CHARTERED ACCOUNTANTS
AUSTRALIA + NEW ZEALAND

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Dear Greg,

## Australia's Adoption of the OECD Multilateral instrument

Chartered Accountants Australia and New Zealand welcomes the opportunity to make a submission on Australia's adoption of the OECD Multilateral Instrument as set out in Treasury's December 2016 Consultation Paper (**Consultation Paper**).

Chartered Accountants Australia and New Zealand is made up of over 100,000 diverse, talented and financially astute professionals who utilise their skills every day to make a difference for businesses the world over. Our members are known for professional integrity, principled judgment and financial discipline, and a forward-looking approach to business. We focus on the education and lifelong learning of members, and engage in advocacy and thought leadership in areas that impact the economy and domestic and international capital markets.

We are represented on the Board of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance, and Chartered Accountants Worldwide, which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

### Introductory comments

The *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (the Multilateral Instrument or **MLI**) has been developed as part of the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project to address those BEPS initiatives that require changes to be made to tax treaties. These are:

- BEPS Action 2: Neutralise the Effects of Hybrid Mismatch Arrangements;

- BEPS Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances;
- BEPS Action 7: Preventing the Artificial Avoidance of Permanent Establishment Status; and,
- BEPS Action 14: Making Dispute Resolution Mechanisms More Effective.

The text of the MLI and its Explanatory Statement[1] were released on 24 November 2016.

**Australia's proposed approach to adopting the MLI**

Chartered Accountants ANZ is in general agreement with the proposed principles to guide the Government's adoption of the MLI articles. We make the following observations/comments in this regard:

- The 2015 German treaty is given as the sole bilateral tax treaty that would be excluded from the MLI. We note that paragraph 22A of the Consultation Paper goes on to say that this treaty incorporates *most* of the BEPS treaty-related measures. As an aside, we recall that the Explanatory Memorandum for this treaty had extensive commentary on its interpretation. It will be interesting to see whether our MLI counterparts concur with this commentary and whether it will be a basis for ATO guidance.

- We expect that Treasury has already analysed the implications of entering into the MLI (e.g. the effect on our overall tax base and tax compliance regimes) and has briefed the Treasurer. An abridged version of this analysis is likely to be sought by any parliamentary committees commissioned to enquire in to the Bill and we would support such scrutiny.

- There needs to be a reasonable take up of the MLI by jurisdictions and reasonable consensus to make the initiative effective. There is currently a lack of understanding of where the "Go – No Go" threshold is for Australia's full commitment to the MLI, especially given uncertainties surrounding the position of the new President's administration in the United States of America.

- The MLI allows Australia to *rapidly* modernise its treaty network, which would otherwise be a very lengthy process. But we lack a clear understanding (or examples) of what the revised wording of an 'MLI-impacted' tax treaty would look like. This is of great practical importance to tax practitioners, their clients, courts, and students of international taxation.

- Overall, there are fears that this is not a package directed at promoting Australia's trade and growth but rather, adding integrity measures into tax treaties. The Regulatory Impact Statement for the MLI legislation will be scrutinised closely to determine the extent to which Treasury has considered the cost-benefits of Australia's MLI strategy.

[1] Available at http://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm

Appropriate transitional rules and implementation timelines as well as timely taxpayer educative guidance will be needed. The contemporaneous publication of ATO guidance will be expected on a number of important issues, such as restructuring designed to adapt to the revised MLI concept of permanent establishment.

**Article 3 – Transparent entities**

We understand that concerns have already been raised about the lack of clarity as to whether discretionary trusts are to be covered under Article 3 as transparent entities. We would have liked to have seen some practical examples in the Consultation Paper to demonstrate the impacts of this article on common scenarios such as:

- 'Public' CIVs in Australia with non-resident beneficiaries
- Private trusts in Australia (including deceased estates)
- Australian partnerships with non-resident partners
- Australian limited partnerships
- Foreign trusts, partnerships and hybrids with Australian investors.

At the very least, the treatment of these structures under Article 3 should be addressed in ATO guidance.

**Article 12 - Artificial Avoidance of Permanent Establishment (PE) Status through Commissionnaire Arrangements and Similar Strategies**

At first glance it might seem that Australia should adopt Article 12 which seeks to address scenarios where foreign entities artificially avoid having a PE given it has similarities, when viewed unilaterally, with Australia's MAAL. Indeed, Australia's initial approach is to adopt Article 12 without reservation.

That said, it is important to consider other factors including:

- The position of outbound activities of Australian based entities that may face increased overseas taxation if a PE in a foreign jurisdiction arises.
- The fact that Australia has legislated the MAAL, is expected to legislate a DPT soon, and already has robust transfer pricing rules. This suite of measures could be seen to perhaps provide sufficient comfort without requiring adoption of Article 12.
- The lack of finalised OECD guidance on the attribution of profits to PEs, an issue that is notoriously complex and where a consensus of OECD members on the topic has to date been elusive. Domestically, the Board of Taxation conducted a review of tax arrangements applying to PEs including attribution of profits. The Board's report of April 2013[2] was released by the government in June 2015 but to date there have been no further developments.

Then there is the restriction on withdrawing adoption choices in that once made and ratified they cannot be narrowed under the MLI (although they can be by subsequent bilateral treaties).

[2] *Tax Arrangements applying to Permanent Establishments*, Board of Taxation 2013 http://taxboard.gov.au/consultation/tax-arrangements-applying-to-permanent-establishments/

We therefore urge Treasury to consider whether it would be prudent to place a reservation on adoption of Article 12 at this point in time, pending further developments.

**Articles 18-26 - Arbitration**

The Consultation Paper states that Australia's initial approach is to adopt the Articles on arbitration but then make a reservation to exclude from scope the general anti-avoidance rule (Part IVA of the *Income Tax Assessment Act* 1936). In particular, this would mean that assessments regarding the proposed DPT would be out of scope even though the DPT due and payable would not be reduced by the amount of foreign tax paid on the diverted profits. Where an amount of foreign tax is paid, double taxation would generally result which clearly is counter to the objective of a tax treaty.

**Entry into effect**

Although early adopters may obtain more effective dispute resolution procedures sooner (dependent on options chosen), there may be risks in being a first mover. Australia might actually be better off in delaying until 2020 if it is already expected that other jurisdictions will do so. This would have the added benefit of allowing more time to consider and implement the changes. We also think it important for Australian Treasury officials to have time to determine the MLI stance of our country's major trading partners and, as noted earlier, the position of the USA will be particularly relevant.

**Miscellaneous comments**

**(a) Interpretation**

Interpretative aspects of the MLI continue to evolve. Most recently, in January 2017, an OECD discussion draft on the principal purpose test in relation to non-CIV funds[3] proposed adding three examples to the OECD Model Commentary. However, it is unclear what status this would have given that the discussion draft issued after the release of the MLI.

To address this situation and others like it (which can be expected given for instance the novel nature of the MLI and its complexity), we submit that the OECD Commentary should receive legislative recognition. We envisage that this would be along the lines of how the OECD Transfer Pricing Guidelines have been legislated in Division 815 of the Income Tax Assessment Act 1997.

**(b) Consolidated versions of modified treaties**

Paragraph 26 of the Consultation Paper states that "consistent with current practice, it is not proposed that the Government would produce consolidated versions of each modified treaty".

Although this is consistent with the current practice for treaties, overlaying MLI amendments brings in added complexity which we think justifies a different approach. To be blunt, it is inappropriate for Treasury to simply vacate the field when it comes to the implementation and educational aspects of MLI.

[3] **Interaction between the tax treaty provisions of the report on BEPS Action 6 and the treaty entitlement of non-CIV funds**

In our view, the applicable MLI amendments should be consolidated with the existing bilateral treaties by Treasury and maintained on the Treasury website.

At the very least, Treasury should work with commercial law publishers (e.g. CCH, Thomson Reuters) to ensure that "authorised versions" of MLI impacted tax treaties are published.

**(c) ATO guidance**

The ATO will be called upon to produce strong, clear and prompt guidance relating to the MLI.

Given the innovative nature of the MLI, we expect that numerous significant issues will be identified by stakeholders. Some of these have been indicated in the above submission points. Our view is that these have merely "scratched the surface" of what will be required and it will be important that the ATO is seen to be proactive.

Chartered Accountants ANZ will raise this for discussion via the ATO's Consultation Steering Group.

**(d) A detailed MLI work program with a post-implementation review**

We strongly recommend that Treasury commit to a published, constantly updated work program which keeps stakeholders fully informed about which countries are being engaged in MLI consultations. This would go beyond the OECD's proposed "speed-dating" approach and inform stakeholders about the thinking behind any reservations and implementation road-blocks encountered.

Tax treaties have such a central role in Australia's tax system that we do not think it appropriate for Parliament to simply enact MLI legislation without adequately monitoring subsequent outcomes. We will certainly be urging parliamentarians to adopt post-implementation review procedures for the MLI.

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Should you have any queries concerning the matters discussed in our submission, or wish to discuss them in further detail, please contact me via email at: michael.croker@charteredaccountantsanz.com or telephone (02) 9290 5609.

Yours sincerely

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