Mains Practice Question

Q. What do you understand by base erosion and profit shifting (BEPS)? What are the steps taken by government in this regard at both national and international levels? (250 words)

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Approach

- Briefly describe BEPS.
- Enumerate and expand steps taken by government to deal with tax avoidance strategies adopted by MNCs.
- Give conclusion

Answer

Introduction

- Base erosion and profit shifting (BEPS) refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations.
- This undermines the fairness and integrity of tax systems because businesses that operate across borders can use BEPS to gain a competitive advantage over enterprises that operate at a domestic level.

Steps taken by government

International Level

- India has signed the **Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("Multilateral Instrument" or "MLI")** to swiftly implement a series of tax treaty measures to update international tax rules and lessen the opportunity for tax avoidance by multinational enterprises. The MLI entered into force on 1st July 2018.
  - The convention will modify India's treaties to curb revenue loss through treaty abuse and BEPS strategies by ensuring that profits are taxed where substantive economic activities generating the profits are carried out.
- India has also signed the **Inter-Government Agreement (IGA) on Foreign Account Tax Compliance Act (FATCA)** with United States.
- India also has become a signatory of the **Multilateral Competent Authority Agreement** on Automatic Exchange of Financial Account Information in 2015.
- India and the US signed an agreement for exchange of country-by-country report to enable the two countries to automatically exchange the reports filed by the ultimate parent entities of the multinational enterprises in the respective jurisdictions pertaining to the years commencing on or after January 1, 2016.

National level

- In Union Budget 2016 an '**equalisation levy' of 6 per cent** on payments exceeding over Rs 1

lakh to online ad services from non-resident entities was introduced. Prominent companies affected would be new economy multinationals with Indian subsidiaries, like Facebook and Google.
- India is the first country to impose such a levy, post the OECD action plans.
- A tax panel has recommended expanding the ambit of this levy to cover a wide gamut of transactions including online marketing, cloud computing, website designing, hosting and maintenance, platforms for sale of goods and services, and online use of or download of software and applications.
- India introduced core elements of the Country-by-Country reporting requirement in the Indian Income Tax Act, 196 through Finance Act 2016, effective from 1 April 2016.

Conclusion

- BEPS is of major significance for developing countries due to their heavy reliance on corporate income tax, particularly from multinational enterprises.
- When domestic taxpayers see multinational corporations legally avoiding income tax, it undermines voluntary compliance by all taxpayers.
- Thus, to ensure tax net is widened and it did not shrink through unfair means India need to ensure effective implementation of BEPS agreement of G20 countries.