

CLIENT ALERT

To: Clients & Friends of the Firm
From: Robert G. Rinninsland & A. Fanny Karaman
Re: O.E.C.D. Public Discussion Draft on Preventing Treaty Abuse
Date: March 18, 2014

On March 14, 2014, the O.E.C.D. added another chapter in its fight against tax evasion by releasing a public discussion draft addressing the disallowance of treaty benefits in inappropriate circumstances. Through this draft, the O.E.C.D. follows up on its 2013 report “Addressing Base Erosion and Profit Shifting” (the “B.E.P.S. Report”) and a 2013 “Action Plan on Base Erosion and Profit Shifting” (the “2013 Action Plan”). The 2013 Action Plan contained 15 actions addressing B.E.P.S. and came with a timeline. The public discussion draft released on March 14 focuses on Action 6 (Prevent Treaty Abuse).

The released draft divides the content of Action 6 into three parts, each constituting a different section of the draft.

1. Develop Model Treaty Provisions and Recommendations Regarding the Design of Domestic Rules to Prevent the Granting of Treaty Benefits in Inappropriate Circumstances

This part of the draft addresses several anti-abuse rules, including a limitation-on-benefits provision, a “derivative benefits” provision, and a general “main purpose” provision. It contains several more specifically targeted anti-abuse rules including a replacement of the “effective place of management” test by a case-by-case analysis. The proposal also suggests changes to domestic law as a way to prevent treaties from being used to avoid provisions of domestic law.

Clearly the focus is on economic substance and business purpose in international tax planning in order to limit allegations of “tax avoidance,” “tax evasion” or “treaty shopping” labels.

2. Clarify that Tax Treaties are not Intended to be Used to Generate Double Non-Taxation

The proposal aims at clearly indicating that the purpose of the Convention is to avoid double taxation and not the creation of double non-taxation in ways not contemplated by the signatories to the treaty. It contemplates achieving this by including an anti-treaty shopping language in the title, the preamble and the introduction of the O.E.C.D. Model Tax Convention.

3. Identify the Tax Policy Considerations that, in General, Countries Should Consider Before Deciding to Enter into a Tax Treaty with Another Country

The proposal questions whether a tax treaty should be signed in the absence of double-taxation risks when a treaty doesn’t exist. Treaties are needed when domestic law does not adequately provide relief against double taxation in the country of residence, high withholding taxes exist in the country where the

income arises and willingness exists in both countries to implement the administrative assistance provisions of the treaty.

The O.E.C.D. invites public comments on the proposals released. These comments must be submitted by April 9, 2014 and commentators can be selected to speak in support of their comments by indicating that they wish to do so by April 3, 2014.

To see the entire public discussion draft, please click on the following link: <http://www.oecd.org/ctp/treaties/treaty-abuse-discussion-draft-march-2014.pdf>.

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