

BEPS Action 6 Treaty Abuse

Irma Johanna Mosquera Valderrama

Greece, 24 October 2019

Associate Professor of Tax Law– Principal investigator *EU-ERC GLOBTAXGOV*



Universiteit
Leiden
The Netherlands



GLOBTAXGOV

A NEW MODEL OF GLOBAL GOVERNANCE IN INTERNATIONAL TAX LAW MAKING



European
Research
Council

Topics

**BEPS Action 6:
TOR**

**BEPS Action 6 and
MLI**

**Practical Problems
Application PPT**



OECD-BEPS

- BEPS Inclusive Framework 4 Minimum Standards: 134 countries
- BEPS MLI: In force as of 1 July 2018; 89 countries (signatories).
- Greece:
 - Committed as BEPS Associate to the BEPS Inclusive Framework.
 - Signatory of the BEPS MLI (57 CTAs). No yet in force, awaiting deposit instrument of ratification.

1. BEPS Action 6: Terms of Reference

- **May 2017: Terms of Reference**

- Preamble

- Treaty provision that will take one of the following three forms:

- PPT
- PPT with either simplified or detailed LOB
- Detailed LOB with anti-abuse measures to counteract conduit financing

- **1st Report on compliance Action 6 by the BEPS Inclusive Framework available 15 February 2019.**

2. Greece: MLI

- “Complex menu of options” due to the opt-in; opt-out clauses: PPT (with or without discretionary relief), Detailed LOB, PPT as interim measure, Supplement PPT with simplified LOB
- Difficult to manage due to capacity constraints and tax treaty policy choices
- Mismatching of choices may result in multiple mini-treaty negotiations
- Some examples:
 - Greece PPT with simplified LOB (7(7)(b)).
 - Cyprus, The Netherlands, Curaçao, Malta and Singapore PPT with discretionary relief
 - Mauritius PPT as interim measure but intend to apply PPT with simplified LOB through bilateral negotiation

2. Greece: MLI

Notification of Existing Provisions in Listed Agreements:

Pursuant to Article 7(17)(a) of the Convention, the Hellenic Republic considers that the following agreement is not subject to a reservation described in Article 7(15)(b) and contains a provision described in Article 7(2). The article and paragraph number of each such provision is identified below.

- Already ratified: Austria, Belgium, Iceland, Poland No yet ratified: Mexico and Portugal. Articles 11 and 12 DTAs.

2. Greece: MLI

Art. 6(1) An additional text in the preamble

“Intending to conclude a Convention for the elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including treaty shopping arrangements aimed at obtaining reliefs provided in this Convention for the **indirect benefit** of residents of third states)”

Art. 6(3) In addition a party may choose to include in the preamble

“Desiring to further develop their economic relationship and to enhance their co-operation in tax matters”

Greece introduces text art. 6(1) and Art. 6(3) to all 61 CTAs.

Relevant for the interpretation of the PPT (objective element).

3. Practical problems PPT

- **Article 7(1): 3 Elements PPT**

- **Benefit under a Covered Tax Agreement:** Art. 6 to 22, art. 23, and art. 24 of the OECD Treaty. It can also include tax sparing para. 175 Comm. Art. 29 2017 OECD Model) – Benefit (tax deduction, exemption, deferral or refund).
- **Subjective element:** *“if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining the benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit”* – **Tax Administration**
- **Objective element:** *“it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the Covered Tax Agreement”* - **Taxpayer**

3. Practical problems PPT

- Tax Administration and Taxpayer: Burden of proof.
 - Subjective element: **Reasonable** to conclude having regard to all relevant facts and circumstances that “one of the principal purposes...” Use of the word reasonable lower the burden for the tax authority vis-à-vis taxpayer.
 - Objective element: **Establish** that granting of a benefit in accordance with the object and purpose of the relevant treaty provisions. Taxpayer must refute clearly and unambiguously

Court a decisive role on whether or not the transaction arrangement satisfied the PPT. If not clear, the benefit of the doubt should go to the taxpayer (*V. Chand 2018*)

3. Practical problems PPT

- ❑ Lower threshold: PPT: One of the principal purposes is a tax benefit. Arbitrary, but reduced if discretionary relief but still MAP will be needed.
- ❑ Medium threshold: GAAR: Main (sole) purpose a tax benefit. GAAR not applicable if economic substance (a minimal business activity, and there are tax and non-tax related motives). e.g. Northern Indiana Public Service Corp. v. Commissioner (115 F3d 506 (7th Cir. 1997))
- ❑ Higher threshold: Wholly artificial transactions or arrangements entered solely for the purpose of avoiding tax. e.g. Cadbury Schweppes CJEU case (see also Webber, 2017)

3. Practical problems PPT

- One of the principal purposes vs. main purpose, sole purpose
 - e.g. commercial reason and tax reason: PPT applies if “one of the principal purposes” is a tax reason
 - However, balance tax purposes vs. genuine commercial/economic objectives. How that this works in practice? See para. 181 Commentary to art. 29 2017 OECD Model
 - Large tax benefit in taxation does not mean always application PPT –if in accordance to the object and purpose of the treaty
 - PPT discretionary relief (or not) may raise competition among countries since the tax administrations will have a discretionary power
- Some scholars: Recommend to choose for artificiality (objective –wholly artificial arrangements) instead of reasonable test (subjective) test.
Desirable?

3. Practical problems PPT

- Two-steps approach: Object and purpose of (i) treaty in general AND (ii) relevant provisions in the treaty? ?
- Preamble: art 6(1) only “indirect benefit of residents of 3rd jurisdictions” and also in the definition of treaty shopping “indirectly the benefits”. How to interpret this?
- Role of the explanatory memoranda and commentaries in the interpretation of the object and purpose?
- Still problems in interpretation of tax treaties create uncertainty (OECD new project). How to deal with this? Is the commentary to art. 29 (Entitlement to benefits) 2017 OECD Model sufficient? Static vs. dynamic ordinary meaning? Context?

3. Practical problems PPT

- **PPT-SAAR:** (*para. 171 to commentary art. 29 OECD 2017 MC*)
- *Lex specialis.* However, PPT wording: Notwithstanding any provisions of a covered tax agreement. Thus, PPT prevails over SAARs.
- PPT apply even if beneficial ownership (BO) requirement is satisfied, or if it has passed the LOB tests. LOB does not address all forms of treaty shopping
- PPT umbrella clause prevails over
 - LOB , BO, SAARs (MLI art. 8(1) and art. 9(1)).
- SAAR: Based objective verifiable (often quantitative, safe harbor) parameters

Scholar (Danon). Not acceptable that still PPT can apply to extend the legal consequences provided therein to other situations beyond the scope of the SAAR.

• ***Result: Uncertainty for taxpayer***

Visit us at

- **Leiden University, Institute of Tax Law and Economics**
- **GLOBTAXGOV project receives funding from the EU H2020 Research & Innovation Programme and European Research Council**
Blog <https://globtaxgov.weblog.leidenuniv.nl/>
- **Twitter: @GLOBTAXGOV @IrmaMosqueraV**



**Universiteit
Leiden**
The Netherlands



**European
Research
Council**

Further reading

- See I.J. Mosquera Valderrama blogpost GLOBTAXGOV <https://globtaxgov.weblog.leidenuniv.nl/2019/07/29/what-does-the-ppf-say-about-global-tax-governance/>
- V. Chand, “The principal purpose test in the Multilateral Convention. An in-depth analysis”. 46 Intertax Issue 1 (2018) pp. 18-44
- D. Duff, “Tax Treaty Abuse and the Principal Purpose Test” Part I. Canadian Tax Journal (2018) pp. 619-677 and “Tax Treaty Abuse and the Principal Purpose Test” Part. II (Forthcoming 2019)
- B. Kuźniacki, “The Principal Purpose Test (PPT) in BEPS Action 6 and the MLI”, World Tax Journal, Vol. 10. No. 2. (2018)
- P. Piantavigna, “The Role of the Subjective Element in Tax Abuse and Aggressive Tax Planning”, World Tax Journal, Vol. 10 No. 2 (2018)
- D. Weber, "The Reasonableness Test of the Principal Purpose Test Rule in OECD BEPS Action 6 (Tax Treaty Abuse) versus the EU Principle of Legal Certainty and the EU Abuse of Law Case Law", Erasmus Law Review, 1, (2017) pp. 48-59
- S. van Weeghel, A Deconstruction of the Principal Purpose Test, World Tax Journal, Vol. 11 No. 1. (2019)