand. Australia proposing comprehensive domestic hybrid mismatch rules based on OECD recommendations. However, we understand Australia is not adopting hybrids recommendation 5 (reverse hybrids) while we are proposing that New Zealand adopt this. <i>Public consultation in 2015/16. Domestic law changes to take effect from 1 January 2018 or six months after legislation is enacted. Draft legislation expected to be consulted on shortly.</i> Australia has also adopted MLI hybrid provisions to strengthen DTAs. <i>Consulted on MLI in December 2016. Australia signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>

Action Report	OECD recommendation	Current law	NZ response to OECD recommendations	Australian response to OECD recommendations
3 – Strengthen Controlled Foreign Company (CFC) rules	Recommendations regarding the design of domestic rules	NZ and Australian CFC rules are already consistent with OECD recommendations.	No proposal to change CFC rules.	Same response as New Zealand. No proposal to change CFC rules.
4 – Limit base erosion via interest deductions and other financial payments	Recommended interest limitation using an EBITDA approach.	New Zealand and Australia both have an asset-based thin capitalisation test to control quantity of debt, which the OECD also recommends. Transfer pricing has limited ability to control high-priced debt.	New Zealand is improving its thin capitalisation rules by limiting interest rates on related party debt having particular regard to the interest rate of the foreign parent, and an adjustment for so-called “non-debt liabilities”. <i>Consulted on interest limitation rules in March 2017. Legislation planned for 2017/18.</i>	Similar response to New Zealand. Australia has already tightened its transfer pricing rules. Since the New Zealand discussion document was published the ATO has released administrative guidelines (in draft) on what arrangements are considered low risk and close alignment with the interest rate of the foreign parent is an important factor. Both these changes will help it challenge high interest rates on related-party debt. New Zealand is proposing the same rules as Australia in relation to the adjustment for non-debt liabilities. Australia already requires an adjustment for non-debt liabilities.
5 – Counter harmful tax practices more effectively, taking into account transparency and substance	Finalise review of member country regimes. Expand participation to non-OECD members and revision of existing criteria.	NZ’s and Australia’s laws are already robust – no harmful tax practices identified.	NZ complies with requirements to exchange binding rulings and advanced pricing agreements as recommended by OECD.	Same response as New Zealand. Australia complies with requirements to exchange binding rulings and advanced pricing agreements as recommended by OECD.

Action Report	OECD recommendation	Current law	NZ response to OECD recommendations	Australian response to OECD recommendations
6 – Prevent treaty abuse	Changes to the OECD Model Tax Convention and changes to DTAs through MLI to insert a general anti-avoidance provision called a “principal purpose test” (PPT).	NZ’s and Australia’s anti-avoidance law is generally strong, but MLI presents opportunity to further strengthen.	NZ to adopt PPT through signing the MLI. <i>Consulted on MLI in March 2017. NZ signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>	Same response as New Zealand. Australia to adopt PPT through signing the MLI. <i>Consulted on MLI in December 2016. Australia signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>
7 – Prevent the artificial avoidance of Permanent Establishment (PE) status	Changes to the OECD Model Tax Convention and changes to DTAs through MLI to prevent PE avoidance.	NZ’s and Australia’s PE definition is generally based on the existing OECD and UN Models.	NZ to implement OECD best practice standards for majority of DTAs by signing the MLI. <i>Consulted on MLI in March and signed MLI on 7 June 2017. Ratification of the MLI will follow.</i> NZ also proposing a new anti-avoidance rule for large multinationals that structure to avoid having PE in NZ. <i>Consultation on PE anti-avoidance rule in March 2017. Legislation planned for 2017/18.</i>	Similar response to New Zealand on some of the PE measures, but Australia has chosen not to implement changes to the DTA dependant agent PE provision through the MLI, but rather adopt them through bilateral negotiations. <i>Consulted on MLI in December 2016. Australia signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i> Australia’s Multinational Anti-Avoidance Law (MAAL) targets PE avoidance. <i>Applies from 1 January 2016.</i>

Action Report	OECD recommendation	Current law	NZ response to OECD recommendations	Australian response to OECD recommendations
<p>Actions 8-10 – relate to transfer pricing to ensure transfer pricing reflects economic substance</p>	<p>Changes to the OECD Transfer Pricing Guidelines.</p>	<p>NZ and Australia currently apply the OECD Transfer Pricing Guidelines.</p> <p>Recent Australian law changes are consistent with the new OECD Transfer Pricing Guidelines.</p> <p>New Zealand law requires updating to reflect new OECD Transfer Pricing Guidelines.</p>	<p>New Zealand will follow the changes to the OECD Transfer Pricing Guidelines. This involves making changes to domestic legislation.</p> <p><i>Consulted on transfer pricing in March 2017. Legislation planned for 2017/18.</i></p>	<p>Similar response to New Zealand on transfer pricing, but generally goes further than New Zealand (and OECD recommendations), by applying a separate Diverted Profits Tax (DPT).</p> <p>Legislation for the separate DPT was introduced on 9 February 2017 and it will take effect in July 2017.</p>
<p>11 – Establish methodologies to collect and analyse data on BEPS and the actions to address it</p>	<p>Recommendations regarding data to be collected and methodologies to analyse them.</p>	<p>NZ and Australia collect and analyse certain data on BEPS as a matter of course.</p>	<p>Since 2015 Inland Revenue has conducted an annual International Questionnaire that collects key data to assess BEPS risks. The most recent survey covered almost 600 foreign owned corporates.</p> <p>Additional data collection from significant enterprises is being considered as part of the BT programme of work.</p>	<p>Similar response to New Zealand. ATO requires taxpayers to complete an international dealings schedule and has implemented an International Structuring and Profit Shifting (ISAPS) initiative.</p> <p>This initiative requested data from certain Australian companies at a level similar to the country-by-country (CbC) data requested under the OECD BEPS Action Plan.</p>

Action Report	OECD recommendation	Current law	NZ response to OECD recommendations	Australian response to OECD recommendations
12 – Require taxpayers to disclose their aggressive tax planning arrangements to revenue authorities	Recommendations regarding the design of domestic disclosure rules.	For both NZ and Australia, no requirement under current law to disclose aggressive tax planning arrangements, however the combination of our strong anti-avoidance laws and the binding rulings and penalties regimes incentivise disclosure.	No law reform planned but existing law incentivises disclosure. Taxpayers will often apply for binding rulings on potentially aggressive transactions to obtain certainty as to the tax treatment – especially in light of our strong anti-avoidance law. Penalties on aggressive transactions are reduced for early disclosure of the arrangement.	Different to New Zealand. While Australia has a rulings regime and reductions in penalties for voluntary disclosure, the Australian Treasury is also consulting on whether to adopt the OECD proposals for mandatory disclosure of tax information. Submissions closed on 15 July 2016. Australia also recently implemented transparency measures allowing the ATO to publish the taxable income and income tax liabilities of large companies.
13 – Re-examine transfer pricing documentation	Changes to OECD Transfer Pricing Guidelines and recommendations regarding the design of domestic rules, including country-by-country (CbC) reporting.	NZ and Australia currently apply the OECD Transfer Pricing Guidelines, but do not have a formal programme for automatic exchange of transfer pricing documentation.	Inland Revenue is implementing CbC reporting. NZ has signed the multilateral agreement on exchanging CbC reports with other tax authorities. NZ also recently entered into a bilateral arrangement with the US Internal Revenue Service to share CbC reports. <i>Where domestic legislation is required to support the changes to the Transfer Pricing Guidelines, this will be introduced in 2017/18.</i>	Similar response as New Zealand. Australia is implementing CbC reporting. It has enacted necessary domestic law and has signed the multilateral agreement on exchanging CbC reports with other tax authorities. In addition, Australia requires large multinationals to file their local and master file documentation with the ATO. <i>Applies from 1 January 2016.</i>

Action Report	OECD recommendation	Current law	NZ response to OECD recommendations	Australian response to OECD recommendations
14 – Make dispute resolution mechanisms more effective	Recommendations on operational minimum standards and best practices for dispute resolution	NZ and Australia have strong dispute resolution systems, but do not currently allow taxpayers to approach the competent authority (CA) ¹ of either DTA partner for resolution of dispute (taxpayer must approach home country CA) and do not generally offer arbitration of CA disputes.	NZ will implement OECD recommendations on dispute resolution by signing the MLI – in particular, NZ will allow taxpayers to approach the CA of either DTA partner in a treaty dispute and provide for arbitration of CA disputes. NZ also recently issued guidance on the mutual agreement procedure (MAP). <i>Consulted on the MLI in March 2017 and signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>	Same response as New Zealand. Australia will implement OECD recommendations on dispute resolution by signing the MLI – in particular, it will allow taxpayers to approach the CA of either DTA partner in a treaty dispute and provide for arbitration of CA disputes. <i>Consulted on the MLI in December and signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>
15 – Develop the MLI to strengthen DTAs	The MLI implements substantive recommendations made in OECD’s Action 2, 6, 7 and 14 reports. Report identified public international law and tax issues; and recommended an Ad-Hoc Group be set up to develop the MLI.	NZ has a network of 40 DTAs. Some of the MLI provisions are already included in a few DTAs.	NZ officials participated in the Ad Hoc Group to develop the MLI and New Zealand signed the MLI on 7 June 2017. NZ expects to ratify the MLI in 2018 and our DTAs are likely to begin to be modified in 2019. <i>Consulted on the MLI in March 2017 and signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>	Same response as New Zealand. Australian officials participated in the Ad Hoc Group to develop the MLI and Australia signed the MLI on 7 June 2017. <i>Australia consulted on the MLI in December and signed the MLI on 7 June 2017. Ratification of the MLI will follow.</i>

¹ CA is a person authorised by a DTA to administer tax treaty provisions and resolve disputes.