MAZARS INTERNATIONAL TAX CONFERENCE 2019

M&A in a post-BEPS world

October 3, 2019

MAZARS

&A IN A POST-BEPS WORLD

Introduction

- OECD has released and the G20 have endorsed the final reports on the BEPS Action Plan
- 15 focus areas reflect recommendations for significant changes in international tax lax and treaties
- Impact on tax departments and tax compliance, but also on companies business models and strategic plans

Tax impact → Legal entity structure → Planning for acquisitions and disposals → Relationship with tax policy makers

Undeniable impact on International Groups' M&A activities

M&A IN A POST-BEPS WORLD

AGENDA

1. What BEPS means for M&A-related tax risks

2. Why the traditional approach to tax due diligence should change

3. How M&A tax structuring should adapt

4. MARKET INSIGHTS

WHAT BEPS MEANS FOR M&A RELATED TAX RISKS?

Overview of BEPS

BEPS – a new global tax environment

Objectives	How?	
Establishing international coherence in corporate taxation	**Action 1** – address challenges of digital economy **Action 2** – hybrid mismatches	**Action 3** – CFC rules **Action 4** – limit base erosion **Action 5** – harmful practices
Restoring full effects and benefits of international standards	**Action 6** – prevent treaty abuses **Action 7** – artificial avoidance of PE	**Actions 8, 9 and 10** – value creation, intangibles, risk and capital, high risk transactions
Ensuring transparency while promoting certainty and predictability	**Action 11** – data collection / analysis **Action 12** – disclosure of aggressive tax planning	**Action 13** – TP documentation **Action 14** – dispute resolution mechanism
Turning tax policies into tax rules	**Action 15** – develop multilateral instrument	

M&A IN A POST-BEPS WORLD

2012 – BEPS project initiated by the G20 countries in conjunction with the OECD

2015 – finalized BEPS work and publication of the 14 BEPS focus areas

End of the recommendation phase

Implementation phase
2016 – OECD established the inclusive framework on BEPS

Inclusive framework on BEPS grew from 82 members at the inaugural meeting to 129 members (as at June 30, 2019)

May 2019 OECD PROGRESS REPORT

KEY TANGIBLE RESULTS

Action 5 (harmful tax practices):

- 255 preferential tax regimes reviewed;
- Exchange of information on 21,000 tax rulings

Action 6 (tax treaty abuse):

- The MLI now counts 89 jurisdictions
- Impact on more than 1,400 bilateral tax treaties once governments will finalize the ratification process

Action 13 (CbCR):

- More than 2,000 relationship in place for the exchange of the CbCR
- 80 jurisdictions (62 in 2018) have engaged the exchange of CbCR on the activities, income and assets of multinational enterprises

The new landscape is clear : across the world, every jurisdiction is amending its domestic tax legislation to implement BEPS inspired measures.

IMPACT ON TAX DUE DILIGENCE

Typical tax due diligence process

- Vendor populates data room / releases VDD
- Advisor and Purchaser agree scope of DD
- Advisors reviews data-room / VDD and publicly available information
- Advisor organizes detailed review at a local country level
- Advisor asks questions of/meets with Vendor's management and advisors
- Advisor collates individual country findings into a global report
- Advisor concludes that a Tax Indemnity is a good idea

The scope of the Tax DD is often driven by fee constraints rather than risk considerations

Focus is on historical events

Historical approach

Review what has happened
- Tax filings submitted on time
- Tax planning / transactions undertaken in the reviewed period
- Tax Authorities audits / enquiries

Identify errors / areas of uncertainty

Compare position to tax accounting

Seek protection for under-provisions / unrecognized tax risks

Elevate due diligence to more than just a « hygiene review »

Use due diligence to drive tax value into the M&A process:
- Assessment of enterprise value
- Risk allocation
- Post-deal integration

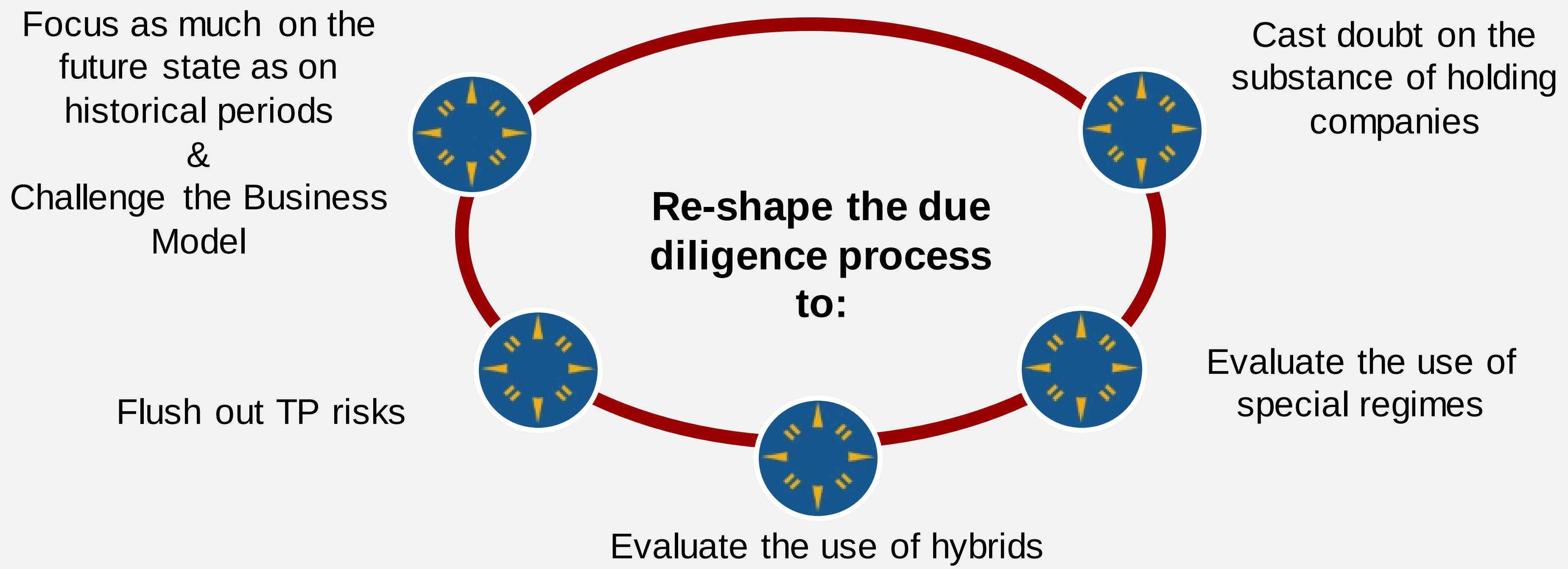
Why the traditional approach to tax due diligence should change?

A different approach is required

New challenges

Business model issues
- Transfer pricing issues
- Permanent establishments

Structural issues
- Corporate residence
- Tax Treaties access



BEPS – THREE KEY QUESTIONS

Relevant BEPS actions	PAST	FUTURE
Action 3 – CFC rules	◔	●
Action 4 – Interest expenses limitations	◔	●
Action 5 – Harmful tax practices	◔	●
Action 7 – Artificial avoidance of PE	◔	●
Action 8 to 10 – Transfer Pricing	◔	●
Action 2 – Hybrid mismatch arrangements	◔	●
Action 6 – Tax treaties	◔	●

➔ The tax due diligence approach must evolve

What does this mean for risk management?

Tax indemnity	- Financial limits - Time limits - Ongoing monitoring required
Deferred consideration / Escrow account	- Requires quantification of the issues - Requires mechanism to allow the issue to be resolved within a suitable time frame
Price reduction via: - Assessment of enterprise value - Locked box or completion accounts	- Requires close discussion with the deal team - Requires quantification / negotiation
Tax risk insurance	- Market still developing - May be cheaper than you think

Tax risk insurance

Insurance in M&A Deals

Overview of the Market

Coverage possible

W&I insurance to cover unknown risks

Tax Insurance

- Good scope and quality of the tax DD process
- Coverage possible for specific tax indemnities

- In M&A deals or not
- Coverage of identified tax issues
- Market updates

IMPACT ON DEAL STRUCTURING AND STRATEGY

Structuring an acquisition in a BEPS environment

The tax landscape governing financing and capital structures for international groups is changing. International groups will need to **assess the impact**, **respond to change** and **report the impact**.

	Actions 2 and 4 Interest deductibility / hybrids	Actions 5 and 6 Treaty abuse	Actions 11, 12, 13 Transparency disclosures	Overlay
Assess the impact	- Identify potential Hybrids and analyse local variation - Model impact/consider strategy - Anticipate potential changes in regulations	- Verify solidity of holding structures	- Identify the communications (transfer of rullings, CBCR, TP) - Evaluate the reputational risks attached to a structure	CBCR MLI CFC rules
	- Assess the impact taking into account potential tax reform scenarios - Assurate group forecasts will allow effective modelling (include impact of responses to other BEPS actions) - Understanding variation in jurisdiction's responses in key – scenario planning			
Respond to change – Resset the Strategy	- Respond in line with group tax policy, strategy and governance, and group risk appetite - Align with group profit forecast, other potential acquisitions - Likely to be a short term (planning opportunities) or a long term strategy			
Report the impact	- Groups will have to communicate their strategy to stakeholders and be ready for any further questions			

EXAMPLE

CASE STUDY

- Acquisition of a group of infrastructure assets
- Proposed acquisition of the entire share capital of UK HoldCo (Target Group in Green)
- Assets physically located in various EU jurisdictions
- Centrally managed investment, financing and services from UK HoldCo

Case Study

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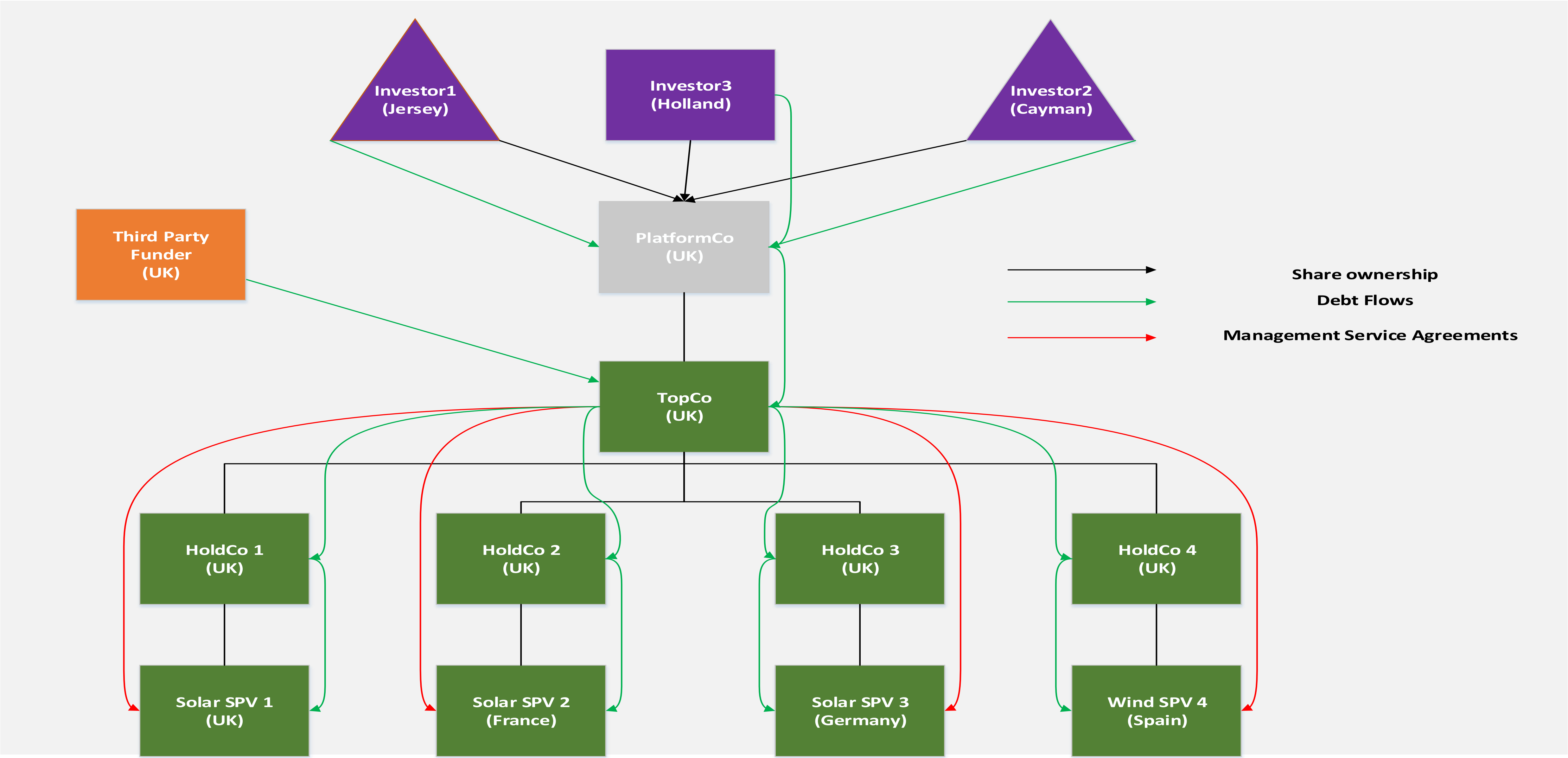

KEY BEPS RISK AREAS

- Tax residency of entities – do the activities of the Holding Company and associated directors impact on the potential tax residency of the overseas SPVs?
- Anti-hybrid arrangements - will the ownership structure of the ultimate investors and the provision of the intra-group financing fall within the anti-hybrid arrangements, either at a UK or overseas SPV level?
- Transfer pricing – the provision of the services through the MSA, and the associated financing through shareholder debt down to the overseas SPVs. What are the transfer pricing basis for the current treatments applied? What if any supporting documentation is prepared, including at a wider group level?
- Interest deductibility – beyong the application of the anti-hybrid and transfer pricing arrangements, what are the implications of the interest deductibility rules in the different jurisidictions and how have these been assessed?
- Controlled Foreign Companies – All within the EU for the purposes of the target group but do any other risks arise?
- SPA or other protections against risks arising?
- What about other taxes outside of Corporation Tax?

TRADITIONAL APPROACH

TAX STRUCTURING POINTS

For the acquirer there are a number of look forward considerations which will impact on the preferred structure:

- Existing transfer pricing policy?
- Local jurisdiction operation of SPVs vs centralised operation
- Nature of financing of the purchase – external funding, debt funding, capitalisation of existing financing –impact/importance of the tax shield

IMPLEMENTATION

TAX STRATEGY

Is the bigger risk the historic risk or the future risk? The implementation

- Does the acquisition impact on the BEPS risk approach of the wider organisation?
- Does the acqusition structure need to change to fit the wider group tax risk profile or vica versa?
- Global footprint of the existing group and whether the post-acquisition re-structuring would provide efficiences
- Are there BEPS specific areas which would need to be re-assessed in the light of the acuqisition- for example transfer pricing policies for intra-group service provision.

NEW APPROACH

MARKET INSIGHTS

INSIGHT INTO INFRASTRUCTURE

- Unprecedented levels of liquidity in the market creates increased pressured on deployment of capital, with a lack of supply of available opportunities
- Impact of wider organisational response to BEPS on commercial arrangements
- Trend towards consolidation of assets into larger portfolios – therefore a greater risk from BEPS
- Still not a great awareness in some commercial teams - Organisational disconnect
- Focus remains on historical risks and transactional costs from a tax perspective within commercial discussion – greatest cash impact is the integration within the organisation's existing tax arrangements
- Growing requirement from our clients on sell side mandates to "get their house in order".

Market insights

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