



Tax Insights

Multilateral Instrument: One step closer

Snapshot

On Thursday 16 August 2018, the [Treasury Laws Amendment \(OECD Multilateral Instrument\) Bill 2018](#) (the Bill) completed its passage through Parliament and now awaits Royal Assent. The Bill amends the *International Tax Agreements Act 1953* to give force of law in Australia to the Multilateral Instrument (the MLI). The MLI (BEPS Action 15) is designed to swiftly implement the tax treaty-related measures arising from the G20/OECD BEPS project without the need to renegotiate each bilateral tax treaty. For more details on the MLI, refer also to the Deloitte Tax Insights publication released on 16 June 2017 that can be accessed [here](#).

The MLI entered into force (following ratification by five jurisdictions - Poland, Austria, Jersey, Isle of Man and Slovenia) on 1 July 2018. The MLI will also come into force for New Zealand, Serbia, Sweden and the UK on 1 October 2018. As additional jurisdictions formally ratify the MLI, the MLI will come into force for those jurisdictions three clear months after such ratification.

The speed at which the MLI has entered into force is exceptional: between the adoption of the text of the MLI (BEPS Action 15) on 24 November 2016 and its entry into force, roughly 18 months has elapsed.

Once the Bill receives Royal Assent, Australia will be able to formally ratify the MLI. If this ratification occurs prior to the end of September 2018, the MLI should enter into force for Australia from 1 January 2019.

83 jurisdictions have signed the MLI and an additional five jurisdictions have expressed their intent to do so (status as of 23 July 2018). The MLI is expected to (over time) update more than 1,100 bilateral tax treaties, referred to as Covered Tax Agreements (CTAs).

Each of the MLI signatories deposited provisional lists of CTAs, reservations and notifications to the MLI. Upon ratification of the MLI, jurisdictions will finalise their CTAs, reservations and notifications.

The MLI does not function in the same way as a protocol to an existing treaty. It does not directly change the underlying text of a CTA, but will be applied alongside the existing CTA, modifying its application on BEPS matters. The MLI provisions, are to be applied in place of, or in the absence of particular provisions in a CTA, or will apply to modify an existing provision of a CTA.

MLI impact for Australia's tax treaties

Based on Australia's tax treaty partners' known positions (provisional and final), the MLI will modify 31 of Australia's 44 tax treaties (refer to Table 1: Who's in who's out for further details). The way in which the MLI will modify these treaties will depend on the final positions taken by each country upon ratification.

- Australia has listed 43 of its 44 bilateral tax treaties as CTAs. The tax treaty with Germany (signed in 2015) was excluded as it is compliant with the OECD's recommended BEPS treaty proposals.
- 8 of our treaty partners have not signed the MLI (as of 23 July 2018), such that the respective tax treaties will not be impacted by the MLI. The US has not signed the MLI and is not expected to do so.
- 4 of our treaty partners have signed the MLI but did not list the tax treaty with Australia as a CTA. For example, whilst Australia has a tax treaty with Austria and Sweden, both of which have already ratified the MLI, Australia's tax treaties with these countries will not be impacted by the MLI as those countries have not listed the treaty with Australia as a CTA.

Australia's first CTAs affected by the MLI should be Australia's bilateral tax treaties with:

- New Zealand (the MLI will enter into force for New Zealand on 1 October 2018),
- The United Kingdom (the MLI will enter into force for the UK on 1 October 2018) and,
- Poland (the MLI entered into force for Poland on 1 July 2018).

It is likely that a number of other jurisdictions will ratify the MLI prior to the end of September 2018 so that the MLI should also enter into force for these jurisdictions as from 1 January 2019. It will be important to monitor additional MLI ratifications prior to the end of September 2018.

Australia's first bilateral tax treaties to be impacted by the MLI will be with New Zealand, the United Kingdom & Poland. Other treaty partners may also ratify before the end of September 2018.

MLI overview

The MLI includes articles on hybrid mismatches (BEPS Action 2), treaty abuse (BEPS Action 6), permanent establishments (BEPS Action 7), improving dispute resolution and arbitration (BEPS Action 14). The BEPS minimum standards address treaty abuse and mutual agreement procedures (MAPs). Further, depending on the reservations and notifications made by each party, optional changes to modify tax treaties in respect of permanent establishments (PEs), transparent entities, residency tiebreakers, minimum shareholding periods, capital gains derived from immovable property and mandatory binding arbitration will be facilitated.

Treaty abuse (Action 6): minimum standard

Article 6 of the MLI modifies a CTA to include preamble language stating that the purpose of the CTA is to eliminate double taxation without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty-shopping arrangements.

Article 7 of the MLI introduces new anti-abuse rules that will enable tax administrations to deny treaty benefits in certain circumstances. Countries may choose between three options: the principal purpose test (PPT), the simplified limitation on benefits (LOB) provision plus PPT or the detailed LOB plus an anti-conduit mechanism. The "PPT only" option was the runaway winner for the signatory jurisdictions, including for Australia. If Australia's treaty partner has also chosen to adopt the PPT, there is a "match" with the Australian approach, and the CTA with Australia will be modified to effectively include the PPT.

Improving dispute resolution (Action 14): minimum standard

Article 16 of the MLI provides that all CTAs will now include a minimum standard for MAPs. If a tax treaty-related case qualifies to be considered under the MAP, upon the request of a taxpayer, the competent authorities should endeavour to agree between themselves how double tax agreements should apply, and implement any agreement.

Optional MLI provisions

The MLI gives the option for jurisdictions to opt into additional provisions in the MLI. The impact on a particular CTA will depend upon the various opt in/opt out choices made by both countries. Based on Australia's provisional positions, Australia is supportive of some of these optional MLI articles including:

- Transparent entities (MLI Article 3);
- Dual resident entities (MLI Article 4);
- PE matters including changes to the preparatory and auxiliary exception (MLI Article 13(1)), anti-fragmentation (MLI Article 13(4)) and contract splitting (MLI Article 14).

Australia has adopted the mandatory binding arbitration mechanism (MLI Articles 18-26), however, has made a reservation to exclude disputes involving the application of Part IVA of the *Income Tax Assessment Act 1936*, thus excluding the Diverted Profits Tax (DPT) and the Multinational Anti-Avoidance Law (MAAL) matters from arbitration.

The MLI constitutes a major change to international taxation: it will enable tax authorities around the world to challenge transactions on a new basis and (hopefully) provide greater certainty for taxpayers by improving dispute resolution mechanisms.

On the other hand, Australia has indicated that it will reserve its position (ie, not adopt the MLI provisions) on matters such as:

- Anti-abuse rule for PEs in third states (MLI Article 10)
- Artificial avoidance of PE status through commissionaire arrangements and similar strategies (MLI Article 12).

MLI Article 12 is, in broad terms, dealing with arrangements similar to those targeted by the MAAL. So as a general position, the MAAL could apply to foreign companies selling into Australia, but there will be no (broadly) equivalent provision via the MLI applying to Australian companies selling into foreign countries. However, it is expected that Australia will be prepared to adopt MLI Article 12 in the context of future bilateral treaty negotiations. For example, this provision was included in Australia's new bilateral tax treaty with Germany.

When will the MLI impact Australia's treaties?

Once the MLI has entered into force in Australia (and subject to its entry into force in the relevant treaty partner jurisdiction), it will enter into effect with respect to a particular CTA with a treaty partner as follows:

- For withholding taxes: the entry into effect of the MLI will happen on or after the first day of the next calendar year that begins on or after the latest of dates on which the MLI enters into force for Australia and the relevant treaty partner jurisdiction. For example, if both treaty partners ratify the MLI before 30 September 2018, the MLI should enter into force on or before 1 January 2019 and the entry into effect of the MLI in respect of a particular CTA for withholding tax purposes should be on 1 January 2019.
- For all other taxes, the MLI will apply to taxable periods beginning on or after six months after the later date of entry into force of the MLI for Australia and the treaty partner. For example, if the MLI enters into force for two countries on 1 January 2019, the MLI should apply to taxable periods starting on or after 1 July 2019.
 - For a taxable period ending 30 June (such as Australia), the MLI should apply to taxes levied by that country for taxable periods commencing on or after 1 July 2019.
 - If a taxable period in a country follows a calendar year, the MLI should apply to taxes levied by that country for taxable periods commencing on or after 1 January 2020.
- For MAP and mandatory binding arbitration, the MLI will apply on or after the latest of the dates of entry into force of the MLI for Australia and the treaty partner. For example, if the both treaty partners ratify the MLI in September 2018, the MLI should enter into effect on 1 January 2019 for MAP and arbitration purposes.

Actions required

The MLI will affect the operation of an existing tax treaty where Australia and a treaty partner country have both ratified the MLI, both countries have identified the existing tax treaty as a CTA and the entry into effect dates have become operative. It is then necessary to analyse the reservations, notifications and choices made by both countries to ascertain the particular provisions of the MLI that will operate in respect of the two countries. This process means that the impact of the MLI on one of Australia's CTAs could be different to the impact of the MLI on another of Australia's CTAs.

The application of the MLI to a particular tax treaty will be complex and will require careful analysis.

Although the MLI will apply prospectively, groups that currently benefit from tax treaties should carefully analyse the impact of the modifications in respect of existing arrangements and transactions. For example, under the new anti-abuse rules (typically the PPT), it may be the case that arrangements entered into prior to the MLI operating (and which are currently resulting in treaty benefits) may cease to be eligible for such benefits once the MLI applies. It is therefore critical for multinational enterprises to understand how the MLI will impact their cross-border arrangements.

In the future, the improved MAP and (where applicable) mandatory binding arbitration provisions should provide taxpayers with greater dispute resolution mechanisms which may be a means of providing greater certainty.

Table 1: Who's in who's out (status as at 23 July 2018)

Australia			Treaty partners		
No	Treaty partners	CTA?	Australia not listed as a CTA by	MLI not signed by	MLI entry into force
1	Argentina	✓	-	-	-
2	Austria	✓	Austria	-	1/07/2018
3	Belgium	✓	-	-	-
4	Canada	✓	-	-	-
5	Chile	✓	-	-	-
6	China	✓	-	-	-
7	Czech Republic	✓	-	-	-
8	Denmark	✓	-	-	-
9	Fiji	✓	-	-	-
10	Finland	✓	-	-	-
11	France	✓	-	-	-
12	Germany	No ¹	-	-	-
13	Hungary	✓	-	-	-
14	India	✓	-	-	-
15	Indonesia	✓	-	-	-
16	Ireland	✓	-	-	-
17	Italy	✓	-	-	-
18	Japan	✓	-	-	-
19	Kiribati	✓	-	Kiribati	-
20	Korea	✓	Korea	-	-

¹ Not listed as a CTA by Australia as it complies with the OECD's BEPS treaty proposals

21	Malaysia	✓	-	-	-
22	Malta	✓	-	-	-
23	Mexico	✓	-	-	-
24	Netherlands	✓	-	-	-
25	New Zealand	✓	-	-	1/10/2018
26	Norway	✓	-	-	-
27	Papua New Guinea	✓	-	PNG	-
28	Philippines	✓	-	Philippines	-
29	Poland	✓	-	-	1/07/2018
30	Romania	✓	-	-	-
31	Russian Federation	✓	-	-	-
32	Singapore	✓	-	-	-
33	Slovak Republic	✓	-	-	-
34	South Africa	✓	-	-	-
35	Spain	✓	-	-	-
36	Sri Lanka	✓	-	Sri Lanka	-
37	Sweden	✓	Sweden	-	1/10/2018
38	Switzerland	✓	Switzerland	-	-
39	Taiwan	✓	-	Taiwan	-
40	Thailand	✓	-	Thailand ²	-
41	Turkey	✓	-	-	-
42	United Kingdom	✓	-	-	1/10/2018
43	United States	✓	-	US	-
44	Vietnam	✓	-	Vietnam	-
Total	44	43	4	8	
Out of Australia's 44 bilateral tax treaties, 31 CTAs should, in time, be modified by the MLI					

² Thailand has now expressed its intent to sign the MLI

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