



Meijburg & Co
Tax Lawyers

Multilateral instrument

BEPS Action 15

The Multilateral Instrument ('MLI') is one of the key outcomes of the OECD's Base Erosion and Profit Shifting ('BEPS') project, which aims to prevent perceived international tax avoidance and improve coordination between tax authorities. The purpose of the MLI is to implement wide-ranging double tax treaty (DTT) changes without requiring each individual treaty to be renegotiated. DTTs are bilateral agreements that are designed to ensure companies operating in multiple jurisdictions do not pay tax twice on the same income.

Overview

On June 7, 2017, 68 countries gathered to formally sign the MLI. Ten other countries have signed since. The MLI will implement minimum standards to counter DTT abuse and to improve dispute resolution, while providing optionality to implement additional specific tax treaty policies.

Depending on when instruments of ratification are deposited, for some treaties the MLI could take effect as early as January 1, 2019.

The MLI aims to implement the following key BEPS Actions:

Action 2 – Hybrid mismatch arrangements
Introducing provisions dealing with:
—tax arbitrage resulting from hybrid entities or instruments;
—treaty entitlements of hybrid entities; and
—changing the residence tie-breaker for companies to a competent authority mechanism.

Action 6 – Treaty abuse
Introducing a Principal Purpose Test ('PPT') and/or Limitation of Benefits ('LOB') clause to prevent treaty benefits being granted in cases of "treaty shopping".

Action 7 – Avoidance of permanent establishments ('PEs')
Significantly extending the definition of a PE in relation to the "dependent agent" concept and "excluded activities".

Action 14 – Dispute Resolution
Developing minimum standards, best practice and monitoring processes to facilitate the resolution of treaty disputes, as well as a binding arbitration mechanism.



How will it work?

Some of the OECD recommendations implemented through the MLI are minimum standards, which means all OECD states must sign up to them. Others are optional, allowing countries to 'opt out' from applying them or to make reservations about certain aspects.

The MLI will apply to treaties between countries that have both chosen to apply the MLI to the relevant treaty and where any options they have chosen are compatible.

The MLI will not actually amend the text of double tax treaties but will work alongside them. Interpreting treaties will therefore be a complex process.

Who will it affect?



Multinational groups that are likely to be affected by the MLI include the following:



Groups who have structured their business in multiple jurisdictions and may therefore be benefitting from double tax treaties to minimize withholding tax exposures;



Groups who have structured their activities to avoid permanent establishments abroad or in the Netherlands;



Groups who have hybrid entities or hybrid instruments in their structure;



Groups that include entities for which there is a degree of uncertainty as to which jurisdiction has taxing rights;



Groups that are considering acquiring or disposing of international subsidiaries or expanding into international markets.

Case study

A company resident outside the European Union (A Co) sets up a regional holding company in the Netherlands (NL Holdco) to manage its investments in a number of European jurisdictions. NL is able to mitigate the withholding tax it suffers on dividends, interest and royalty payments by claiming a reduction or an exemption under DTTs between the Netherlands and the payer jurisdictions, as well as reducing the corporate income tax on, for example, dividends received under the Dutch participation exemption regime.

Under the anti-treaty abuse provisions of the MLI, tax authorities will examine – having regard to all relevant facts and circumstances – the reasons behind the decision to establish a holding company and for choosing the Netherlands as its location. If the tax authorities can reasonably conclude that the main reason for establishing a holding company and/or for using the Netherlands as its location was to take advantage of tax benefits, they may deny the benefits of the treaties concluded between the Netherlands and the investment jurisdictions. The group will need to clearly document the business reasons for and the background to the decision to set up NL Holdco as a regional company and what commercial benefits (e.g. significant costs savings, access to skilled labor with relevant knowledge and experience, etc.) it derived or expected to derive from the arrangement.

Next steps

It is important for multinational groups to identify which jurisdictions that are relevant for their operations have signed up for the MLI, which treaties will be affected and to what extent, as well as the relevant timelines for entry into force. Doing this will help them better understand the impact on current treaty benefits and answer questions such as:



Are there any exposures as a result of the changes? If so, does the exposure have a material impact on the group's tax profile?



Can anything be done to minimize the impact of the exposure? What options are available?



Given current trends, could the group's reputation be at risk as a result of its corporate structure?

How we can help?

Meijburg & Co has an experienced team of tax professionals who can provide clients with tailored services taking into account your company's operations and exposure. We also have access to the worldwide network of BEPS professionals from KPMG International member firms, who have experience with the OECD and local tax authorities and practical knowledge of all aspects of BEPS.

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