Glossary

Arm's length principle (ALP). Under the ALP, companies within the same group are treated as if they were unrelated, independent entities and intragroup prices are expected to be similar with the prices which would be charged by independent parties.

Anti-tax avoidance rules. General of specific tax rules targeting to curb BEPS / tax avoidance / profit shifting (OECD, 2015b).

Base erosion and profit shifting (**BEPS).** Base erosion and profit shifting or tax avoidance or profit shifting refers to legal tax planning strategies that exploit **gaps and mismatches in tax rules** to certain extent even artificially shift profits to low or no-tax locations, resulting in little or no overall corporate tax being paid. (OECD, 2015b).

Base erosion and profit shifting (**BEPS) countermeasures.** General of specific tax rules targeting to curb tax avoidance (OECD, 2015b).

Capital structure. Capital structure could be defined as the way a firm finances its assets through different combinations of equity, (short-term and long-term) debt or other hybrid securities.

Corporate income tax (CIT). Corporate income tax is a type of tax on capital; it is a tax on company profits which are usually recognised on accrual basis

Debt shifting. Conversion of capital structure from equity financed to debt financed to benefit from debt tax shield. It may take form of internal (intra-company, related party) or external (financial institutions, third party) debt, performed via extra borrowing in high-tax countries, lending from low-tax countries and generating low effective rate at the consolidated level of MNE.

Earnings before interest and taxes (EBIT) is a measure of an operating profitability that includes all expenses except interest and tax expenses. It is the difference between operating revenues and operating expenses (OECD, 2015c).

Earnings before interest, taxes, depreciation and amortization (EBITDA) is operating profitability measure as well as a proxy for cash flow calculated using a company's net profits, before interest expenses, taxes, depreciation and amortization (OECD, 2015c).

Earnings stripping rules. New, separate type of thin capitalisation rules which limits interest deductibility up to certain proportion to EBIT or EBITDA. In most cases, it applies to both third- and related-party loans, in some cases it applies only to one type of loans – related party loans. Interest expenses or net interest expenses (interest expenses less interest income) are deductible up to the *de minimis* level without restriction. If the net interest expenses are above the limit, the rule is applied on the total amount of net interest expenses ignoring the limit. If firms incur net interest expenses above the limit, the expenses are deductible but only up to a another (upper) limit calculated as percentage of (tax adjusted) EBIT or EBITDA. The predominant EBITDA percentage is 30% which can be found in EU (European Commission, 2015).

Effective tax rate (ETR) is the average ratio of total tax expenses divided by profit before tax, expressed as a percentage and calculated for one tax period (OECD, 2015a).

Permanent establishment (PE) is a fixed place of business of a foreign company in other country which gives rise to a corporate income tax liability in that country even without legal registration (OECD, 2015a).

Profit shifting. Profit shifting refers to legal tax planning strategies that exploit gaps and mismatches in tax rules to certain extent even artificially shift profits to low or no-tax locations, resulting in little or no overall corporate tax being paid. Although the arrangement could be legal (i.e. in line with the "letter of the law"), it is usually in contradiction with the intent of the law it purports to follow (i.e. against "the spirit of the law") (OECD, 2015b).

Safe harbour approach to thin capitalisation rules. Some countries apply fixed ratio (safe harbour) approach which is based on a certain ratio derived from balance sheet of a firm. The most commonly used ratio is the debt to equity ratio; however, the allowed level of debt may vary from country to country, may apply only to related party debt (i.e. targeting internal debt shifting) or to both internal and external debt (targeting also external debt shifting). Generally, deduction of interest on the debt exceeding the fixed ratio of debt to equity is disallowed for corporate income tax purposes.

Statutory tax rate (STR) is the standard tax rate indicated in the law of a particular country. The statutory tax rate is applied on a tax base which is taxable profits calculated under the tax law of a particular country (OECD, 2015a).

Tax avoidance. Tax avoidance refers to legal tax planning strategies that exploit gaps and mismatches in tax rules to certain extent even artificially shift profits to low or no-tax locations, resulting in little or no overall corporate tax being paid. Although the arrangement could be legal (i.e. in line with the "letter of the law"), it is usually in contradiction with the intent of the law it purports to follow (i.e. against "the spirit of the law") (OECD, 2015b).

Tax Base is the amount of taxable income or profits which is subject to corporate income tax.

Thin capitalisation rules (TCR). The rules that limit interest deductions for tax purposes. The thin cap rule acts as a BEPS countermeasure, it restricts firms from incurring excessive debt solely for the purpose of reducing taxes, but it allows firms to incur debt, and take a tax deduction, when such debt is a normal part of a firm's business model.