



International Fiscal Association Joint Meeting of the Switzerland and USA Branches

Practical BEPS Consequences Anti-Avoidance, Disclosure, Related Matters



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Agenda

- BEPS Multilateral Instrument
- BEPS Action 6 – Preventing Treaty Abuse
- Swiss Developments
 - Corporate tax reform
 - US-Swiss Protocol
 - Swiss perspective on Multilateral Instrument
- Update on Selected BEPS Implementation Issues
 - Exchange of Rulings
 - Country-by-Country Reporting
- U.S. Tax Reform Proposals



BEPS Multilateral Instrument



BEPS Multilateral Instrument (MLI)

- Aim is to transpose BEPS treaty-related measures into existing tax treaties quickly, as mandated by Action 15
- Ad Hoc Group (99 States plus some observers) agreed text on November 24, 2016 – OECD released text and accompanying Explanatory Statement
- Open for signature as of December 31, 2016
- Lots of flexibility – countries will need to identify matches with treaty partners
 - Meeting on that in February 2017
- OECD expected to host signing ceremony in June 2017
- Countries' level of participation (e.g., US: unlikely, UK: limited, Australia: enthusiastic)



BEPS MLI – Outline of Provisions

- Part I – Scope and Interpretation of Terms
- Part II – Hybrid Mismatches
- Part III – Treaty Abuse
- Part IV – Avoidance of Permanent Establishment Status
- Part V – Improving Dispute Resolution
- Part VI – Arbitration
- Part VII – Final Provisions



Approach Taken in the MLI

- Doesn't amend text of treaties – must be read alongside them
- Provides flexibility regarding:
 - Treaties affected
 - Alternatives for satisfying minimum standards
 - Opting out of non-minimum standard provisions:
 - Entirely
 - For all treaties that contain specified substitute provisions
 - To select alternative or optional provisions



MLI – Some Initial Highlights

- Text is very complicated – States, Parliaments, taxpayers likely to need help deciphering effect on treaties
- No mechanism provided or required for MLI Parties to commit to, or even to be transparent about their position on, BEPS Commentary
- No text of detailed LOB provided – that’s left to treaty partners to agree
- No incorporation of new US Model provisions regarding special tax regimes, subsequent changes in law



MLI – Some Initial Highlights (Cont'd)

- Arbitration provisions:
 - More detailed than OECD Model Article 25(5)
 - “Last best offer” is default, but States can opt for “independent decision” form
 - States may be able to limit scope of eligible cases
- Not much information on what ratification procedures will be in participating countries
 - MLI gives so much flexibility, its effects on individual treaties may be very customized – will each Party need to know all other Parties’ positions before any ratification package can be submitted?



BEPS Action 6 – Preventing Treaty Abuse



BEPS Action 6 – 2015 Report

- In 2013, the OECD BEPS Action Plan identified tax treaty abuse, and treaty shopping in particular, as one of the most important sources of BEPS concerns
- BEPS Action 6, in the 2015 Final Report, established a three-part approach to address tax treaty abuse and treaty shopping:
 - First, a clear statement that states enter into a tax treaties intending to avoid creating opportunities for non-taxation or reduced taxation
 - Second, mechanical limitation on benefits (“LoB”) rules, patterned after the provisions employed in US tax treaties
 - Third, adopt a “more general anti-abuse rule based on the principal purposes of transactions or arrangements” – a so-called “PPT rule”



MLI – Treaty Abuse

- The MLI implements the treaty purpose test with –
 - “Intending to eliminate double taxation with respect to the taxes covered by this agreement without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents or third jurisdictions)”
- Meanwhile, there has been some evolution in the view taken of mechanical LoB rules
 - The Action 6 Final Report served up 2 possibilities:
 - A “simplified” LoB, patterned after the US-style rules but very bare bones, and
 - A detailed LoB, articulated to resemble closely US treaty provisions



MLI – Treaty Abuse (Cont'd)

- The simplified LoB contains one dramatic broadening, in the derivative benefits provision –
 - The LoB test is satisfied if “equivalent beneficiaries” – i.e., residents of a 3d state that has a treaty with the source state – own at least 75% of the resident entity
 - Note that there is no limit to the number of equivalent beneficiaries
 - US treaties typically call for 95% or greater ownership by 7 or fewer equivalent beneficiaries
 - Also note the absence of any base erosion test, again much less restrictive than the typical US derivative benefits provisions



MLI – Treaty Abuse (Cont'd)

- The detailed LoB was not finalized following adoption of the new US model in 2015, with the recognition that further changes could be made
- The MLI commentary states that because a detailed LoB clause requires “substantial bilateral customization, which would be challenging in the context of a multilateral instrument” no such provision is included in the MLI



MLI – PPT Rule

- Concerned that the simplified LoB left open tax avoidance opportunities, Action 6 required the test be paired with a PPT
- The MLI suggests a continuing drift in the direction of the PPT
- Rule 1 under Art. 7, Prevention of Treaty Abuse, is the PPT rule
 - As such it will become a feature of virtually every treaty under the *aegis* of the MLI
 - The PPT rule effectively displaces similar provisions in underlying treaties
 - An election out is permitted, but only where the parties intend to meet the minimum standard with a detailed LoB plus a conduit rule (or PPT)



MLI – PPT Rule (Cont'd)

- How will a PPT overlay to existing treaties affect tax planning?
 - Action 6 includes 10 examples in the commentary, but these leave many questions unanswered
 - The case of non-CIV funds has triggered attention by practitioners as well as the OECD
 - Initial guidance from the OECD regarding non-CIV funds appeared in the form of 3 examples issued on January 6, 2017
 - The examples are helpful but significant additional detail will be needed to understand the treatment of corporate blockers generally
 - The deadline for comments on the examples closed on February 3
 - Stay tuned



Swiss Tax Developments



Swiss Tax Policy - Overview

- Lawmaker favors capital import neutrality policy:
 - No CFC legislation
 - Unilateral unconditional exemption of foreign PE income with no switch over clause → Triangular clause of Swiss-US 1996 DTC (art. 22 para. 4)
 - Participation exemption (reduction) with no subject to tax clause but with anti-hybrid rule
 - As per the law, foreign legal entities are to be assimilated to Swiss legal entities
- Effective tax rates: currently from approx. 12% to 24% (Geneva). But impact of tax reform ?



Swiss Tax Policy – Overview (Cont'd)

- 35% WHT on corporate distributions
 - Reduced to 0% under Swiss-EU Savings Agreement (Art. 9, May 2015 protocol) for qualifying Swiss-EU (25%) shareholdings
 - 5% under 1996 Swiss-US DTC (10% shareholdings)
- No WHT on interests on commercial loans and royalties



Swiss Tax Policy – Overview (Cont'd)

- Recent case law (and administrative practice) tackles international double non-taxation, for example:
 - **Unilateral exemption of offshore finance branch denied** (restrictive interpretation of outbound PE concept but *de facto* switch over clause), Federal Tribunal Judgment of 5.10.2012, ATF 139 II 78
 - **Wider interpretation of domestic PoEM test**
 - **Hybrid entities: US LLC case:** treated as fiscally transparent in Switzerland because of its tax treatment in the US, Federal Tribunal Judgment of 18.9.2015, 2C_894/2013



Swiss Tax Policy– International Framework

- OECD and EU framework (2014 MoU)
 - Abolition of Swiss cantonal tax privileges (holding, mixed, auxiliary, domicile company regimes) and certain federal special regimes (finance Branch, principal company) by 2019
 - Measures of tax reform planned to keep Switzerland's appeal to international business
- EU Anti Tax Avoidance Package and Switzerland as third country (CFC rules, etc...)



Swiss Tax Policy– Corporate Tax Reform

Draft of Federal Council – June 2015

- Abolition of cantonal regimes
- **Abolition of federal issuance stamp tax**
- **Adjustment of partial taxation of dividends (70%) (Cantonal and Federal)**
- Exemption of hidden reserves/goodwill (“step-up”) in case of immigration into Switzerland (Federal/Cantonal)
- Transitional preferential taxation upon shift from privileged regime to ordinary taxation (Cantonal)
- R&D super deduction for R&D activities in Switzerland (Cantonal and non-compulsory)
- Nexus based patent box with max 90% reduction (Cantonal and compulsory)
- Cantonal tax reduction for participation and IP assets (Cantonal and non-compulsory)

Package rejected by referendum on 12.2.2017

- Abolition of cantonal regimes
- Exemption of hidden reserves/goodwill (“step-up”) in case of immigration into Switzerland (Federal/Cantonal)
- Transitional preferential taxation upon shift from privileged regime to ordinary taxation (Cantonal)
- R&D super deduction (**max 150%**) for R&D activities in Switzerland (Cantonal and non-compulsory)
- Nexus based patent box with max 90% reduction (Cantonal and compulsory), **broader catalogue** (copyrighted software, certified IP assets of SMEs)
- Cantonal tax reduction for participations, IP assets **and intra group loans** (Cantonal and non-compulsory)
- **Notional interest deduction (Federal and Cantonal non-compulsory). At cantonal level, minimum partial dividend taxation requirement of 60% for individuals**
- **General limitation of incentives: minimum residual taxable profit of 20% (cantonal)**

General reduction of cantonal tax rates



Swiss Tax Policy– Corporate Tax Reform (Cont'd)

- What's next ?
- New draft bill expected
- Impact on international standards (OECD/EU) ?
- What will be the content of the future reform ?
 - Plan B or C ?
 - Impact on the general reduction of tax rates by the cantons ?
Impact on intercantonal competition ?



Swiss Topics (Cont'd)

- Alignment with OECD standards on transparency
 - Full OECD art. 26-type exchange of information on request – implemented in many Swiss tax treaties
 - Automatic exchange of account information → from 2018, information collection starts in 2017
 - Spontaneous exchange of tax ruling information → from 2018
 - BEPS Action 13: Automatic exchange of CbC Reports → minimum standard, planned from 2020



BEPS Implementation in Switzerland

- BEPS Action 6: Curbing the abuse of tax treaties, in particular treaty shopping (1)
 - LOB clause in US-CH income tax treaty, since 1996
 - Specific anti-abuse clauses in 20 other CH tax treaties (see next slide)
 - LOB in treaty with Japan
 - Other treaties: Anti-conduit rules (e.g. UK, FL, Albania; France); economic substance/no artificial arrangements (e.g. Malta); reservation of domestic anti-abuse rules (e.g. Germany, P.R. China)



BEPS Implementation in Switzerland (Cont'd)

- Unilateral anti-abuse rules (“1962 Decree”) → against treaty shopping by Swiss resident entities
- CH doctrine and jurisprudence: All CH tax treaties are subject to
 - an unwritten reservation of "abuse of tax treaty rights" (principle of good faith interpretation) and
 - a strict beneficial owner requirement (even where this is not explicitly stated in the treaty text)
 - Very far-reaching interpretation of "beneficial owner" concept by Swiss courts → substance requirements, substance-over-form, anti-conduit → see recent case law on "dividend stripping" etc. → facts & circumstances of each single case are key



Preventing Treaty Abuse

- Swiss Double Taxation Treaties with Anti-Abuse Provisions

- Albania
- Australia
- Belgium
- Bulgaria
- Chile
- China
- Estonia
- France
- Hongkong
- Iceland
- India
- Italy
- Japan
- Liechtenstein
- Malta
- Morocco
- Mexico
- Netherlands
- Oman
- Peru
- Portugal
- Qatar
- Russia
- Slovenia
- Taiwan
- United Arab Emirates
- UK
- USA



BEPS Implementation in Switzerland (Cont'd)

- BEPS Action 6: Curbing the abuse of tax treaties, in particular treaty shopping (2)
 - MLI implications (Art. 6-13 MLI)
 - Minimum standard to curb tax treaty shopping:
 - Treaty preamble to included language to prevent double non-taxation and treaty shopping/abuse to benefit 3rd country residents:
“...without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States”



BEPS Implementation in Switzerland (Cont'd)

- Inclusion of anti-treaty shopping tests (3 alternative options → art. 7 MLI)
 - Option 1: Introduction of PPT (Principal Purpose Test) → standard option
 - Option 2: PPT combined with a LOB clause
 - Option 3: LOB clause combined with anti-conduit clause



BEPS Implementation in Switzerland (Cont'd)

- BEPS Action 6: Curbing the abuse of tax treaties, in particular treaty shopping (3)
 - Expected CH approach to MLI:
 - Adaptation of title and preamble of CH tax treaties to minimum standard
 - Adoption of (narrow) PPT option
 - Probably: Replacement of all existing anti-abuse provisions in CH treaties by PPT
 - Abolition of unilateral 1962 anti-treaty shopping Decree
 - Implementation of 365-day minimum holding period for treaty benefits on dividends? (art. 8 MLI) → might be a solution to Swiss problems with (perceived) "dividend stripping"



BEPS Implementation in Switzerland (Cont'd)

- Plan to implement the "Multilateral Instrument" (MLI) - to "automatically" amend existing CHF tax treaties (>100), to adapt to BEPS Actions 2, 6, 7 and 14
 - CH actively participated in drafting the MLI, to ensure that it will contain certain options and reservations needed by CH
 - Federal Council will decide whether to sign the MLI before June 7, 2017 (MLI signing ceremony).
 - A preliminary list of treaty partners will be established, in relation to which CH will implement the MLI



BEPS Implementation in Switzerland (Cont'd)

- Federal Council will indicate the changes to existing tax treaties that CH will be inclined to implement
- If there is a 'match' between CH and the respective countries on the preliminary list at the signing ceremony, the CH MLI can go ahead, *that is*:
- Preliminary country list with proposed changes of treaty provisions will then be subject to public hearing process
- Based on comments received, Federal Council will elaborate legislative bill with explanatory report
- Federal Parliament to approve the MLI implementation and to decide on Swiss options and reservations to MLI



BEPS Implementation in Switzerland (Cont'd)

- BEPS Action 14 Implementation: Improving on Dispute Resolution Mechanisms
 - Inclusive Framework on BEPS (IF) launched in Kyoto (June 2016), to oversee implementation of BEPS Actions. CH is represented on IF Committee (1 of 20 country representatives).
 - IF publishes main documents for review of implementation of minimum standards under BEPS Actions 5, 6, 13 and 14. With regard to Action 14, main document was published in Oct. 2016
 - First review phase for CH started in Dec. 2016



Competent Authority Issues

- Competent authority clauses in place under CH treaties
 - MAPs
 - Bilateral/Multilateral APAs
- Over 20 CH treaties already include *arbitration* provisions
 - E.g. US, UK, Germany, Austria, France (only corporates), Lux, NL, Canada (limited), South Africa, Hong Kong,
 - Most of those treaties follow current OECD Model
 - Under US and German treaties, Competent Authorities may agree that arbitration is excluded/ not suitable (see e.g. Competent Authority Agreement of Dec. 21, 2016 on MAP and arbitration under German treaty)



Competent Authority Issues (Cont'd)

- Arbitration generally only after 2 or 3 years of MAP without results
- Where a decision by a *judicial* authority of one of the Contracting States already exists, arbitration is usually excluded
- Recent SCH treaty policy generally follows OECD Model approach on arbitration
- Use of info exchange provisions by SFTA to gather info on foreign taxpayers seeking treaty relief (typically for Swiss WHT)
- SFTA, SIF very busy with BEPS implementation, all forms of info exchange



Update on Selected BEPS Implementation Issues



Exchange of Rulings

- Background
- Implementation update
- Actions 5 monitoring
- Challenges and opportunities



Country by Country Reporting

- Guidance on voluntary filing for tax year 2016
- CbC reporting form and instructions
- Bilateral competent authority arrangements
- Confidentiality and data safeguards reviews
- Action 13 monitoring
- Challenges and opportunities



U.S. Tax Reform Proposals



President Trump's Tax Reform Proposal

- 15% corporate tax rate
- Deferral - initial plan repealed deferral, most recent plan is silent on deferral
- Current expensing is elective, but at a cost - no deduction for net interest expenses
- Mandatory tax on untaxed foreign earnings and profits - 10% for cash and 4% for other earnings
- Repeal corporate AMT and many unspecified business tax expenditures (e.g., section 199, LIFO)



U.S. House of Representatives Blueprint

- House of Representatives Blueprint (“A Better Way: Our Vision for a Confident America”), released on June 24, 2016, contains a high level overview of a tax reform proposal
 - Corporate tax rate reduced to 20%, and most credits/special deductions repealed (except for research credit)
 - The House Blueprint would move the corporate income tax to a consumption tax
 - Mandatory current expensing of all tangible and intangible assets, but at a cost – loss of net interest expense deductions



U.S. House of Representatives Blueprint (Cont'd)

- Border adjusted tax
- Gross revenue from exports (goods, services and intangibles) would be exempt from US tax
- The cost of imports (goods, services and intangibles) would not be deductible, and therefore would be subject to US tax
- This approach is similar to a subtraction-method VAT and is known as Growth and Investment Tax (GIT), one of the tax reform options presented by the President's Advisory Panel on Federal Tax Reform in 2005

International tax reform under the House Blueprint

- Move from a worldwide tax system to a territorial system
- Repeal most categories of subpart F, other than the foreign personal holding company income
- Mandatory repatriation of accumulated foreign profits



U.S. Senate Finance Committee

- Republicans and Democrats pursuing divergent paths
- Chairman Hatch: Corporate Integration
 - Previewed proposal in staff white paper, Comprehensive Tax Reform for 2015 and Beyond
 - Plan is expected to provide corporations with a dividends-paid deduction and impose a non-refundable withholding tax on interest and dividends (including on foreign and tax-exempt parties)
- Ranking Member Wyden: Staff drafts on depreciation, financial instruments, and international



Thank you

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