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The Confederation of Swedish Enterprise: Comments on the OECD Public Discussion Draft entitled "Follow up Work on BEPS Action 6: Preventing Treaty Abuse" 21 November 2014 – 9 January 2015

The Confederation of Swedish Enterprise is Sweden's largest business federation representing 49 member organizations and 60 000 member companies in Sweden, equivalent to more than 90 per cent of the private sector.

The Confederation of Swedish Enterprise is pleased to provide comments on the OECD Discussion Draft entitled "Follow up Work on BEPS Action 6: Preventing Treaty Abuse" 21 November 2014 – 9 January 2015 (hereinafter referred to as the Draft).

General Comments

The Confederation of Swedish Enterprise supports the OECD's work to prevent abuse of tax treaties. It is however important to make any new provision sufficiently targeted toward abuse in order not to negatively impact bona fide businesses. The initial and prime objective with tax treaties is and should continue to be to facilitate cross-border trade through the allocation of taxing rights between countries and to provide for mechanisms to eliminate double-taxation. By doing so, tax treaties provide certainty and eliminate major obstacles to cross border trade.

We acknowledge the time pressure in the BEPS project. However, we fear that the proposed amendments to the Model Treaty will have a major impact not only on abusive cases but also have negative effects on genuine business activities. We are seriously concerned about the lack of new guidance in the Draft, considering the added complexity and unpredictability that will follow, should these proposals be implemented.

Although the prevention of tax evasion and avoidance may be important purposes of a tax treaty, they do not constitute a prime objective, equal to the prevention of double taxation, and should not be a main objective for entering into a tax treaty.

Before entering into treaty negotiations States should carefully analyse and study relevant provisions etc. in the other country, in order to identify potential areas that could open up for treaty abuse. If countries applied this in a consistent manner as indicated in the report on the work on Action 6 (the Report), there would be fewer loopholes to exploit and thus less need for Anti-Abuse rules. This approach would minimize the impact on genuine business activities. In case of abuse treaties should be renegotiated or as a last resort terminated.

It is of utmost importance that anti-abuse rules are designed so that they have a minimum impact on genuine business operations. Consequently, we believe that perceived inappropriate behaviour is best addressed with specific and targeted anti-abuse provisions. We believe that both the proposed LOB provision and the PPT fail in this respect, since they are too general in nature and not limited to abusive situations.

In particular, anti-abuse provisions should recognize that holding, financing and investment activities are normal and legitimate business activities that should not suffer blanket exclusions from treaty protection, which seems to be the case in the proposed LOB provision. Despite numerous comments from public commentators we find, regrettably, that these issues still have not been properly addressed.

The Principal Purpose Test (PPT), previously called the Main Purpose Test (MPT), is still very wide and vague. We still have difficulty in understanding how there could be more than one principal purpose. The test should naturally focus on the principal purpose of the arrangement or transaction.

Although we find both the LOB and the PPT rule to be too far-reaching we are positive to the fact that the OECD at least has dropped the requirement to have them both in a treaty and settled for a minimum standard of either a PPT or a LOB supplemented by a restricted PPT for conduit financing arrangements.

Apart from the fact that the LOB seems overly restrictive, a number of paragraphs in the proposed LOB could also be in violation with EU law. In addition, certain provisions such as subdivision 2 c) i) B seems to relate to specific US issues and should consequently be dealt with on a bilateral basis and not be inserted into the Model Treaty.

We have limited our comments to some of the issues in the Draft.

A. Issues related to the LOB provision

1. Collective investment vehicles: application of the LOB and treaty entitlement

An indirect investment through a CIV should not be treated worse than if the investment had been made directly. Consequently, we believe it is important to provide treaty benefits for CIVs and are positive to an inclusion of a specific paragraph in the LOB that would grant CIVs treaty benefits.

With the exception of para 42, the approaches in the report on action 6 require a test to establish that a certain amount of the investors in a CIV would have been entitled to treaty benefits had they invested directly. Such an approach would impose a high

compliance burden on the CIV. Para 42 suggest that a CIV could be a qualified person if the principal class of shares in the CIV is listed and regularly traded on a recognised stock exchange. Even though this latter condition would be fairly easy to comply with, the problem is that it would only be applicable to a small portion of CIVs. Many CIVs are not traded on a stock exchange and would thus be excluded from treaty benefits.

In our opinion, a CIV should be entitled to treaty benefits if it is registered in one of the contracting states.

3. Commentary on the discretionary relief provision of the LOB rule

The Confederation of Swedish Enterprise would welcome a statement in the discretionary relief provision to ensure a prompt response from the competent authorities. A set time period of would be preferable.

4. Alternative LOB provisions for EU countries

The Confederation of Swedish Enterprise agrees that the LOB rule needs to be adapted to reflect EU law requirements.

In particular, our concern is with the prohibition of non-resident intermediaries in the ownership tests, the local stock exchange requirement in the publicly traded test and the PPT rule.

Non-resident intermediaries in the ownership tests in subdivision 2 c) (ii) and 2 e) (i) of the LOB rule:

Apart from the fact that we believe the conditions regarding intermediate owners to be too restrictive, we also are concerned that they are in violation of EU law since both provisions disqualify companies from treaty protection if they are owned by companies in the EU/EEA. In our view, the LOB should focus on testing the ultimate beneficial owner and not intermediary companies. The Confederation of Swedish Enterprise proposes to delete the reference to intermediate companies in both provisions. Under any circumstances, the provisions should at least be amended to provide for intermediate ownership within the EU/EEA.

The local stock exchange requirement in subdivision 2 c) i) a) in the LOB rule:

The local stock exchange requirement is likely to be in violation with EU law since only the stock exchange in the Contracting State of which the company is a resident is accepted, thus preventing companies to list their share on other stock exchanges in the EU. Some treaties including the one between Sweden and the US contain a list of accepted stock exchanges as suggested in para 6 of the proposed LOB. Consequently, the Confederation of Swedish Enterprise proposes that the list in para 6 a) should include every stock exchange in the EU and any other State in the EEA.

The PPT rule

In addition to the fact that we find the PPT to be vague and not sufficiently targeted on abusive cases we are also concerned that the PPT could be in violation with EU law. The Cadbury Schweppes case (C-196/04) concludes that anti-abuse legislation should only target “wholly artificial arrangements”. As currently drafted, the PPT does not seem to provide such certainty.

In our opinion, these aspects, and possibly others, definitely require analysis in light of EU law. Should the conclusion be that the provisions are in violation of EU law, a significant number of OECD members would not be able to adopt the LOB provision as it stands.

5. Requirement that each intermediate owner be a resident of either Contracting State

As indicated above, we believe that the LOB rule should focus on the ultimate beneficial owner and not intermediate companies. We fully support the comments and examples made by BIAC on this issue.

6. Issues related to the derivative benefit provision

We strongly support a derivative benefit provision in the LOB. The derivate benefit provision would extend the granting of treaty benefits to entities that are controlled by entities that are resident of a third country and that would enjoy the same treaty benefits with the contracting state in question. In such situations, there is no incentive for treaty shopping.

9. Conditions for the application of the provision on publicly-listed entities

We refer to our comments made under item 4 above.

10. Clarification of the “active business” provision

We fully support the comments and examples made by BIAC on this point.

B. Issues related to the PPT rule

12. Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT is only applied after approval at a senior level

The Confederation of Swedish Enterprise is in favour of such a requirement in order to prevent excessive use of the PPT.

13. Whether the application of the PPT rule should be excluded from the issues with respect to which the arbitration provision of paragraph 5 of Article 25 is applicable

Introducing a substantive provision such as the PPT without the possibility of mutual agreement procedures or arbitration is not acceptable. Furthermore, it is not unlikely that the Competent Authorities in many cases will be unable to reach an agreement on the application of the PPT with double taxation as the end result. Consequently, the Confederation of Swedish Enterprise strongly recommends that the application of the PPT should be under mandatory arbitration.

15. Whether some form of discretionary relief should be provided under the PPT rule

The Confederation of Swedish Enterprise is supportive of having a discretionary relief provision under the PPT rule.

16. Drafting of the alternative "conduit-PPT rule"

The provision needs clarification. The wording **"all or substantially all of that income (at any time or in any form)"** is unclear and could be interpreted too widely. At some point in time, every company will pay all or substantially all of its income to its shareholders.

We support the inclusion of examples to illustrate that the rule is not intended to apply to a company merely because that company's policy is to distribute most of its profits in the form of dividends.

C. Other issues

19. The design and drafting of the rule applicable to permanent establishments located in third States

We question the necessity of a provision like this in the Model Treaty. This topic may be of interest in relation to some countries and should naturally be carefully considered before entering into a treaty with such a country. At any rate, those situations could be solved bilaterally. In addition, we fully support the comments made by BIAC.

20. Proposed Commentary on the interaction between tax treaties and domestic anti-abuse rules

The Confederation of Swedish Enterprise supports the comments made by BIAC.

Concluding remarks

Introducing provisions like the proposed LOB and PPT will undoubtedly induce further uncertainty into the Model Treaty and make treaty application even more

difficult. Although, a number of countries have a LOB in their treaty with the United States, similar to the one proposed in The Draft, it is an entirely different matter to insert such a provision into the OECD Model, to be used on a global basis. As proposed, the LOB, apart from being very complex, seems overly restrictive and runs the risk of having a very negative impact on genuine business operations. Furthermore, some provisions seems to relate to specific US issues and it is questionable why such provisions should be included in the Model Treaty and not be dealt with on a bilateral basis.

Whereas the LOB provision is technically complex, it leaves less room for subjective and arbitrary assessments and provides for some certainty. The PPT on the other hand takes the opposite approach. It does not provide much guidance with respect to when the treaty benefits will be granted. Instead, it opens a door for tax administrations to disqualify taxpayers from treaty benefits where that tax administration finds it appropriate. The problem with the PPT is not its complexity. Rather, our concern lies with the fact that it is very subjective and leaves significant room for arbitrary assessments.

Considering the fact that a large number of OECD countries are also members of the EU, we are, however, pleased that the OECD has acknowledged the fact that the LOB needs to be compliant with EU law. As indicated in our comments, we believe that the same is also relevant in relation to the PPT rule. We are, however, very disappointed that a proper analysis ensuring EU law compliance has still not been undertaken.

In view of the implications of introducing these new provisions in the Model Treaty we had expected the Draft to provide more guidance in relation to the issues still to be resolved. As currently drafted, the provisions could seriously undermine the certainty and predictability needed for investment decisions and also lead to an increase of double taxation cases. The effect would be very negative on investments, jobs and growth.

Consequently, we urge the OECD to carefully consider these aspects in the process ahead.

On behalf of the Confederation of Swedish Enterprise

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