OECD releases report under BEPS Action 15 on feasibility of developing multilateral instrument to amend bilateral tax treaties

Executive summary

On 16 September 2014, the Organization for Economic Co-operation and Development (OECD) released a report on the feasibility of developing a multilateral instrument to amend bilateral tax treaties in connection with Action 15 of its Action Plan on Base Erosion and Profit Shifting (BEPS). The report titled Developing a Multilateral Instrument to Modify Bilateral Tax Treaties examines the desirability and feasibility of a multilateral instrument as a way to implement treaty-based measures developed under the other BEPS Actions. Drawing on an analysis from experts in public international law and taxation, the report concludes that a multilateral instrument is both desirable and feasible, citing facilitation of swifter implementation of such treaty measures and increasing the consistency of outcomes. The report recommends convening an International Conference in 2015 which should be open to all interested countries to develop, and negotiate the content of, the multilateral instrument. The mandate of the International Conference is proposed to be limited in time to two years and to be limited in scope by focusing on the treaty-related BEPS outputs once they are finalized.

Detailed discussion

General
On 16 September 2014, the OECD released a series of deliverables that address seven of the focus areas in its BEPS Action Plan. This EY Tax Alert discusses the report issued on Action 15: “Developing a Multilateral Instrument to Modify Bilateral Tax Treaties” (the Report).
Action 15 called for a report to “Analyse the tax and public international law issues related to the development of a multilateral instrument to enable jurisdictions that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties.” In the introduction, the Report states that the current network of over 3,000 bilateral tax treaties ensures broad consistency in cross-border tax rules, but that “gaps and frictions” have grown over time resulting for instance in amounts of income not being taxed in any jurisdiction. Due to the time required to renegotiate each treaty, the treaty network is not well-synchronized with treaty models, so that a change in treaty models would not satisfy the political imperative to address BEPS in a reasonable timeframe.

Desirability and feasibility of a multilateral instrument
The Report begins with an examination of the desirability and feasibility of a multilateral instrument.

It notes that a multilateral instrument facilitates swift implementation of the treaty-related BEPS outputs by avoiding the need to individually negotiate existing bilateral tax treaties. Furthermore, the Report indicates that such an instrument would allow developing countries that could otherwise have difficulties concluding or renegotiating treaties to fully benefit from the BEPS project. In addition, it is noted that a multilateral instrument can be an easier way to address multilateral issues, such as multilateral agreement procedures (MAP), than bilateral treaties. Finally, the Report states that it can increase the consistency and clarity of the tax treaty network, and it could also allow countries to provide assurance to each other regarding their determination to address BEPS simultaneously so that each of them would “feel comfortable moving ahead in tackling BEPS.”

For all these reasons, the Report considers that such an instrument is desirable but that, in order to create a level playing field, broad participation to the multilateral instrument needs to be achieved. The Report goes on to identify obstacles to a multilateral instrument from a technical (public international law and international tax law) and political perspectives and the solutions to address those obstacles.

First, in the choice between (i) a “self-standing instrument” that would wholly supersede existing treaties, (ii) an instrument that would merely operate as a set of protocols amending each of the existing bilateral treaties specifically, and (iii) an instrument that would coexist with bilateral treaties, only the third option appeared to preserve tax sovereignty and achieve an efficient outcome. Under that latter option, the instrument would amend a limited number of provisions commonly found in bilateral tax treaties and, where not already included in those treaties, would add new anti-BEPS measures. The instrument would be legally binding on the contracting parties, but would only govern the relationship between those that already have a bilateral tax treaty in place among themselves. However, the Report suggests that a multilateral dispute resolution mechanism could operate among all parties to the multilateral agreement.

Second, on the more technical challenges around, for example, the interaction with bilateral tax treaties, the Report derives solutions from numerous examples of multilateral treaties in areas other than tax. For instance, “compatibility” clauses to resolve a conflict with similar provisions in existing or even future bilateral treaties (giving priority to the multilateral instrument); an explanatory report providing interpretative guidance; different dates of entry into force for different provisions; mechanisms for expeditious amendment procedures in the future; and the use of official languages and unofficial translations. More importantly, the Report suggests that flexibility could be provided to tailor the extent of rights and obligations created by the multilateral treaty by the recourse to opt-out or opt-in mechanisms or leaving parties a choice between alternative provisions.
The Report thus concludes that a multilateral instrument also appears to be feasible.

**Scope of the multilateral instrument**

The Report lists some of the treaty-related measures to be developed in the BEPS project that are multilateral in nature and would be more effective if implemented by a multilateral instrument. These treaty-related measures include addressing multilateral mutual agreement procedure, dual resident structures, hybrid mismatch arrangements, triangular cases involving a permanent establishment (PE) in third states, and treaty abuse.

The Report suggests that some or all of the above could be part of a set of core provisions to which all parties to the multilateral instrument should adhere. Other outputs of the BEPS project that are more bilateral in nature would require that more flexibility be granted to contracting parties in order to tailor their level of commitment towards other parties.

Finally, the Report indicates that the instrument could also be used for a wider range of BEPS-related issues, such as rules regarding the confidentiality of information obtained by tax administrations (thereby facilitating the implementation of the country-by-country reporting template developed under Action 13 for example), a multilateral interest expense allocation agreement, or new dispute resolution mechanisms to avoid the potential for unilateral and uncoordinated responses to BEPS resulting in double taxation.

While the precise content of a multilateral instrument can only be defined once outputs of the BEPS project have been finalized, the Report concludes that the scope of the multilateral instrument should at this stage only include agreed treaty-based outputs of the BEPS project in order to ensure that it can be put in place within a reasonable timeframe. The instrument could then be used to host additional multilaterally agreed provisions in the future and should thus be viewed as dynamic.

**Next step: convene an International Conference**

Stressing the urgency of creating a multilateral instrument, the Report recommends convening an International Conference in early 2015 under the aegis of the OECD and the G20. The goal of such International Conference would be to develop and negotiate a multilateral instrument that implements the agreed treaty-based recommendations of the BEPS project. The International Conference would take those recommendations into account once they are finalized, with the Report noting that a number of these will only be delivered in 2015.

The International Conference should be open to all interested countries and should be limited in time to two years. Although the Report recommends limiting the scope to implementing the BEPS-related treaty measures, it also suggests that such International Conference should reflect on further ways to “foster a more effective international tax environment.”

**Implications**

As the delivery of the September 2014 output underscores, the OECD is focused on meeting the target dates established in the BEPS Action Plan. The multilateral instrument contemplated under Action 15 is likely to be an important element of the OECD’s efforts to maintain momentum and to achieve success in a timely manner. However, as a practical matter, the role of any multilateral instrument and the impact such an instrument may have on businesses are unclear at this stage. Moreover, the appetite of countries to sign up to a multilateral instrument approach also is unclear. Global businesses will want to continue to monitor developments with respect to this Action 15.

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**Endnotes**

1. The Report contains a technical annex called *A toolbox for a multilateral instrument for the swift implementation of BEPS measures*, based on input by a group of experts in tax and public international law.
For additional information with respect to this Alert, please contact the following:

**Ernst & Young LLP, International Tax Services, Washington, DC**
- Barbara Angus  +1 202 327 5824  Barbara.Angus@ey.com

**Ernst & Young LLP, Global Tax Desk Network, New York**
- Gerrit Groen  +1 212 773 8627  Gerrit.Groen@ey.com
- Dirk Jan Sloof  +1 212 773 1363  DirkJan.Sloof@ey.com
- Daniel Brandstaetter  +1 212 773 9164  Daniel.Brandstaetter@ey.com
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