Euro Tax Flash from KPMG's EU Tax Centre

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting

OECD – BEPS Action 15 – Multilateral Instrument – Hybrid mismatches – Treaty abuse – Permanent establishment – Dispute resolution

More than 100 jurisdictions have concluded negotiations on a Multilateral Convention (or 'multilateral instrument') that is intended to implement certain tax treaty related aspects of the OECD/G20 Base Erosion and Profit Shifting (BEPS) initiative. The Convention is designed as a quick and effective mechanism to allow governments to bring their treaties into line with these aspects of the BEPS project, instead of renegotiating individual treaties. The OECD anticipates that up to 2000 treaties could be amended in this way.

Background

In the course of the OECD BEPS project over 60 countries jointly developed 15 actions to tackle tax avoidance, improve the coherence of international tax rules and ensure a more transparent tax environment (see [ETF 218](#)). The final reports were published on 5 October, 2015.

As part of the BEPS Action Plan, the Final Report on Action 15 demonstrated the need for a multilateral instrument to enable countries to swiftly modify their bilateral tax treaties to implement measures related to BEPS. The Convention was developed over the past year, via negotiations involving more than 100 jurisdictions, including OECD member countries, G20 countries and other developed and developing countries under a mandate delivered by G20 Finance Ministers and central Bank Governors at their February 2015 meeting.

The text of the Convention (see: here) was published on 24 November, 2016 together with an Explanatory Statement (see: here).

Scope

Parties

The Convention will be open for signature by any country as of 31 December 2016.

Tax agreements to be modified by the Convention

The existing agreements for the avoidance of double taxation with respect to taxes on income, whether or not other taxes are also covered of the signing party, will be modified after the Convention comes into effect. Parties will have to make a notification to the OECD (which will be the depositary of the multilateral instrument) listing the exact agreements they wish to be covered by the Convention.

BEPS Actions covered by the Convention

1. Hybrid Mismatch Arrangements (BEPS Action 2)
   - Transparent entities (Article 3)
   - Dual-resident entities (Article 4)
   - Application of methods for elimination of double taxation (Article 5)
2. Treaty Abuse (BEPS Action 6 – minimum standard)
   - Prevention of treaty abuse – Limitation-on-benefits and principle purpose test rules (Article 7)
   - Dividend transfer transactions (Article 8)
   - Capital gains from alienation of shares in real estate entities (Article 9)
   - Anti-abuse rule for permanent establishments situated in third jurisdictions (Article 10)
   - Application of tax agreements to restrict a party's right to tax its own residents (Article 11)
   - Tie-breaker rule for determining the treaty residence of dual-resident persons other than individuals (Article 4)
3. Avoidance of Permanent Establishment Status (BEPS Action 7)
   - Commissionaire arrangements and similar strategies (Articles 12 and 15)
   - Specific activity exemptions (Article 13)

- Splitting-up of contracts (Article 14)

4. Improving Dispute Resolution (BEPS Action 14 – minimum standard)
   - Mutual agreement procedure (Article 16)
   - Corresponding adjustments (Article 17)
   - Commitment to mandatory binding Mutual Agreement Procedure arbitration (Articles 18 through 26)

Options

Minimum standards

As set out in the Final reports on the BEPS project, in terms of four BEPS measures all OECD and G20 countries have committed to consistent implementation. These minimum standards cover Country-by-Country Reporting, fighting harmful tax practices, preventing treaty shopping and improving dispute resolution. Of these, the Convention implements the two treaty related minimum standards: countering treaty abuse and improving dispute resolution mechanisms while providing flexibility to accommodate specific tax treaty policies.

Where a provision reflects a BEPS minimum standard, opting out of that provision is possible only in limited circumstances, such as where a tax treaty to be modified already meets that minimum standard. Where a minimum standard can be satisfied in different ways, the Convention does not give preference to a particular way of meeting the minimum standard. In cases where contracting jurisdictions each adopt a different approach to meeting a minimum standard that requires the inclusion of a specific type of treaty provision, those jurisdictions must endeavour to reach a mutually satisfactory solution consistent with the minimum standard.

Reservations

Parties can make reservations in line with the provisions of the Convention. Where a substantive provision does not reflect a minimum standard (e.g. provisions related to hybrid mismatches and measures against avoidance of permanent establishment), the signing party is generally given the flexibility to opt out of that provision entirely (or, in some cases, out of part of that provision).

Where a party uses a reservation to opt out of a provision of the Convention, that provision will not apply as between the reserving country and all other parties to the Convention. Accordingly, no modifications will be made to any of the covered tax treaties of the reserving party in this respect.

Timeline

The Convention enters into force after five countries have ratified, accepted or approved it. In terms of a specific tax treaty it will enter into effect, after all parties to that treaty have ratified the instrument and a certain period defined by the Convention has passed to ensure clarity and legal certainty.

Next steps

Governments are currently preparing their lists of treaties to be covered by the Convention and are considering which options to select and reservations to make.

A first high-level signing ceremony is expected to take place in early June 2017. As mentioned above, an Explanatory Statement has been published together with the text of the Convention, but also other guidance will further be developed by the OECD to support governments to prepare their own processes for signature, ratification and implementation. The covered treaties, reservations and options of the jurisdictions will be published online at a later stage.

EU Tax Centre comment

We agree with the OECD's statement that the Multilateral Convention is a major achievement. The OECD expressed the view that this will result in more certainty and predictability for businesses, and a better functioning international tax system for the benefit of citizens. Whether this will be the case remains to be seen, in particular given the opportunities under the Convention to make reservations and choose options. It should also be noted that this is just the first step in the process and the Convention still needs to be ratified and the tax treaties specified to which it is to apply.

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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