Joint Opinion Statement FC 2/2015 on the OECD Discussion Draft "Follow-up work on BEPS Action 6: Preventing treaty abuse"

Prepared by the CFE Fiscal Committee, agreed by AOTCA and submitted to the OECD in January 2015

CFE (Confédération Fiscale Européenne) is the umbrella organisation representing the tax profession in Europe. Our members are 26 professional organisations from 21 European countries (16 OECD members) with more than 100,000 individual members. Our functions are to safeguard the professional interests of tax advisers, to assure the quality of tax services provided by tax advisers, to exchange information about national tax laws and professional law and to contribute to the coordination of tax law in Europe. CFE is registered in the EU Transparency Register (No. 3543183647-05).

AOTCA (Asia-Oceania Tax Consultants´ Association) was founded in 1992 by 10 tax professionals' bodies located in the Asian and Oceanic regions. It has expanded to embrace 20 leading organizations from 16 countries/regions.

Introduction

The following comments relate to the OECD's Public Discussion Draft "*Follow-up work on BEPS Action 6: Preventing Treaty abuse*[1]" (hereinafter: Discussion Draft) of 21 November 2014. This Discussion Draft follows up on the OECD Discussion Draft of 14 March 2014 on the same topic[2] on which the CFE has commented in its Opinion Statement FC 5/2014 of April 2014[3].
We will be pleased to answer any questions you may have concerning our comments. For further information, please contact Mr. Piergiorgio Valente, Chairman of the CFE Fiscal Committee, or Rudolf Reibel, Fiscal and Professional Affairs Officer of the CFE, at brusselsoffice@cfe-eutax.org.

AOTCA and CFE comments

The objective of BEPS Action 6 is the prevention of treaty benefits in inappropriate circumstances. It is felt however that the proposals put forward may be disproportionate to the objective intended and may create a situation of double taxation even if the primary intention had not been treaty abuse. More importantly, the subjective nature of certain proposals and the lack of certainty in the accompanying commentary creates scope for uncertainty in their application.

There are concerns that some of the changes proposed to date could have a disproportionate impact on businesses in smaller economies, with smaller capital markets, who are naturally more likely to seek capital and finance abroad.

Discretionary relief provisions

This suggestion is intended to provide treaty relief where a resident of a contracting state would otherwise be denied treaty benefits under the LOB rule. There are concerns that this may be difficult to apply in practice as experience has indicated that it can be very difficult to get agreement from tax authorities that discretionary relief should be afforded to a taxpayer even in circumstances where a company has very clear and substantial links with and operations in its company of residence.

In any case, a time limit should be imposed on the competent authority to process the request for the application of discretionary relief.

Derivative benefit provisions

We welcome the suggestion of an inclusion of a derivative benefits test in the LOB (limitation of benefits) although we note that this is not supported by all the countries. The requirement that all entities in the chain of ownership should be "equivalent beneficiaries" is restrictive and the definition of equivalent beneficiaries excludes private companies. This should be changed so that the full range of persons including private companies are capable of being equivalent beneficiaries.

Timing issues related to the various provisions of the LOB rules

Listing is an onerous time consuming process that requires regulatory approval. A company that lists in the middle of a taxable year would have initiated the process way before that. The intention to list would have

[1] http://www.oecd.org/ctp/treaties/discussion-draft-action-6-follow-up-prevent-treaty-abuse.pdf
[2] http://www.oecd.org/ctp/treaties/treaty-abuse-discussion-draft-march-2014.pdf
[3] http://www.cfe-eutax.org/node/3668

been there and consequently the requirement listed throughout the taxable period should be revised to "is listed during a taxable period".

Active business test

The active business test provides an important opportunity for substantive businesses to pass the LOB.

The proposed LOB states that where income is derived from a related party, the active business test will only be considered to be satisfied if the business activity carried on in the small country is substantial in relation to the business activity carried on by the associated enterprise in the other state. Ideally, the substantiality requirement would be dropped because it will often be difficult for an entity in a small country to be able to meet this test.

The OECD commentary does helpfully note that due regard will be given to the relative sizes of the economies and markets in the two contracting states.

There also needs to provide clarification on what constitutes "active" business. It is quite possible that there is a substantial presence in the small country concerned which carries out substantial activity, but which is not "active" (as currently defined by US tax law). There should be clarification that business support activities (where the workforce in the small country concerned conduct substantial managerial and operational activities over those support services) can qualify as an active business even where those activities are provided for the benefit of related group parties.

It would also be useful to consider whether a "safe harbour" might be included similar to those contained in some US treaties currently – either a mathematical safe harbour or a purpose test.

Publicly Traded test

The definition of "another recognised stock exchange" should be extended to include major country exchanges (such as the US) and exchanges in regional groupings such as the EEA. There are valid and particular reasons why many non-US companies choose to list on NASDAQ as an example.

Principal Purpose test

There are concerns that the principal purpose test (PPT) will be much more difficult to pass for businesses in smaller economies. It is more likely that the benefits of being able to access a tax treaty to avoid double tax in relation to a cross border transaction or business arrangements will be more evident in the case of the taxpayer based in a smaller economy. This benefit could more easily be identified as one of the main benefits that arise to that taxpayer from the cross border transaction. Smaller country businesses face considerable uncertainty as to whether they can ever pass the PPT test.

A business operating in a large economy will find it much easier to pass the PPT than a business operating in a smaller economy, simply by virtue of the size of the economy. This is a distortionary effect and creates an un-level playing field as well as very significant uncertainty and cost for businesses in smaller countries.

The PPT rule should be redrafted to provide that treaty benefits can arise except where the main purpose of the arrangement or transaction is to obtain the treaty benefit. This should achieve a balance between protection from treaty shopping and reflecting and preserving the benefits that treaties offer to taxpayers in smaller economies.