International and EU Tax Multilateralism:

Challenges Raised by the MLI

Editor: **Ana Paula Dourado**

IBFD

International and EU Tax Multilateralism: Challenges Raised by the MLI

Why this book?

This book on international tax multilateralism is composed of 11 chapters, which comprehensively discuss the meaning of multilateralism in international taxation from various complementary perspectives, as well as the impact of the base erosion and profit shifting project (BEPS Project) in the move towards international tax multilateralism. The insightful research on the topics now published started in preparation for the 13th GREIT Conference held in Lisbon in 2018.

In order to assess international tax multilateralism, the book focuses on the OECD Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI), the Inclusive Framework, as well as on EU multilateralism.

The reader will find a thorough and ground-breaking analysis on the following subjects: formal versus substantial multilateralism; the features and challenges of the MLI; the obligations of MLI non-signatories within the Inclusive Framework, interpretation of the MLI and implementation issues; whether multilateralism is the purpose of the EU and TFEU Treaties and EU multilateralism, tax good governance, and its development policy; specific MLI regimes; and multilateral dispute resolution mechanisms.

The comprehensive research and complementary angles of analysis published in this volume make for essential reading on the issue. The book is addressed to academics, state, international and EU institutions, and practitioners dealing with the MLI and EU multilateral fiscal policies, and the intricate interpretation challenges they raise.

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Introduction

International Tax Multilateralism or Reinforced Unilateralism?

Ana Paula Dourado

0.1. Multilateralism vs unilateralism

This book on international tax multilateralism comprehensively discusses the meaning of multilateralism in international taxation from various complementary angles, as well as the impact of the base erosion and profit shifting project (BEPS Project)[1] in the move towards international tax multilateralism. The insightful research on the topics now published, started in preparation for the 13th GREIT Conference held in Lisbon in 2018.

The book focuses on the OECD Multilateral Convention (MLI),[2] and the Inclusive Framework, as well as on EU multilateralism, from various legal and policy angles: formal versus substantial multilateralism; the features and challenges of the MLI; the obligations to MLI non-signatories within the Inclusive Framework, interpretation of the MLI and implementation issues; whether multilateralism is the purpose of the EU and TFEU Treaties; EU tax good governance, and its development policy; specific MLI regimes; and multilateral dispute resolution mechanisms.

The subject of international tax multilateralism gained prominence in the second decade of the 21st century, in the aftermath of the 2008 financial crisis, first as an attempt to achieve worldwide tax transparency, later as a further step to achieve tax coordination.

International tax multilateralism, as has been interpreted by the G20/OECD and the Inclusive Framework,[3] is not equivalent to a superposed state or to international tax justice, but it possibly aims at the single tax principle (as has been claimed), and some coordination on minimal taxation in the jurisdiction where value is created.

1. http://www.oecd.org/tax/beps/beps-actions/
2. *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting*, signed on 7 June 2017.
3. https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf

It has been claimed that the BEPS Project leaves room for tax planning and further tax competition. However, there is also a risk, broadly acknowledged, that international tax multilateralism, as interpreted by the BEPS Project, the multilateral convention with its openness to reservations and opt-outs, and the subsequent OECD work on taxation in the digital economy[4] results in more legitimacy for the overlapping of residence, source and market state taxation. Overlapping (international double taxation) increases (and legitimizes) unilateralism and discrimination against taxpayers with cross-border activity and income, instead of promoting multilateralism.

This risk is an outcome of the primary focus on recapturing states' taxing rights and the fight against aggressive tax planning. There is certainly legitimacy in the aforementioned effort to recapture states' taxing rights, as the state is the only or main instance for promoting redistribution, and therefore tax justice.

However, this role does not – and should not – legitimize state discrimination against taxpayers engaged in international activity. International tax multilateralism should therefore and instead focus primarily on the taxpayer, as a global player, and acknowledge his mobility rights. Focusing on the taxpayer and on the fundamental right to cross-border activity would lead to an efficient and fair international tax system. This practice could be inspired by the European Union fundamental freedoms or the US constitutional commerce clause.

Mobility rights cannot be interpreted as the right to discriminate against immobile taxpayers, though. Whereas non-discrimination between mobile and immobile taxpayers seems intuitively obvious, tax competition and the corresponding fight against aggressive tax planning seem to neglect the fact that international tax justice starts with an acknowledgment of taxpayers' rights and freedoms.

The single tax principle[5] narrows its scope by focusing on mobile taxpayers and their rights. This principle plays a role in international tax justice

4. https://www.oecd-ilibrary.org/docserver/9789264293083-en.pdf?expires=1588945962&id=id&accname=guest&checksum=E42411A0425C723B70131CFD3B1955D4; https://www.oecd.org/tax/beps/public-consultation-document-secretariat-proposal-unified-approach-pillar-one.pdf; https://www.oecd.org/tax/beps/public-consultation-document-global-anti-base-erosion-proposal-pillar-two.pdf.pdf.

5. R. S. Avi-Yonah, *Full Circle? The Single Tax Principle, BEPS, and the New US Model* (October 13, 2015), 1 Global Tax'n 12, U of Michigan Public Law Research Paper No. 480, U of Michigan Law & Econ Research Paper No. 15-019 (2016), available at SSRN: https://ssrn.com/abstract=2673463 or http://dx.doi.org/10.2139/ssrn.2673463.

when linked with a two-fold acknowledgment: (i) an acknowledgment of the taxpayers' fundamental right (freedom) to choose how to organize their activity (whether domestically or cross-border) without being discriminated against; and (ii) an acknowledgment of the states' right not only to tax, i.e. be granted allocation of taxing rights, but also to fight against aggressive tax planning. The latter is a necessary condition for the state to ensure the taxpayers' fundamental rights and its redistributive function.

Interpreted in this way, the single tax principle and international tax justice require multilateralism, and the latter requires the aforementioned two-fold approach. The substance of international tax multilateralism should then lie in a non-discrimination principle between mobile and immobile taxpayers and investment without forgetting that redistribution is one of the main states' budgetary functions, and in the current international tax system, redistribution is a function played by the state.

This efficient and fair international tax system can be achieved by a multilaterally acknowledged, balanced and consistent allocation of taxing rights, with the taxpayer as the beneficiary.

The MLI has merely granted states leeway to fight against aggressive tax planning, but the fact that multilateral binding measures are minimal increases tax competition and endangers multilateralism.

0.2. In this book

In the first chapter of this book, Ricardo García Antón discusses the meaning of substantive multilateralism, and analyses the characteristics of the MLI and whether it fulfils the conditions of such a concept.[6]

The author notes that substantive multilateralism is a normative symbolic aspiration for universal and binding rules, with the purpose of overcoming partial and fragmentary bilateral arrangements.[7]

According to the author, the assessment of the MLI in light of substantive multilateralism requires consensus on (i) whether it is heading towards customary international law; (ii) whether the flexibility of the MLI jeopardizes the consensus achieved; and (iii) whether the consensus achieved in

6. R. García Antón, *Substantive Multilateralism in the Context of the MLI*, ch. 1.
7. Id., at sec. 1.3.

its approval of the four minimum standards (the fight against harmful tax practices, Action 5; prevention of treaty shopping, Action 6; country-by-country reporting, Action 13; and improving dispute resolution, Action 14) is enough to protect the MLI against interference.[8]

García Antón concludes that the MLI is meaningful in the shift from bilateralism towards multilateralism; that it reaches a formal dimension "meeting of several governments"; that its substantive concept is anchored in building on its constituent elements, and therefore, that the MLI is still at an embryonic stage in the long process towards the achievement of customary international law on anti-avoidance. The main reasons for his conclusion lie in the flexibility of the system, which allows for the introduction of numerous reservations, and the lack of binding arbitration.[9]

Frans Vanistendael, in the second chapter of this book ("Is there a Role for Multilateralism Regarding the Euro in the EMU?"),[10] notes that the European Union is not characterized in the treaties as a multilateral relationship but as a separate supranational legal order. However, having examined the European and Monetary Union, Vanistendael is inclined to conclude that multilateralism characterizes the European Union. According to the author, although article 1(2) of the Treaty on European Union (TEU) provides the basis for a political union among the peoples of Europe, the conditions for managing a common currency demonstrate that the Lisbon Treaty functions like a multilateral arrangement, as Member States retain their sovereign power on decision-making.[11]

Whereas multilateralism within the international tax system suggests an improvement of the system, Vanistendael sees EU multilateralism as an indicator of the Union's weakness and deficiencies.[12]

Vanistendael highlights deficiencies in the decision-making process, the absence of a common economic approach for the currency union and of a separate and independent budget, and non-application of the "no taxation without representation" principle.

8. Id., at secs. 1.1.-1.3.
9. Id., at sec. 1.5.
10. F. Vanistendael, *Is there a Role for Multilateralism Regarding the Euro in the EMU?*, ch. 2.
11. Id., at secs. 2.1.-2.2.
12. Id., at sec. 2.3.

He therefore proposes:
– replacing the European Monetary System (EMS) with a European Monetary Fund (EMF);
– completing the setting up of a banking union;
– reforming the European Central Bank into an effective lender of last resort;
– establishing a central Euroland authority for economic policy subject to European parliamentary control;
– establishing a separate and independent euro budget;
– financing this separate and independent euro budget by uniform, separate and independent euro taxes; and
– reforming the decision-making process to provide for the "no taxation without representation" principle.[13]

Richard Lyal, in "The EU and Tax Good Governance in a Multilateral Environment",[14] claims that multilateralism is a central idea of the EU's development policy, given its natural role in the Union's efforts. The author then focuses on tax good governance as an element of the Union's external relations. Lyal first states the principles that should underpin tax policy aimed at reaching the desired level of tax revenue, and the relationship between tax authorities and the taxpayers.

He then addresses the international dimension of EU tax good governance – the necessity for cooperation, confidence and honesty; and the major issues for developing countries, such as capital flight and illicit financial flows – and notes the 2009 Communication on good governance in tax matters (whose elements include transparency, cooperation on the exchange of information and fair tax competition).[15] He also analyses the existing initiatives on tax good governance with third countries, including state aid clauses, technical assistance, a coordinated response to tax havens, common principles of cooperation and transparency, and international tax initiatives such as country-by-country reporting.[16]

Although Lyal judges the EU's external tax policy a "positive story", he contends that some Member States are failing to adequately address harmful

13. Id., at sec. 2.5.1.
14. R. Lyal, *The European Union and Tax Good Governance in a Multilateral Environment*, ch. 3.
15. Id., at secs. 3.1.-3.2.
16. Id., at secs. 3.2.-3.3.

tax competition, and that the promotion of tax transparency to third countries reveals, to a certain extent, EU self-interest.[17]

Paolo Arginelli, in "Binding Coordination in the EU: Status Quo and Ideas for a Bright Future",[18] recommends a Directive on the allocation of taxing rights among Member States that would improve the current situation and shift the competence to conclude tax treaties with third countries.

He analyses the current situation and the impact of the BEPS Project on national and EU law, namely the Anti-Tax Avoidance Directive (ATAD), taxation of the digital economy, and the common consolidated corporate tax base (CCCTB). Arginelli analyses possible conflicts between ATAD 2[19] (and its anti-hybrid rules) and previously concluded treaties, and puts forward some suggestions on eliminating cross-border juridical double taxation.[20]

Rita Szudoczky and Daniel Blum in "Multilateral Instrument Signatories and the Inclusive Framework" define the MLI as "a multilateral treaty which includes both substantive and procedural provision and which is aimed at amending existing bilateral tax treaties, the number of which reaches more than three thousand".[21]

Their article aims at determining to what extent the obligations imposed on the signatories and parties to the MLI express a multilateral facet of the MLI, and focuses on the technical questions arising from the novel interplay of multilateral and bilateral instruments (covered tax agreements), and on the identification of substantive obligations accruing from the signatories to the MLI.[22]

The authors criticize the MLI's conservative nature on the basis that its main purpose is the modification of existing bilateral treaties, which essentially preserves the bilateral nature of international tax relations. They highlight its ambivalence, namely, its multilateral character for the sake of efficiency

17. Id., at sec. 3.4.
18. P. Arginelli, *Binding Coordination in the European Union: Status Quo and Ideas for a Bright Future*, ch. 4.
19. Id., at sec. 4.2.
20. Id., at secs. 4.3.-4.4.
21. R. Szudoczky & D. Blum, *Unveiling the MLI: An Analysis of its Nature, Relationship to Covered Tax Agreements and Interpretation in Light of the Obligations of its Parties*, sec. 5.1.
22. Id., at sec. 5.2. et seq.

combined with its novelty (of being multilateral) and potential for future reforms.[23]

Given that there is no multilateral commitment, and that the MLI's objective is merely to implement the tax treaty-related BEPS recommendations, the MLI does not qualify as multilateral in substance. Moreover, Szudoczky and Blum note that according to article 2(2) of the MLI, an undefined term therein should be interpreted by reference to the covered tax agreement (CTA). This means that both the MLI and the CTA have the same legal value. In light of the Vienna Convention on the Law of Treaties (VCLT), the MLI simply adds an additional layer of interpretation, losing all its strength as a multilateral instrument in substance.[24]

Luís Eduardo Schoueri and Guilherme Galdino, in their chapter "Obligations to MLI non-signatories within the Inclusive Framework",[25] highlight the (lack of) participation of developing countries in the BEPS Project. They make reference to the meeting in September 2014, when the G20 finance ministers and Central Bank governors met in Cairns, Australia, and agreed on the need for more engagement from development countries.[26]

The authors criticize the fact that most of the BEPS minimum standards had been determined before the establishment of the Inclusive Framework, and claim that the major challenges for developing countries do not coincide with the BEPS minimum standards. As source countries, their viewpoint differs from that of OECD jurisdictions, and the BEPS Project raises fairness issues between residence and source countries.[27]

The authors put forward some priorities for developing countries and list some of the deficiencies of the BEPS Project, such as the trade-off between the need to address preferential tax regimes on the one hand, and to attract foreign direct investment on the other, noting moreover that while transfer pricing is a top priority for Asian countries, it is not satisfactorily addressed in the BEPS Project.[28]

23. Id., at sec. 5.2.2.
24. Id., at secs. 5.2.-5.3.
25. L.E. Schoueri & G. Galdino, *Obligations to MLI non-signatories within the Inclusive Framework*, ch. 6.
26. Id., at sec. 6.2.
27. Id., at secs. 6.2.2.-6.2.3.
28. Id., at sec. 6.2.3.

Schoueri and Galdino further criticize the amount of resources required to implement the BEPS Project; its lack of fairness, as it does not re-examine the allocation between residence and source countries; and the BEPS Project's complexity in combination with the lack of technical resources in developing countries.[29] The authors then examine the monitoring process and complexity of the implementation of the minimum standards of Action 6.[30]

Rainer Prokisch and Fernando Souza de Man's chapter addresses the interpretation of the MLI and implementation issues.[31] They note that the MLI as well as bilateral tax agreements are subject to the interpretation provisions in the VCLT.[32]

Among other things, they stress that since tax treaties do not change automatically with the MLI, the degree to which a specific tax treaty is amended by the MLI is up to the interpreter. Furthermore, due to opt-outs and reservations, the MLI may also be used for tax policy purposes. The authors claim that states that have made extensive reservations on the MLI provisions should consider developing their own treaty policy and renegotiate unamended treaties.[33]

With respect to interpreting the MLI, the authors contend that it is not a subsequent agreement in terms of article 31(3)(a) of the VCLT. The MLI's purpose is not to deal with the interpretation of the covered tax agreements (CTA). Moreover, the MLI's general purpose of dealing with tax evasion, avoidance and double non-taxation is not sufficient to prevent the granting of tax treaty benefits. There is a need to clarify that tax treaties are now part of the fight against aggressive tax planning.[34]

One of the particularities of the MLI is that countries may introduce provisions in their CTA but those provisions remain independent parts of the MLI. There is a parallel effect, whereby the MLI's terms are part of the context of both the MLI and the CTA. Prokisch and de Man also claim that the MLI is not similar to an amending Protocol signed by treaty partners in

29. Id., at secs. 6.2.3.-6.3.
30. Id., at sec. 6.4.3.
31. R. Prokisch & F.S.de Man, *Multilateralism and International Tax Law: The Interpretation of Tax Treaties in Light of the Multilateral Instrument*, ch. 7.
32. Id., at sec. 7.1.
33. Id., at sec. 7.1.
34. Id., at secs. 7.1.-7.2.

order to change the existing treaty, since the OECD aims at a simultaneous application of existing tax treaties and the MLI.[35]

Cécile Brokelind reflects on "The Multilateral Instrument and Asymmetric Choices under Articles 12-15 on the Permanent Establishment Threshold Purpose".[36] She is also sceptical about substantial multilateralism in the MLI, and demonstrates that source taxation remains subject to a symmetric application of the text, and therefore, the determination of the permanent establishment (PE) threshold remains technically bilateral. The author acknowledges, however, a multilateral effort to define common notions, such as the "commissionaire agreement".[37]

She then examines the impact of the MLI PE threshold in light of EU law and the fundamental freedoms. Brokelind contends that the EU discussion on the most-favoured-nation clause may be raised again, due to the asymmetric results of MLI implementation by EU Member States. And owing to the two-speed PE threshold created by this implementation, corporate taxpayers may receive different treatment depending on their place of source, i.e. depending on whether there is a more severe threshold in their place of source.[38]

Brokelind also notes that the ATAD creates an anti-mismatch rule, allowing the residence state to disregard the PE abroad for tax purposes, in case the PE state does not implement the MLI PE threshold. She further notes that the ATAD also authorizes the Member State of residence to disregard the exemption or deduction in the source state and tax the foreign income.[39]

Marcus Livio Gomes ("Implementation of the Principal Purpose Test and the Limitation on Benefit Clauses"[40]) analyses the transition from the guiding anti-avoidance principle in the pre-MLI world to the principal purpose test (PPT) included in the MLI. He analyses the guiding principle in the 2003 OECD Commentary (paragraph 9.5.), which can be used to determine the existence of abuse, noting that it could not work as an anti-avoidance rule, and refers to the controversial meaning of this paragraph.[41]

35. Id., at secs. 7.3.-7.5. et seq.
36. C. Brokelind, *The Multilateral Instrument and Asymmetric Choices under Articles 12-15 on PE Threshold*, ch. 8.
37. Id., at sec. 8.2.
38. Id., at sec. 8.3.
39. Id., at secs. 8.4.-8.5.
40. M.L. Gomes, *From the Guiding Principle to the Principal Purpose Test: Burden of Proof and Legal Consequences*, ch. 9.
41. Id., at sec. 9.2.

The author then focuses on the role played by the beneficial ownership provisions in the OECD Model Tax Convention (OECD MC) and bilateral tax treaties and examines the evolution of tax treaty policy towards a general anti-avoidance rule (GAAR). He further notes that GAARs were not a common feature of tax treaties.[42]

Gomes then engages on an analysis of similar elements and language of GAARS, such as "scheme, arrangement or transaction", "tax benefit, gain or advantage", and "purpose, motive or intent". He also analyses the attempt to replace subjective criteria with more objective tests, such as burden of proof, and the legal consequences of the PPT rule. Finally, he proposes the doctrine of "core commercial activity", or "bona fide purpose" as a balanced approach to reducing legal vagueness in the PPT rule.[43]

Błażej Kuźniacki's chapter is entitled "Implementation and Application of LOB Clauses in BEPS Action 6/MLI: Legal and Pragmatic Challenges".[44] The author focuses on the MLI's simplified limitation on benefits (LOB) clause (article 7 (8-13)), and demonstrates that it follows, to a large extent, the LOB clause in the 2016 US Model Convention, and that it has been included by some signatories to the MLI as a complement to the PPT rule.[45]

Kuźniacki's analysis aims at explaining why the MLI's LOB clause, in its function as a tool to prevent treaty abuse, has only attracted a few states. In his analysis, the author examines the LOB's scope, complexity, interrelations, asymmetry, effectiveness and discretionary application by the tax authorities. He defines the MLI's LOB clause as an anti-abuse rule aimed at addressing a large number of treaty-shopping situations based on the legal nature, ownership and general activities of residents of a contracting state. He then addresses the complexity of the clause, the stock exchange test, the ownership test and the active business test.[46]

Kuźniacki criticizes the stock exchange test as favouring large multinationals, optimistically assuming that public companies cannot be used for treaty shopping, and contends that the ownership test should be accompanied by a base erosion test. He also criticizes the discretionary powers allowing tax authorities to grant treaty benefits even if the taxpayer fails to meet the

42. Id., at sec. 9.2.
43. Id., at sec. 9.3.
44. B. Kuźniacki, *Implementation and Application of LOB Clauses in BEPS Action 6/MLI: Legal and Pragmatic Challenges*, ch. 10.
45. Id., at sec. 10.1.
46. Id., at sec. 10.3.

criteria of the objective tests under the MLI's LOB clause, as well as the LOB's ineffective and discriminatory solutions in general.[47]

Sriram Govind and Jérôme Monsenego ("Multilateralism in Dispute Resolution: Some Thoughts on the OECD Multilateral Instrument and the EU Dispute Resolution Directive"[48]) examine the dispute resolution procedures set out in the MLI and the EU Directive, their features and elements of multilateralism.

In respect of the dispute resolution mechanism in action 14 and the MLI, the authors make reference to their purpose of improving dispute resolution measures. Article 16 of the MLI is largely similar to article 25 of the OECD MC (2017) in scope, but comes with the novelty of being implemented by the covered tax agreements, as a minimum standard (access to mutual agreement procedure (MAP) and effective implementation).[49] They note that Part VI of the MLI provides for arbitration to supplement MAP in tax treaties, but only as an optional tool, and in the absence of reservations.[50] Govind and Monsenego note that the MAP does not provide for taxpayers' involvement, and does not guarantee timely solutions or the solution of disputes.[51] They then examine the whole dispute resolution procedure: the request stage, the MAP stage, the arbitration stage. They regret the MLI's failure to substantially improve the MAP, as well as the missed opportunity for setting up an international tax court.[52]

The authors also analyse the Dispute Resolution Directive,[53] and judge it a well-balanced tool that offers competent authorities a genuine means to solve disputes by mutual agreement, and can be complemented with a binding mechanism to ensure timely and effective solutions.[54] They envisage the possibility of Member States circumventing application of the Directive by enacting anti-abuse BEPS measures in their national legislation, instead of doing so in their bilateral tax treaties, and criticize the Directive's complexity and duration.[55]

47. Id., at secs. 10.3.1.-10.3.4.
48. S. Govind & J. Monsenego, *Multilateralism in Dispute Resolution: Some Thoughts on the OECD Multilateral Instrument and the EU Dispute Resolution Directive*, ch. 11.
49. Id., at secs. 11.2.1.-11.2.2.
50. Id., at sec. 11.2.1.
51. Id., at sec. 11.2.1.
52. Id., at secs. 11.2.2.-11.2.4.
53. Council Directive (EU) on tax dispute resolution mechanisms in the European Union (2017/1852), OJ L 265 of 10 October 2017.
54. Govind & Monsenego, *supra* n. 49, at sec. 11.3.
55. Id., at sec. 11.3.5.

Biographies

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Jérôme Monsenego is a full professor of international tax law at Stockholm University, and Chairman of IFA Sweden. He obtained his PhD summa cum laude and was awarded an honourable mention by the jury of the IFA Mitchell B. Carroll Prize. He has published articles in English, French and Swedish on various issues of international tax law, a book on transfer pricing, and a book on state aid. He has previously worked at PwC in Paris and in Stockholm.

Rainer Prokisch studied law at the University of Munich, Germany. After some years in practice in Germany and abroad, he became Assistant Lecturer for Public Law and Tax Law at the chair of Prof. Dr Klaus Vogel at the University of Munich, where he finished his doctoral thesis in 1992. The research underpinning his thesis focused on the issue of the powers of the German Constitutional Court in respect of the provisions of the German financial constitution. He subsequently became Deputy Head of

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