OECD BEPS Project: Over 2,000 tax treaties to be amended by the Multilateral Convention

With more than 100 jurisdictions onboard, the signing ceremony of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS on June the 7th will bring about one of the most notable international tax law developments in recent years. We take this opportunity to recap its implications and highlight the challenges lying ahead of tax administrations and legal practitioners.

The need for a uniform instrument to counter BEPS

The introduction of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (hereinafter referred to as the "**Convention**") is a part of the combined effort of OECD and G20 to tackle base erosion and profit shifting ("**BEPS**"). In a nutshell, BEPS denotes tax planning strategies that exploit gaps and mismatches in tax rules and enable artificial shifting of profits to low or no-tax jurisdictions.

In October 2015, the OECD published the BEPS Package, a series of 15 actions that aim at equipping governments with domestic and international instruments to address systemic weaknesses that create opportunities for BEPS. The actions cover various practices, such as hybrid instrument\entity misuse or treaty shopping and propose anti-abuse solutions, inter alia guidance on CFC regimes or effective transfer pricing rules.

BEPS, being a progeny of globalization, may occur through the legal application of a vast network of international tax treaties. In fact, many BEPS strategies are designed to utilize the gaps or mismatches between these treaties. Effective implementation of the BEPS Package, therefore requires modifying existing tax treaties in line with its recommendations. But with over 3 000 tax treaties in force worldwide, the bilateral negotiations could take years and that would significantly reduce the impact and effectiveness of the BEPS actions in this regard.

With this in mind, 2016 has seen more than 100 jurisdictions involved in developing the Convention – a multilateral, international agreement intended to impact a significant number of existing tax treaties in one move. With its final text published last November, the Convention aims to prevent treaty abuse, i.e. granting of treaty benefits in inappropriate circumstances, artificial avoidance ofpermanent establishment status, as well as eliminate negative effects of hybrid mismatches. Furthermore, the Convention should improve mechanisms of tax treaty dispute resolution between the countries.

Uniformity and flexibility - are they reconcilable?

The Convention should allow for swift implementation of all tax treaty-related BEPS Actions. Moreover, being a single document it should in principle also guarantee consistency in the implementation of the BEPS action points and maintain uniformity of solutions. Nevertheless, being the result of political compromise, the Convention is also designed to allow countries some extent of flexibility in its application.

This is intended to be achieved through a complex system of notifications and reservations made by the participating countries. A particular tax treaty will be amended by the Convention only if all parties thereto notify such intention. In absence of a clear negotiation framework for the treaty parties this could mean some tax treaties shall remain outside the scope of the Convention altogether.

Furthermore, in some cases the Convention allows the countries to choose the preferable solution from amongst the options deemed to satisfy an applicable minimum standard (e.g. it provides for three alternative options for limitation of treaty benefits). If the two or more parties to a particular tax treaty choose different options, they should "endeavor to reach a mutually satisfactory solution". Unfortunately, the Convention is silent on how the "mutually satisfactory solution" should be reached, again leaving room for possible inconsistency in application and lengthy bilateral discussions.

Implications for legal advisors

The Convention will clearly add spice to the practice of international tax advisors. The Convention will not revoke or replace existing tax treaties, instead it will be applied alongside them and therefore current texts will require careful review. Familiar provisions may take on different shades read in the context of the overlying provisions of the Convention.

Moreover, the parties to revised tax treaties will be allowed to subsequently amend their wording through mutual agreement. At the same time, the publication of consolidated versions of treaties will not be prerequisite to applying the changes introduced by the Convention. In effect it may be a challenge to follow all the texts which eventually make up the actual treaty. International tax law practitioners will need to tread carefully and be fully aware of the possible inconsistencies that may arise.

Uncertain timetable

The Convention, to be signed on 7th of June, will enter into force once is ratified by five of its signatories. Unfortunately, the timetable for ratification remains uncertain at this stage, so tax and legal advisors should follow the news closely to make sure they don't miss it.

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