New Zealand's implementation of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS*

An officials' issues paper

March 2017

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Terms and abbreviations

Term	Description
Competent authority (CA)	Person authorised by a double tax agreement (DTA) to administer tax treaty provisions and resolve disputes.
Compatibility clauses	Implementation clauses that explain how CTAs are modified by operative clauses.
Covered tax agreement (CTA)	A DTA that both parties have chosen to be modified by the MLI.
Double tax agreement (DTA)	A bilateral tax treaty.
Explanatory statement	Commentary accompanying the MLI to explain the operation of the instrument. It does not address substantive issues – these are covered by the relevant OECD Action Report.
MAP	Mutual Agreement Procedure.
Minimum standards	BEPS Action Plan recommendations countries are expected to adopt (for example, the DTA preamble).
Multilateral instrument (MLI)	The OECD Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting.
Notifications	Each jurisdiction must provide a list of CTAs, options chosen, reservations and articles of CTAs modified by the MLI to the OECD Depository.
OECD	Organisation for Economic Cooperation and Development.
Operative clauses	Clauses that implement substantive changes to treaties as per the Action Plan recommendations.
Options	Some Action Plan items allow countries choices (for example, methods to relieve double taxation).
Reservations	Countries are permitted to reserve on non-minimum standard clauses.

CHAPTER 1

Background

Introduction

1.1 Since late 2012, there has been significant global media and political concern about evidence suggesting that some multinationals pay little or no tax anywhere in the world. This problem is referred to as base erosion and profit shifting or BEPS".

1.2 BEPS is a global problem and many BEPS strategies exploit technical differences between different countries' tax rules. Accordingly, New Zealand has been working with the OECD and G20 to develop a co-ordinated global solution to address BEPS through the 15-point G20/OECD BEPS Action Plan.

1.3 The Government has already implemented a number of BEPS-related policy reforms and is working on a number of others, including hybrid mismatch rules and strengthened transfer pricing and permanent establishment (PE) rules.

1.4 This issues paper seeks feedback on New Zealand's implementation of another OECD BEPS measure – the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (referred to as the multilateral instrument or MLI). The MLI will modify a number of New Zealand's existing double tax agreements (DTAs) in order to bring them into line with OECD recommendations.

OECD's multilateral instrument

1.5 DTAs are bilateral agreements that aim to mitigate double tax on cross border transactions, often by requiring states to exempt income or provide tax credits. There is the potential for these bilateral agreements to be misused to reduce or eliminate a multinational's worldwide tax. Misuse of DTAs in this way has been a feature of a number of cross-border tax avoidance arrangements.

1.6 Therefore, addressing treaty abuse has been a major part of the BEPS project and a number of the Action items in the BEPS Action Plan make recommendations that can only be implemented through changes to DTAs, including:

- preventing the granting of treaty benefits in inappropriate circumstances (Action 6);
- preventing the artificial avoidance of permanent establishment status (Action 7);
- neutralising the effects of hybrid mismatch arrangements that have a treaty aspect (Action 2); and

- providing improved mechanisms for effective dispute resolution (Action 14).

1.7 Some of these recommendations are BEPS "minimum standards" that countries that commit to solving BEPS are required to adopt. The minimum standards are the treaty abuse provisions contained in the Action 6 report and certain elements of the dispute resolution provisions contained in the Action 14 report.

1.8 All other provisions are optional, but are DTA "best practice" and now form part of the OECD Model Tax Convention following adoption of the G20/OECD Action Plan.

1.9 Countries were presented with the difficulty of how to quickly and efficiently implement these measures without requiring the bilateral renegotiation of several thousand existing DTAs.

1.10 In this respect, Action 15 of the OECD BEPS Action Plan recommended developing a multilateral instrument that would swiftly amend the DTAs of all participating jurisdictions.

1.11 The Ad-Hoc Group of officials from approximately 100 jurisdictions (both OECD and non-OECD jurisdictions) was formed to develop the text of the MLI.[1]

1.12 The OECD held public consultation on the MLI concept in Paris in July 2016. Material related to this consultation and a video recording of submissions is available on the OECD's website at http://www.oecd.org/tax/treaties/public-consultation-beps-action-15-multilateral-instrument.htm.

1.13 The text of the MLI and the accompanying Explanatory Statement was published by the OECD in November 2016 at http://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm.

1.14 New Zealand expects to be in a position to sign the MLI in mid-2017. Following signature, the MLI will go through the domestic process for ratification, including being submitted for parliamentary treaty examination.

Summary of issues paper

1.15 In chapter 1, this issues paper explains what the MLI is and, at a high level, how it will operate to amend our DTAs. Chapter 2 then explains how the substantive provisions will address BEPS concerns. Chapter 3 sets out the implementation process and next steps.

1.16 The MLI provides New Zealand with a unique opportunity to strengthen our DTAs and ensure they are consistent with international best practice.

[1] A list of participating jurisdictions can be found in the OECD's Brochure on the MLI published in November 2016 at http://www.oecd.org/tax/treaties/multilateral-instrument-BEPS-tax-treaty-information-brochure.pdf.

Accordingly, the Government has already indicated it intends to sign the MLI, and has made preliminary decisions on which DTAs to cover and provisions to adopt. Broadly speaking, New Zealand intends the MLI to cover the majority of its DTA network and to adopt all applicable minimum standard and optional provisions.

1.17 Due to the novel nature of the MLI and its interaction with New Zealand's DTAs, officials are interested in receiving submissions on the implementation of the MLI and practical issues associated with its adoption.

How to make a submission

1.18 Officials invite submissions on the suggested changes and points raised in this issues paper. Submissions should be sent to policy.webmaster@ird.govt.nz with "NZ's implementation of the MLI" in the subject line.

1.19 Alternatively, submissions can be addressed to:

New Zealand's implementation of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS*
c/- Deputy Commissioner, Policy and Strategy
Inland Revenue Department
PO Box 2198
Wellington 6140

1.20 The closing date for submissions is 7 April 2017.

1.21 Submissions should include a brief summary of major points and recommendations. They should also indicate whether it would be acceptable for Inland Revenue and Treasury officials to contact those making the submission to discuss the points raised, if required.

1.22 Submissions may be the subject of a request under the Official Information Act 1982, which may result in their release. The withholding of particular submissions, or parts thereof, on the grounds of privacy, or commercial sensitivity, or for any other reason, will be determined in accordance with that Act. Those making a submission who consider that there is any part of it that should properly be withheld under the Act should clearly indicate this.

CHAPTER 2

The multilateral instrument and how it will amend our DTAs

2.1 The MLI is a multilateral international treaty that will enable participating countries to quickly and efficiently modify their network of DTAs to address the treaty-specific BEPS concerns outlined in the OECD's Action 6, 7, 2 and 14 reports.

2.2 While this is a novel approach to modifying DTAs, it is not unprecedented in international law. Experts in both international tax and public international law participated in the OECD Ad Hoc Group that developed the MLI.

2.3 The MLI is a flexible instrument that allows countries to choose:

- which of their existing DTAs they wish to modify through the MLI;
- alternative ways of meeting BEPS minimum standards on treaty abuse and dispute resolution; and
- whether they want to adopt the OECD-recommended provisions for non-minimum standards. Within some of these provisions, there are alternative ways of addressing BEPS concerns and the ability for countries to enter a variety of reservations.

2.4 To ensure the operation of the MLI is clear and transparent, signatories to the MLI must notify the OECD Depository of which DTAs it wishes to cover, which reservations it wishes to enter, optional provisions it wishes to choose and which provisions in its nominated DTAs will be modified by the MLI. The OECD will publish this information online and it will be readily accessible to the public.

2.5 In addition, the OECD has adopted an **Explanatory Statement** that provides detailed commentary on the operation, and in limited cases, the substance of the MLI. The Explanatory Statement is available on OECD's website at http://www.oecd.org/tax/treaties/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf

2.6 This chapter outlines the structure and high level operation of the MLI. Chapter 3 further explains how the substantive provisions will address BEPS concerns and sets out New Zealand's position on the MLI. Chapter 4 then sets out the implementation process and next steps.

Structure of the multilateral instrument

2.7 Before describing how the MLI operates, it is useful to understand its broad structure.

Section	Relevant Article(s)	Description
Title and preamble		Sets out the context and purpose of the MLI.
Part I: Scope and Interpretation of Terms	1 to 2	Governs application of the MLI and defines key terms including Covered Tax Agreement.
Parts II – V: Substantive BEPS measures	3 to 17	Contains the **operative clauses** on hybrid mismatches, treaty abuse, PE avoidance, and improved Mutual Agreement Procedure (MAP). Each operative clause has a corresponding **compatibility clause**, **reservation clause** and **notification clause**. Some articles also permit **choices** between alternative clauses. This structure is explained further below.
Part VI: Arbitration	18 to 26	Contains a framework for independent binding arbitration.
Part VII: Final provisions	27 to 39	Contains mechanical provisions including those governing signature, ratification, amendment, notifications, language, entry into force and entry into effect.

Operation of substantive provisions of the multilateral instrument

2.8 Broadly speaking, the MLI will modify any bilateral DTA[2] to which New Zealand is a party to include the strengthened provisions to the extent:

- both New Zealand and the other party choose to include that DTA as a **Covered Tax Agreement**; and
- both New Zealand and the other party choose to adopt the relevant article in a way compatible with each other's choice.

2.9 In this way, the MLI could be viewed as a way of facilitating a large scale simultaneous negotiation to modify bilateral DTAs to include treaty-related BEPS measures (and in particular, to enable jurisdictions to meet the OECD's minimum standards on treaty abuse and dispute resolution).

2.10 It is important to note that jurisdictions cannot generally choose to apply different articles of the MLI to different DTAs. Jurisdictions must decide which DTAs they want to include as Covered Tax Agreements and what their choices of articles will be – those choices will apply for *all* Covered Tax Agreements.

2.11 For example, New Zealand could not choose for the MLI to apply to the New Zealand-Australia and New Zealand-Japan DTAs, but choose for the new dual resident entity provision in Article 4(1) of the MLI to be included in the New Zealand-Japan DTA, but not the New Zealand-Australia DTA.

[2] The MLI only applies to existing, full DTAs, not to future treaties or to treaties such as tax information exchange agreements (TIEAs).

2.12 There are limited exceptions to this principle. Some reservations allow jurisdictions to make reservations with respect to the application of specific articles in relation to certain Covered Tax Agreements or provisions within Covered Tax Agreements with certain objectively defined characteristics. For example, jurisdictions can choose for certain MLI provisions not to apply to Covered Tax Agreements that already contain equivalent provisions.

2.13 The OECD will maintain a public list of Covered Tax Agreements, reservations and choices of options and a list of affected Covered Tax Agreement provisions online to make it easy for the public to find out which DTAs are modified by the MLI and to assist in determining how a particular Covered Tax Agreement is modified.

2.14 The following paragraphs explain in more detail the structure of the MLI and how it will operate.

Covered Tax Agreements: Part I of the MLI: Scope and Interpretation of Terms (Articles 1–2)

2.15 In identifying the effect of the MLI on a DTA, the first question to be asked, is whether the DTA in question is a Covered Tax Agreement. This is governed by Part I of the MLI.

2.16 At the time of signature, every adopting jurisdiction must provide the OECD Depository with a list of the DTAs it wishes to modify via the MLI. If a party to a DTA does not list it, then it will not be a Covered Tax Agreement and it will not be modified by the MLI.

2.17 If there is a bilateral match (both parties list the DTA), that DTA is a Covered Tax Agreement for the purpose of the MLI and will be modified in accordance with the choices made by the parties to that agreement.

2.18 New Zealand has 40 DTAs in force and New Zealand's general approach is to include the majority of these as Covered Tax Agreements. This gives New Zealand the best chance of strengthening our DTAs with as many countries as possible. The only DTAs we propose to omit are ones where we:

- know the other jurisdiction is not intending to sign the MLI; or
- are renegotiating our DTA and the other party also agrees that it should not be covered because the provisions are expected to be included in the new DTA.

Modifying provisions: Parts II – VI of the MLI (Articles 3–26)

2.19 Once a DTA is identified as a Covered Tax Agreement, the second question is how it would be modified by the MLI. This is governed by Parts II to VI of the MLI.

Specific BEPS measures: Parts II – V of the MLI (Articles 3 – 17)

2.20 These articles implement the measures recommended in the:

- Action 2 report – neutralising the effects of hybrid mismatch arrangements that have a treaty aspect (Articles 3 to 5);[3]
- Action 6 report – preventing the granting of treaty benefits in inappropriate circumstances (Articles 6 to 11);
- Action 7 report – preventing the artificial avoidance of PE status (Articles 12 to 15); and
- Action 14 report – improving dispute resolution (Articles 16 and 17).

2.21 Generally speaking, each substantive provision contains an operative clause, compatibility clause, a reservation clause and a notification clause:

- **Operative clause**. This is the substantive provision to be read into the Covered Tax Agreement. For example, Article 4(1) contains the new dual resident entity provision recommended in the Action 6 report.
- **Compatibility clause**. Explains the operative clause's relationship with provisions of Covered Tax Agreements. Many of the MLI provisions overlap with provisions found in Covered Tax Agreements. In some cases, they can be applied without conflict with the provisions of Covered Tax Agreements. However, where the MLI provisions conflict with existing provisions covering the same subject matter, this is addressed by the compatibility clauses. The language in, and operation of, the compatibility clauses varies. For example, some clauses use the phrases "applies in the place of", "applies to", "modifies", or "applies in place of or the absence of". Regardless of the wording used, the compatibility clauses make it clear how the MLI modifies the existing Covered Tax Agreement. For example, Article 4(2) explains that the new Article 4(1) applies "in place of or in the absence of" an equivalent provision in a Covered Tax Agreement.
- **Reservation clause**. This defines the specific reservations parties are able to make with respect to the operative clause (for example, Article 4(3) allows parties to make five alternative reservations with respect to Article 4, and choose one optional alternative to the wording in Article 4(1)); and
- **Notification clause**. The notification clause requires parties to notify the OECD Depositary of choices of options, reservations and existing provisions in Covered Tax Agreements that are within the scope of the compatibility clause (for example, Article 4(4) requires parties to notify the OECD Depository of articles in its Covered Tax Agreements that are described in the compatibility clause and are not subject to a reservation). Notification is very important. If the notification required by an article is not completed, generally speaking, an article in a Covered Tax Agreement is not modified pursuant to the compatibility

[3] Article 4 relates to dual resident entities and, while it relates to a hybrid entity, the new provision originated in the Action 6, rather than the Action 2 report.

clause. The reason for this approach is to ensure clarity and transparency about the application of the MLI. The table below shows how the compatibility clauses and notification process work together.

<table>
<tr><th>If the compatibility clause states that the MLI provision…</th><th>Then the notification provision states that the MLI provision will apply…</th></tr>
<tr><td>applies “in place of” an existing provision of a Covered Tax Agreement, the provision is intended to replace an existing provision if one exists, and is not intended to apply if an existing provision does not exist</td><td rowspan="3">only in cases where all parties to the particular Covered Tax Agreement make a notification with respect to the existence or absence (as applicable) of a relevant provision of the Covered Tax Agreement.</td></tr>
<tr><td>“applies to” or “modifies” an existing provision of a Covered Tax Agreement, the provision of the Convention is intended to change the application of an existing provision without replacing it, and therefore can only apply if there is an existing provision</td></tr>
<tr><td>applies “in the absence of” an existing provision of a Covered Tax Agreement</td></tr>
<tr><td>applies “in place of or in the absence of” an existing provision of a Covered Tax Agreement</td><td>in all cases.

If both parties to the particular Covered Tax Agreement notify the existence of an existing provision, that provision will be replaced by the MLI provision (to the extent described in the relevant compatibility clause).

If the parties to a particular Covered Tax Agreement do not notify the existence of a provision, the MLI provision will still apply. If there is a relevant existing provision which has not been notified by all parties, the MLI provision will override that existing provision if it is incompatible with the relevant MLI provision. If there is no existing provision, the MLI provision will in effect be added to the Covered Tax Agreement.</td></tr>
</table>

2.22 For a more detailed discussion on how these provisions operate, see paragraphs 13 to 18 of the OECD’s Explanatory Statement (see paragraph 2.5 for details).

Arbitration – Part VI (Articles 18 to 26)

2.23 This Part of the MLI was developed by a separate OECD Sub-Group on Arbitration. Its structure differs from that described above in respect of Parts II to V. Generally speaking, it allows parties to insert an entirely new framework for dispute resolution through mandatory binding arbitration.

2.24 It requires parties to "opt-in" to the arbitration provisions by notifying the OECD Depository that it wishes to apply Part VI, rather than "opting-out" by making a reservation.

2.25 It has a single compatibility clause for the entire Part in Article 26, rather than article-by-article compatibility clauses. It also allows parties to make bespoke reservations as to the scope of arbitration, subject to acceptance by DTA partners (rather than the set of defined reservations permitted under Parts II to V).

2.26 For Parts I to VI, the OECD will maintain a public list of reservations, choices of options and affected Covered Tax Agreement provisions to assist all interested parties to determine how Covered Tax Agreements are modified.

2.27 Once the MLI comes into effect for a particular Covered Tax Agreement (explained further in chapter 3), the MLI will operate as a stand-alone treaty that modifies the Covered Tax Agreement according to its terms.

CHAPTER 3

How the multilateral instrument provisions will address BEPS concerns

3.1 As discussed in chapter 2, the MLI's substantive provisions fall into two categories: minimum standards and optional provisions. These provisions to address BEPS concerns in four key areas, which are summarised at a high level in the table below. Generally speaking, New Zealand intends to adopt the minimum standards and optional provisions.

3.2 Further detail of each provision and New Zealand's approach is provided in the table in the appendix.

Substantive BEPS provisions	**Minimum standard?**
Preventing the granting of treaty benefits in inappropriate circumstances (for example, treaty shopping) This will be achieved primarily by inserting a "principal purpose test" (PPT) or equivalent provision into Covered Tax Agreements. The PPT is a treaty anti-abuse rule similar to our domestic law general anti-avoidance rule (GAAR) and New Zealand intends to adopt the PPT. This corresponds to Action 6 of the BEPS Action Plan.	Yes
Preventing the artificial avoidance of permanent establishment status Unless a multinational's activity in a jurisdiction reaches a sufficient threshold level known as a PE, that jurisdiction cannot tax any business profits made by that multinational. If a multinational is able to avoid having a PE in a jurisdiction, then it can avoid paying tax on its profits in that jurisdiction. DTAs contain the definition of a PE and this needs to be strengthened to prevent entities structuring around it. This corresponds to Action 7 of the BEPS Action Plan.	No
Neutralising the effects of hybrid mismatch entities These arrangements allow multinationals to structure their commercial arrangements to pay little or no tax by arbitraging the different domestic law treatment of certain instruments and entities between jurisdictions. For example, one jurisdiction may see income as being derived by a partnership as an entity, whereas another jurisdiction may treat that income as being derived directly by the underlying partners (that is, they disregard or look-through the partnership). The changes implemented through the MLI complement the domestic law changes outlined in the recently released officials' issues paper on hybrid mismatch arrangements. This corresponds to Action 2 of the BEPS Action Plan.	No

Substantive BEPS provisions	Minimum standard?
Providing improved mechanisms for effective dispute resolution This is a taxpayer-friendly measure allowing for mandatory binding arbitration of disagreements between competent authorities (CAs). It recognises the fact that measures to counter BEPS should not lead to unnecessary uncertainty for compliant taxpayers and to unintended double taxation. Improving dispute resolution mechanisms is therefore an integral component of the work on BEPS issues. The changes in the MLI will improve the MAP – which allows taxpayers to ask the CAs of each treaty partner to agree the correct interpretation and application of a DTA in a particular case – and will also allow the taxpayer to refer the case to an independent arbitrator (or panel of arbitrators) if the CAs cannot agree on the correct treaty position. This corresponds to Action 14 of the BEPS Action Plan.	Yes (in respect of MAP only, arbitration is optional)

CHAPTER 4

Implementation and entry into effect

Signature and ratification

4.1 The MLI will be signed by a number of participating jurisdictions in June 2017. At the time of signature, a list of reservations, notifications and choices will be provided to the OECD Depository.[4] Jurisdictions will also be able to sign up to the MLI at a later date.

4.2 After signing, the MLI will need to go through New Zealand's domestic treaty-making process. This will be the same process as for DTAs and amending protocols. Recent amendments to section BH 1 of the Income Tax Act 2007 – the empowering provision for New Zealand's DTAs – make it clear that multilateral agreements can be implemented under this section.

4.3 This treaty-making process will involve the tabling of the MLI and a national interest analysis (NIA) in the House of Representatives for treaty examination. Following consideration by Select Committee, an Order in Council will be submitted to Cabinet for approval and once this is in force, New Zealand will formally ratify the MLI by submitting an instrument of ratification to the OECD Depository. At the time of ratification, New Zealand must confirm its list of reservations, notifications and choices.

4.4 After this point in time, jurisdictions are able to add new DTAs as Covered Tax Agreements and withdraw their reservations (or enter more limited reservations), but are unable to enter new reservations. The effect of this is that, following ratification, New Zealand (and other) jurisdictions can expand, but not narrow, the application of the MLI to their DTA network.

Entry into force

4.5 The MLI will enter into force generally (in its own right) and for the states that have ratified it, three to four months after the fifth jurisdiction has ratified the MLI.

4.6 For each jurisdiction ratifying the MLI after it has entered into force, it will enter into force three to four months after that jurisdiction deposits its instrument of ratification.

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[4] The notification process is very important as the operation of many of the articles of the MLI turn on notification. To facilitate the notification exercise, the OECD is hosting a meeting in February 2017 to enable jurisdictions to ensure their bilateral notifications match.

4.7 This entry into force does not mean that a jurisdiction's Covered Tax Agreements are modified by the MLI at this point in time. For a specific Covered Tax Agreement to be modified by the MLI, the MLI must have come into effect for that Covered Tax Agreement.

Entry into effect for a specific Covered Tax Agreement

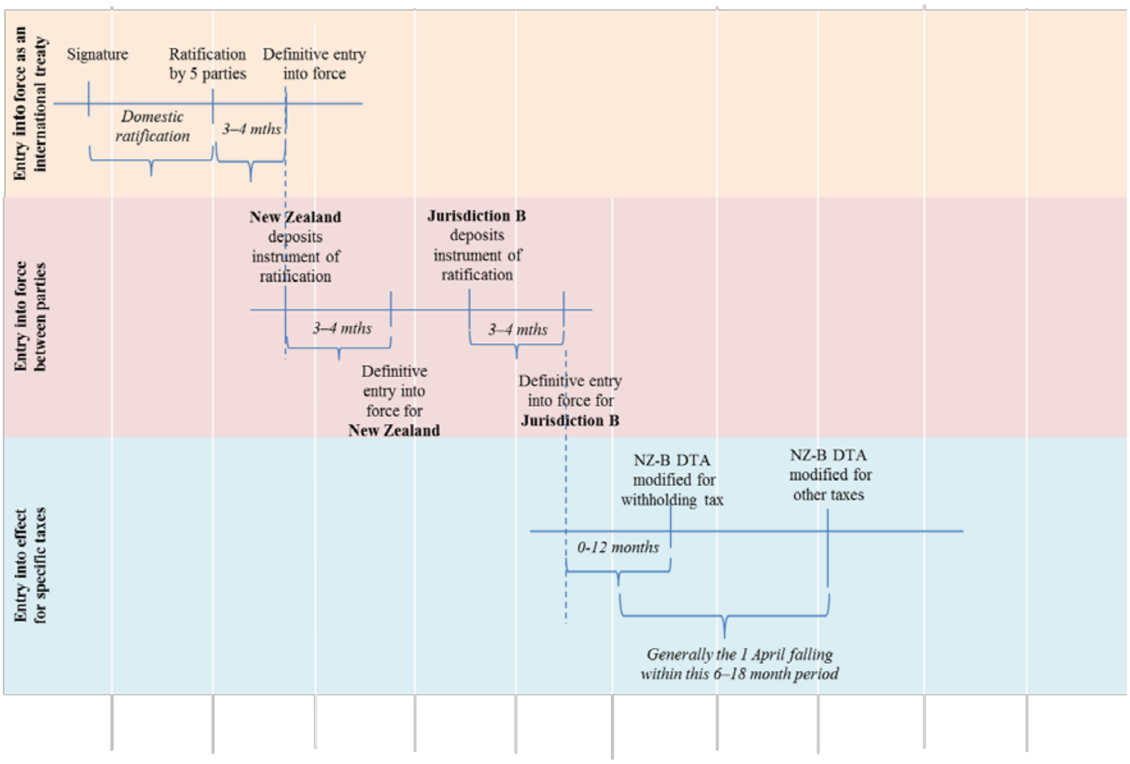
4.8 The MLI will enter into effect to modify each bilateral DTA, on a phased-in basis, once both parties to the DTA have signed and ratified the MLI.

4.9 For withholding tax, it will apply where the event giving rise to the tax occurs on or after 1 January of the next calendar year beginning on or after the latest date on which the Convention enters into force for each of the parties to the Covered Tax Agreement.

4.10 For income tax, it will apply to taxable periods (in New Zealand's case, income years) beginning on or after a 6 month period from the latest date on which the Convention enters into force for each of the parties to the Covered Tax Agreement.

4.11 The example below illustrates the theoretical timeline for how the entry into force and effect could work for a DTA between New Zealand and Jurisdiction B.

Multilateral instrument entry into force and entry into effect for New Zealand–Jurisdiction B DTA



4.12 While the precise dates on which New Zealand's DTAs will begin to be modified are unknown, it is likely that the earliest modifications will occur in 2019.

4.13 Part VI (Arbitration) will generally apply to cases presented to Competent Authorities (CAs) on or after the latest date on which the MLI enters into force for each of the parties to the Covered Tax Agreement. By mutual agreement, jurisdictions can agree to submit a case to arbitration that was presented to the CAs prior to this time.

Notification of entry into effect for specific Covered Tax Agreements

4.14 As each jurisdiction submits its instrument of ratification to the OECD Depository, New Zealand will be notified. When the MLI comes into force for each of New Zealand's DTAs the Government will announce the fact.[5] This is to advise taxpayers that the DTA has been modified.

Domestic law changes

4.15 Some domestic law changes may be needed to facilitate the modifications to New Zealand's DTAs by the MLI.

4.16 For example, officials anticipate there may need to be some amendments to the dispute procedures in Part 4A of the Tax Administration Act 1994 to enable cases to be submitted to arbitration without prejudicing taxpayer rights under the domestic law.

4.17 Officials are interested to receive submissions on these and other aspects of domestic law that may need to be similarly amended.

Consolidated versions of DTAs

4.18 The Government will not be producing consolidated versions of each DTA modified by the MLI. This is consistent with existing practice for amending protocols. Commercial publishers are likely to produce consolidated versions.

Submissions points

We are interested to hear from readers:

- Are there any significant implementation issues the Government should consider in adopting the MLI?
- What practical options exist to minimise uncertainty and compliance costs associated with New Zealand adopting the MLI?
- What domestic law changes may be needed to facilitate the implementation of the MLI?

[5] Published at http://taxpolicy.ird.govt.nz

APPENDIX

Substantive BEPS provisions in the multilateral instrument

BEPS measure	Detail	Minimum standard	Should NZ adopt?
1. Neutralising the effects of hybrid mismatch arrangements that have a treaty aspect (Action 2 report)	**Fiscally transparent entities** The MLI introduces or amends a fiscally transparent entity (FTE) provision. FTEs (like trusts or partnerships) create arbitrage opportunities because they are treated differently for tax purposes by different countries. The MLI provision clarifies that treaty benefits will only be allowed to the extent to which the item of income is taxed in the state in which the entity is resident. New Zealand already includes this provision (or an equivalent provision) in its DTAs with Australia, United States, Chile and Japan. *Article 3 of the MLI*	No	Yes
	Dual resident entities The MLI introduces or amends a dual resident entity (DRE) tie breaker provision. Like FTEs, DREs can be used to take advantage of arbitrage opportunities. The proposed provision will require CAs to agree the residence status of a DRE and the DRE will only be entitled to such treaty benefits as the CAs agree. *Article 4 of the MLI*	No	Yes
	Relief of double taxation The MLI allows countries to strengthen their application of the exemption method to relieve double taxation. New Zealand already applies the (more robust) credit method in all of its DTAs, and therefore proposes not to adopt any of the options. *Article 5 of the MLI*	No	Not applicable
2. Preventing the granting of treaty benefits in inappropriate circumstances (Action 6 report)	**Preamble language – minimum standard** The MLI will amend the preamble to DTAs to emphasise that as well as aiming to relieve double taxation, the treaty also aims to prevent opportunities for non-taxation, reduced taxation or tax avoidance. *Article 6(1) and (2) of the MLI*	Yes	Yes
	Preamble language – optional amendment The MLI allows countries to adopt the following optional amendment to the preamble to DTAs: "Desiring to further develop their economic relationship and to enhance their co-operation in tax matters," *Article 6(3) and (6) of the MLI*	No	Yes

BEPS measure	Detail	Minimum standard	Should NZ adopt?
	Treaty anti-abuse rules The MLI requires jurisdictions to introduce an anti-abuse rule into DTAs. Jurisdictions can meet this minimum requirement in one of three ways: 1. a principal purpose test (PPT) alone; 2. a PPT plus a "simplified limitation on benefits" (LOB) clause. The LOB is a mechanical provision that seeks to identify, through a series of black-letter tests, whether a person is genuinely entitled to the benefits of a DTA; or 3. enter into bilateral negotiations to include a detailed LOB provision plus a PPT or anti-conduit rules. In the case of New Zealand, officials' favour adopting a PPT alone. The PPT is very similar to New Zealand's domestic law GAAR and will deny treaty benefits if the principal purpose of an arrangement was to secure those benefits. Also, in officials' view, it generally covers the same treaty shopping issues as the alternative approaches. *Article 7 of the MLI*	Yes	Yes
	Dividend transfer transactions The MLI introduces a provision that requires shares to be held for a minimum of 365 days for the shareholder to be entitled to the reduced withholding tax (WHT) rates on dividends. This is to stop shareholders buying shares temporarily to access the reduced WHT rates and then immediately selling them. *Article 8 of the MLI*	No	Yes
	Land rich company rules The MLI introduces a treaty provision that strengthens the anti-abuse "land-rich company" test (land rich companies are companies whose assets are mainly land). Some treaties do not contain this provision at all, so the MLI also allows it to be inserted into those treaties. The new rule reinforces the position that the source jurisdiction can tax land held by non-resident owners in the other jurisdiction through corporate vehicles. To prevent artificial and temporary dilution of the amount of land held by a company just before sale, the MLI provision requires the threshold for the amount of land ownership which triggers the rule to be measured on every day in the 365 day period leading up to the sale of the shares. The MLI provision also ensures the same rule applies to other investment vehicles such as partnerships and trusts. *Article 9 of the MLI*	No	Yes

BEPS measure	Detail	Minimum standard	Should NZ adopt?
	Third-state PE rules The MLI introduces a treaty provision that denies treaty benefits in the case of income derived by a PE of a resident of one of the parties to the DTA, where that PE is situated in a low tax third-state. *Article 10 of the MLI*	No	Yes
	Right to tax own residents The MLI introduces a provision that preserves a jurisdiction's right to tax its own residents (for example, this prevents New Zealand residents engaged in a tax avoidance arrangement claiming a DTA prevents New Zealand from using the domestic law GAAR to impose tax). *Article 11 of the MLI*	No	Yes
3. Preventing the artificial avoidance of PE status	**Commissionaire arrangements and similar strategies** Currently, a number of artificial structures including the civil law concept of a "commissionaire" can be used to avoid having a PE in a jurisdiction. A new provision will deem non-residents using these structures to have a PE in the jurisdiction. *Articles 12 and 15 of the MLI*	No	Yes
	Specific activity exemptions – preparatory and auxiliary qualification Certain specific activities carried on in a jurisdiction are deemed **not** to constitute a PE (for example, premises used for simply storing goods or stock maintained for display or delivery). These specific carve-outs from the PE definition allowed quite substantial economic activities to fall within them. The MLI proposes clarifying that the specific carve-outs listed in the DTA must be subject to an additional requirement that they be "preparatory and auxiliary" in nature. There are two options for dealing with this issues – Option A (which New Zealand favours) which subjects all of the existing specific activities to an explicit "preparatory and auxiliary" test, and Option B, which does not subject the specific activities to the "preparatory and auxiliary" test (because these activities are considered to be inherently preparatory and auxiliary in nature), but subjects any other activity or combination of activities to the "preparatory and auxiliary" test. *Articles 13 and 15 of the MLI*	No	Yes
	Specific activity exemptions – Anti-fragmentation rule The MLI introduces an "anti-fragmentation" rule that will prevent an enterprise from dividing up all of its activities so that related parties each carry on a separate part of the business (that fall within the PE exceptions), but taken together they constitute a PE. *Articles 13 and 15 of the MLI*	No	Yes

BEPS measure	Detail	Minimum standard	Should NZ adopt?
	Anti-contract splitting rule Currently a construction, installation or building project does not constitute a PE unless it last for more 12 months. Entities were abusing this 12 month limit by having back-to-back 12 month contracts so they never exceeded the 12 month threshold. Generally the contracts were undertaken by different companies within the same group of companies. The new an "anti-contract splitting" rule will aggregate related projects to prevent PE avoidance. *Articles 14 and 15 of the MLI*	No	Yes
4. Providing improved mechanisms for effective dispute resolution	**MAP – access to the CAs of either jurisdiction** In covered tax agreements that do not already have it, the MLI will introduce a provision allowing taxpayers to request mutual agreement procedure (MAP) in cases where they believe taxation is not in accordance with the treaty. If a MAP provision is already contained in a DTA, the MLI will amend it to allow taxpayers to approach the CA of *either* jurisdiction to resolve uncertainty as to how the DTA applies (New Zealand's DTAs currently contain MAP provisions, but taxpayers are only entitled to approach the CA of the jurisdiction of which they are a resident). *Article 16 of the MLI*	Yes	Yes
	MAP – corresponding adjustment Requires contracting states to make appropriate corresponding adjustments in transfer pricing cases. *Article 17 of the MLI*	No	Yes
	Arbitration If, under the MAP process, the CAs do not agree on the correct interpretation of the DTA, the CAs can submit the matter to an independent arbitrator (or a panel of three arbitrators) for decision. The arbitrators will decide which of the CAs is correct. The CAs are generally bound by the decision of the arbitrators, but the taxpayer is not. Therefore, the taxpayer could pursue a court case if it disagrees with the arbitrators' decision. New Zealand's approach is to adopt what is referred to as "final offer" or "last best offer" arbitration (in Article 23(1)), but to accept "independent opinion" arbitration if the other party to the Covered Tax Agreement chooses this (by entering a reservation under Article 23(2)). In the case of "independent opinion" arbitration, New Zealand will adopt Article 24(2) and (3) which means that the arbitrators' decision will not be binding on the CAs if they come to an alternative resolution of all unresolved issues within 3 calendar months of the delivery of the arbitrators' decision. New Zealand also proposes to require undertakings of confidentiality by all parties involved in arbitration (Article 23(5)) and reserves the right not to include arbitration provisions in Covered Tax Agreements with jurisdictions that do not require the same (Article 23(6) and (7)). New Zealand intends to enter a free form reservation in respect to arbitration to carve out cases that involve the application of New Zealand's general anti-avoidance rule contained in section BG 1 of the Income Tax Act 2007. *Articles 18 – 26 of the MLI*	No	Yes