



THE POTENTIAL IMPACT OF THE OECD'S MULTILATERAL INSTRUMENT ON GLOBAL TAX STRUCTURING

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What is the MLI?

- “Multilateral Convention to Implement Tax treaty related measures to prevent **Base Erosion and Profit Shifting**”
 - Result of **BEPS** Action 15 and **implementation** of various BEPS Actions
 - **98 Countries** joined forces in the MLI Ad Hoc Group and developed this MLI
 - Stand-alone multilateral treaty which **swiftly implements** BEPS measures into the bilateral tax treaties of participating jurisdiction:
 - **Not** through an **amendment** of existing treaties
 - **Instead**, the MLI provisions need to be read and applied **alongside** existing treaties
 - Requires ‘normal’ **treaty ratification** in each country
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How does the MLI work?

- The MLI includes some mandatory ***minimum BEPS standards***, to ensure effective application;
- Countries have flexibility through ***opt-in and opt-out*** mechanisms (***except*** for the mandatory ***minimum standards***), as well as ***alternative provisions***;
- For treaties that already contain provisions: “***compatibility clauses***” provide how an MLI provision will interact with related provisions of an existing tax treaty;
- The MLI will only apply to existing tax treaties that are **explicitly listed** by both contracting states;
- Optional MLI provisions: only if the **two countries** concerned indicate the **same choice**;
- **Reservations** (resulting in opt-out): apply between that state and **all other parties** to the MLI.
- **Notify** the **OECD** (as depositary of the MLI): Which treaties, which options and which reservations?

Which topics are included in the MLI?

- Transparent entities / hybrids (art. 3 MLI);
- Dual resident entities (art. 4 MLI);
- Prevention of treaty abuse (through PPT/LOB) (art. 7 MLI);
- Capital gains on shareholdings in real estate entities (art. 9 MLI);
- Anti-abuse rule for low-taxed third country PEs (art. 10 MLI);
- Artificial avoidance of PE through commissionaire arrangements (art. 12 MLI);
- Artificial avoidance of PE through specific activity exemptions (art. 13 MLI);
- Splitting-up of contracts (art. 14 MLI);
- Mutual agreement procedure (art. 16 MLI and 17 MLI).

When does the MLI enter into force?

- For withholding taxes:

Taxable events occurring on or after the **first day of the calendar year** that begins **on or after the latest** of the two dates on which the MLI enters into force for each of the two Contracting States

For example, if the MLI enters into force for Country A on 1 March 2018 and for Country B on 1 March 2019, the MLI will take effect with respect to withholding taxes relating to an event occurring from 1 January 2020 onwards

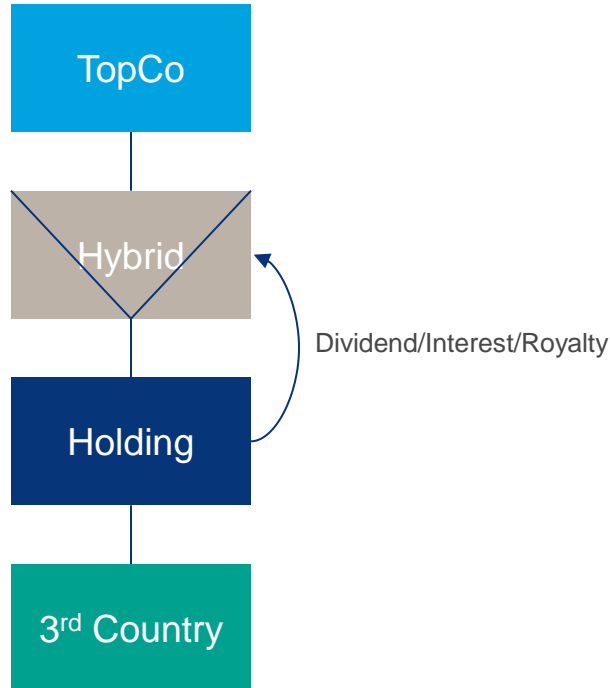
- For other taxes (including CIT):

Taxes levied with respect to **taxable periods** beginning **on or after** expiration of a period of **6 calendar months** (or a shorter period if Contracting States agree on this) **from the latest** of the two dates on which the MLI enters into force for each of the two Contracting States

For example, if the MLI enters into force for Country A on 1 March 2018 and for Country B on 1 September 2018, the MLI provisions that will affect the A-B tax treaty will take effect with respect to taxable periods beginning on or after 1 March 2019 (and in case the taxable year coincides with the calendar year: as of 1 January 2020)

Most impact in practice – MLI articles (3, 7 and 12)

Transparent entities (art. 3 MLI)



Measures of art. 3 MLI

- Tax treaty benefits are denied if the income is not taxed on a current basis in one of the Contracting States (art. 3(1) MLI); and
- No double taxation relief is provided if the other Contracting State does not tax income either as (i) source state or (ii) PE state (art. 3(2) MLI)

Practical impact and attention points

- Art. 3 MLI denies treaty benefits on payments through “reverse hybrids”, e.g. in a CV/BV structure

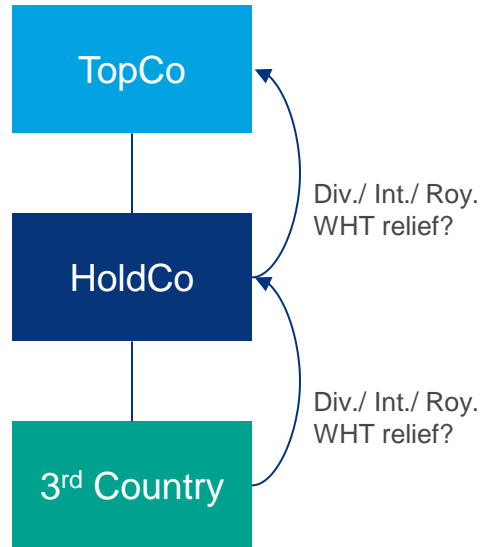
Compatibility clause

- Art. 3(1) MLI applies in place of, or in the absence of general or specific Tax Treaty provisions that deal with income of fiscally transparent entities.

Permitted reservations

- This MLI provision does not reflect as a minimum standard. Consequently, Parties may opt out of art. 3 (1) or (2) MLI entirely or choose to keep existing provisions included in treaties and protocols.

Prevention of treaty abuse (art. 7 MLI)



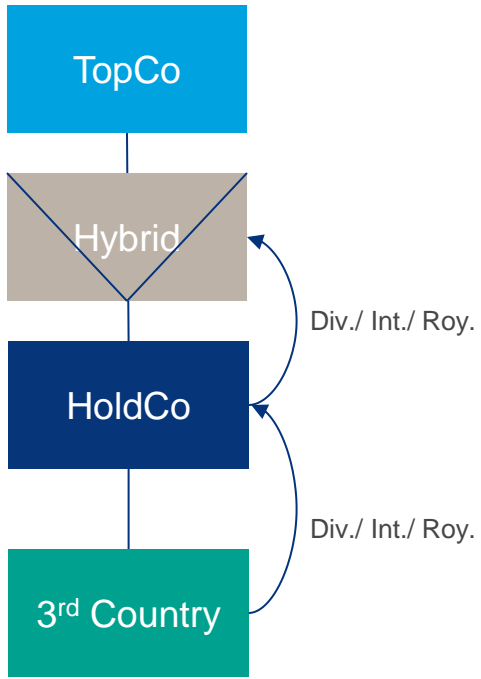
Measures of art. 7 MLI

- The Principal Purpose Test (**PPT**) is the default option (→ it **satisfies** the **minimum BEPS standard** on its own)
- Parties may supplement the PPT by opting for a simplified Limitation on Benefits (**LOB**)
- Parties may opt out of the PPT and choose a detailed LOB. However, a detailed LOB should be negotiated **bilaterally** and is not included in the MLI provision
- Parties that choose to bilaterally negotiate a detailed LOB may apply the **PPT** as an interim measure

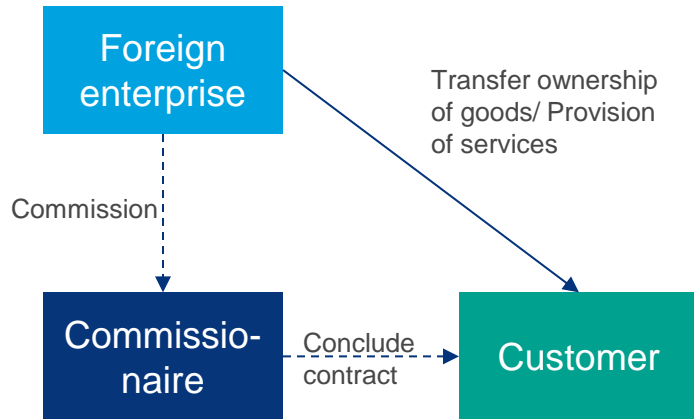
Practical impact and attention points

- Expected to have a substantial impact on treaty eligibility in new and existing holding, financing and royalty structures → increasing substance and functionality are required
- Most Parties are expected to apply the **PPT only**, in particular within the EU (given the EU compatibility concerns regarding the LOB)
- Limited guidance on the PPT.

Combination of art. 3 MLI and art. 7 MLI; often seen in US context



Artificial avoidance of PE through commissionaire arrangements (art. 12 MLI)



Measures of art. 12 MLI

- The PE threshold for dependent agent PE is lowered if the contracts, that are routinely concluded without material modification, are:
 - in the name of the foreign enterprise;
 - for the transfer of property owned by the foreign enterprise; or
 - for the provision of services by the foreign enterprise
- A person that acts (almost) exclusively on behalf of one or more 'closely related' enterprises is not an independent agent

Practical impact and attention points

- Art. 12 MLI significantly lowers the threshold for a dependent agent PE
- New definition requires a material analysis of functions and powers of a potential agent and its principal;
- No longer relevant whether the agent has the formal authority to sign contracts, or not;
- Art. 12 MLI is not intended to address **low-risk distributor arrangements!**

Conclusions

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- Implementation phase of BEPS has taken off! → **Globally**
- Significant impact on many MNE structures → **restructurings required**
- Only 1-2 years before entry into effect → **not much time left...**
- Period of significant uncertainty expected → **Chaos?**
- But the good news is... → **Chaos creates new work!**

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