



# International Fiscal Association Joint Meeting of the Switzerland and USA Branches

## Practical BEPS Consequences Anti-Avoidance, Disclosure, Related Matters



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# Agenda

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- 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



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# BEPS Multilateral Instrument



# BEPS Multilateral Instrument (MLI)

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- 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

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- 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

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- 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

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- 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)

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- 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?





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# BEPS Action 6 – Preventing Treaty Abuse



# BEPS Action 6 – 2015 Report

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- 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

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- 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)

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- 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)

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- 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

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- 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)

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- 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



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# Swiss Tax Developments





# Swiss Tax Policy - Overview

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- 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)

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- 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)

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- 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

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- 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)

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- 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)

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- 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

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- 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)

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- 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

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- 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)

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- 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 3<sup>rd</sup> 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)

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- 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)

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- 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)

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- 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)

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- 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)

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- 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

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- 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)

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- 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



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# Update on Selected BEPS Implementation Issues



# Exchange of Rulings

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



# Country by Country Reporting

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- 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



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# U.S. Tax Reform Proposals



# President Trump's Tax Reform Proposal

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- 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

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- 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)

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- 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

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- 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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