Global Tax and the impact of BEPS on financial services

Deloitte's 2020 global survey on the OECD's Base Erosion and Profit Shifting (BEPS) initiative shines a spotlight on the next wave of the Global Tax Reset.

The BEPS agenda in 2020 – Financial services industry highlights

By all accounts, financial services firms are highly engaged in the OECD's BEPS project. This is unsurprising as the changes still being discussed at the OECD level could have significant impact on their tax liabilities, their business structures, and the operation of their tax functions.

The survey results suggest the financial services industry remains deeply concerned about the future outcomes of those discussions. Not perhaps that governments will fail to reach consensus at a policy level on issues like the Pillar One / Pillar Two project or the taxation of the digital economy; but rather that tax authorities will fail to implement the resulting regulatory decisions and guidelines consistently. For any financial services firm with an international footprint or foreign clients and investors, the specter of added complexity is concerning.

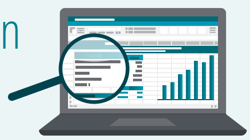
While this survey was conducted just prior to the outbreak of COVID-19, Deloitte's experience suggests the crisis has done little to ease the minds of financial services executives. In many markets, banks have been asked to play the role of both the stewards of national stimulus programs and the defenders of critical financial infrastructure. That has thrust them further into the spotlight. Financial services executives know they can't make any mistakes when it comes to tax.

From an industry perspective, the responses from this year's survey reveal financial services firms are taking solid and strategic steps to respond to the changing tax environment. Some are entering into new Advanced Pricing Agreements (APAs) and working with tax authorities to achieve greater certainty. Others are implementing new policies, creating greater transparency, and investing into new technologies aimed at reducing the complexity and risk of BEPS-related changes. Finding the right mix of operating models, controls, and processes will be key. Based on responses collected from our survey, this industry spotlight explores how financial services companies are responding to this continuously – changing environment.

Tax governance never fell from the agenda

Having suffered a historic loss of public trust during the last financial crisis, most financial services firms recognize this financial crisis must be different. Given the role some financial services firms are playing as conduits of government stimulus programs, they recognize their actions must be beyond reproach.

83% of financial services executives say they are concerned about the high public scrutiny on corporate taxation



The good news is that financial services executives and boards seem to be highly engaged in helping to manage the changing tax environment. More than six out of ten financial services executives say they have implemented new policies and procedures to tighten tax governance. And more than eight out of ten say their boards are actively engaged in tax governance.

The leading financial services companies—multinational banks, in particular – are working to create greater alignment between their finance functions, tax leadership, and audit committees to ensure that every interaction between the company and the tax authorities is understood and managed. Many are also embedding tax professionals into their corporate approval processes to ensure any tax impacts are well understood.

Craving consistency

Perhaps what worries global financial services firms the most is the potential for a lack of consistency in the way new international tax rules and guidance are applied.

In our survey, only 31% say they think tax administrations will interpret changes to the OECD's Transfer Pricing guidelines in a consistent manner. Just 55% think there will be global consensus on the taxation of the digital economy. More than half are concerned about the lack of guidance from tax authorities about the Principal Purpose Test in the Multilateral Instrument (MLI).

21%

of financial services firms are working to secure APAs with their tax authorities

In response, one-in-five financial services firms say they are now working to obtain more bilateral APAs. 45% say they anticipate higher withholding tax obligations as a result of treaty changes, whether under the MLI or as a result of renegotiations of double tax treaties.

Changes to withholding tax obligations in particular could create significant challenges for financial services firms. Those that serve as distributors of dividends, interest and capital gains, for example, will likely face increased complexity if global consistency isn't achieved. Private equity and venture capital firms and their portfolio companies may also find that their business and affiliate relationships require updating.

59% of financial services organizations say they are actively involved in the OECD's Pillar One/Pillar Two process

That being said, our data suggests that financial services firms seem to be working to help understand and influence the OECD's process. According to our survey, around six-in-ten financial services firms are actively engaged in the OECD's Pillar One/Pillar Two project consultations, either directly or through other channels. That is providing them with some additional certainty, clarity, and influence as the process evolves.

BEPS and beyond

The OECD's Base Erosion and Profit Shifting (BEPS) initiative grew out of a perception that many multinationals were not paying their 'fair' share of tax. The G20 tasked the OECD with addressing this, and the result was the OECD BEPS Action Plan focused on 15 key areas.

In addition to the BEPS project, in recent years we have seen other significant initiatives including the introduction of the Automatic Exchange of Information (AEOI) and the Common Reporting Standard (CRS), the EU Anti-Tax Avoidance Directives (ATADs 1 & 11), US Tax Reform and the Inclusive Framework's OECD-led Pillar One/Pillar Two project.

From in-house tech to outsourced innovation

At the time the survey was conducted—prior to COVID-19 – many financial institutions saw technology as the clearest path to dealing with the added complexity of BEPS-related changes. Most had a long-term tax technology roadmap that aligned to their organization's overall digital journey. The expectation was that, eventually, they would get the systems and tools they require.

The pandemic may have changed all of that. Enterprise digitization journeys were suddenly disrupted. Despite the crisis accelerating digital change, often the data is being housed in ways which prevents the tax function from effectively managing their processes internally. At the same time, CFOs' capital investment budgets have shrunk; few are looking to invest into new tax technologies at the moment.

"Financial services tax leaders need to ensure they are highly engaged in the OECD process and that they are keeping their leadership teams abreast of the changing dynamics in the tax environment. In this environment, ensuring strong relationships with tax authorities by maintaining a steady dialogue and providing transparency is critical."

John Rieger, Deloitte Global Tax & Legal – Financial Services Leader

What are financial services tax functions doing to cope with the pressure of BEPS?

- **41%** Investing into new tax technology
- **28%** Securing additional resources/ headcount
- **14%** Co-sourcing or outsourcing

While just 14% of financial services executives say they would leverage outsourced or co-sourced models to deal with BEPS-related changes, our view is that proportion would be much higher if the survey were re-run today. Financial services tax functions now understand that outsourcing is, in many cases, the only viable way to manage increasing complexity without increasing risk.

"Financial services tax leaders simply do not have the capital or the bandwidth to be managing these more complex, data-heavy processes internally," adds John Rieger, Deloitte Global Tax & Legal, Financial Services Leader. "It's not just that it's complex work. It's also very labor intensive, sophisticated and quality-driven. Given the risks facing financial services today, I expect to see more and more organizations start to explore how BEPS-related processes could be outsourced."

Get more information

To learn more about Deloitte's 2020 global survey on the OECD's Base Erosion and Profit Shifting (BEPS) initiative, we encourage you to contact the authors listed below or your local Deloitte office.

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