

Luxembourg Tax Alert

OECD BEPS Multilateral Convention: Luxembourg's choices published

9 June 2017

The OECD BEPS package contains tax-treaty related measures addressing gaps and mismatches in the application of tax rules in an international context. The implementation of these measures on tax treaties one-by-one could take decades to finalize. In order to avoid this situation, the Multilateral Convention to Implement Tax Treaty-Related Measures to Prevent Base Erosion and Profit Shifting (hereafter referred to as “the Multilateral Convention”) enables states to update their tax treaties consistently and in a reasonable timeframe.

Last Wednesday, Luxembourg, together with 67 other states, signed this Multilateral Convention. Apart from those signatories, nine other jurisdictions formally expressed their intent to sign, meaning [77 jurisdictions](#) in total (and about 90 expected by the end of the year).

The Multilateral Convention provides various choices, so that it could be applied to multiple, sometimes considerably different, tax treaties and tax systems, which is why the convention contains two groups of provisions.

In the first place, states willing to implement the Multilateral Convention must comply with its minimum standards, which cover measures to counter treaty abuse and to improve dispute resolution.

Apart from these provisions, the Multilateral Convention lists multiple others, which the countries can, but are not obliged to, choose to apply to all, some, or none of their double tax treaties. Luxembourg wishes to apply provisions in connection with transparent entities (Article 3), the application of methods for eliminating double taxation (Article 5), artificial avoidance of permanent establishment status through specific activity exemptions (Article 13), and the arbitration procedure.

Please find below an overview of [Luxembourg's choices](#).

Minimum standards

Like all states willing to implement the Multilateral Convention, Luxembourg must comply with the minimum standards of this convention, except where it is possible to apply alternative ways to meet the standards (for example, the adoption of a detailed Limitations of Benefits provision with rules to address conduit financing structures).

The minimum standards of the convention covers different aspects. The first one introduces a new preamble into the tax treaties to ensure they do not lead to double non-taxation. The second tackles situations where transactions are executed for obtaining a treaty benefit. The third is especially favorable for the taxpayers as it aims to improving dispute resolution. They are described in more detail below.

First of all, Luxembourg will include the preamble wording as per Article 6 of the Multilateral Convention in its double tax treaties, stating that the states intend to *eliminate double taxation with respect to the taxes covered by [the treaty] without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance*. This preamble wording is already included in the tax treaty between Luxembourg and Senegal (not yet in force).

Article 6 also proposes additional preamble wording stating that both jurisdictions desire *“to further develop their economic relationship and to enhance their co-operation in tax matters.”* Luxembourg chose to include this additional preamble text in its tax treaties.

Second, it will tackle cases of treaty abuse by introducing a general anti-avoidance rule—the Principal Purpose Test (PPT)—from Article 7 of the Multilateral Convention. It denies granting a benefit under a tax treaty if obtaining this benefit could have been one of the principal purposes of the arrangement or transaction that resulted in that benefit, unless in the circumstances of the case, the object and purpose of the relevant provisions allow for it. This provision is already included in the tax treaty between Luxembourg and Senegal (not yet in force).

Under Article 7, countries can choose to apply the Simplified Limitation on Benefits (S-LOB) provision in addition to the PPT, which puts further limitations on granting benefits only to specified qualified persons. For this additional provision there are three choices: a state can either agree to apply it for the tax treaties with parties that chose it, or to permit this provision to be applied unilaterally by those parties, or to disallow its application for its tax treaties. Luxembourg disallowed the application of the S-LOB provision for its tax treaties (therefore the other party to the Multilateral Convention cannot apply it unilaterally).

In addition to the PPT clause, Luxembourg also chose the optional provision that requires the state applying the PPT to consult with the other state before rejecting a taxpayer's request for treaty benefits (the PPT consultation in favor of the taxpayer).

The last minimum standard provisions are Articles 16 and 17, respectively covering the mutual agreement procedure and the corresponding adjustments. Opting out of those provisions is allowed only if the country proves that it satisfies the minimum standard in a different manner.

The mutual agreement procedure grants every taxpayer, reasonably assuming that in his case the provisions of a treaty are not complied with (or might not be in the future), the right to complain with any of the parties to that treaty. This procedure can be launched if the authority considers such a complaint to be justified, but cannot solve the issue by itself. It foresees resolving difficulties and doubts as to the interpretation of the double tax treaty, as well as consultation on cases outside of its scope. This provision should result in a better complaint procedure on treaty implementation in specific cases.

Additional Luxembourg choices

Apart from the above-mentioned clauses, the parties to the Multilateral Convention have a choice of multiple other provisions reflecting various BEPS actions. Luxembourg wishes to apply provisions in connection with transparent entities (Article 3), the application of methods for eliminating double taxation (Article 5), artificial avoidance of permanent establishment status through specific activity exemptions (Article 13), and the arbitration procedure.

Article 3 of the Multilateral Convention, concentrating on transparent entities, states that income derived by or through a wholly or partly fiscally transparent entity or arrangement shall be considered income of a resident, but only to the extent that the income is treated, for purposes of taxation by that state, as the income of a resident of that state. Provisions of treaties that exempt income from tax or provide for credit or deduction in the same state shall not apply, where the sole reason for the benefit is that such income is also income of (a) resident(s) of the other party to the treaty.

For Article 5 of the Multilateral Convention, which provides three different options for the elimination of double taxation, Luxembourg decided to apply option A. It states that the residence state shall not apply the exemption method where the source state already applied the treaty provisions to exempt concerned income or capital from tax. This article allows for unilateral application, which means that even if the other parties do not choose it, it will still apply with respect to Luxembourg residents, unless the other party specifically makes a reservation for it not to apply. The Luxembourg also decided to not allow the other state to apply option C (full credit method) to nominated tax treaties.

The third provision chosen by Luxembourg relates to the permanent establishment status. Various optional articles of the Multilateral Convention address this point. Luxembourg selected article 13, option B, tackling the artificial avoidance of permanent establishment status through some specific activity exemptions, but without the adoption of the anti-fragmentation rule. Under this option, apart from those already specifically excluded in the tax treaty, the list of exceptions will also include maintenance of a fixed place of business for carrying on an activity of a preparatory or auxiliary character, as well as any combination of these two first types, provided that the overall resulting activity will be of a preparatory or auxiliary character. This option will only apply to the tax treaties for which the other party also opted for its application (symmetrical application).

Finally, Luxembourg decided to also implement the arbitration procedure (part VI of the Multilateral Convention), which can be launched if the mutual agreement procedure did not resolve the issue at hand within two years.

As mentioned by the OECD, the lists of choices provided at the time of signature for the signatories may be subject to change and the definitive position for each jurisdiction will be provided upon the deposit of its instrument of ratification, acceptance, or approval of the Multilateral Convention.

The changes will apply to a nominated double tax treaty if both parties to this tax treaty ratify the Multilateral Convention, as well as agree to adopt their choices in the same way, unless the concerned article allows, under conditions, for an asymmetrical adoption. Since several procedural steps still need to be completed, it seems unlikely that the changes will be applicable before 1 January 2019.

Your contacts

Raymond Krawczykowski

Partner | Tax Leader

Tel: +352 45145 2500

rkrawczykowski@deloitte.lu

Bernard David

Partner - International Tax Leader

Tel: +352 45145 2799

bdavid@deloitte.lu

François Guilloteau

Partner - International Tax

Tel: +352 45145 2577

fguilloteau@deloitte.lu

Deloitte Luxembourg

560, rue de Neudorf

L-2220 Luxembourg

Tel: +352 451 451

Fax: +352 451 452 401

www.deloitte.lu

Deloitte is a multidisciplinary service organisation which is subject to certain regulatory and professional restrictions on the types of services we can provide to our clients, particularly where an audit relationship exists, as independence issues and other conflicts of interest may arise. Any services we commit to deliver to you will comply fully with applicable restrictions.

Due to the constant changes and amendments to Luxembourg legislation, Deloitte cannot assume any liability for the content of this leaflet. It shall only serve as general information and shall not replace the need to consult your Deloitte advisor.

About Deloitte Touche Tohmatsu Limited:

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/lu/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu Limited and its member firms.

Deloitte provides audit, tax, consulting and financial advisory services to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 150 countries, Deloitte brings world-class capabilities and deep local expertise to help clients succeed wherever they operate. Deloitte has in the region of 200,000 professionals, all committed to becoming the standard of excellence.

© 2017 Deloitte General Services

Designed and produced by MarCom at Deloitte Luxembourg