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International tax alert

BEPS Action 15: Developing a multilateral instrument to modify bilateral tax treaties

September 22, 2014

On September 16, 2014, ahead of the G20 Finance Ministers' meeting on September 20-21, 2014, the OECD published seven papers as a first tranche of deliverables under the base erosion and profit shifting (BEPS) project, including a report on Action 15: Developing a multilateral instrument to modify bilateral tax treaties. The OECD will be continuing its work on the remainder of the 15 BEPS Actions throughout 2015. The G20 and OECD member governments intend that the recommendations under each of the Actions will form a comprehensive and cohesive approach to the international tax framework, through domestic legislation and international principles under the model tax treaty and transfer pricing guidelines. As a result, the proposed solutions in the first seven papers, while agreed to, are not yet finalized and may be affected by decisions and future work on BEPS in 2015.

Deloitte's comments

This report confirms that a multilateral instrument is feasible from a legal and a practical perspective, and is the most effective way of implementing treaty outcomes under the BEPS project. The implementation process will not be without technical issues, such as preserving national sovereignty over bilateral treaties, and ensuring transparency and clarity as well as compatibility with other bilateral and multilateral obligations.

Business will welcome an efficient multilateral dispute resolution mechanism (a multilateral mutual agreement procedure) that results in an outcome binding on the tax authorities within a reasonable timeframe.

Multilateral instrument proposals

The OECD recognizes that updating more than 3,000 existing bilateral tax treaties (varying widely in their details) for any BEPS recommendations would require significant time and resources.

The report contains an analysis of the benefits, feasibility and tax and public international law issues relating to the development of a multilateral instrument, which would have the same effect as simultaneous renegotiation of the bilateral treaties that are currently in effect. The report concludes that such a multilateral instrument is both desirable and feasible, and that a mandate should be quickly developed for the instrument to be implemented.

The report concludes that the multilateral instrument will exist alongside current bilateral tax treaties. This option is preferred over others such as an instrument that replaces existing tax treaties or one that directly modifies existing treaties. The main advantages of this approach are that (i) it ensures that the multilateral instrument is

highly targeted; (ii) it allows existing bilateral treaties to be modified in a synchronised way; and (iii) it allows BEPS abuses to be swiftly curtailed and enables governments to achieve their international tax policy goals without violating existing bilateral treaties.

A number of areas in which a multilateral instrument may be useful are identified in the report. They include addressing abuse in cases of dual residence, transparent entities (hybrids), and “triangular cases” of payments to permanent establishments from third countries. The report suggests that permanent establishment definition amendments will require flexibility given existing country practices, but that boundaries will be required to ensure a consistent and coherent outcome.

Notably, the report identifies that the multilateral instrument could consider provision for multilateral mutual agreement procedures to allow for dispute resolution between several countries at once. This would assist in particular with complex transfer pricing matters, and may be of significance in relation to the likely increase in the use of the transactional profit split method for cases involving, for example, intangibles. In addition, the report notes that the multilateral instrument could be used to assist with confidentiality issues in relation to the sharing mechanism for country-by-country reporting and for the allocation of interest deductions.

A key theme of the report is the importance of respecting sovereign autonomy in tax matters - countries will only be bound by amendments to which they have consented. The report contains an annex that presents a range of possible mechanisms for the development of a multilateral instrument, drawing on examples that have been successfully implemented in other areas of international law.

Timetable and next steps

The report concludes that the multilateral instrument should be negotiated through an international conference of OECD, G20 and other interested countries. The objective will be to implement the BEPS outputs related to treaties and also to recommend possible mechanisms for implementation of future changes to the model tax conventions. It is recognized that the treaty-based BEPS actions must be completed before the substantive components of the multilateral instrument can be finalized, but the report recommends that the international conference begin its work in early 2015.

Deloitte resources

The upcoming Deloitte Dbriefs webcast will include a discussion of some of the recent OECD actions. We welcome you to [register](#).

In addition please refer to the Deloitte [BEPS site](#) which has useful resources and updates.

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