

## BEPS Action 6: Preventing treaty abuse

On 21 November the OECD, as part of its work on the Action Plan to address Base Erosion and Profit Shifting ('BEPS'), released a follow-up Discussion Draft on Action 6 in relation to preventing treaty abuse.

### Deloitte Comments and Business Next Steps

This follow-up Discussion Draft invites comments on a number of areas, which were either not covered or fully covered in the September paper, and is not restricted to the application of the limitation on benefits (LOB) rule to collective investment vehicles (CIVs).

This Discussion Draft provides potentially affected businesses with the opportunity to comment on how greater certainty could be provided through the model treaty and/ or commentary in these open areas.

### Issues to be addressed as part of the follow-up work: Limitation on benefits

Comments are invited on the following in respect of the LOB rule:

**Widely held CIVs:** whether the recommendations of the 2010 OECD Report, 'The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles' are adequate or whether improvements could be made.

**Non-widely held CIVs:** This could include, for example, sovereign wealth, alternative and private equity funds. These funds may not qualify as residents and, even if they do, may fail to meet the current draft of the LOB rule.

**Pensions:** The residence of pension funds, the exemption of income where both States generally exempt from tax the investment income of domestic pensions, the 50% ownership test and the definition of pension funds.

**Competent authority discretionary relief:** The factors that competent authorities should take into account when determining whether relief should be available.

**Derivative benefit provisions/ equivalent beneficiaries:** This is tied in with other BEPS Actions. Comments are invited on possible ways in which a derivative benefits test could be included to allow intermediate companies used for valid commercial reasons to access treaty benefits.

**Timing issues:** In particular how to treat a company which becomes or ceases to be publicly-listed during a taxable period.

**Small countries with non-substantial stock exchanges:** Modifying the publicly-listed provision to reflect the fact that listings may not be sought on smaller local markets whilst ensuring that the entity has sufficient nexus to warrant the application of the treaty.

**Interpretation of the active business provision:** including head office operations, and the combination of different activities (for example, manufacturing and investment) carried on in the same country.

### Issues to be addressed as part of the follow-up work: Principal purposes test

The Discussion Draft identifies a number of possible issues with the principal purposes test (PPT):

**Establishing an administrative process to ensure that the PPT is only applied after senior approval:** There is a recognition that general anti-abuse rules found in domestic law may be subject to approval by a committee of

senior officials. The commentary on the PPT could include the suggestion that countries consider establishing a similar process for applying the PPT.

**Arbitration:** The majority of countries support the application of the PPT being a matter that is suitable for arbitration.

Comments are invited on:

#### **Extending the list of examples in the PPT commentary**

**Alignment with LOB commentary:** In particular, in respect of the competent authority discretionary LOB rule which also considers purpose.

**Availability of discretionary relief:** As currently drafted, if the PPT applies, the relevant income would be taxable under domestic law without any treaty benefits. In some cases, however, it may be appropriate to provide some form of treaty relief. The example given is a transaction which transforms dividends into a capital gain on shares. Tax authorities may consider it appropriate to apply the relief provided under the dividends article.

**The alternative 'conduit-PPT rule':** This is the alternative to the PPT which States may use to address treaty-shopping conduit strategies that would not be caught by the LOB rule. The commentary could include possible examples, which could be taken from the exchange of notes between the United Kingdom and United States in respect of the conduit arrangement rules in the 2001 treaty.

#### **Other issues to be addressed as part of the follow-up work**

**New treaty tie-breaker rule:** The possible encouragement of competent authorities to address as quickly as possible requests that will be made under the new rule.

**Triangulation/ permanent establishment in third state:** Comments are invited on whether the rule should be extended to situations beyond where the profits of the permanent establishment are exempt, and whether the exemptions from the rule are broad enough.

#### **Timetable**

Comments should be sent to the OECD by 9 January 2015 and there is a public consultation meeting on 22 January 2015.

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