

European Business Initiative on Taxation (EBIT)

**Comments on the OECD's Revised Discussion Draft on BEPS ACTION 6
on Preventing Treaty Abuse**

Members of EBIT at the time of this submission: AIRBUS, BP, CATERPILLAR, DEUTSCHE LUFTHANSA, DIAGEO, INFORMA, JTI, LDC, MTU, NUTRECO, RELX GROUP, ROLLS-ROYCE, SAMSUNG ELECTRONICS, SCHRODERS and TUPPERWARE.

EBIT Comments on the OECD's Revised Discussion Draft on BEPS ACTION 6: Preventing Treaty Abuse

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Submitted by email to: taxtreaties@oecd.org

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Dear Marlies,

EBIT welcomes this opportunity to provide comments to the OECD on the Revised Discussion Draft on “BEPS Action 6 Preventing Treaty Abuse” (hereinafter “the Discussion Draft”). We refer to EBIT Members’ previous comments submitted to you on 9 April 2014 and 9 January 2015, which commented more extensively on the Action 6 proposals, many of which remain relevant. The comments in this note focus on the main concerns we have with the Discussion Draft.

- EBIT Members generally support the OECD’s work on preventing Treaty Abuse, but urges the Working Group to ensure that the proposals to mitigate any BEPS concerns around treaty abuse are in line with the fundamentals of international tax treaty policy, continue to promote bilateral trade and investment, and provide access to tax treaties to their intended beneficiaries. Last but not least, the OECD’s proposals should be targeted, proportionate, and even-handed.

PART 1 - ALTERNATIVE “SIMPLIFIED” LOB RULE AND PRESENTATION OF THE LOB RULE IN THE OECD MODEL

- EBIT Members welcome the introduction of the concept of a simplified limitation of benefits (LOB) article. We note that the proposed Entitlement to Benefits article (ETB) was strongly inspired by the most recent US LOB rule and is seemingly introduced for US domestic policy concerns. We also note that a new US Model Income Tax Convention is being developed which includes revisions to the LOB. In our view having these evolving US centred rules and proposals in a new OECD Model Convention, or in a multilateral convention, is not helpful. EBIT strongly believes that such domestic policy concerns should be addressed under domestic law, however, and not through treaties
- We are particularly concerned that the proposals in the Discussion Draft appear to prescribe a combination of the use of the proposed simplified LOB to treaties with a principal purpose test (PPT) test, i.e. the simplified LOB would only be available to the limited number of treaties where both treaty partners agree to this combined test. EBIT Members note, however, that the LOB rule and the PPT rule are targeting distinct treaty shopping issues, respectively, eligibility of treaty residents for treaty benefits and targeting abuse of treaties by eligible treaty residents, which must therefore not be combined, especially given countries’ prerogative to choose to apply either a LOB rule or a PPT rule. We strongly urge the OECD to propose the simplified version and to allow bilateral treaty partners to customise a treaty LOB provision as deemed appropriate.

PART 2 – ISSUES IDENTIFIED IN THE NOVEMBER 2014 DISCUSSION DRAFT

A. ISSUES RELATED TO THE LOB PROVISION

3. Commentary on the discretionary relief provision of the LOB rule

- In EBIT’s view, the Discussion Draft imposes new standards rather than adds further clarification of the existing standards. The objective tests for eligibility for treaty benefits deny

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access to the treaty to treaty residents that are not treaty shopping. We note the proposed additional requirement in new paragraph 63 that in order to be granted treaty benefits a claimant must establish, to the satisfaction of the competent authority of the State from which benefits are being sought, that there were clear non-tax business reasons for its formation, acquisition, or maintenance and for the conduct of its operations in the other Contracting State. In practice this is in many instances not at all a straightforward process, however. On the contrary. For instance, one EBIT Member has had an application for discretionary relief with a tax administration for two and a half years, in a case where the facts were quite straightforward. EBIT Members are concerned that this new additional requirement is unnecessary and inappropriate, especially given the already broad discretion tax administrations have in determining whether to grant benefits. Also, situations where a taxpayer had no interest in the relevant treaty at the time of establishing residency in the treaty jurisdiction, could be caught by the proposed provision.

- We understand that there is currently no consensus view on Action Item 6. The reference in the proposed new paragraph 64 of the Discussion Draft that the discretionary grant process in all the BEPS-44 countries “should be handled expeditiously” is not helpful. EBIT urges the OECD to include a hard time limit of 6 months in its proposals for finalisation of applications for discretionary relief by competent authorities. Ensuring the appropriate application of anti-abuse provisions such as the discretionary relief provision of the LOB risks otherwise depending too heavily on competent tax authorities’ levels of technical expertise and notions of “reasonable behaviour”.

5. Requirement that each intermediate owner be a resident of either Contracting State

- EBIT Members are concerned that the Discussion Draft proposes to deny treaty benefits to subsidiary companies which have an intermediate owner that is not a resident of either Contracting State. We are concerned that this proposal is not compatible with today’s legitimate international business models and reality whereby it is commonplace that subsidiaries have an intermediate owner in a third jurisdiction, as a consequence of international acquisition or regional structuring choices. We also wish to note that subsidiaries, under most tests, will already have to meet a base erosion test, so adding another test is pointless, but it will mean an unwelcome additional compliance burden for multinational business.

6. Issues related to the derivative benefits provision

- We welcome the Working Party considering the proposed language regarding pension funds but are concerned at the proposed introduction of the exclusion of special regimes and the partial treaty abrogation rule with no discussion or proper consultation at this late stage of the BEPS process. The term ‘special tax regime’ is for instance broadly defined which could create considerable uncertainty for business. EBIT recommends that any concerns over ‘special tax regimes’ should be addressed as part of Action 5 (harmful tax practices).

7. Provisions dealing with “dual-listed company arrangements”

- EBIT Members welcome the requirement for competent authorities to deal with requests regarding dual residence “expeditiously” - but here again - we believe it is important to add a concrete timeline. Our suggested wording is: *“The competent authorities to which a request for determination of residence is made under paragraph 3 should deal with it within 6 months, unless there are exceptional circumstances preventing this, and should communicate their response to the taxpayer as soon as possible.”*

10. Clarification of the “active business” provision

- EBIT does not believe that the active business test is really clarified. We note that in almost all US tax treaties with an LOB, the business activities in the residence country of an affiliate can be

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attributed to the resident company claiming the treaty benefits. The Discussion Draft states that the Delegate for the United States has proposed that the attribution rule should not apply if the claimant itself is not conducting business in the residence jurisdiction. We strongly believe that once the business nexus to the jurisdiction is established, the taxpayer should not be deprived of the treaty benefit if the taxpayer chooses a local organisation involving multiple entities. The proposal from the Delegate for the United States is not helpful as it would force businesses to arrange their operations in such a way as to have the operating company hold the shares rather than the holding company.

B. ISSUES RELATED TO THE PPT RULE

14. Aligning the parts of the Commentary on the PPT rule and of the Commentary on the LOB discretionary relief provision that deal with the principal purposes test

- EBIT Members welcome the inclusion of concrete examples to try to provide further clarity around the concept of “principal purpose” as used in the Discussion Draft. The examples provided give only very limited guidance and clarification, however, because they are very straightforward and do not cover complex situations. We urge the OECD to add further examples which could be based on some of the suggestions which have been made by stakeholders earlier on in this public consultation process.
- With regard to the alignment of the standards under the discretionary grant procedure in the LOB article with the standards applied to the PPT, we refer to our earlier comments aimed at ensuring an even-handed and equitable approach to the discretionary grant (or denial) of treaty benefits.
- EBIT recommends to replace the last sentence of proposed paragraph 63.1, to ensure that information requests by tax authorities are sufficiently targeted and offer some protection to taxpayers, with: *“All evidence relevant to the determination of a principal purpose must be provided to the competent authority in order to enable it to determine whether this is the case.”*

C. OTHER ISSUES

19. The design and drafting of the rule applicable to permanent establishments located in third States

- EBIT urges the OECD to reinstate paragraph f): excepting royalty income from the rule if the royalties are earned with respect to intangible property produced or developed by the enterprise through the permanent establishment. From an EU law perspective, the Cadbury Schweppes case would suggest that taxing rights on an arm's length profit earned by activities undertaken in the jurisdiction of the PE should remain with the source country, irrespective of the effective rate of tax.
- EBIT trusts that the above comments are helpful and will be taken into account by the OECD in finalising its work in this area, and EBIT is always happy to discuss with the OECD.

Yours sincerely,

European Business Initiative on Taxation – June 2015

For further information on EBIT, please contact the EBIT Secretariat via Bob van der Made, Tel: +31 6 130 96 296; Email: bob.van.der.made@nl.pwc.com).

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