

# **OECD BEPS: Multilateral Instrument signed by Switzerland and 67 other countries**

**8 June, 2017**

**On 7 June 2017, officials from more than 70 countries participated in the signing of the multilateral instrument ("MLI"), which is a result of negotiations of more than 100 jurisdictions. The Organization for Economic Cooperation and Development ("OECD") aims for a swift implementation of a series of tax treaty measures to update international tax rules and reduce the opportunity for tax avoidance. Impacts for Swiss companies are mainly expected in the field of dispute resolutions.**

## **Let's talk**

For a deeper discussion of how this might affect your business, please contact:

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The MLI is one of the outcomes of the OECD/G20 Project to tackle Base Erosion and Profit Shifting ("BEPS") and has the goal to enable countries to swiftly modify bilateral tax treaties (more than 3'000 worldwide) to include the measures developed in the course of the BEPS work. In this respect, an ad hoc group, consisting of 99 countries, four non-state jurisdictions and seven international or regional organizations participating as observers, developed the MLI. In their negotiations, the ad hoc group focused on the following BEPS measures and how the MLI would need to modify the provisions of bilateral or regional tax agreements. Aiming to swiftly implement those measures, some of which are minimum standards and others representing best practice recommendations only:

- **Hybrid mismatch arrangements** in accordance with BEPS Action 2 (best practice recommendation);
- Granting of **treaty benefits** in inappropriate circumstances under BEPS Action 6 (minimum standard);
- Amendments to the definition of "**permanent establishment**" as recommended under BEPS Action 7 (best practice recommendation);
- Facilitating of access to and resolution of **mutual agreement procedures** consistent with BEPS Action 14 (minimum standard).

The outcome of this work is the MLI which is 49 pages long as well a 86 pages Explanatory Statement. Signing of the MLI took place at a formal signing ceremony in Paris on June 7, 2017. Switzerland signed the MLI together with 67 other countries, including China, Germany, India, the Netherlands and UK to name just a few. In addition, 8 other jurisdictions have expressed their intent to sign the MLI soon.

## **How it works**

The MLI operates to modify tax treaties between two or more parties to the instrument. However, it will not directly amend the text of an existing treaty but will be applied alongside existing tax treaties, supplementing and modifying their application with respect to the specific BEPS measures (no override or substitution).

As mentioned above, the purpose of the MLI is to enable all parties to swiftly meet the treaty-related minimum standards (BEPS Action 6 and 14). Given that each minimum standard can be satisfied in different ways and given the broad range of countries and jurisdictions involved, the MLI needs to be flexible in relation to provisions that did not reflect minimum standards, in particular in relation to how such provisions interact with provisions in bilateral tax treaties.

The MLI provides flexibility in the following ways:

- **Covered treaties:** Countries can specify the tax treaties to which the MLI applies.
- **Minimum standard:** Opting out of a provision which reflects a minimum standard (Action 6 and 14) is only possible in limited circumstances (e.g. in case a bilateral treaty already meets such minimum standard). However, where a minimum standard can be satisfied in multiple ways, the MLI allows countries to choose which option to implement. Signatories need to notify their choice to the OECD.
- **Opting out of non-minimum provision:** Countries can opt out of a provision which does not reflect a minimum standard (Action 2 and 7). Opting out of the entire or, in some cases, out of part of the provision is possible. Countries can always opt in later.
- **Opting-out of specific provisions:** Even though in general, no opting out of minimum standard provisions is possible, countries can opt out of provisions in situations where the bilateral treaty goes beyond the minimum standard or in case special treaty features have been negotiated by the parties.
- **Choice to apply optional and alternative provisions:** In some cases, the output of the work on BEPS produced multiple alternative ways to address a particular BEPS issue. In other cases, the work resulted in a main provision that could be supplemented with an additional provision. The MLI incorporates a number of alternatives or optional provisions that generally will apply only if both jurisdictions being part of a specific treaty affirmatively choose to apply them.
- **Opt in for mandatory binding arbitration:** Signatories have the possibility to opt in for mandatory binding arbitration if no agreement in a mutual agreement procedure has been achieved within 2 or 3 years. Important to note is that the mandatory binding arbitration clause in the MLI is intended to apply only between parties that explicitly choose to apply it (notification required). As in a bilateral treaty situation, this clause will apply only if both jurisdictions involved notify the OECD that they choose to apply it. At the time of signing, 25 jurisdictions have signed up for mandatory arbitration, including amongst others Australia, Austria, Canada, France and Germany, which will lead to the introduction of arbitration to over 150 existing treaties.

### **Next Steps & Legal Aspects**

After signing, the MLI will have to be ratified by the participating states for it to come into effect. This will take varying lengths of time, depending on the state. In this respect, the MLI will enter into force on the first day of the month following a three calendar months period after the fifth country has ratified the MLI.

The MLI comes into effect for Mutual Agreement Procedure and Arbitration cases generally from the date of entry into force for both contracting states, but otherwise generally thereafter, according to the following:

- **Withholding tax** - on amounts due from the next 1 January (or at the start of the tax year if a state so elects, even if the other doesn't).
- **Other taxes** - unless both contracting states elect for a shorter delay, in respect of taxable periods beginning on or after six months (or the following 1 January if a state elects even if the other doesn't).

We currently understand that it is possible that signatories to the MLI could have ratified the instrument before October 1, 2017 in order for it to be effective for withholding taxes from January 1, 2018, although for most countries the process will take longer and January 1, 2019 is more likely.

### **What does it mean for Switzerland?**

Switzerland has been part of the countries that have signed the MLI at its signing ceremony yesterday. Switzerland will implement the BEPS minimum standards into its tax treaties either within the framework of the MLI or by means of the bilateral negotiation of double taxation agreements.

The Federal Council will submit the BEPS Convention for public consultation towards the end of 2017. It will undergo the standard parliamentary approval process before entering into force and hence entry into force is not expected before January 1, 2019.

Initially, the tax treaties with Argentina, Chile, India, Iceland, Italy, Liechtenstein, Lithuania, Luxembourg, Austria, Poland, Portugal, South Africa, the Czech Republic and Turkey will be amended by the MLI.

Switzerland took the position that it adopts the modified description of the preamble of, the mandatory provisions (mainly the "Treaty Abuse Provisions" (Action 6)). Switzerland currently opts out for all other options such as e.g. Action 7 (Permanent Establishments) but opted in for mandatory binding arbitration.

In case of Action 6, Switzerland will adopt a so-called Principal Purpose test (PPT) (potentially in combination with an abuse clause). According to unofficial information from the State Secretariat for International Financial Matters ("SIF"), the current Swiss practice with regard to determine whether treaty benefits are available should basically not be substantially affected. Hence, the implementation of the MLI in this respect is expected to have limited impact for Swiss companies.

The opting in for mandatory binding arbitration will be of significant importance for Swiss companies since today double taxation cannot be successfully resolved in all cases. Whilst currently, arbitration clauses are included in approx. 32 double tax treaties which Switzerland has signed, not all of them are effective yet. However, the practical impact of the arbitration clause in the MLI will depend on the number of parties which ultimately will also opt in for this clause.

### **Key takeaway**

Whilst the MLI may have limited impact on Swiss companies, international groups with operations and cross border transactions in multiple foreign jurisdictions are best advised to perform a MLI-impact assessment. This to identify the potential risks the signing of the MLI may trigger on existing structures but also the potential benefits which may become available.