BIAC THE VOICE OF BUSINESS AT THE OECD

ACTION 6: PREVENTING THE GRANTING OF TREATY BENEFITS IN INAPPROPRIATE CIRCUMSTANCES

Background Documents:

OECD 1st Discussion Draft: March 14th, 2014
BIAC 1st Response: April 9th, 2014
OECD 2nd Discussion Draft: November 21st, 2014
BIAC 2nd Response: January 9th, 2015
OECD 3rd Discussion Draft: May 22nd, 2015
BIAC 3rd Response: June 17th, 2015
OECD Report: October 5th, 2015

Last updated: 30 November 2015

TOPIC	BIAC COMMENTS	OECD RESPONSE
General	1. Defining abuse/abusive	No definition provided.
	2. Treatment of tax sparing needs to be clarified specifically.	The only reference to tax sparing is in the commentary to the Principal Purposes Test ("PPT") clause. Accordingly, tax sparing is a tax treaty limitation and as such falls within the definition of "benefit" for PPT rule purposes.
	3. Anti-avoidance clauses should not be used by one State to counter tax policy decisions made by the other State.	Comment not acknowledged.
	4. Recognise that holding, financing and investment activities (including licensing) are normal and legitimate business activities that should not suffer blanket exclusions from treaty protection.	Although not explicit, it could be inferred from paragraph 3(a) of the detailed Limitation of Benefits ("LoB") clause and 4(a) of the simplified LoB clause that financing & investment activities when carried on by a bank, an insurance company and a registered securities dealer are entitled to treaty benefits. Para 48 of the commentary to the LoB clause states that a company functioning solely as a HQ will not be considered to be engaged in the active conduct of a business. Example E of para 15 of the commentary of the PPT rule implies that a holding company does not necessarily lead to a conduit arrangement.
	5. Provisions to request up-front competent authority confirmation that a structure is not abusive.	Although not explicitly acknowledged, para. 5 of the LoB article allows a resident to request a facts and circmstances based assessment from the competent authority if not automatically entitled to treaty benefits.
	6. Action 15 should not incorporate the outcomes of Action 6	Comment not acknowledged. Work on the multilateral instrument will include the outcome of Action 6 and measures to prevent treaty shopping were agreed as minimum standards.
	7. The special tax regime addition should be removed.	The special tax regime addition remains in the final report. However, the proposal needs to be reviewed and, if necessary, finalised in the first part of 2016.

	8. No automatic and unilateral denial of treaty benefits when there is change in domestic legislation exempting "substantially all" foreign source income.	The new treaty rule intended to make a tax treaty responsive to certain future changes in a country's domestic law remains in the final report. However, the proposal needs to be reviewed and, if necessary, finalised in the first part of 2016.
LoB	9. Adopt LoB or GAAR, but not both.	Final report acknowledges that the combination of an LoB clause and a PPT rule may not be appropriate or necessary for all countries, but at a minimum countries should implement a PPT rule or an LoB clause supplemented by a mechanism that would deal with conduit arrangements.
	10. LoB should be as simple and unrestrictive as possible, alternative wording should be considered (TT US/UK, US/NL, JP/SWZ, JP/NL)	Final report contains two model versions of the LoB clause, one detailed and one simplified. The LoB clause proposed was based on the LoB clause in treaties concluded by US, Japan and India.
	11. LoB ownership requirement is duplicative/ unwarranted.	The ownership requirement remains in the final report, both in the simplified LoB and the detailed LoB. Follow up work on the inclusion of a derivative benefits provision in the LoB to be carried by the first part of 2016.
	12. Essential to include a provision for regional HQ companies.	No provision included. Para 48 of the commentary to the LoB clause states that a company functioning only as an HQ will not be considered to be engaged in the active conduct of business (and not be entitled to treaty benefits).
	13. The RDD does not address situations of mixed active and investment income.	Final report does not address situations of mixed active and investment income.
	14. "The same or similar line of business" requirement is ambiguous and unclear. It is also unclear how it interacts with the "in connection or incidental to" test that establishes the necessary relationships between the related businesses.	The "same or similar line of business" requirement is not included in the final report. Para 44 et seq. of the commentary to the LoB addresses the terms "in connection with" and "incidental to". Follow up work on the LoB to be carried by the first part of 2016.
	15. Joint venture agreements should be considered	No reference to joint ventures.
	16. Active trade or business rule should apply to other industries (banking, insurance, securities) and the test should be at a group level, rather than company level.	Final report refers to *"the active conduct of a business"* rule in the detailed LoB clause and to the *"carrying on business"* rule in the simplified LoB clause. Both versions include the business of banks, insurance companies, and registered securities dealers. The test is not at a group level.
	17. Should contain reasonable objective tests that can be applied by taxpayers and confirmed by tax authorities.	Paras. 1 to 4 of the LoB clause are objective tests. There is no reference to the possibility to request confirmation from the tax authority on the application of these criteria. As last resort, if a resident is not entitled to treaty benefits under para. 1 to 4, that resident can request consideration of the facts and circumstances to the tax authority. This analysis, according to the para. 64 of the commentary to

		the LoB clause, has to be objective as well.
	18. OECD should provide clear guidance on information requirements, timing aspects & other procedural matters	No guidance on this aspect is provided.
	19. Make clear the treatment of CIVs – i.e. output of CIV report is not impacted unless CIV is abusive.	CIV Report has been confirmed as part of the work on Action 6. Para. 2(f) to the LoB clause allows the inclusion of CIVs as qualified persons depending on how CIVs are treated in the Convention.
	20. Indirect relief for persons operating exclusively for charitable purposes.	No indirect relief for persons operating exclusively for charitable purposes.
	21. LoB should provide for the determination of *"principal class of shares"* after excluding special voting shares or Dual Listed Company ("DLC") shareholdings.	Para. 6(b) of the detailed LoB clause and para. 73 of its commentary provides that the principal class of shares of a company must be determined after excluding special voting shares issued as a means of establishing a DLC arrangement.
	22. Pension funds should not be subjected to LoB clause or PPT rule.	Pension funds are included in para 2.d) of the LoB clause. Accordingly, a resident pension fund will qualify for treaty benefits if more than 50 per cent of the beneficial interests in that person are owned by individuals resident of either Contracting State or if more than a certain percentage of these beneficial interests are owned by such residents or by individuals who are residents of third States provided that two conditions are met. Additional work, to be carried by early 2016, will also ensure that a pension fund should be considered to be a resident of the State in which it is constituted regardless of whether that pension fund benefits from a limited or complete exemption from taxation in that State.
	23. Should ensure treaty-entitled investors in non-CIVs receive the relief negotiated by their States	The final report did not confirm the conclusion of the 2008 REIT Report. In the first part of 2016, the OECD will address some of the concerns regarding the treaty entitlement of non-CIV funds.
	24. Regarding discretionary relief, a rebuttable assumption of non-abuse should be included where the treaty with the ultimate parent provides for a rate of WHT which is not higher than the one with the direct beneficiary of income.	Commentary 63 to the LoB clause explains that the fact that the treaty with the parent provides for a rate of WHT which is not higher than the one with the direct beneficiary of the income is a relevant factor, but is not necessarily sufficient to establish that the conditions for granting discretionary relief are met.
	25. Intermediary company testing should be removed. The Model Treaty should focus on the Contracting State of the ultimate beneficial owners ("UBO").	The final report keeps the test on intermediary companies is necessary to prevent the interposition of a company in a tax haven. No reference to UBOs.
	26. Recommend that the Model Treaty contains a "safe harbour" based on objective metrics (e.g. NL-US treaty - where three	No safe harbour proposal.

	ratios are examined).	
	27. Para. 46 of the RDD may result in denial of benefits unless the listed entity is resident in the same territory as the entity seeking benefits. This seems overly restrictive and unnecessary.	The final report contains para 2.f) as was proposed in para 46 of the RDD. Thus, the listed entity needs to be resident in the same territory as the entity seeking benefits..
PPT	28. PPT rule should be limited to circumstances where a structure has been wholly artificially set up solely to secure treaty benefits.	There is no reference to whether a structure needs to be wholly or partially artificial to deny treaty benefits.
	29. "One-of-the-main-purposes" test is too widely framed, it should focus on substance.	"One-of-the-main-purposes" test has been replaced with PPT rule; however, the PPT rule remains widely framed. No reference to considering substance.
	30. General Anti Abuse Rule should be very limited and focused (given Specific Anti Abuse Rules)	Comment not acknowledged: the PPT rule is still widely framed.
	31. If Contracting States are unable to agree, there should be an underlying assumption that it is not reasonable to conclude that obtaining a benefit was a principal purpose.	Comment not acknowledged.
	32. Discretionary relief should be available for the PPT rule.	The RDD proposed in para. 90 to include a paragraph 8 dealing with the discretionary relief for the PPT rule. However, the final report did not contain such paragraph.
	33. Disputes under the PPT rule should be rectified under mandatory arbitration	Comment not acknowledged.
SAAR	34. Article 10(2): a 3-month period plus a mechanism to recover any withholding tax after completing the time threshold if did complete it at the moment of paying the dividend.	Comment not acknowledged – Minimum shareholder period set at 365 days. No mechanism to recover any withheld tax once the time threshold is completed.
	35. Tie-breaker Rule: to retain Place of Effective Management (PoEM), but with a recourse to ascertain a single residency via Competent Authorities. Only in exceptional circumstances, where structures are set up for abusive purposes.	Final report states that competent authorities shall endeavour to determine through MAP where a person shall be deemed resident. However, para 24 of the commentary to Art. 4 provides that States that consider the PoEM as a better approach can include that when negotiating a treaty.
Abuse D.L.	36. A provision to ensure that in enforcing local laws, double taxation is not created.	Comment not acknowledged.
	37. Model convention should include specific, clear pieces of local legislation that are not overridden by the Treaty to avoid uncertainty and protracted discussions	New para 25 et seq. of the commentary to article 1 provides guidance on how such conflicts can often be avoided, although each case must be analysed based on its own circumstances. No clear suggested legislation that will not be overridden by the treaty.

	38. Local law changes should not immediately impact application of the Treaty without a specific Protocol.	The proposal 2 in the tax policy considerations chapter of the final report provides that if a contracting party provides an exemption from taxation to resident companies/individuals for substantially all foreign source income some treaty provisions may cease to have effect. Notifications through diplomatic channels would be required and cessation shall begin 6 months after the aforesaid notification.
	39. Domestic anti-avoidance rules should be allowed to override the Treaty, to ensure their proper application, but the circumstances for overriding must be clear.	It can be inferred from the new para 23 of art. 1 that domestic anti-avoidance rules can override a treaty if the application of such rules in domestic law were to result in a tax treatment that is in accordance with the provisions of the tax treaty.
Objectives TT	40. Draw a clear line between unlawful activities and lawful ones.	Comment not acknowledged.