taxsutra

BMR Advisors

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SCALING BEPS

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SCALING BEPS

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INTRODUCTION

Note from the Editor:

The ambitious BEPS project has entered a crucial phase, as we unveil the 3rd edition of our bi-monthly newsletter - 'Scaling BEPS.' The February 6th announcement by OECD, announcing a definitive date for Country by Country reporting - January 2016, is among the most significant developments in the BEPS project so far. MNCs with operations spread out over dozens of countries, have their work cut out and need to hit the ground running to meet the CbC timeline.

This edition of our newsletter won't disappoint our readers as we dissect OECD guidance on place of taxation for B2C supplies of services & intangibles, get you a no holds barred interview with industry veteran and former VP, Shell International - Theo Keijzer, Expert Gaze by Carol P. Tello on Multilateral Instrument being a potential game changer and a lot more.

Mr. Keijzer, while critiquing some of the BEPS Action Plans makes an important point, which some may consider philosophical but one that also goes to the very root of this BEPS project - that countries are merely legally sovereign but not economically! With e-commerce ruling the roost and valuations of companies in this space going through the rooftop, it comes as no surprise that Digital Economy taxation is the 800 pound guerrilla in the BEPS project. Indirect tax expert Mr. Rajeev Dimri (BMR) gives a thumbs up to the destination based consumption tax proposed by the OECD guidance on B2C supplies, terming them a 'reasonable as well as reasoned attempt' to bring to tax some of the most complex transactions!

Our newsletter would be incomplete without Philip Baker's 'Shooting Straight' piece and the OECD as well as our readers have a pleasant surprise awaiting them. Mr. Baker complimenting the OECD for its big ticket announcements earlier this month with respect to CbC reporting, Multilateral Instrument and modified nexus approach for IP regimes and we leave you with his parting shot - " If the BEPS Project stopped now, these three outcomes are themselves significant developments. In retrospect, the 6th February 2015 announcements may be one of the high points of the whole project. "

1 DISSECTING BEPS ACTION PLANS

1.1 DRAFT OECD GUIDELINES ON PLACE OF TAXATION FOR BUSINESS-TO-CONSUMER (B2C) SUPPLIES OF SERVICES AND INTANGIBLES

1.1.1 Taxsutra Brief

5 things you should know on OECD's Guidance

- Destination principle key for B2C supplies (like B2B) to maintain VAT neutrality in international trade.
- In digital economy & B2C context, for services whose consumption bears no necessary relationship to the location in which the supply is performed and in which the person performing the supply is located, a rule based on the customer's usual residence is the most appropriate approach for determining the place of taxation.
- For 'On-the-spot supplies', the jurisdiction in which the supply is physically performed has the taxing rights. For other services, jurisdiction in which customer has its 'usual residence' has the taxing rights.
- Reverse charge mechanism recommended for cross-border B2B supplies but not relevant for B2C and hence suggests registration and payment by non-resident as the most effective and efficient approach for B2C transactions.
- Simplified registration and compliance regime for non-resident suppliers recommended.

Background

BEPS Action Plan 1 on "Addressing the Tax Challenges of the Digital Economy" seeks to identify issues and solutions to tax digital economy transactions. Effective collection of VAT/GST on cross-border supply of digital goods and services is one of the most critical aspects identified under BEPS Action Plan 1. OECD, in its first BEPS related recommendations released in September 2014, identified the main tax challenges related to VAT in the digital economy as relating to (i) imports of low value parcels from online sales which are treated as VAT-exempt in many jurisdictions, and (ii) remote digital supplies to consumers.

OECD was already working on developing International VAT/GST Guidelines to address issues of double taxation and unintended non-taxation resulting from inconsistencies in the application of VAT to international trade. The first three chapters of the Guidelines were already endorsed as a global standard in April 2014.

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OECD's latest draft on taxing B2C transactions

In continuation of its earlier work and especially in light of BEPS project, OECD has on December 18, 2014 released two discussion drafts. The first one provides draft guidance on the place of taxation of business-to-consumer (B2C) supplies of services and intangibles. The second draft includes provisions to support the application of the B2C Guidelines in practice. The Guidelines are intended to provide Governments and businesses with recommendations as to the proper taxing of B2C transactions so that a smooth interaction between national VAT systems and their application to international trade can be facilitated.

BEPS TRIVIA

Which country, in its recent tax reforms, has acted on BEPS hybrid proposals to restrict interest deductibility?

a. Japan
b. Germany
c. Spain

See answer on page 10

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'Destination' – a core principle for determining the place of taxation in an international context for both business-to-business (B2B) and B2C supplies

To apply the destination principle, VAT systems are required to identify the jurisdiction of consumption. This is generally done by connecting the supplies to the jurisdiction where the final consumption of the supplies is expected to take place.

For consumption tax purposes, internationally traded services & intangibles should be taxed according to the rules of the jurisdiction of consumption.

- The Guidelines have recommended approaches that reflect the destination principle for determining the jurisdiction of taxation for international supplies of services & intangibles while ensuring that:
  - international neutrality is maintained;
  - compliance by businesses involved in these supplies is kept as simple as possible;
  - clarity and certainty are provided for both business and tax administrations;
  - the costs involved in complying with the tax and administering it are minimal, and
  - barriers to evasion and avoidance are sufficiently robust.
- The primary objective, in the B2C context, is to predict with reasonable accuracy the place where the services or intangibles are likely to be consumed while taking into account practical constraints.

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DISSECTING BEPS ACTION PLANS

1.1 DRAFT OECD GUIDELINES ON PLACE OF TAXATION FOR BUSINESS-TO-CONSUMER (B2C) SUPPLIES OF SERVICES AND INTANGIBLES

B2C transactions - General Rules

➤ The OECD draft states that "the primary objective for place of taxation rules in the business-to-consumer context is to predict with reasonable accuracy the place where the services or intangibles are likely to be consumed while taking into account practical constraints, and such rules should be simple and practical for taxpayers to apply, for customers to understand and for tax administrations to administer."

➤ Two general rules are recommended for determining the place of taxation for B2C supplies of services and intangibles:

Place of taxation rule based on the place of performance – This is relevant for "on-the-spot supplies" i.e. supplies physically performed at a readily identifiable location and ordinarily consumed at the same time and place, in the presence of both the supplier and consumer.

(Examples - hairdressing, massage, beauty therapy,physiotherapy; accommodation; restaurant and catering services; entry to cinema, theatre performances, trade fairs, museums, exhibitions, and parks; attendance at sports competitions).

Place of taxation rule based on customer's usual residence – This is relevant for supplies that are not covered by the rule based on place of performance. The usual residence is suggested to be the place where the consumer regularly lives / has established a home, not a place where they are only temporary, transitory visitors.

(Examples - Consultancy, accountancy and legal services, financial and insurance services, long-term rental of movable property;telecommunication and broadcasting services, online supplies of software and software maintenance; online supplies of digital content (movies, TV shows, music etc.; digital data storage; and online gaming.

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➤ Determining the jurisdiction of the usual residence of the customer - As B2C supplies require minimal interaction and communication with the consumer, jurisdictions are suggested to provide clear and realistic guidance for suppliers on the information required to determine the place of usual residence of their customers. Examples - bank details and credit card information, notably country of the bank account, customer's trading history, i.e., phone number, language, billing address and Internet Protocol address.

B2C transactions - ***VAT collection where supplier is not located in the jurisdiction of taxation:***

➤ For cross-border B2B supplies of services and intangibles that are taxable in the jurisdiction where the customer is located, the Guidelines recommend the implementation of a **reverse charge mechanism** that shifts the liability to pay the tax from the supplier to the customer.

➤ A reverse charge mechanism is not fit for B2C supplies since the level of compliance is likely to be low. To ensure appropriate collection of VAT on B2C supplies from non-resident suppliers, the most effective and efficient approach is to **require the non-resident supplier to register and account for the VAT in the jurisdiction of taxation.**

➤ Maintaining traditional registration and compliance procedures for non-resident suppliers would risk creating barriers that may lead to non-compliance or to certain suppliers declining to serve customers in jurisdictions that impose such burdens.

➤ A simplified registration and compliance regime for non-resident suppliers would operate separately from the traditional registration and compliance regime, without the same rights (e.g. input tax recovery) and obligations (e.g. full reporting) as a traditional regime.

- Reverse-charge mechanism not fit for B2C supplies since the level of compliance is likely to be low.
- Maintaining traditional registration and compliance procedures for non-resident suppliers would risk creating barriers that may lead to non-compliance.

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➤ Annex 3 to Chapter 3 identifies the possible simplification measures for each of the following core elements of a simplified administrative and compliance regime:

❖ Registration - Information requested could be limited to necessary details which could include:

Name of business, including the trading name	Name of contact person responsible for dealing with tax administrations	Postal and/or registered address of the business and its contact person
Telephone number of contact person	Electronic address of contact person	Web sites URL of businesses
National tax identification number, if any.		

❖ Input tax recovery – Jurisdictions could limit the scope of the regime to collection of VAT by non-resident suppliers, without making the recovery of input tax available under the simplified regime. Where applicable, the input tax recovery could remain available for them under the normal VAT refund or registration and compliance procedure.

❖ Returns – Non-resident businesses may file less-detailed returns confining the information to:

Supplier's registration identification number	Tax period	Currency and, where relevant, exchange rate used
Taxable amount at the standard rate	Taxable amount at reduced rate(s), if any	Total tax amount payable.

1.1 DRAFT OECD GUIDELINES ON PLACE OF TAXATION FOR BUSINESS-TO-CONSUMER (B2C) SUPPLIES OF SERVICES AND INTANGIBLES

- Payments - Use of electronic payment methods is recommended.

- Record keeping - Electronic record keeping systems should be allowed.

- Invoicing – This requirement may be eliminated since customers involved generally will not be entitled to deduct the input VAT paid on B2C supplies. If invoices are required, it is recommended that information on the invoice remain limited to the data required to administer the VAT regime.

- Availability of information – All necessary information to register and comply with the regime should be made available online, preferably in the languages of their major trading partners.

- Use of third-party service providers - They may act on behalf of the non-resident suppliers in carrying out certain procedures, such as filing returns.

Special considerations for tangible property related services

➤ For internationally traded supplies of services and intangibles directly connected with immovable property, the taxing rights may be allocated to the jurisdiction where the immovable property is located. This is most likely to be the case when there is a supply of services or intangibles belonging to one of the following categories:

- transfer, sale, lease or the right to use, occupy, enjoy or exploit immovable property,

- supplies of services that are physically provided to the immovable property itself, such as constructing, altering and maintaining the immovable property, or

- other supplies of services and intangibles that do not fall within the first two categories but where there is a very close, clear and obvious link or association with the immovable property.

➤ For the supply to be considered as directly connected with immovable property, the connection with immovable property must be at the heart of the supply and must constitute its predominant characteristic. This is particularly relevant as to composite supplies involving immovable property.

➤ In respect of movable tangible property in case of B2C supplies, jurisdictions might consider implementing an approach based on the location of movable tangible property for identifying the place of taxation of supplies of services and intangibles connected with such property. For B2B supplies, the application of the general rule based on customer location will generally lead to an appropriate result.

1 DISSECTING BEPS ACTION PLANS

1.1 DRAFT OECD GUIDELINES ON PLACE OF TAXATION FOR BUSINESS-TO-CONSUMER (B2C) SUPPLIES OF SERVICES AND INTANGIBLES

Supporting the Guidelines in Practice - Mutual Cooperation, Dispute Minimisation, and Application in Cases of Evasion and Avoidance

The Guidelines focus on facilitating the minimization of disputes over potential double taxation or unintended non-taxation and for dealing with evasion and avoidance by applying the General Administrative Principles approved by the OECD Forum on Tax Admission in 2001. Jurisdictions have been encouraged to follow the multilateral conventions such as the Convention on Mutual Administrative Assistance in Tax Matters, as it provides for all possible forms of administrative cooperation so as to combat tax evasion and avoidance. It also states that the countries should cooperate bilaterally by following Model Agreement on Exchange of Information on Tax Matters, Tax Information Exchange Agreements and OECD Model Tax Convention.

The closing date for response from stakeholders to this draft Guidelines is February 20, 2015 and a public hearing on the draft is scheduled for February 25, 2015.

BEPS QUOTES

Paul Morton (Vice Chair of the ICC's Commission on Taxation) "ICC strongly cautions against countries taking unilateral action before the BEPS project has successfully been concluded and consensus has been reached."

1 DISSECTING BEPS ACTION PLANS

1.1 DRAFT OECD GUIDELINES ON PLACE OF TAXATION FOR BUSINESS-TO-CONSUMER (B2C) SUPPLIES OF SERVICES AND INTANGIBLES

1.1.2 BMR POINT OF VIEW

By Rajeev Dimri, Partner at BMR & Associates, LLP with inputs from JayashreeParthasarathy Director, BMR & Associates, LLP and TR Venkateswaran, Associate Director, BMR & Associates LLP

A robust tax regime is typically benchmarked against the parameters of neutrality; simplicity and certainty; effectiveness; efficiency of compliance and administration; and fairness or sufficiency of controls to prevent misuse. Against this backdrop, the OECD's draft guidelines for determining the place of supply and consequently taxation of business-to-consumer ('B2C') supplies of services and intangibles appears to be a reasonable as well as reasoned attempt at meeting the aforesaid criteria for taxing arguably some of the most complex supplies.

Rationale for the OECD draft guideline

Being a 'destination based consumption tax', Value Added Tax ('VAT') system aims to levy and collect tax at the point of consumption of goods / services. Based on the premise that supplies of services to consumers are typically made available by the supplier at the location of the consumer, the rules presently provide for taxation of B2C supplies on the basis of the location of the service provider. However, with globalization of economies coupled with technology enabled global trade, services including intangibles are increasingly supplied from a remote location requiring a relook at the proxy for taxation of such supplies.

The OECD draft is therefore well timed in terms of urging a relook at the proxies for determining the place of supply in the context of B2C supplies of services and intangibles.

In other words increasingly, these services are not consumed at the place of the supply (i.e. at the location of the service provider). The OECD draft is therefore well timed in terms of urging a relook at the proxies for determining the place of supply in the context of B2C supplies of services and intangibles. While the effort may be well timed, the following discussion is aimed at evaluating how the proposals fare against the key parameters of a robust and ideal VAT regime.

BEPS TRIVIA

Which tax has UK recently sought to introduce, that is consistent with the ongoing BEPS Project?

a. Google Tax

b. Diverted Profits Tax

c. Bedroom Tax

See answer on page 16

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Neutrality

The underlying principle of tax neutrality is that services and intangibles acquired by final consumers from foreign suppliers should be taxed on the same basis and at the same rate as domestic supplies. In proposing to tax B2C supplies based on the location of performance (on the spot supplies) and usual residence of the consumer (other than on the spot supplies), the guidelines appear to make a reasonable assumption that final consumers ordinarily consume services and intangibles in the jurisdiction where they receive the services / have their usual residence.

The proposed guideline should meet the aforesaid objective of ensuring that overseas supplies are treated at par with domestic supplies when made to an end consumer in a particular jurisdiction.

This effectively eliminates any tax advantage for final consumers in buying from low or no tax jurisdictions. Accordingly, the proposed guideline should meet the aforesaid objective of ensuring that overseas supplies are treated at par with domestic supplies when made to an end consumer in a particular jurisdiction.

Simplicity and certainty

According to this parameter, tax laws should be clear and simple to understand so that taxpayers can anticipate the tax consequences in advance of a transaction, including knowing when, where and how the tax is to be accounted.

Specifically in the context of digital or online / electronic supplies, determining the place of supply (based on location of the supplier) is often fraught with challenges; for example, a technician in one country using infrastructure in another country may render technology support services to an individual's home computer located in a third country. In such a case, it could be difficult to reach a consistent conclusion on whether the place of performance is where the technician is, where the infrastructure is or somewhere in between. The draft guidelines seek to provide a clear connection to a readily identifiable place or location where the services are likely to be consumed by a final consumer; in this example, at his usual place of residence where his home computer is likely to be installed. Therefore, the guidelines appear to score well on the aspect of certainty.

The draft guidelines seek to provide a clear connection to a readily identifiable place or location where the services are likely to be consumed by a final consumer

As regards the parameter of 'simplicity', while at a conceptual or theoretic level determination of the place of supply as proposed does appear simple and clear in terms of the rationale and logic deployed, implementation of the same could pose certain specific challenges. Some of these issues and challenges are discussed in the context of ease of compliance and administration of the guidelines.

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Efficiency of compliance and administration

The underlying principle here is that compliance costs for taxpayers and administrative costs for the tax authorities should be minimized as far as possible. Against this parameter, ensuring effective compliance and administration of the tax, especially where it stands imposed at a jurisdiction in which the supplier does not have a business presence is likely to be the most challenging aspect of implementing the proposed guideline.

While cross border supplies typically come under a reverse charge mechanism, mandating compliance from an end consumer is likely to yield low compliance results; coupled with this is the impracticability including economic unviability of monitoring and enforcing a large tax base of small tax payers. However, the alternative of making the service provider to set up a presence, register and pay tax in each and every country where his consumers reside has historically been viewed to be extremely complex and cumbersome on the service provider from a time as well as resource cost perspective.

In this backdrop, the draft OECD guideline attempts to address some of these complexities by advocating effective use of technology coupled with a streamlined processes and documentation for reporting as well as accepting compliances.

While the guideline specifies a simplified online registration and reporting process, from a service provider's perspective, irrespective of how simplified the process is, multiple registrations and reporting including gathering knowledge of and complying with the tax legislations of every consuming jurisdiction could be a daunting challenge. In requiring the service provider to report transactions across several jurisdictions the guidelines seek to substantially transform the compliance environment and increase the extent of compliances for these suppliers.

…multiple registrations and reporting including gathering knowledge of and complying with the tax legislations of every consuming jurisdiction could be a daunting challenge.

While the use of technology should be effective where the core elements of the administrative and compliance (including documentation) process are sufficiently clear and simple, what is required is an alignment of the legislations including minds of tax legislators across tax jurisdictions. Specifically, while electronic reporting and compliance is clearly an option, that would inter alia entail all jurisdictions involved to adopt identical or at least similar technology portals and easy online formats for payment / assessment of taxes. Further, for administrators in the consuming jurisdiction, remote assessment of taxes could entail sufficient reporting safeguards being brought in.

Additionally, the degree of co-operation required in terms of information sharing can be expected to be high and this aspect has also been duly recognized in the draft guidelines.

One related aspect could be additional documentation that a service provider may be required to gather to assure himself of the individual status of the consumer including evidence of location of consumption of the service to ensure tax is reported to the account of the correct and relevant jurisdiction.

1.1 DRAFT OECD GUIDELINES ON PLACE OF TAXATION FOR BUSINESS-TO-CONSUMER (B2C) SUPPLIES OF SERVICES AND INTANGIBLES

Effectiveness

In terms of this parameter, the tax rules should produce the right amount of tax at the right time and the right place. Should the implementation challenges discussed above be overcome, with specific yet minimal exceptions being carved for unique circumstances, the proposed levy is likely to be reasonably effective in taxing B2C supplies of services and intangibles based on the location of their consumption.

Fairness including controls for tackling tax evasion and avoidance

The underlying principle here is that the potential for tax evasion and avoidance should be minimized while keeping counter-acting measures proportionate to the risks involved. Given that the base case scenario could involve the service provider not having a presence in the relevant taxing jurisdiction, the chances of non-taxation of the supply could potentially be high. In this regard, for robust counter-acting measures to be put in place, a significant level of information sharing and co-operation may be entailed between various taxing jurisdictions.

This parameter may at best be partially satisfied, atleast in the initial years, as fulfilment of this parameter would hinge on a significant level of co-operation between various taxing jurisdictions in sharing information with a view to compare disclosures being made across jurisdictions. Subject to a desired level of bi-lateral as well as multi-lateral co-operation being achieved, this should be possible. It is moot if presently government machineries across countries are geared up to undertake the required level of co-operation in this regard. While the level of co-operation may be more in instances where a common market principle (such as European Union) or free trade agreements have been entered into, this could be a potential challenge in other cases.

Conclusion

Overall, despite potential implementation concerns including compliance challenges for service providers, the draft guideline appears to be a reasonable attempt to address complexities surrounding the taxation of B2C supplies of services and intangibles. Its success is however likely to hinge on its acceptance and uniform implementation across tax jurisdictions.

India is on the verge of transitioning into a Goods and Services Tax or GST regime under which proxies similar to these are expected to be adopted for the taxation of cross border supply of goods and services into, from and within India. Consideration of these guidelines could pave the way for enabling the Indian tax regime and administration to be in sync with the global best practices on the manner of determining place of supply. Specifically, should these principles and proxies be applied in the context of cross border taxation of B2C supplies of services and intangibles from one Indian state to another, a similar level of alignment and co-operation could be required between Indian state governments.

The views of the authors are personal

BEPS TRIVIA

(answer is b - DPT)

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

1.2.1 Taxsutra Brief

In September 2014, as part of its first seven deliverables, OECD released its report on BEPS Action Plan 6[1] - "Preventing the granting of treaty benefits in inappropriate circumstances" (Report).

Sept 2014 report on **Preventing Treaty Abuse**

- Three-pronged approach to address treaty shopping arrangements:
  - Clear statement of intent to avoid creation of double non-taxation
  - Introduction of specific anti-abuse rule based on the limitation-on-benefits (LOB)
- More general anti-abuse rule - the principal purposes test (PPT)
- Multiple alternatives to reach the goal of ending treaty shopping.
- Countries to agree on minimum level of protection.

In November 2014, OECD released a discussion draft on follow-up work on BEPS Action 6[2]. The discussion draft has identified 20 issues on which follow-up work is required. In particular, work related to LOB rule as well as issues related to treaty entitlement to collective investment vehicles (CIVs) and non-CIV funds (e.g. Sovereign wealth funds, pension funds etc) have been identified as focus areas and specific comments were invited to address the issues without creating treaty-shopping opportunities.

Various stakeholders have submitted their opinions and suggestions which were released by OECD in January 2015. The detailed comments of all the parties running over 700 pages are available on OECD website[3] . A summary of some of the key suggestions submitted to OECD, with regard to OECD's "Follow up work on BEPS Action 6 – Preventing Treaty Abuse" is provided below.

OVERALL COMMENTS
OECD has not presented a clear strategy for implementing measures against treaty abuse and many aspects of the proposals continue to risk removing treaty benefits on genuine commercial situations.
A few parties opine that the primary route to tackle avoidance should be through local tax law and treaties should remain focused on removing double taxation and promoting international trade.
Either a Principal Purposes Test (PPT) or LOB is appropriate, but a combination will be unnecessarily burdensome.
Current proposals are too ambiguous and open to inconsistent interpretations by Tax Authorities. Parties urge OECD to provide additional clarification within the commentary to reduce areas of subjectivity.

BEPS Monitoring Group (BMG):A second key issue is how to decide which type of anti-abuse provisions will be applied to each treaty. If a non-G20 developing country has a strong preference for a specific provision, we suggest that the choice of the developing country should be decisive in determining the type of provision in its treaties with OECD and G20 partners.

[1] http://www.oecd-ilibrary.org/taxation/preventing-the-granting-of-treaty-benefits-in-inappropriate-circumstances_9789264219120-en

[2] http://www.oecd.org/ctp/treaties/discussion-draft-action-6-follow-up-prevent-treaty-abuse.htm

[3] http://www.oecd.org/ctp/treaties/public-comments-action-6-follow-up-prevent-treaty-abuse.pdf

DISSECTING BEPS ACTION PLANS

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

SPECIFIC COMMENTS

OECD PROPOSAL	COMMENTS FROM STAKEHOLDERS
Application of the LOB and treaty entitlement to CIV & Non CIV funds	
OECD in its September 2014 Report provides for the inclusion of collective investment vehicles (CIVs) in the list of "qualified persons", to avail benefits of treaty entitlement. The Commentary on the LOB rule includes a discussion of how CIVs could be dealt with as well as a number of alternative provisions that correspond to the various approaches included in the 2010 OECD Report "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles" (2010 CIV Report). In the discussion draft on Follow Up work, OECD intends to review these alternative approaches and examine whether it would be possible to suggest a single preferred approach with respect to the application of the LOB to CIVs. Comments were invited as to whether the recommendations of the 2010 CIV Report continued to be adequate for widely-held CIVs. Further, OECD invited comments to address treaty entitlement issues of non-CIV funds like sovereign wealth funds, pension funds and alternative funds / private equity funds.	The commenting parties have unanimously opined that **recommendations of 2010 CIV Report are sound & should not be modified.** Further, a few parties believe that a **preferred approach is not practical, given the variety of structures** for CIVs which are dictated by local law considerations, the targeted investor base, and the targeted investments. Non-CIV funds such as pension funds and sovereign wealth funds promote long-term financial security and are not viewed as "tax-abusive" vehicles. **A few parties thus opine that it is important that these benefits are not negatively impacted by any changes to the PPT and LOB rules.**
Discretionary relief provision of the LOB rule	**The Taxes Committee of the International Bar Association (IBA) :** The combination of the LOB discretionary relief rule, the PPT rule and domestic GAAR provisions or specific anti-avoidance provisions with different tests of purpose (e.g. "dominant purpose" (Australia), "main purpose" (UK), "more than merely incidental purpose" (New Zealand)), will lead to complexity and confusion that is antithetical to the purpose of bilateral tax treaties.
OECD LOB rule contains a provision that allows Competent Authority of Contracting State discretion to grant treaty benefits in some situations where a resident of a Contracting State would otherwise be denied treaty benefits under the LOB rule (the "discretionary relief" provision). The key factor to be evaluated by the Competent Authority would be "the establishment, acquisition or maintenance of the resident and the conduct of its operations did not have as one of its principal purposes the obtaining of treaty benefits".	A few parties **have welcomed the Discretionary Relief rule as a fall-back provision.** However, others believe that the ability to give discretionary relief could generate many problems. **Citing the recent example of Luxembourg leaks files, the parties state that large firms would seek discretionary advantages.** **Therefore, it is suggested that OECD clarifies that discretionary relief is intended for exceptional situations only.**

DISSECTING BEPS ACTION PLANS

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

Issues related to the derivative benefit provision	
A "derivative benefits" provision is recommended to allow certain entities owned by residents of other States to obtain treaty benefits if 7 or fewer equivalent beneficiaries own shares representing atleast 95% of the aggregate voting power and value of the company and atleast 50% of any disproportionate class of shares. Ownership may be direct or indirect. The 'base erosion test' must also be satisfied. OECD has requested comments on possible changes that could be made to Derived Benefits test to strike a balance between preventing BEPS and providing treaty benefits in cases where intermediate companies are used for valid commercial reasons.	The commenting parties have stated that the derivative **benefits test is too restrictive and would lead to denial of treaty benefits where there is no treaty shopping and thus should be removed.** It is suggested that the Model Treaty should focus on the Contracting State of the ultimate beneficial owners ("UBO"), and not test intermediary companies. It is also suggested to lower the ownership requirement to 75%-80% to allow greater flexibility.
Issues related to the PPT rule	
OECD Report on BEPS Action 6 provides, in part, that countries should adopt a minimum standard to eliminate treaty shopping and suggests that one of the ways to meet that standard would be to implement a more general anti-abuse rule i.e. **the principal purpose test (PPT).** OECD proposes that treaty benefits shall not be granted in respect of an item of income or capital if it is reasonable to conclude that obtaining that benefit was one of the principal purposes of any arrangement / transaction that resulted directly or indirectly in that benefit, unless granting that benefit in those circumstances would be in accordance with the object and purpose of the treaty.	A few parties opine that the **PPT test is widely framed and poses a risk of misinterpretation, or misapplication by tax authorities.** Parties have **urged OECD to eliminate such a subjective test** or to make modifications to the test to make it more practical. **Further, it is viewed as an unnecessary reclaim procedure in the backdrop of the introduction of automatic exchange of information initiatives, including US FATCA and CRS.**

BEPS TRIVIA

How many public comments have been received on the follow-up work on Action Plan 6 (Prevent treaty abuse)?

a. 80 b. 85 c. 94

See answer on page 35

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

1.2.2. BMR POINT OF VIEW

The Report on "Preventing the Granting of Treaty Benefits in Inappropriate Circumstances" (Report on Action 6) released by OECD in September 2014 emanates from Action 6 (Preventing treaty abuse) of the BEPS Action Plan. A major portion of the Report on Action 6 covers the suggested model treaty provisions in the OECD Model Tax Convention ("Convention") and recommendations to prevent treaty abuse. **The major recommendations for changes to the Convention are the inclusion of a specific anti-abuse rule [the "Limitation on Benefit" (LOB) rule] and a more general anti-abuse rule [the "Principal Purpose Test" rule] to prevent the granting of treaty benefits in inappropriate circumstances.** While incorporating the LOB and PPT rules in the draft provisions, the Report acknowledged that further work was needed on the model provisions and related Commentary on these anti-abuse rules. **The Report also flagged the need for further follow-up work on the policy considerations regarding the treatment of collective investment vehicles (CIVs) and non-CIV funds as draft provisions specifically covering these had been incorporated in the model provisions of the LOB rule to prevent treaty shopping.**

OECD subsequently released a Public Discussion Draft ("Follow up Work on BEPS Action Plan 6: Preventing Treaty Abuse") in November 2014 seeking public comments on issues relating to the LOB rule, the PPT rule and some more issues emanating from its Report on Action 6. The Discussion Draft seeks inputs on a number of issues relating to the LOB rule including the treatment of CIV/non-CIV funds.

<u>CIV/non-CIV funds and the LOB rule</u>

The Discussion Draft points out that the alternative provisions for treatment of CIVs incorporated in the Report on Action 6 correspond to the approaches for treatment of CIVs included in the earlier 2010 OECD Report on "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles" ("CIV Report"). For the purposes of the CIV Report, the term "CIV" is limited to funds that are widely held, hold a diversified portfolio of securities and are subject to investor protection regulation in the country in which they are established. Non-CIV funds would include sovereign wealth funds, pension funds and alternate funds / private equity funds. Comments have been sought from stakeholders as to whether the recommendations of the CIV Report continue to be adequate for CIVs or whether any improvements are required. Similarly, the Discussion Draft briefly describes treaty entitlement issues for non-CIVs and seeks inputs as to whether these issues are adequately described, as well as the preferred approach to deal with such issues without creating opportunities for treaty shopping.

The main questions which give rise to treaty entitlement issues for CIVs are – whether the CIV should be treated as a person, whether it should be regarded as a resident of a Contracting State and whether it should be regarded as a beneficial owner of income it receives.

1 DISSECTING BEPS ACTION PLANS

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

The CIV Report acknowledges that pooling of funds by portfolio investors in securities to create collective investment vehicles for making and holding such investments is economically efficient owing to distribution of costs, diversification of risk and other advantages. Tax systems therefore try to maintain tax neutrality for domestic investors making investments in domestic securities, whether they invest directly or through a CIV. With the growth of international fund flows, cross border investments in securities in the source country are increasingly made by CIVs located in another country while the CIV investors are themselves located in various third countries. Many tax jurisdictions have therefore started specifically addressing issues regarding the entitlement to treaty benefits and plugging opportunities for treaty shopping by cross-border CIVs in their bilateral tax treaties.

The main questions which give rise to treaty entitlement issues for CIVs are – whether the CIV should be treated as a person, whether it should be regarded as a resident of a Contracting State and whether it should be regarded as a beneficial owner of income it receives. Relevant tax treaties do not generally include provisions specifically addressing the treatment of CIVs. Because the principles set out are necessarily general, their application to a particular type of CIV may not be clear. The CIV Report recognizes the fact that clarity is critical for a CIV since it affects the calculation of its NAV and the basis for all purchases, sales and redemptions.

The CIV Report suggests alternatives for the treatment of CIVs under tax treaties, however at the same time also provides reservations against adopting approaches which could give rise to treaty shopping.

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

Comments received from stakeholders on the issue

Various comments have been received by the OECD from stakeholders including Venture Capital associations across the world. Most of these comments impress upon the fact that BEPS recommendations should not duly impact CIVs, whose situation becomes problematic when the standard LOB test is applied since the interests in the CIV are not publicly traded, such interests are held by residents of third countries and the CIV is used for investment purposes rather than for active conduct of a business. Suggestions include specific insertions to state categories of CIVs which would automatically be regarded as "qualified persons" for the purposes of fulfilment of the LOB test. Other suggestions include inserting some broad tests which the CIV may need to fulfil in order to avail treaty entitlement without creating opportunities for treaty shopping. These include requirement for the fund to be diversely held, appropriately regulated, ensuring a minimum level of substance in terms of investment in the local economy, and suitable reporting requirements. More or less stakeholders have been unified in their thinking that the current CIV report is sufficient to address treaty entitlement issues, with some scope for improvement.

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Regarding the PPT test, the general view seems to be that the PPT is extremely wide since it requires that "one of the principal purposes" of the arrangement should be to obtain a treaty benefit. Even if the CIV were to satisfy the LOB test, there is a high chance it would not be able to satisfy the PPT test. To mitigate against this risk, recommendations which have been provided include redrafting of the PPT test to provide that "the principal purpose" of the arrangement should be to obtain treaty benefit, excluding CIVs from the PPT, or providing a rebuttable presumption that a CIV should be otherwise presumed to have a bonafide purpose. Further, in recognition of the bilateral nature of a treaty, a Contracting State should be able to challenge a CIV on the basis of a PPT only if the other Contracting State agrees that PPT could apply under the circumstances. It has also been suggested that Treaty Relief and Compliance Enhancement (TRACE) Implementation Package in coordination with US FATCA and the Common Reporting Standard (CRS) can be used to overcome treaty abuse concerns before introducing anti-avoidance measures.

Conclusion

While OECD is considering all stakeholder comments to determine appropriate manner of addressing issues relating to CIVs and non-CIVs, and impact of Action Point 6 on treaty entitlement issues, it has acknowledged that a "one size that fits all" approach may not work for investment funds, which follow a completely different business philosophy and approach. **More work is probably required to determine the differentiation in approach for CIVs vis-à-vis non-CIVs since many of the issues faced by either two categories of investment funds may be similar.** For example, while a private equity fund is categorized as a non-CIV, it could also very well fit into the bracket of a CIV. Further, the CIV Report also recommends that in order to address issues of treaty

1.2 PUBLIC COMMENTS ON FOLLOW UP WORK ON BEPS ACTION 6 – PREVENTING TREATY ABUSE

shopping and double non taxation a sizeable portion of the investors into the CIV should be residents of the jurisdiction where the CIV is set up, since such investors would themselves have been entitled to treaty benefits. However, while dealing with such issues, one also needs to bear in mind that a common approach of requiring a certain percentage of investors to be resident in the same jurisdiction may not work since the choice of jurisdiction also depends on a number of factors. For example, many times the investors may exempt funds themselves, who may not depend on treaties for claiming a tax exemption. Further, issues regarding non availability of tax credits for investors for tax paid by the CIV is also an important determinant criteria. Investment funds do not usually have an objective of abusing treaties, however given the peculiar nature of their set up, a special treatment needs to be accorded to them with respect to availability of treaty benefits including passing of tax credits to investors to deal with issues concerning inappropriate use of treaty benefits.

**Contributed by Parul Jain (Partner), BMR & Associates, LLP*

FACE TO FACE

INTERVIEW WITH THEO KEIJZER, FORMER VP, SHELL INTERNATIONAL B.V.

Mr Theo Keijzer – Former VP, Tax Policy at Shell International B.V. & worked there for 35 years, and Past Chairman of the Taxation Commission of the International Chamber of Commerce (ICC) in Paris and a member of the EU Platform for Tax Good Governance, representing the ICC. Vice Chair of the EU Joint Transfer Pricing Forum in Brussels from 2007-2011.

On the direction of BEPS Project

Parul Jain (BMR): OECD has come out with a plan on how to go about each action plan with deadlines. Are you satisfied with the process adopted by OECD in arriving at solutions for each of the action plans and with the industry consultations that have taken place?

Theo Keijzer: I'm not very happy with it. The reason is simple. Going back to the G20 plan to fight 'Base Erosion and Profit Shifting', the OECD has started a very ambitious project. What we can now see is weariness, people are getting increasingly tired. OECD tries to do too much in too short a time frame. This is not good if only because it doesn't allow time for reflection and ripening of ideas. Each and every next release by OECD means more work and at the same time the question what will be the impact of our efforts. If you are an external advisor, that's fine; it's part of the job. But if you are working with a company, there is strain on the business. You should not only continue to do your normal day-to-day job but also all this additional work. The additional work is more than a significant add-on. Possibly, OECD should conduct specific sessions with corporates alone enabling them to get their message across more efficiently.

"G20 in its initial declaration made a major mistake. It accepted that countries are sovereign and this is the basis for any BEPS process. However, one should realise that countries are merely legally sovereign, they are not sovereign economically."

The single most important issue is about dispute resolution. If G20/OECD would focus first on resolving disputes between countries such that any friction, any dispute is resolved without double tax, then all the BEPS issues would have a much easier process. Who would care much if the friction between countries would anyway be resolved? If there is no double taxation in case of mismatches between countries?

G20 in its initial declaration made a major mistake. It accepted that countries are sovereign and this is the basis for any BEPS process. However, one should realise that countries are merely legally sovereign, they are not sovereign economically. Consequently, G20/OECD accept countries continue to draft their own rules without regard to what other countries are doing. This results in frictions and disputes. Hence we need the mandatory and binding arbitration to ensure disputes are resolved without double tax.

Parul Jain (BMR): BEPS project started with an objective "to end double non-taxation". Considering the paper released by the OECD thus far, such as the action plan on treaty abuse, permanent establishment or transfer pricing, is the focus really to prevent shifting of the tax base or is it really to enforce ‘source’ based taxation?

Theo Keijzer: Countries seem to be moving more towards source based taxation. We see this quite clearly in the recent OECD Model Convention texts. The UN approach and specifically countries like China, India, Brazil and few others are really saying ‘We must be able to tax any activity connected to our territory, meaning source taxation’. For that reason, I won’t be surprised to see even more focus on source taxation.

The recent discussions in the UN Tax Expert Group points also to a sharp increase in source tax instead of residence taxation. These discussions not only addressed the permanent establishment concept but even more specifically a newly proposed article dealing with Technical Services. Problem would be that if resident-concept countries do not yield to the new source concept, business will face double taxation. This could make it rather expensive to do business in such a framework. In general, countries consider that if they adopt source taxation, they would be secure from ‘Base Erosion and Profit Shifting’. The problem is that if countries use different definitions, we will have chaos.

“Countries seem to be moving more towards source based taxation. We see this quite clearly in the recent OECD Model Convention texts.”

Parul Jain (BMR): Some countries have tried to pre-empt some of the BEPS proposals and fast-track them under their respective domestic tax law. For example UK published a report setting out their priorities for the BEPS project but there have been other countries who have already introduced some BEPS compliance measures such as Canada which proposed unilateral BEPS compliance measures. So given that this is a very ambitious project, what are your thoughts on some of these unilateral initiatives?

Theo Keijzer: It’s wrong that countries do that. As I mentioned earlier, mistake has been made by G20 by agreeing that countries are sovereign and in BEPS context work on proposals respecting this fictitious sovereignty. Politicians want to be seen as strong leaders and get re-elected; that’s the reason countries are jumping the gun and enacting BEPS related rules prematurely. This will lead to more friction, more disputes, more double tax.

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Mandatory Arbitration

AmeyaKunte (Taxsutra): Fact is that a country like India is opposing to mandatory arbitration even today. How do you think the friction be resolved?

Theo Keijzer: I believe we are already in a chaos. Advisors and corporate taxpayers will not know what to do once the BEPS rules come out, because in some countries the rules will be implemented as drafted and some countries will implement them differently. In a global landscape, more rules mean more friction between countries. Let me be as precise as I can be in this context. Different rules is not the only cause for friction between countries and for taxpayers. Interpretation of even those very same rules is also a major stumbling block. For example, suppose all 28 countries in the EU would have the same GAAR definition. Do you think that there are common interpretations of these same rules? If not, as I expect, it will be chaos because the same words do not mean the

same to different people, different countries. So my suggestion is to stop the BEPS process, and first focus on mandatory binding arbitration. Once we have a framework where disputes will be resolved, the BEPS project can continue.

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There will be other chaos. In Action plan 14, it is proposed that Competent Authority must have room to manoeuvre. The job of Revenue officials in India is to raise money in line with the budgeted numbers of the Government. Their job is not to apply the law and be good at that but to maximize revenue proceeds; this is an incorrect approach and ensures conflicts between the law as drafted and the compliance with the law. I have mentioned this some time ago to the Indian Government and Revenue officials. I understand that quality of applying the law is not a parameter for judging the officials. Numbers must be achieved; assessments must be issued. Consequently, if the Indian Competent Authority follows this, how will they be able to really negotiate with other Competent Authorities?

"The job of Revenue officials in India is to raise money in line with the budgeted numbers of the Government. Their job is not to apply the law and be good at that but to maximize revenue proceeds".

Only a handful of cases worldwide have gone all the way to arbitration (for those countries where arbitration exists). All other cases / disputes have winged their way through the process but stopped just short of final arbitration phase and were settled in whatever manner. Why, because countries do not want to go to arbitration; they lose control over the process and outcome. This is one of the reasons why India and many other countries do not want mandatory binding arbitration, because they cannot control the outcome. This is a rather inward looking view and conflicts with the arrival of globalised businesses.

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SHOOTING STRAIGHT

PHILIP BAKER

Mr. Philip Baker, Queen's Counsel, UK

Just when one began to think that the BEPS Project was going nowhere fast, the OECD suddenly announced on 6th February 2015 the publication of three short documents which contain steps towards the implementation of the outcomes of the Project. At least two of these were not anticipated for this stage, though all three reflect decisions taken in 2014. Announcing the implementation now of decisions taken in 2014 might be seen as a sensible approach to start moving from discussion to implementation. However, they can also be seen as the OECD recycling news about matters already agreed, to hide the lack of agreement on other issues.

The three areas on which implementation steps have been announced are: Action 5: Agreement on Modified Nexus Approach for IP Regimes; Action 13: Guidance on the Implementation of Country-by-Country Reporting ("CbCR"); and Action 15: a Mandate for the Development of a Multilateral Instrument.

One of the primary targets of the BEPS Project was the growing number of patent box and similar IP regimes, particularly in European countries, offering the carrot of low or no taxation on income derived directly or indirectly from various forms of research and development. The OECD Forum on Harmful Tax Practices was deep into discussions about how to limit these regimes, with a split of views between those countries that favoured a transfer pricing approach and those that favoured a nexus approach. Early in November 2014, the UK and Germany effectively seized control of the process and reached a bilateral agreement on a modified nexus approach. They then persuaded the other G20 countries to come on board at Brisbane, and the approach has since been endorsed by all OECD and G20 countries. In effect, the UK and Germany have reached a private deal, and persuaded all the other countries to go along with it. A cynic would analyse this as the UK and Germany reaching their own private deal, and bouncing both the OECD and the EU into accepting this private deal.

The paper published on 6th February sets out further details on the modified nexus approach. The basic idea behind the approach is that a country can offer a preferential tax regime to income arising from qualifying research and development. The two problems with the nexus approach are, first, that a strict nexus approach would only allow the preferential regime to the company that carried out the research and development. Aside from problems with European Union Law, this does not sit very well with the practice of multinational companies to outsource and buy-in research results. The modified nexus approach allows up to 30% of qualifying expenditure to come from the acquisition of IP or from payments for outsourcing research. The second difficulty with a nexus approach is identifying the link between the original research and development and the income arising: the problem of developing principles for identifying this link has been passed to the Forum on Harmful Tax Practices. So, not only has the Forum been circumvented by two of its most powerful members, but the Forum has been handed the hard task of doing the real work on developing this proposal.

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SHOOTING STRAIGHT

The second paper published on 6th February concerns Guidance on the Implementation of Country-by-Country Reporting. In 2014, the multinational companies effectively conceded that they would have to go down the line of CbCR, but information supplied will be kept confidential between revenue authorities (at least, that's the theory). This paper starts to deal with the implementation: the first CbCR reports will be filed by 31st December 2017 and will contain information relating to fiscal years beginning on or after 1st January 2016. There are also details of those small groups that will not be required to file these reports. The document also starts to identify the use that can be made of these reports, requiring confidentiality and only appropriate use by governments. Most commentators feel that some governments will fail to observe confidentiality, and others will make inappropriate use of these reports.

Finally, and perhaps most significant, the third paper published on 6th February was a Mandate for the Development of a Multilateral Instrument. Action 15 of the BEPS Project foresaw the possible use of a multilateral instrument to implement some of the BEPS outcomes. In particular, some of the outcomes will require amendments to the existing network of bilateral tax treaties. The amendments that are already under discussion include: anti-treaty shopping provisions, amending the permanent establishment definition, introducing provisions dealing with hybrid entities and hybrid instruments, and accelerating the inclusion of arbitration provisions in tax treaties. If these changes were to be implemented by bilateral protocols amending treaties, the process would take decades; a multilateral instrument is intended to speed up the process.

An OECD report in 2014, assisted by a group of international public law and tax law experts, concluded that a multilateral instrument was feasible and desirable. Originally, it was thought that the drafting of this instrument might wait until the end of the BEPS Project in December 2015, so that the drafting would only begin in 2016. Very sensibly, however, the OECD and G20 have decided to bring that process forward, and have now published the Mandate for the development of the multilateral instrument. A drafting conference will be called together by the middle of 2015, with a view to preparing a draft multilateral instrument by 31st December 2016. The multilateral instrument will be limited only to amending bilateral tax treaties (and not wider BEPS issues, which was one possibility for the instrument). Not only will this drafting conference provide a forum for the drafting of the instrument, it also provides something which the BEPS Project originally lacked: an ongoing conference in which different countries could trade-off concessions to one another in order to process towards a final outcome.

The Multilateral Instrument is potentially one of the most important outcomes of the BEPS Project. It will contain some treaty amendments that some countries do not want: an example of that is arbitration in tax treaties which (goodness knows for what reasons) countries like India do not want. However, much of the discussion about a Multilateral Instrument concerned optionality – the possibilities for countries to accept parts of the instrument but not others. Thus, if India continues to retain its head-in-the-sand attitude to arbitration, it will be possible for India still to participate in the Multilateral Instrument, but not adopt that particular element. Similarly, the Multilateral Instrument may give countries the option to choose between a limitation on benefit clause and a principal purpose rule for treaty abuse. So, there is no reason why countries should not participate in the work of drafting the Multilateral Instrument, nor should they block the inclusion provisions that other countries want, on the basis that they may themselves choose not to adopt these particular provisions.

If the BEPS Project stopped now, these three outcomes are themselves significant developments. In retrospect, the 6th February 2015 announcements may be one of the high points of the whole Project.

4 EXPERT GAZE

PROPOSED OECD MULTILATERAL INSTRUMENT – WILL IT BE A GAME CHANGER? BY CAROL P. TELLO

Carol P. Tello
Partner, Sutherland Asbill & Brennan LLP, Washington, D.C.

Action Item 15 of the BEPS project is to develop a multilateral instrument to modify the bilateral network of income tax treaties, which is composed of over 3000 such treaties. As the multilateral instrument will implement the treaty-related provisions of the other BEPS action plans, it necessarily would be the last action item to be implemented.

The Discussion Draft of October 2014 discusses the issues that make a multilateral instrument desirable and feasible. An Annex is included in the Discussion Draft that provides a toolbox or list of options based on public international law precedents. The Annex is based upon the work of a 13-member informal committee composed of civil and common law jurisdiction members set up by the OECD Committee on Fiscal Affairs that included experts in public international law and international taxation. The group included a member from the United States and 10 other OECD countries, while one member was from South Africa. The United Kingdom was represented by two members.

Key Conclusions

The Annex is organized around the three key conclusions of the informal working group concerning the effect of a multilateral instrument:

- How to implement BEPS measures by modifying the existing network of bilateral tax treaties
- Provide appropriate flexibility for States to enable effective coordination on solving the BEPS problems while preserving State sovereignty; and
- Ensure transparency and clarity for stakeholders.

Clearly, if BEPS is to be implemented in the near future, to renegotiate over 3000 bilateral tax treaties is not practical.

Clearly, if BEPS is to be implemented in the near future, to renegotiate over 3000 bilateral tax treaties is not practical as the negotiation of just one treaty can take several years even when the treaty is being renegotiated and the treaty partners have experience with each other and their tax systems. A multilateral instrument would likely take a similar amount of time to be negotiated, but as it will modify all existing bilateral treaties once implemented, the time to effectuate a multilateral instrument necessarily will be much less.

2015 International Conference

The Discussion Draft recommends the formation of an International Conference to be convened in early 2015 to negotiate the substantive provisions of the multilateral instrument. The International Conference would be open to all interested countries under the aegis of the OECD and the G20. The purpose of convening the International Conference in 2015 is to maintain the momentum of the BEPS work. As the Discussion Draft was released in the fall of 2014, early 2015 likely seemed

entirely feasible at that time. As not all of the other BEPS discussion drafts have yet been finalized, it would seem unlikely that an International Conference could be organized and convened before the end of the first quarter of 2015. To date, no public announcements have been made concerning the convocation of the International Conference.

Scope of the Multilateral Instrument

The Discussion Draft for Action Item 15 indicates that the multilateral instrument initially should be limited in scope to contain provisions concerning the following items, all of which are the subject of other BEPS Action Items.

- Address treaty abuse to prevent the grant of treaty benefits in inappropriate circumstances
- Address dual-residence structures
- Address "triangular" cases involving PEs in third States
- Provide improvements to dispute resolution procedures
- Address transparent entities in the context of hybrid mismatch arrangements
- Provide new multilateral MAP procedures to resolve multi-country disputes
- Facilitate country-by-country reporting by providing rules relating to confidentiality of information

Further Expansion - A Step toward Multilaterism?

Although the current plan is to limit the scope of a multilateral instrument as described above, the Discussion Draft notes that the multilateral instrument should be conceived in a "dynamic" way and could be expanded at a later date. Although the Discussion Draft views such further steps as a positive means of streamlining the implementation of changes made to income tax treaties, the Discussion Draft does state that any decision to address a broader range of issues would represent a change in the historic direction of bilateral tax treaties and would represent a significant step toward multilateralism. The Discussion Draft concludes that at the present time, a multilateral instrument should be narrowly targeted while other incremental opportunities should be considered.

State Sovereignty

The issue of the sovereignty of each State in this process likely will be the most sensitive issue. The Discussion Draft recognizes that sovereign autonomy is a basic principle that underpins the international order and provides the foundation for the negotiation of international treaties.

In the negotiation of bilateral treaties, each State varies its domestic law to achieve a more harmonious treatment of taxpayers engaged in cross-border activities between those two treaty partners. In so varying domestic law to provide a new bilateral treaty law, each State has necessarily, but voluntarily, eroded its sovereignty to some degree, but also achieved the benefit of increased certainty of the tax treatment of taxpayers who invest in the other treaty partner.

The issue of the sovereignty of each State in this process likely will be the most sensitive issue.

The sovereignty issue has been raised in the context of arbitration provisions in which competent authorities cede their authority to arbitrators, generally chosen by the competent

In actuality, very few competent authority cases go to arbitration because the arbitration provision acts as an in terrorem measure.

authorities, who in turn determine a third arbitrator. In actuality, very few competent authority cases go to arbitration because the arbitration provision acts as an in terrorem measure. To date, the U.S.-Canadian experience has been positive in that many back-logged cases have been resolved with only a few cases being submitted to arbitration. As a result, although the sovereignty issue caused concern, in actuality, those concerns have been allayed due to the infrequent use of arbitration procedures.

Multilateral MAP

A multilateral MAP process is needed to address multi-country tax disputes resulting from the globalization of business structures that necessarily involves multiple countries. While interest exists for multilateral MAP processes, a number of countries believe that explicit legal authority is needed to authorize such multilateral proceedings. A multilateral MAP provision would provide the legal basis for multi-country MAP proceedings.

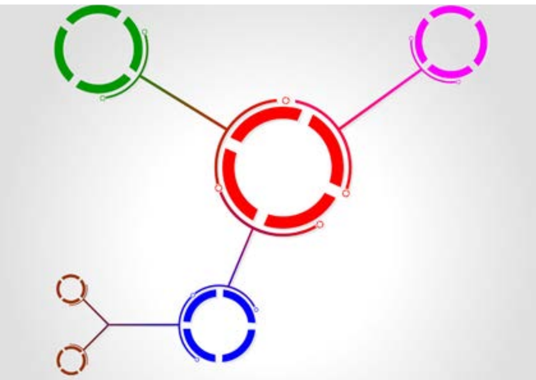
The United States has proposed to expand the scope of MAP cases to include other treaty countries to resolve all potential MAP issues in a timely manner. This expansion of the scope of MAP cases would be authorized under Section 2.08 of Notice 2013-78, which is a proposal to revise the existing U.S. MAP procedures. The proposed procedures have not yet been finalized to date, but are expected to be finalized shortly.

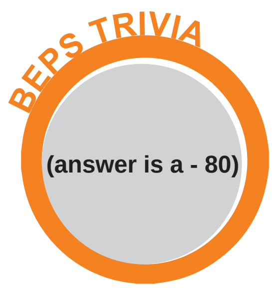
Potential Effective date of Multilateral Instrument

Because the Discussion Draft anticipates that the International Conference should last no more than two years, it is likely that the earliest that countries could begin adopting a multilateral instrument would be in 2017 with it coming into force at the beginning of 2018.

Conclusion

The concept of a multilateral instrument in the context of global business organization and practices makes sense and would enable governments to amend existing bilateral income tax treaties in an efficient and timely manner. As there are no comments to date on the multilateral instrument concept to amend the bilateral income tax treaty network, it is too early to determine whether this is a concept that will be effectuated. However, the BEPS project has been meeting its ambitious deadlines so it may be anticipated that an International Conference will be convened in 2015 to begin the work on a multilateral instrument.





"The article was authored before Feb 6, 2015 Press Release of OECD.

The OECD Press Release states that OECD and G20 countries have agreed for a mandate to launch negotiations on a multilateral instrument to streamline implementation of tax treaty-related BEPS measures. The mandate authorises formation of an ad-hoc negotiating group, open to participation from all states. The group will be hosted by the OECD and will hold its first meeting by July 2015, with an aim to conclude drafting by 31 December 2016."

2 FACE TO FACE

INTERVIEW WITH THEO KEIJZER, FORMER VP SHELL INTERNATIONAL B.V.

Continued from page 26

Arm's Length & Transfer Pricing

Parul Jain (BMR): What are your views on the arm's length standard in BEPS context?

Theo Keijzer: Whether it's the arm's length standard or another standard, I am fine as long as all countries in the world agree to it. Many countries like Brazil do not use the arm's length standard as prescribed by the OECD because it's too cumbersome to work with by the Revenue. China wants to use parameters not agreed by OECD countries. Basically China wants to set aside legal and contract reality and apply their vision on how the chain should be. An example given by a Chinese official was the following: If say a Gucci bag is made for $100 in China and is sold at $2000 in Europe, China wants to tax the difference of $1900, with some adjustments for direct sales expenses in Europe. That the chain shows the bag is sold to an intermediate company holding ownership of the design, before on-selling to the store in Europe is irrelevant for China. This means China is not adhering to commercial realities, and basically saying 'We do not follow the OECD transfer pricing principles.' This is what the whole conflict is about. For more on this, suggest you read Chapter X of the UN TP Manual published two years ago.

"China wants to use parameters not agreed by OECD countries. Basically China wants to set aside legal and contract reality and apply their vision on how the chain should be."

Countries are sovereign. So what you will see is that the United States and many other European countries will continue to insist on arm's length standard. At the same time, a number of countries will try to say no.

My plea is that scope of mandatory binding arbitration be expanded. If there is mandatory arbitration, it can deal with disputes on pricing standards amongst countries. If this does not happen (and I don't believe for a second that mandatory arbitration will be accepted by all counties), the only alternative left is to go for global taxation.

"My plea is that scope of mandatory binding arbitration be expanded. If there is mandatory arbitration, it can deal with disputes on pricing standards amongst countries."

Treaty-Abuse & Principal Purpose Test

Parul Jain (BMR): The stakeholders on BEPS Action 6 – Prevent Treaty Abuse have commented that Principal Purpose Test is widely framed and have urged OECD to eliminate such a subjective test or make modifications to make it more practical. Do you agree with this? If yes, what could be the alternatives?

Theo Keijzer: The answer is really quite simple. If you look at the actual proposal, you find that no one really knows what 'Principal Purpose' is. My example would be the GAAR Rules in Europe. It's not like you can clearly determine, do I have a problem or not. This is a very subjective and complex test. You only have to look at the length of the proposed texts to understand that it is complex and likely to result in disputes between countries. The objective behind the PPT is to analyse whether a transaction will result either directly or indirectly in benefit. One side is white and the other side is black. The test is too widely framed.

Digital Economy

AmeyaKunte (Taxsutra): Coming back to digital economy, especially taxing businesses via VAT on B2C supplies from non-resident suppliers instead of corporate income tax, do you think this approach is practicable from business stand point?

Theo Keijzer: Who really has the vision regarding what falls within the definition of digital service? Even the current economies and current main stream companies have significant digitalised activities. It is a chaotic topic. The best I can say is that digital economy should not be treated differently and all corporate income tax and all the other taxes should be levied and not replaced.

Multilateral Instrument

Parul Jain (BMR): Quick thoughts on where do you think this project is headed given its speed, and what do you think is the right way to implement this and whether multilateral instrument would be effective?

"A multilateral instrument might not change anything."

Theo Keijzer: A multilateral instrument might not change anything. The number of disputes will not be reduced by such instrument. For a true solution we need two things: binding mandatory arbitration and acceptance that countries (including for example - India, China or the United States) are no longer economically sovereign. They think they are. The countries must accept they compete with each other. Competition is difficult for countries and politicians to accept. The best example I can give you, is the introduction of the UK patent box, which is basically a call to companies to re-organise their affairs and benefit from a new tax incentive in the UK. Result being that the existing tax base (read "business") leaves the various countries where it operated and is transferred to the UK. The UK sees this quite rightly as an incentive, to make Britain "great", according to the UK Government flyer published. That is why the UK introduced the patent tax in the first place. At the same time the UK PM Cameron publicly despised tax avoidance and tax planning. What he really meant to say was, "I don't care companies avoid tax in other countries, as long as they are not doing it in my country." How else can you introduce legislation that only works if you transfer tax base away from another country? For clarity's sake: I like tax incentives and competition between countries. What I don't like is politicians not being honest and not providing leadership by telling all facts to their voters. All this, and there are many more stories about tax incentives in other countries, indicates that politicians don't know how to handle the tax affairs of globalised business whilst being allowed to retain their sovereignty.

"For clarity's sake: I like tax incentives and competition between countries. What I don't like is politicians not being honest and not providing leadership by telling all facts to their voters."

There are so many systems of taxes in different countries and the question is how we link all these different systems together. As I've said repeatedly, we must first agree on how to resolve disputes and that is by mandatory arbitration argument. Then all other things and G20/OECD BEPS processes will take it from there.

As a final issue: corporates in general do not have a problem in which country they are paying taxes. What companies do not like is the call by politicians and NGOs they allocate more profits to and pay more tax in less developed countries and at the same time the developed countries insist their revenue base is not affected. How can you expect a company be willing to report a tax base higher than 100% of the global profits? This is double taxation in optima forma.

5 NEWS WRAP UP

December 10-11, 2014 – Officials from 14 developing countries(including South Africa, Philippines and Bangladesh) participated in a workshop held in Parisand discussed ways to maximize benefits from their recent commitment to enhanced engagement in the BEPS Project. RaffaeleRusso, underlined the importance of internal coordination among tax policy and administrative officials & stressed on the use of central contact points and identification of priority actions as useful ways to become effectively engaged.

December 15, 2014 - The fifth OECD webcast on ‘BEPS Project Update – 2015 Deliverables and Beyond’ provided an overview of the follow up work on the 2014 deliverables and discussed the 2015 deliverables that are in progress. Pascal Saint-Amans, Director, Centre for Tax Policy and Administration highlighted the satisfaction of G-20 Finance Ministers with the outcome of 2014 deliverables. On digital economy follow up work, Raffaele Russo, Head of BEPS Project stated that the Task Force would meet in February to decide if there was a need to publish request for input or a full-fledged discussion draft or wait till other action items were developed. Further, Amans expressed hope that UK’s recent Diverted Profit Tax legislation (popularly referred to as 'Google Tax') would be compatible with development of Action 1 – Digital Economy and the solution provided would result in a coordinated approach which is not detrimental to investment / government revenues.

December 19, 2014 – OECD released a Discussion Draft on revisions to Chapter I of TP Guidelines (including risk, recharacterisation and special measures) (Actions 8, 9 and 10). The Discussion Draft emphasizes the importance of accurately delineating actual transactions and includes guidance on relevance and allocation of risk. Comments are invited on “Moral hazard”, where one party assumes a risk without the ability to manage the behaviour of the party creating its risk exposure. The deadline for receiving comments is Feb 6, 2015.

December 19, 2014 – OECD invited public comments on BEPS Action 4 dealing with Interest deductions and other financial payments. The deadline for receiving public comments is February 6, 2015.

January 2015 – The UK Government published draft legislation to enable the introduction of Country-by-Country (CbC) Reporting after adopting the CBC Reporting template developed by OECD as part of its BEPS project. The legislation will be included in the Finance Act 2015 and confirms that UK parented MNEs will be required to provide CbC tax related data to HMRC. It is expected that MNEs will be required to prepare the CbC template for financial years beginning on or after January 2016.

January 19, 2015 – OECD published the comments received on the Discussion Draft on Action Plan 14 – Make dispute resolution mechanisms more effective. Stakeholders opine that while the discussion draft fairly acknowledges existing problems with MAP procedures, the proposed options may not entirely solve the problems. Stakeholders believe that an effective dispute resolution mechanism should be carefully constructed, with adequate procedural safeguards, especially transparency. The comments will be discussed at a public consultation at the OECD Conference Centre on January 23, 2015.

January 20, 2015 - OECD published the comments received on the Discussion Draft on Action Plan 10 – Proposed Modifications to Chapter VII of the Transfer Pricing Guidelines to Low Value-Adding Intra-Group Services. Stakeholders have recommended that OECD should include guidance on appropriate documentation to be maintained by MNE groups as authentic base to accept cost pool / allocation keys. The comments will be discussed at public consultation meeting on March 19-20, 2015.

January 2015 – The Spanish Secretary of State for the Treasury announced that the Government will include a CBC Reporting obligation for multinationals in the new Corporate Income Tax Regulations. This new reporting obligation is aligned with Action 13 of the BEPS project and is expected to enter into force on 1 January 2016.

ISSUE 1 RECAP: Just in case you missed the inaugural edition of our special newsletter, which featured an exclusive interview with OECD Tax Policy Director Pascal Saint-Amans as also our dissection of Action Plans 8 & 13 , click here.

ISSUE 2 RECAP: Dissecting Action Plan 6, Face to Face with Dr. Jeffrey Owens and 'Counter View' from Christian Kaiser of Siemens, click here.

About Taxsutra

Launched in 2011, India based B2B portal-Taxsutra.com is a trusted online resource for corporate tax directors, policymakers and practioners. Taxsutra's instant news alerts & incisive analysis on both domestic and international tax, coupled with unique features like tax ring, Taxsutra Insight, Litigation Tracker, Taxsutra TV and blogs make it a "must-have" for every tax professional.

Given the increasing focus of tax administrations on Transfer Pricing, **www.tp.taxsutra.com** was launched in October 2011, as India's first exclusive portal on TP. Apart from a comprehensive database of over 1000 Indian TP cases, the portal offers several new editorial features including Case Tracker, International Rulings, APA Space, TP Talk, Expert Corner, TP Personalities and 'Around the World.' Taxsutra's thought leadership and continuous engagement with tax professionals has been on display through several unique initiatives/microsites/ special coverage on burning tax issues, controversies and important developments, be it APA, the $2bn Vodafone tax case, BEPS, our roadblocked coverage of Union Budget and even some light tax banter with our microsite on Soccer World Cup & tax! Taxsutra has also championed various niche events and workshops. In 2013,Taxsutra also launched the portal on Central Indirect Taxes–**www.idt.taxsutra.com**

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