TAX EXECUTIVES INSTITUTE, INC.

29 June 2016

Centre for Tax Policy and Administration
Organisation for Economic Co-Operation
and Development
Paris, France

Via email: multilateralinstrument@oecd.org

RE: Development of a Multilateral Instrument to Implement the Tax Treaty Related BEPS Measures

To Whom It May Concern:

The Organisation for Economic Co-Operation and Development (OECD) published final reports pursuant to its base erosion and profit shifting (BEPS) project on 5 October 2015. The reports were the culmination of the OECD's *Action Plan on Base Erosion and Profit Shifting* (hereinafter the Plan) published in 2013. The Plan set forth 15 actions the OECD would undertake to address a series of issues that contribute to the perception of tax bases being eroded or profits shifted improperly. Included in the October 2015 final reports was the report under Action 15 of the Plan, *Developing a Multilateral Instrument to Modify Bilateral Tax Treaties*. The OECD issued a public discussion draft under Action 15 (the Discussion Draft) on 31 May 2016, requesting comments on technical issues related to development of the Multilateral Instrument (the Instrument).

I am pleased to respond to the OECD's request for comments on behalf of Tax Executives Institute, Inc. (TEI). TEI also requests the opportunity to speak in support of these comments at the public consultation to be held on 7 July 2016 in Paris.

TEI Background

TEI was founded in 1944 to serve the needs of business tax professionals. Today, the organization has 56 chapters in Europe, North and South America, and Asia. As the preeminent association of in-house tax professionals worldwide, TEI has a significant interest in promoting tax policy, as well as the fair and efficient administration of the tax laws, at all levels of

government. Our nearly 7,000 individual members represent over 2,800 of the leading companies in the world.[1]

General Comments

TEI commends the OECD for providing the opportunity to comment on technical issues related to the development of the Instrument, which ordinarily would be the subject of confidential negotiations solely between potential treaty partners. In particular, TEI appreciates the OECD's request for comments regarding "the approach to be taken in developing the optional provision on mandatory binding MAP arbitration . . . ."[2] As noted in one of TEI's first letters to the OECD regarding the BEPS project, the multilateral instrument under Action 15 and the efforts to improve the mutual agreement procedure (MAP) under Action 14 – including the possibility of mandatory binding arbitration – are the two BEPS action items most critical to multinational enterprises.[3] This remains the case more than two years later and TEI urges the OECD and the 96 countries participating in the Ad Hoc Group to continue their work on a flexible Instrument promoting uniformity in international tax treaties and their underlying policy.

Regrettably, Actions 14 and 15 were left to the end of the BEPS project before they received the OECD's and participating states' full attention. While TEI appreciates aspects of dispute resolution under Action 14 have been determined to be minimum standards, excluding mandatory binding arbitration from the standards is a grave disappointment. Business stakeholders consistently warned throughout the BEPS project of the massive increase in MAP cases likely to arise from the substantial changes to the international tax regime resulting from the project. Significant improvements to the MAP process are needed in the business community's view to efficiently and effectively process the anticipated increase in MAP cases in a timely manner. This would help alleviate the double-taxation sure to arise from the anti-BEPS measures and provide multilateral enterprises with certainty and finality in their cross-border business operations.

The primary key to an effective and improved MAP process was (and is) a mandatory binding arbitration procedure to motivate competent authorities to reach a decision on a MAP case and, should they fail, quickly resolving the case under arbitration. Just as important, the prospect of arbitration to settle MAP cases would likely prevent many MAP disputes from arising in the first place as tax authorities who may be tempted to make unprincipled or aggressive adjustments refrain from doing so, knowing an arbitrator would likely adopt the treaty partner's position in arbitration. While we are encouraged by the number of countries declaring their

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[1] TEI is a corporation organized in the United States under the Not-For-Profit Corporation Law of the State of New York. TEI is exempt from U.S. Federal Income Tax under section 501(c)(6) of the U.S. Internal Revenue Code of 1986 (as amended).

[2] Discussion Draft, page 3.

[3] *See* TEI Letter to OECD, 16 October 2013, available at http://www.tei.org/news/Pages/Further-Comments-on-OECD-BEPS-Action-Plan.aspx.

commitment to mandatory binding MAP arbitration, it is unfortunate such arbitration will not be more widely adopted as a result of the BEPS project.

Responses to Specific Requests for Input in the Discussion Draft

The Discussion Draft requests comments on technical issues arising from implementing the treaty-related BEPS measures in the context of the existing network of bilateral tax treaties. Comments were requested in four areas, which are discussed below.

Mandatory Binding MAP Arbitration

The Discussion Draft requests input regarding

> The approach to be taken in developing the optional provision on mandatory binding MAP arbitration, taking into account that it would need to serve the needs of the countries that have already committed to implement mandatory binding arbitration, as well as countries that are considering committing in the future.[4]

With respect to countries that have already committed to mandatory binding arbitration, TEI's recommended flexible approach (discussed below) would permit such countries to continue their current arbitration process if it is already in place and available to taxpayers. Further, if they have committed to such arbitration but have not implemented the process, TEI recommends the OECD encourage such countries to adopt the approach reflected in the Instrument, which could include alternative forms of arbitration as options for treaty partners to select from.

TEI recommends for the arbitration provision itself the Instrument include a specific process (or processes) for mandatory binding arbitration coming into force upon ratification of the Instrument by two treaty partners. That is, the Instrument should include sufficient details regarding the arbitration process so taxpayers may avail themselves of the process without waiting for the respective competent authorities to agree on, *e.g.*, the type of arbitration to use, the schedule, deadlines, *etc*. Alternatively, the arbitration provision could take effect one year after ratification of the Instrument by bilateral treaty partners to provide competent authorities time to decide upon further details while also not permitting the design process to continue indefinitely.

The Instrument in this regard should also include a specified time limit for treaty partners to reach agreement on a MAP case, after which it would be submitted to arbitration. Taxpayers in many MAP cases will have paid the assessed tax making the associated cash unavailable for regular business operations until the case is resolved. Depending on the size of the dispute at issue this may present significant cash flow and other operational issues for taxpayers. TEI

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4 Discussion Draft, page 3.

recommends to the OECD the two-year time period for competent authorities in the U.S.-Canada treaty to settle a MAP case before it moves to arbitration as an appropriate time limit. Similarly, TEI recommends the Instrument include a deadline for completing the arbitration process of no more than 18 months.

With respect to a specific type of arbitration, TEI recommends the Instrument incorporate so-called "baseball" or "last best offer" arbitration. This type of arbitration is already in use by the United States[5] and has proven to effectively motivate treaty partners to settle MAP cases before they reach arbitration. Baseball arbitration type should also be briefer and less expensive for taxpayers and competent authorities than reasoned decision/independent opinion arbitration. Nevertheless, in TEI's view it would be preferable to have some kind of mandatory binding MAP arbitration included in a tax treaty rather than none. Thus, if there is disagreement among the states wishing to include arbitration in their treaties over the type of arbitration to use, perhaps the best approach is to provide for both baseball and reasoned decision arbitration in the Instrument and let treaty partners choose the one that fits their particular situation.

TEI recommends with respect to the scope of MAP cases eligible for arbitration all such cases be eligible. There is no reason why a particular category of MAP cases should be excluded from mandatory binding arbitration as all such cases have the potential to result in double taxation. Should it be a matter of scarce competent authority resources, then, at a minimum, all transfer pricing cases should be eligible for arbitration, and then other categories can be considered depending on the resources of the two competent authorities. However, the OECD should state the preferred option for mandatory binding arbitration is all MAP cases shall be eligible.

Technical Issues in Modifying or Superseding Bilateral Tax Treaties and Tools to Assist Understanding Such Changes

The Discussion Draft also requests input regarding

> Technical issues that should be taken into account in adapting the BEPS measures to modify or supersede existing provisions of bilateral tax treaties that may vary from the OECD model, including:
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> - Existing provision or types of provisions that serve the same purpose as the BEPS measures and that would need to be replaced

[5] "Baseball" arbitration is also provided for under Article 25 of the 2016 United States Model Income Tax Convention, which is available at https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-US%20Model-2016.pdf.

- Existing provisions or types of provisions that are similar to BEPS measures but that would need to be retained[6]

A separate request for input asks for comments on "[t]he types of guidance and practical tools that would be most useful to taxpayers in understanding the application of the multilateral instrument to existing tax treaties."[7]

Many of the issues related to these two requests for input were the subject of a panel at the recent OECD International Tax Conference held in Washington, DC, on 7 June 2016 (the Panel). The Panel provided additional background and context on the Discussion Draft, including specific questions and concerns of the OECD and Ad Hoc Group. These included the degree of flexibility countries will have to adopt some provisions of the Instrument and not others, whether all countries must agree to the BEPS project's minimum standards as a condition to signing the Instrument, how to implement specific provisions such as the saving clause, and how to account for current bilateral treaty provisions meeting or exceeding a BEPS minimum standard, among others.

The overarching theme of these concerns and questions is the need to determine to what, exactly, has each signatory agreed. Secondarily, they implicate the flexibility of the Instrument, i.e., will the Instrument look like a single protocol applicable to all bilateral treaties of all signatories, will it act as an aggregate of various amendments to individual bilateral treaties at the discretion of the original parties to those treaties, or will it fall somewhere in between?

TEI appreciates the OECD's concern of undermining the BEPS project and possibly future OECD work if countries were permitted to sign the Instrument without also agreeing to the project's minimum standards. However, requiring each country's agreement to each minimum standard would likely limit participation in the Instrument. For example, it would exclude countries who wish to adopt an Instrument provision that is not a minimum standard (*e.g.*, certain changes to the permanent establishment (PE) definition under BEPS Action 7) but do not want to adopt all of the minimum standards. A country agreeing to even a single aspect of the Instrument would promote one of the underlying goals of the BEPS project: to coordinate tax authority responses to base erosion and profit shifting concerns. While this might turn the Instrument into an aggregation of bilateral tax treaty amendments, this is its practical effect in any event even if the Instrument required a certain level of participation – whether adopting the minimum standards or otherwise – for countries to join the Instrument.

That said, TEI recommends all signatories to the Instrument be required to adopt the Action 14 minimum standard. In an ideal world this standard would include the adoption of mandatory binding MAP arbitration, as discussed above. The absence of an arbitration provision, however, vastly increases the importance to the business community of the minimum

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6 Discussion Draft, page 3.

7 *Id*.

standards that *were* adopted under Action 14 under the BEPS project. Requiring signatories to the Instrument to adopt the Action 14 minimum standards would show that while the BEPS project was overwhelmingly concerned with the elimination of double non-taxation and other base erosion and profit shifting concerns, the OECD is still cognizant of, and interested in addressing, double taxation, in accord with its historical role in tax matters. Action 14 is the one action of the BEPS project that businesses can wholeheartedly support, and its inclusion as a mandatory part of the Instrument would assuage some of the business community's concerns regarding the overall impact of the project.

Beyond the Action 14 minimum standards, TEI recommends that states signing the Instrument be permitted to choose which of the remaining treaty-related measures they are willing to adopt. This approach, in addition to promoting uniformity in the international tax arena, would also serve the purpose of the Instrument to quickly adopt the treaty-related BEPS measures without the need for countries to renegotiate several thousand bilateral tax treaties. Indeed, the BEPS project has already substantially accomplished the most difficult part of bilateral treaty negotiations by achieving consensus on the underlying treaty language (with the exception of the provision on arbitration). Thus, for example, the final report on Action 7 sets forth the modified treaty provisions regarding the definition of a PE and countries merely need to have such language replace the relevant PE article in their tax treaties without any further negotiation with its treaty partners. TEI therefore recommends countries be permitted to sign the Instrument and choose which treaty-related BEPS project measures they wish to incorporate into their bilateral tax treaties. To assist this process, TEI recommends the OECD set forth in the body of the Instrument the clear and non-negotiable language with respect to each treaty-related BEPS provision that a party could sign and implement.

In addition, TEI recommends countries signing the Instrument be permitted to choose the treaty partners and relevant tax treaties to which they would apply the BEPS provisions. That is, countries should be permitted to apply, for example, the modified PE language of Action 7 to some of their treaty partners but not others. Countries may wish to do so for a variety of reasons, including the historic relationship with the partner, the partner's consistency in implementing the treaty, the partner's sophistication in administering and interpreting the treaty, among other things. Again, a primary goal should be to encourage as many countries to adopt as many of the treaty-related BEPS measures as possible in the interest in promoting uniformity in treaty policy around the world. Thus, in our view it is better for countries to agree to modify treaty language to be consistent with the new OECD standard in some cases even if not others, rather than refraining from signing the Instrument at all or refraining from signing on to certain provisions of the Instrument with all treaty partners because of one or two unreliable treaty partners.

Should the OECD find this approach too flexible, and perhaps excessively complicated or unmanageable, an alternative would be to permit countries to sign the Instrument and then choose which of the treaty related measures they would apply on a measure-by-measure basis.

Thus, for example, a country could choose to apply the new PE definition to all of its bilateral tax treaties, but decline to implement another treaty measure, and still be permitted to sign the Instrument.

With respect to determining to what, exactly, countries signing the Instrument have agreed, TEI appreciates this may be a complicated task made more difficult by the flexibility we recommend above. That said, a way to simplify tracking which country has agreed to what provision with what treaty partner is through the use of a matrix (or table) for each country. An individual country's matrix could list its treaty partners down the left side and then the BEPS treaty-related measures along the top. Assuming the precise language of the BEPS treaty-related measures are set forth in the Instrument, in the alternative where necessary, they could then be numbered or otherwise given a short-hand label for use in the matrix as a cross-reference to the relevant text. Upon signing, each country could submit its matrix listing the relevant provisions and treaties it was willing to agree to modify using the Instrument. The same matrix could then be used to track when a particular provision is ratified (if necessary). We have attached a simple example of such a matrix in the appendix.

We believe this approach could be helpful because, while the thousands of bilateral tax treaties are far from uniform, they generally contain the same basic components, such as a definition of a PE and resident, the taxation of dividends and interest, provisions for dispute resolution, among others. Treaties based upon the U.N. and OECD models generally include these and other components. Thus, it should in most cases be clear what provisions have been replaced or amended, even though they do not appear in the same order or have identical language from one treaty to another. In addition, we believe this approach can minimize or eliminate the need to cross reference the particular treaty article and paragraph being replaced in each treaty.

This leaves some open questions. First, as noted in the OECD's request for input, is what to do about existing treaty provisions serving the same or similar purpose as those in the Instrument but need to be replaced, retained or modified. The Panel stated "compatibility clauses" would be drafted to describe in detail what approach is intended to be used in specific circumstances. Other than for existing provisions needing to be modified, the flexible approach described above should be simple to implement for provisions to be retained or replaced. Should provisions of a particular treaty be retained (because they satisfy the purpose of the relevant provision in the Instrument), then the treaty partners would omit agreeing to that portion of the Instrument. On the other hand, an existing provision needing to be replaced would simply be removed by the two treaty partners agreeing to the relevant Instrument provision.

The more difficult case of existing provisions needing to be modified, rather than replaced, remains. As a threshold matter it is unclear why such provisions could not simply be replaced rather than modified. In other cases, such as treaties that define a services PE, then perhaps the OECD's suggested compatibility clause approach is necessary, although in TEI's

view the Instrument should not serve as a vehicle to introduce unique or one off treaty clauses not developed as part of the BEPS project. In any event, the flexibility of TEI's suggested approach should reduce the need for compatibility clauses and countries could agree to append short explanations for provisions that are to be modified upon signing.

A second open question, as mentioned during the Panel, is interweaving a "saving clause" along with the exceptions thereto into existing treaties. This is admittedly a difficult task to coordinate through the Instrument because exceptions to the saving clause are typically implemented via cross reference to other provisions within a single bilateral tax treaty. Preferably in this case bilateral treaty partners could simply signal their willingness to employ a saving clause with exceptions in their treaty and then work out the specific exceptions on their own, perhaps within a time frame specified in the Instrument. Alternatively, the signatories could include their own list of cross references for each treaty to include a saving clause.

Consistent Application and Interpretation

The last request for input is for recommendations of "[m]echanisms that could be used to ensure consistent application and interpretation of the provisions of the multilateral instrument." Consistent application and interpretation of the tax law is perhaps the tax administrator's most difficult task. TEI's members have substantial experience with personnel of the same tax authority taking varying positions with respect to the same tax provisions depending on the circumstances. Thus, persuading multiple tax authorities to agree on consistent positions with respect to treaty provisions is a monumental undertaking, even if the underlying provisions are identically worded.

The OECD has already taken one step toward this objective through the development of the detailed commentary during the BEPS project. The Instrument should make clear that such commentary is the relevant commentary to reference when interpreting the Instrument's provisions and each signatory should agree to so use the new commentary. The Instrument should also make clear that the updated commentary supersedes the prior commentary, which is now out of date and should not be used for interpretation.

Further, the Instrument should specify that the modified provisions and relevant commentary agreed to by the signatories are effective only upon final ratification by the respective treaty partners to each bilateral tax treaty modified by the Instrument, and tax authorities should only apply the new treaty wording and commentary prospectively. Moreover, a country that has adopted a "non-standard" interpretation of common treaty language should not be permitted to continue to use such an interpretation when joining the Instrument. For example, if a country has a non-standard interpretation of the meaning of a "fixed place of business" under the current PE definition, it should not be permitted to adopt the new PE definition while maintaining the non-standard interpretation.

Finally, the OECD should facilitate a peer review process for treaty application and interpretation beyond what it has already proposed. This would provide pressure for countries to, at least, adopt sensible and firmly grounded interpretive positions, even if they are not always consistent across the board. Publishing any such peer review reports would provide additional incentive for countries to act reasonably when initiating an adjustment. Ultimately, however, consistent interpretation and application will be determined by the training and professionalism of the tax authorities administering the provisions, along with the level of resources provided to carry out their duties.

Conclusion

TEI appreciates the opportunity to comment on the Discussion Draft regarding the development of a multilateral instrument. As noted above, TEI requests the opportunity to speak in support of these comments at the Public Consultation on the Discussion Draft to be held on 7 July 2016 in Paris.

These comments were prepared under the aegis of TEI's European Direct Tax Committee, whose Chair is Nick Hasenoehrl. If you have any questions about the submission, please contact Mr. Hasenoehrl at +41 786 88 3772, nickhasen@sbcglobal.net, or Benjamin R. Shreck of the Institute's legal staff, at +1 202 638 5601, bshreck@tei.org.

Sincerely yours,
TAX EXECUTIVES INSTITUTE, INC.

C.N. Macfarlane

C.N. (Sandy) Macfarlane
International President

Appendix

Illustrative example of a multilateral instrument signatory matrix.

BEPS MULTILATERAL INSTRUMENT SIGNING MATRIX:
UNITED STATES

Provision	**Action 6**		**Action 7**		**Action 14**	
Alternatives	LOB	Anti-Abuse	Para 5(4)	Para 5(5)	"Baseball"	Reasoned Decision
Australia			X		X	
Canada			X[1]	X		
Germany			X	X	X	
UK						X

Key
X = Provision signed
= Ratification pending
= Ratified
= Ratification rejected
= Current provision in compliance with minimum standard or Instrument provision

[1] = Services PE provision in current Article 5 to continue in effect after ratification of the Instrument.