

ASPECTS REGARDING BASE EROSION AND PROFIT SHIFTING IN ROMANIA**Lecturer PhD Marius-Sorin CIUBOTARIU***Stefan cel Mare University of Suceava, 720229, Romania
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corina_petrescu23@yahoo.com***Abstract**

In a world characterized by globalism and initiatives of harmonization in almost every aspect of the social and economic life, showing interest, support and credibility towards the international common struggle against base erosion and profit shifting (BEPS) phenomenon has been seen like a duty by the Romanian government, which in June 2016 approved the country's adherence to the BEPS Implementation Forum. This huge step involved Romania in an international complex system of communication, exchange of information and strategical planning, which includes many other countries from all over the globe, every one of them having their irreplaceable role in this entire process, because an extra country that accessed this system, means more power and resources in the global fight against BEPS. What are the steps to be made and what are the legal and procedural implications of Romania adhering to the BEPS Implementation Forum is what this article is going to focus on, finding out the progress made until now and the domains with deficiency that need improvement, so that everything to be according to the international demands in the field.

Key words: *BEPS, tax practices and policies, OECD, BEPS Action Plan, legal framework*

JEL Classification: *F23, F38, F61, H26, M48*

I. INTRODUCTION

Being a member country of the European community and other international or regional treaties and economic or strategic communities and organizations, Romania is an open country to foreign investments, encouraging and facilitating them through a relatively low level of taxation – among the lowest from Europe. Given this fact, many multinational companies operate on the territory of the Romanian state, so they have to comply with the Romanian tax legislation and pay the taxes provided by the mentioned legal framework. However, broadly speaking, many multinational companies don't have an ethical behaviour and they exploit the interpretability, the gaps and the misunderstandings existing in a legal framework, just to make sure they do not pay the correct amount – or not at all - of taxes in the countries they operate and obtain their profits, because they consider that the level of taxation is high or they simply don't want that their income and profit to be taxed. In this situation, we can talk about the manifestation of the BEPS phenomenon – the erosion of tax base through non-declaration of the profits or through shifting them to subsidiaries or affiliated companies from low or zero tax jurisdictions (tax havens), fact that creates the premises of a tax evasion operation.

This kind of situations are not isolated cases, but an entire international system of well thought out and planned practices, where the majority of multinational companies is involved, affecting this way the equity and the fairness of the global trade system. The most affected countries by this phenomenon are those in the African and Asiatic continents, countries that are rich in resources but poor in the legal and administrative capacity of their leaders to manage them, many of them being exploited by multinational giants that give back very little to their society, compared with the high value of the resources they use from them. We consider that all of us realize the tremendous inequalities and injustice that are generated by these practices, in terms of the chances of people to education, success, public services and facilities, infrastructure and the list can go on.

To help governments all over the world to have legal instruments to approach this kind of situations, the Organization for Economic Co-operation and Development (OECD) issued in 2015 the BEPS Action Plan that is structured in 15 Actions that tackle the domains in which the BEPS phenomenon could have an impact, giving in the same time practical and real solutions for a better management of this kind of situations. These 15 Actions can be implemented progressively or simultaneously by the countries in their domestic legal framework for substantiating the national fight against BEPS phenomenon. Romania has opted for the progressive domestic implementation of the BEPS Action Plan, making the corresponding changes in the tax regulations, that could meet the national needs in this field.

II. LEGAL FRAMEWORK ON BASE EROSION AND PROFIT SHIFTING IN ROMANIA

Acknowledging the need of a stronger enactment in the fiscal field and being strongly affected by BEPS practices, on 2nd June 2016, Romania became an associate to the BEPS Implementation Forum, together with many other member countries of the OECD and of the Group of Twenty (G20), engaging itself in a challenging process for complying the national regulations to the international standards and recommendations in domain (Roşca, 2016). To support this decision, in June 2017 the Romanian authorities issued the *Law no. 124/2017 regarding the approval of Romania’s participation as an associate member to the BEPS Project*, published in the Official Gazzete no. 415, in the same month (<http://legislatie.just.ro/Public/DetaliiDocumentAfis/189904>).

According to the memorandum regarding the law Project for Romania’s participation as an associate member to the BEPS Project, our country engaged some obligations resulting from this quality of associate, as we can see in Figure 1 below.

Romania's commitments regarding BEPS Action Plan implementation	→ will participate in activities related to technical aspects, in domains like transfer pricing or tax treaties, participation that can consist in the improvement and development of the transfer pricing guidelines and of the conventions regarding the avoidance of double taxation;
	→ will implement the minimum standards of the BEPS Action Plan that consist in: Action 5 regarding harmful tax practices, Action 6 regarding tax treaty abuse, Action 13 regarding Country by Country Reporting (CbC Reporting) and Action 14 regarding mutual agreement procedures.
	→ will monitor and supervise the evolution of taxes determined by the digital economy challenges (Action 1) and through economic analysis of BEPS (Action 11);
	→ will join the main making decision organisms regarding the international tax system, such as Commission of tax affairs of the OECD and its subsidiary bodies;
	→ will implement the 2, 3 and 4 Actions of the BEPS Plan, starting from the transposition of the European Union (EU) Directive 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (Anti Tax Avoidance Directive - ATAD) adopted by the Council (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02016L1164-20200101);
	→ will be involved in the OECD's working groups that have assigned a domain of research;
→ will implement Action 15 of the BEPS Action Plan, by signing in 7th June 2017 the Multilateral Convention to Implement Tax Treaty related Measures to Prevent BEPS (https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf).	

Figure 1 - Romania's commitments regarding BEPS Action Plan implementation

Source: <https://sgg.gov.ro/new/wp-content/uploads/2017/03/EM.pdf>

Therefore, romanian authorities have had and still have a lot of work to do, such that all these commitments to be entirely and correctly achieved. The main part of the work refers to the elaboration of a legal and procedural national framework that would perfectly mirror the principles and the values promoted at an international level through the provisions of the BEPS Action Plan.

Regarding the minimum standards implementation, changes have been made to the *Law no. 227/2015 regarding the Fiscal Code* and to the *Law no. 207/2015 regarding Fiscal Procedural Code*, considering the fact that the main problem of the BEPS phenomenon refers to tax policies and practices. In the first place, the CbC Reporting system was implemented through the *Emergency Ordinance (OU) no. 42/2017* and later through the *Government Ordinance no.5/2020 for modification and completion of the Law regarding Fiscal Procedural Code* that internally implemented the provisions of the *Council EU Directive 822/2018 in relation to cross-border tax arrangements (DAC6)*. This regulation brought new stipulations regarding the CbC Reporting, both for taxpayers and intermediaries involved in transactions (WtsGlobal, 2020). According to the romanian law, this kind of reporting must be done by a Romanian tax-resident entity that is the ultimate parent entity of a multinational enterprise (MNE) group with consolidated revenues of 750 million euro or more, by a so-called ‘surrogate parent’ and by some companies that meet certain exceptional criteria (PricewaterhouseCoopers - PwC, 2020). Through this kind of reporting system - that exposes information regarding the global allocation of profit, income, taxes paid and economic activity among the jurisdictions where the MNEs operate (Bancescu & Rus, 2020) - high level risks regarding transfer pricing and BEPS can be evaluated and supervised by tax authorities. If the subjects do

not meet these legal requirements along with their implementation deadlines, they would face significant financial sanctions together with some reputational risks on international level. To determine a clear content and template of the CbC Reporting, there was issued the *Order no. 3049/2017 regarding the approval of the model and content of the R404 and R405 forms*.

For the implementation of the Action 14, the Romanian Government issued the *Ordinance no.19/2019* that establishes the mutual agreement procedure (MAP), a cross-border dispute settlement mechanism, which applies when two jurisdictions do not agree with some of the avoiding double-taxation regulations, each one of them trying to obtain the money - from the taxes paid by the same contributor - for their budget, fact that generates a conflict of interest situation. In Romania, the solving period for these disputes are quite long – up to 86 months, compared to the European average of 25 months, fact that highlights a lack of involvement and a low level of management from the tax authorities, that should be more opened to dialogue with other jurisdictions for obtaining a bilateral solving agreement for the matter (Popa, 2020).

Aspects referring to Action 2, 3 and 4 of the BEPS Action Plan, respectively those regarding the interest deductibility and the anti-hybrid rules and the controlled foreign companies are regulated in the Romanian Fiscal Code and in the Fiscal Procedural Code. Therefore, according to the law, the interest deductibility rate for corporate income tax purposes is 30% of the tax base, when the borrowing costs registered in a fiscal year exceed the threshold of 1 million euro. The hybrid mismatches refer to the situation in which the same instruments, entities or transactions are differently qualified in the jurisdictions involved, most of the time leading to double non-taxation situations or double deductions, fact that significantly reduces the governments revenues (Chrenko & Hrdlicka, 2012). To solve this kind of situations, one of the jurisdictions involved should deny the deduction that is the subject of the hybrid mismatch.

Regarding the transfer pricing Romanian legal framework, it is based on the *OECD Transfer Pricing Guidelines* and on other international recommendations and regulations. Therefore, we can mention the *Order no. 442/2016 regarding the amount of transactions, the deadlines for preparation, the content and the conditions for requesting the transfer pricing file and the adjusting/estimating the transfer pricing procedure*. This regulation applies to the contributors that have intra-group transactions, imposing them to prepare the transfer pricing file, which should prove to tax authorities that the arm's length principle has been taken into account in their activity. Otherwise, the authorities have the right to adjust the practiced transfer prices, in such a way that they could observe no preferential treatment in the transactions with affiliated companies.

Contributors have also the possibility to obtain unilateral or bi/multilateral Advanced Pricing Agreements (APA) - by submitting an application to the tax authorities that can be solved between 12-18 months - in order to secure their position regarding the transfer pricing policies for the next fiscal years. This way, they can assure that for 5 years – the validity period of the agreement - there will not be adjustments from the tax authorities, if the conditions and the terms of the established APA are taken into account, they having the obligation to report their implementation for every fiscal year (<https://www.atipics.ro/>). We can say that these kind of agreements are quite expensive, their price falling between 10.000 – 20.000 euro, depending on the size of the company (<https://www.fiscalitatea.ro/acordul-de-pret-in-avans-175/>). These agreements are regulated by *Order no. 3735/2015 for approving the procedure regarding the issue and the modification of the advance pricing agreements*.

The engagement of our country in the implementation of the BEPS Action Plan represents a real challenge for the Romanian authorities, given the fact that it implies not just a simple textual modification of the existing legal framework, but much more than that: changing the mentality and the way of approaching tax matters, both from taxpayers and authorities. We can say that a solid framework regarding BEPS Plan implementation is outlining in Romania, fact that helped and will continue to help our country to simplify the international relations with other jurisdictions and to obtain the right amount of money from taxes from the contributors.

III. ROMANIA FROM THE POINT OF VIEW OF THE PROGRESS MADE IN THE FIGHT AGAINST BASE EROSION AND PROFIT SHIFTING PHENOMENON

As we already know, Romania engaged itself in the global fight against BEPS phenomenon, making this in a progressive manner through creating new regulations or updating those existents, supporting and encouraging this way an ethical behaviour of the multinational companies that activate on its territory. Although there was certainly a significant legislative and procedural progress, there are still domains and activities that need a serious improvement for a more transparent and efficient tax system in our country, aspect demonstrated by the results obtained by Romania for two main indexes - presented by Tax Justice Network - that can measure the progress of a country in the anti-BEPS fight.

Therefore, we can talk about the Financial Secrecy Index (FSI) and about the Corporate Tax Haven Index (CTHI), which complement each other. FSI ranks the countries according to their level of secrecy of information and of their offshore financial activities (<https://fsi.taxjustice.net/en/introduction/introducing-the-fsi>) and CTHI

ranks the jurisdictions depending on how much they help multinational companies to underpay corporate income tax (<https://cthi.taxjustice.net/en/>).

The main question FSI is trying to answer is “What is the level of the prejudice that every jurisdiction is responsible for, when they provide offshore financial activities simultaneously with a lack of information transparency” (Tax Justice Network, 2020: 3)? When calculating the FSI, a qualitative and a quantitative component is taken into account, respectively the Secrecy Score and the Global Scale Weight. Romania is ranked on the 56th position from 133 analysed jurisdictions, with 63/100 points for the Secrecy Score and with a value of 0.08% for the Global Scale Weight component, meaning a tiny contribution to the global amount of offshore financial activities (<https://fsi.taxjustice.net/PDF/Romania.pdf>). The value of the Secrecy Score is determined by analysing twenty indicators from four different domains: ownership registration (1), legal entity transparency (2), integrity of tax and financial regulation (3) and international standards and cooperation, indicators whose results can be seen in Figure 2 below.

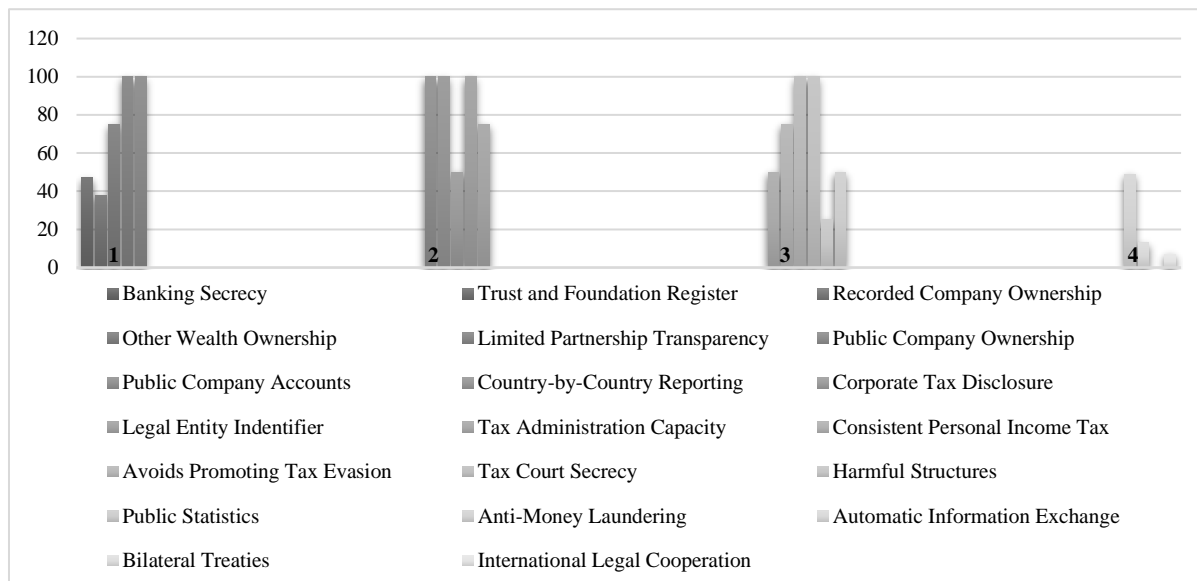


Figure 2 – Results for the indicators of Secrecy Score component of FSI 2020 for Romania

Source: Adapted after <https://fsi.taxjustice.net/PDF/Romania.pdf>

The higher the value of an indicator, the more critical is the situation to which it refers and the lower the value of an indicator, the more optimal is the situation to which it refers. If we look at the chart above, we can see that the majority of indicators have high values, seven of them having the maximum value of 100 points, fact that shows a quite low level of financial and tax information transparency in Romania. We can see that the lowest obtained values are in the domain of the international standards and cooperation, where we can find the indicator “Bilateral Treaties,” the only one that obtained zero points, highlighting the fact that Romania focused mainly on improving the international relations and cooperation with other jurisdictions. The first three approached domains need a quick and efficient improvement, so that Romania could have a better position in the FSI ranking. Regarding the ownership registration domain, there was already issued the *Law no. 129/2019 for the prevention of money laundering and terrorism financing* that forbids new issues of bearer shares and provides for mandatory conversion – until January 2021 – of all existent bearer shares into nominative shares, otherwise they will be cancelled.

While FSI focuses more on how the rich people and the criminals tend to hide their wealth and illegal transactions, CTHI focuses on the possibilities of multinational companies to avoid paying their taxes. This index has also two components: Haven Score that is the qualitative component, its value being given by the data collected for twenty indicators and the quantitative component – Global Scale Weight - which measures the relevance of each jurisdiction for cross-border direct corporate investment (Ates, Cobham, Harari, Janský, Meinzer, Millan-Narotzky & Palanský, 2020: 9). In the CTHI ranking, Romania is on 43rd position from 63 analyzed jurisdictions, with 56/100 points for Tax Haven component and with a small contribution for global cross-border direct corporate investment (<https://www.corporatetaxhavenindex.org/PDF/Romania.pdf>). Occupying this position, Romania can’t be considered the ideal tax haven for the investors, but neither a destination that doesn’t deserve to be taken into account by them. The areas of analysis of the twenty indicators for the determination of Haven Score value are: lowest available corporate income tax (1), loopholes and gaps (2), transparency (3), anti-avoidance (4) and double tax treaty aggressiveness (5), the results being available in the Figure 3 below.

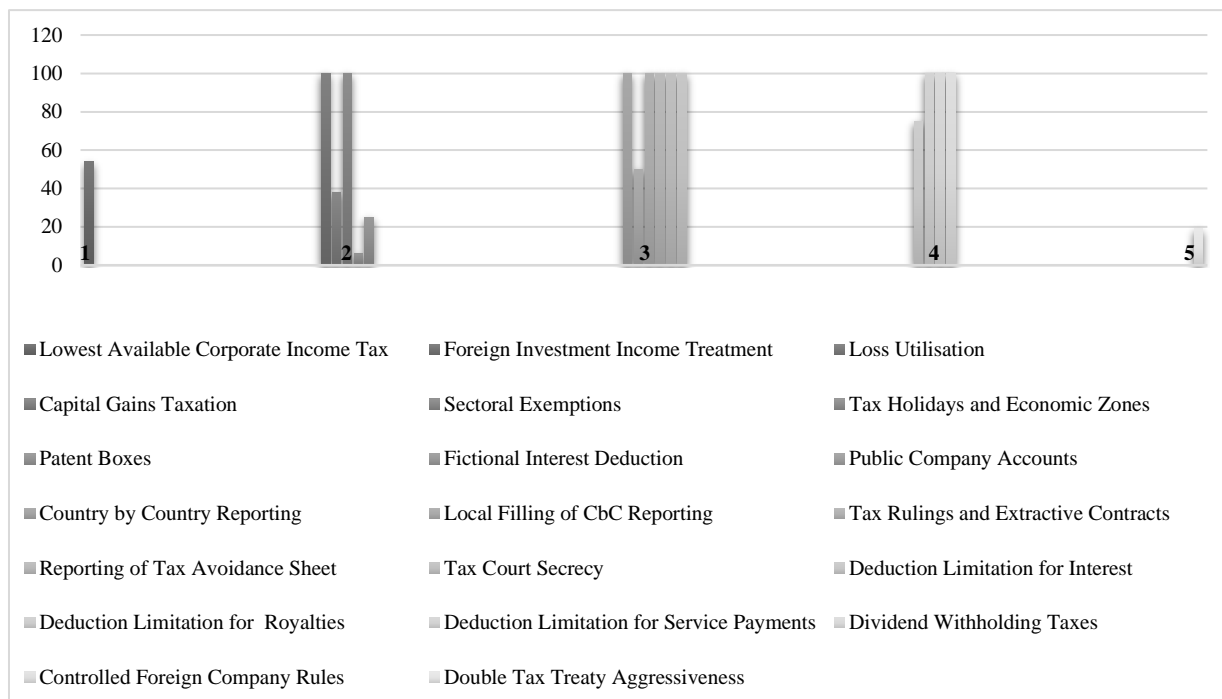


Figure 3 - Results for the indicators of Haven Score component of CTHI 2019 for Romania

Source: Adapted after <https://www.corporatetaxhavenindex.org/PDF/Romania.pdf>

As in the case of FSI, the higher the value of the indicator, the more critical the situation. As we can see, the most critical situation is in the transparency area, where five indicators have 100 points and the sixth – CbC Reporting - has 50 points, fact that highlights a real high level of secrecy of financial and tax information in Romania. The most optimal situation is in the domain of loopholes and gaps of the legal framework, where two of the indicators – Patent Boxes and Fictional Interest Deductibility - obtained 0 points, meaning that Romania has a quite efficient regulation on interest deductibility and on patents management. We can see a serious problem in the anti-avoidance measures domain too, where three indicators obtained 100 points after evaluation, because of a quite high level of deductibility when calculating the tax base.

We can see that both of the analyzed indexes highlight the lack of information and transaction transparency in the economic activity of multinational companies in Romania. Although Romania made a significant progress, there is still need for many other improvements and for a reinforcement of the law through new and updated measures that could determine a better profile of our country in the global ranking regarding the progress made in the anti-BEPS fight.

IV. CONCLUSION

Romania, together with other countries that have been victims of the BEPS mechanisms and practices used by multinational companies to minimize their taxes, had the opportunity to give an appropriate answer to this matter by officially joining into the global fight against the effects of this phenomenon. Since then, the legal tax framework is constantly improving and updating, in order to meet the new challenges and requirements of the international economic environment. Like any other beginning, the first steps in the domestic implementation of the BEPS Action Plan provisions were not easy, but full of difficulties, given the new concepts and procedures that needed to be transposed into the national legislation and then into practical guidelines that could support the companies in respecting the law. As we have seen, Romania made a significant progress in obtaining the tax revenues that was entitled to receive, which results in more funds for sustaining the public activities and services, therefore a better quality of life for its citizens. However, we all know that there are many things that need to be done for Romania to achieve the global requirements on combating the BEPS phenomenon, but at least, be know for sure that it is on the right track and the results will not be long in coming.

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