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# OECD Base Erosion & Profit Shifting: Action Item 6

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*Abstract: On 5 October 2015, the Organization for Economic Cooperation and Development (OECD) released the final package of measures to reform the international tax system under the Base Erosion and Profit Shifting (BEPS) project. The BEPS project pursued 15 Action Items that concerned a broad range of international tax topics, centered around three themes: coherence, substance, and transparency and certainty.*

*The Action Plan to implement the BEPS project seeks to align taxation with economic activity and ensure that taxable profits cannot be artificially shifted. Action Item 6 of the Action Plan identifies treaty abuse (particularly, treaty shopping) as a principal source of concern because it enables taxpayers to gain access to tax treaty benefits in situations where the benefits were not intended.*

*This Comment reviews the results of the finished BEPS project, specifically focusing on Action Item 6. I find that the BEPS project made remarkable progress considering the scope and complexity of the undertaking, as well as the political and corporate interests involved. While the efforts of the OECD have been impressive in scope, ambition, and the ability to find common ground on this issue, the results of the BEPS project thus far are insufficient to truly address the problem identified in Action Item 6. Moreover, significant challenges await the OECD before it can achieve the goal that it established for this effort.*

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## I. INTRODUCTION

On 5 October 2015, the Organization for Economic Cooperation and Development (OECD) released the final package of measures to reform the international tax system under the Base Erosion and Profit Shifting project.[1] Base Erosion and Profit Shifting (BEPS) refers to tax avoidance strategies that exploit mismatches in international tax rules to avoid taxation or to shift profits to low- or no-tax locations.[2] The BEPS project seeks to provide international guidelines to address this problem.[3]

Mismatches arise when national tax laws are not coordinated across borders, and the resulting inconsistencies provide the opportunity to avoid taxation. For instance, there is no international consensus on the allocation of income (for tax purposes) for products developed in one country but sold in a second country by a business located in a third country.[4] The BEPS project is founded on the idea that progress in addressing international tax avoidance can only be achieved through enhanced multilateral cooperation.[5]

While some mismatches occur unwittingly, others may be designed intentionally to undermine the tax regulation of other jurisdictions.[6] Indeed, analysis performed by Anthony Ting of the University of Sydney showed that "the U.S. Government knowingly facilitated the avoidance of foreign income tax by its multinational enterprises, thus creating double non-taxation."[7] The BEPS project foreshadows potentially significant change in the nature and operation of international taxation.

The BEPS project is a key point in the transition from an international tax system based on bilateralism to a collaborative international regime.[8]

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[1] Newsroom, OECD, OECD to Release BEPS Package for Reform of the International Tax System to Tackle Tax Avoidance on Monday 5 October 2015 (Sept. 25, 2015), http://www.oecd.org/newsroom/oecd-to-release-beps-package-for-reform-of-the-international-tax-system-to-tackle-tax-avoidance-on-monday-5-october-2015.htm; OECD, ACTION PLAN ON BASE EROSION AND PROFIT SHIFTING (2013), https://www.oecd.org/ctp/BEPSActionPlan.pdf.

[2] OECD, ABOUT BASE EROSION AND PROFIT SHIFTING (BEPS) (2015), http://www.oecd.org/ctp/beps-about.htm.

[3] OECD, *supra* note 1; Testimony of Pascal Saint-Amans Director, Centre for Tax Policy and Administration, Organisation for Economic Co-operation and Development (OECD) Before the United States Senate Committee on Finance (2014), https://www.finance.senate.gov/imo/media/doc/Testimony%20of%20Pascal%20Saint-Amans.pdf.

[4] *Hearing on Ways and Means International Tax Reform Discussion Draft: Hearing Before the H. S. Comm. On Select Revenue Measures of the Comm. On Ways & Means*, 112th Cong. 2 (2011) [hereinafter *House Hearing*] (statement of Paul W. Oosterhuis, Partner, Skadden, Arps, Slate, Meagher & Flom LLP).

[5] Reuven S. Avi-Yonah & Haiyan Xu, *Evaluating BEPS: A Reconsideration of the Benefits Principle and Proposal for UN Oversight*, 6 HARV. BUS. L. REV. 185, 194 (2016).

[6] NICHOLAS SHAXSON, TREASURE ISLANDS: TAX HAVENS AND THE MEN WHO STOLE THE WORLD 233 (2012) (attributed to a conversation with Richard Murphy).

[7] Antony Ting, *iTax — Apple's International Tax Structure and the Double Non-Taxation Issue*, 2 BR. TAX REV. 40, 71 (2014).

[8] Pasquale Pistone, *Coordinating the Action of Regional and Global Multilateralism in International*

Participation in the BEPS project was not limited to OECD member states, and "the effects are intended to have a broader geographical scope than past [OECD] model treaty updates."[9] An international tax system based upon bilateral treaties creates competition among jurisdictions to attract corporate residents for tax purposes.[10]

By at least one account, international tax has never known a more exciting era.[11] Others believe that the BEPS project represents "an unprecedented challenge" to the status quo regarding "the taxation of cross-border investment."[12] Though any changes in the international tax regime are likely to be gradual, they will nonetheless impact government revenue collection as well as the attractiveness of jurisdictions to host corporations; in turn, they will affect jobs and economic influence.[13]

The BEPS project pursued fifteen Action Items that concerned a broad range of international tax topics.[14] These were centered around three themes: coherence, substance, and transparency and certainty. The Action Items identify areas of concern for OECD governments.[15] According to the OECD, the international tax issues addressed in the BEPS Action Plan are among the most difficult ones confronted by the international tax regime.[16] The sweeping scope of the project is at once impressive and unrealistic.[17]

This Note reviews the results of the finished BEPS project. In particular,

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*Tax Law*, WORLD TAX J. 3, 3 (2014).

[9] Marie Sapirie, *The Impact of BEPS Implementation for U.S. Tax Planning*, 149 TAX NOTES 594 (Nov. 2, 2015), http://www.taxnotes.com/tax-notes-today/base-erosion-and-profit-shifting-beps/news-analysis-impact-beps-implementation-us-tax-planning/2015/11/02/16965211.

[10] Reuven S. Avi-Yonah, *Globalisation, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1575 (2000); *see* Reuven S. Avi-Yonah & Nicola Sartori, *Symposium on International Taxation and Competitiveness: Foreword*, 65 TAX L. REV. 313, 316 (2012).

[11] Yariv Brauner, *BEPS: An Interim Evaluation*, WORLD TAX J. 10, 10 (2014).

[12] H. DAVID ROSENBLOOM & JOSEPH P. BROTHERS, THE INTERSECTION OF US TAX TREATY POLICY, TAX REFORM AND BEPS (2015), http://www.capdale.com/files/16375_The%20intersection%20of%20US%20tax%20treaty%20policy,%20tax%20reform%20and%20BEPS.pdf.

[13] *See* Avi-Yonah & Sartori, *supra* note 10, at 320.

[14] These 15 items include the following: Address the tax challenges of the digital economy; Neutralize the effects of hybrid mismatch arrangements; Strengthen controlled foreign corporation rules; Limit base erosion via interest deductions and other financial payments; Counter harmful tax practices more effectively, taking into account transparency and substance; Prevent treaty abuse; Prevent the artificial avoidance of permanent establishment status; Assure that transfer pricing outcomes are in line with (value creation; intangibles, risks and capital; and other high-risk transactions); Establish methodologies to collect and analyze data on BEPS and the actions to address it; Require taxpayers to disclose their aggressive tax planning arrangements; Re-examine transfer pricing documentation; Make dispute resolution mechanisms more effective; and Develop a multilateral instrument. OECD, *supra* note 2.

[15] Michael Plowgian, *BEPS: The Shifting International Tax Landscape and What Companies Should Be Doing Now*, THE TAX EXECUTIVE, 2013, at 255.

[16] Hugh J. Ault, Wolfgang Schon & Stephen E. Shay, *Base Erosion and Profit Shifting: A Roadmap for Reform*, 68 BULL. INT'L TAX'N 275 (2014).

[17] *See* Brauner, *supra* note 11, at 37–39.

it focuses on Action Item 6 and provisions that seek to eliminate treaty abuse (specifically, the limitation on benefits (LOB) provisions).[18] The international tax efforts of the OECD have not previously included provisions of this nature. While the efforts of the OECD have been impressive in scope, ambition, and the ability to find common ground on this issue, the results of the BEPS project thus far are insufficient to truly address the problem identified in Action Item 6. Moreover, significant challenges await the OECD before it can achieve the goal that it established for this effort.

## II. BACKGROUND OF INTERNATIONAL TAX - PROBLEMATIC NATURE

Historically, international tax treaties were conducted on a bilateral basis, each treaty modified to the specific circumstance. In 1872, Britain and Switzerland concluded the first double taxation treaty.[19] Transaction taxes and other international capital controls emerged during World War I to capture tax revenue to finance the war (they also prevented capital flight).[20] Capital controls decreased thereafter but returned at least partially during the Great Depression, and they were integrated into the Bretton Woods system following World War II.[21] Governments progressively dismantled these controls starting in the 1970s.[22]

As long as there have been taxes, there has been tax avoidance both domestically and internationally. Inconsistencies among bilateral treaties create opportunities for exploitation (such as double nontaxation). The ensuing opportunities for tax avoidance are widely recognized.

One particularly famous case concerns William Vestey (later, 1st Baron Vestey), an Englishman who transformed a Liverpool butchery business into a multinational meat-processing conglomerate (at one point the largest private conglomerate in the world) in the late 1800s and early 1900s.[23] The

[18] "ACTION 6, Prevent treaty abuse: Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances. Work will also be done to clarify that tax treaties are not intended to be used to generate double non-taxation and to identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country. The work will be co-ordinated with the work on hybrids." OECD, *supra* note 1.

[19] Sunita Jogarajan, *The Conclusion and Termination of the "First" Double Taxation Treaty*, 3 BR. TAX REV. 283, 283 (2012).

[20] SHAXSON, *supra* note 6 at 57–58; Michael J. Graetz & Michael M. O'Hear, *The "Original Intent" of U.S. International Taxation*, 46 DUKE L.J. 1021 (1997).

[21] Christopher J. Neely, *An Introduction to Capital Controls*, FED. RESERV. BANK ST. LOUIS REV. 13, 13 (1999).

[22] *Id.* at 13.

[23] Stuart Millar & Alex Brummer, *Heirs and disgraces*, THE GUARDIAN (Aug. 10, 1999), https://www.theguardian.com/theguardian/1999/aug/11/features11.g2.

Vestey family was once Britain's wealthiest business dynasty, as well as "the country's most astute tax avoiders."[24] Through a tax avoidance scheme centered on a trust in Paris, their chain of butcheries paid 10 British Pounds of tax on a profit of 2.3 million British Pounds in 1978.[25]

Growing concern in many OECD countries about tax shelters and other tax avoidance schemes motivated their governments to ask the OECD to undertake the BEPS project. The 2009 financial crisis raised awareness about international tax avoidance, and brought the consequences into focus. Moreover, it created the platform for widespread popular concern. Knowledge of extensive tax avoidance, which shifts the burden of taxation onto smaller businesses and less sophisticated taxpayers, brought popular resentment and anger to the surface.[26]

Increasing media attention on international tax avoidance, and the corresponding public awareness, prompted political action.[27] Legislative hearings throughout this period gained widespread attention and laid bare the extent to which large multinationals escaped taxation.[28] As a result, G20 governments asked the OECD to lay the foundation for an internationally coordinated and collaborative tax regime.[29] According to the OECD, revenue losses from BEPS are estimated at $100 billion to $240 billion annually.[30]

A large number of U.S. multinationals have subsidiaries in tax havens or banking secrecy jurisdictions.[31] According to the Congressional Research Service, U.S. multinationals report a disproportionate share of profits in tax-preferred countries.[32] U.S. multinational corporations reported earning 43% of their overseas profits in the country group comprised of Bermuda, Ireland, Luxembourg, the Netherlands, and Switzerland, while having less than 4% of their foreign employees in those locations.[33]

Congressional testimony provides further detail on the legislative intent to allow for tax minimization strategies and suggests that tax authorities need not concern themselves with the impact of tax rules on the revenue of other

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24 *Id.*

25 SHAXSON, *supra* note 6, at 44–45.

26 Plowgian, *supra* note 15, at 255.

27 *Id.*

28 *See generally Offshore Profit Shifting and the U.S. Tax Code—Part 2 (Apple Inc.): Hearing Before the Permanent S. Comm. on Investigations of the Committee on Homeland Sec. & Governmental Affairs*, 113th Cong. (2013) [hearinafter *Apple Hearing*].

29 Plowgian, *supra* note 15, at 255. Two policy tools to prevent double taxation are the OECD Model Income Tax Convention and the OECD Transfer Pricing Guidelines.

30 OECD, POLICY BRIEF: TAXING MULTINATIONAL ENTERPRISES, BASE EROSION AND PROFIT SHIFTING (BEPS) 1 (2015), https://www.oecd.org/ctp/policy-brief-beps-2015.pdf.

31 JAMES R. WHITE, UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE, INTERNATIONAL TAXATION: LARGE U.S. CORPORATIONS AND FEDERAL CONTRACTORS WITH SUBSIDIARIES IN JURISDICTIONS LISTED AS TAX HAVENS OR FINANCIAL PRIVACY JURISDICTIONS 4 (2008).

32 MARK P KEIGHTLEY, CONG. RESEARCH SERV., R42927, AN ANALYSIS OF WHERE AMERICAN COMPANIES REPORT PROFITS: INDICATIONS OF PROFIT SHIFTING (2013).

33 *Id.*

countries.[34] The U.S. Congress employed this approach when it obstructed the U.S. Treasury and the IRS's efforts to write regulations that would limit the use of the check-the-box rules to achieve foreign tax minimization.[35] Congress thereafter codified the permissibility of foreign-tax minimization when it enacted United States Code Section 965(c)(6), which allowed multinational corporations to minimize their foreign taxes without giving rise to a domestic tax liability.[36]

Opportunities to avoid tax internationally are not limited to the United States; neither are the resulting problems. European nations, who suffered a slow recovery following the financial crisis, have been assertive in addressing the problem.[37] For instance, France created a task force to create recommendations to address tax matters related to the digital economy.[38] British and Italian revenue agencies scrutinized Google, Amazon, Facebook, and Apple.[39] Australia also criticized the tax avoidance schemes of technology companies.[40]

## III. INTERNATIONAL TAX AVOIDANCE: THE BASICS

A variety of widely acknowledged transactions demonstrate the extent of international tax avoidance. A particularly well-known transaction (for U.S. companies), the "Double Irish Dutch Sandwich,"[41] was pioneered by Apple, Inc.[42] However, other technology companies later used it,[43] until it was closed in 2014.[44] This arrangement allowed companies to take advantage of a U.S.–Irish Treaty and an Irish law that provides "an exemption from the Irish withholding tax for royalty payments to a European Union (EU) member state."[45]

In this arrangement, a U.S. company shifts its intellectual property

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34 *House Hearing*, *supra* note 4.

35 *Id.*

36 *Id.*

37 Plowgian, *supra* note 15, at 255.

38 PIERRE COLLIN & NICOLAS COLIN, TASK FORCE ON TAXATION OF THE DIGITAL ECONOMY, REPORT TO THE MINISTER FOR ECONOMY AND FINANCE, THE MINISTER FOR INDUSTRIAL RECOVERY, THE MINISTER DELEGATE FOR THE BUDGET AND THE MINISTER DELEGATE FOR SMALL AND MEDIUM-SIZED ENTERPRISES, INNOVATION, AND THE DIGITAL ECONOMY (2013).

39 KEIGHTLEY, *supra* note 32, at 1–2.

40 Gary Hufbauer et al., *The OECD's "Action Plan" to Raise Taxes on Multinational Corporations* 3 (Peterson Inst. for Int'l Econ. Working Paper Series, Paper No. 15-14, 2015).

41 Dave Davies, *How Offshore Tax Havens Save Companies Billions*, NAT'L PUB. RADIO, 2011.

42 Charles Duhigg & David Kocieniewski, *How Apple Sidesteps Billions in Taxes*, N.Y. TIMES, Apr. 29, 2012, at A1.

43 Chris William Sanchirico, *As American as Apple Inc.: International Tax and Ownership Nationality*, 68 TAX L. REV. 207, 209 (2014).

44 Stephen Castle & Mark Scott, *Ireland to Phase Out "Double Irish" Tax Break Used by Tech Giants*, N.Y. TIMES, Oct. 14, 2014, at B1.

45 Steven A. Bank, *The Globalization of Corporate Tax Reform*, 40 PEPP. L. REV. 1307, 1312 (2013).

rights outside the United States to an Irish subsidiary, headquartered in Bermuda. The headquarters then sublicenses the intellectual property rights to an Irish operating company (distinct from the subsidiary), which receives the profits in Ireland.[46] However, these profits are reduced by the sublicensing fees paid by the Irish operating company to the headquarters in Bermuda (delivered through yet another subsidiary registered in the Netherlands).[47]

This arrangement worked to reduce income tax significantly (particularly in Europe). However, closure of the provision is but a small deterrent; corporate taxpayers can achieve significant tax avoidance through other strategies that take advantage of the low corporate tax rate in Ireland.[48] Anthony Ting noted that Irish law pairs well with that of the United States to create a company that is not a tax resident in any country. Because the United States defines corporate tax residence according to place of incorporation, while Ireland uses the location of central management and control, a company incorporated in Ireland with central management and control in the United States is a tax resident of neither country.[49]

Ireland has other characteristics that make it an attractive jurisdiction for international tax structures. It has a corporate tax rate of 12.5%, and because it is an EU Member State, subsidiaries established in Ireland can avail themselves of EU laws that allow them to avoid corporate tax as well as value added tax in other EU Member States where they do business (which often have higher tax rates).[50]

Using these elements (though not the double Irish strategy, per se), from 2009 to 2012, Apple, Inc. avoided U.S. $44 billion in taxes.[51] By creating subsidiaries in low-tax jurisdictions like Ireland, the Netherlands, Luxembourg, and the British Virgin Islands (some little more than a letterbox), Apple allocated about 70% of its profit to overseas jurisdictions, significantly reducing the tax it paid around the world.[52]

Apple is not the only multinational benefiting from the mismatching tax

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[46] Davies, *supra* note 41.

[47] *Id.*

[48] Ting, *supra* note 7, at 40.

[49] *Id.* at 46.

[50] *Id.* at 54.

[51] *Apple Hearing*, *supra* note 28, at 8 (statement of Sen. John Mccain, Permanent S. Comm on Investigations); Ting, *supra* note 7, at 40 ("The double non-taxation of the profits was achieved primarily by the combined effect of the following: Definitions of corporate residence in Ireland and the US; Transfer pricing rules on intangibles; Controlled foreign corporation (CFC) regime in the US; Check-the-box regime in the US; and Low-tax jurisdiction.").

[52] Duhigg & Kocieniewski, *supra* note 42; *see also* Tracy A. Kaye, *The Offshore Shell Game: U.S. Corporate Tax Avoidance Through Profit Shifting*, 18 CHAPMAN L. REV. 185 (2015); *Offshore Profit Shifting and the U.S. Tax Code—Part 2 (Apple Inc.): Hearing Before the Permanent S. Comm. on Investigations of the Committee on Homeland Sec. & Governmental Affairs*, 113th Cong. 23 (2013) (statement of J. Richard Harvey, Professor, Villanova University School of Law).

rules.[53] Google used the Double Irish Dutch Sandwich strategy to avoid approximately $2 billion in worldwide income taxes in 2011 by crediting $9.8 billion in revenue (80% of its pre-tax profit) to a Bermuda company.[54] Microsoft indicated that "it had benefit[ed] partly from a policy of channeling sales through low-tax regional centers in Ireland, Singapore and Puerto Rico."[55] Starbucks also used these techniques, prompting the observation that its "opacity of international tax planning, [leads to a situation] in which neither investors nor the tax authorities in any particular jurisdiction have a clear picture of what the firm is up to."[56]

At the same time, Europe suffered through the worst period of the global financial crisis, which increased political awareness about tax avoidance among multinationals. This circumstance compelled the observation in the U.K. that "if Google doesn't pay [its tax], somebody else has to pay or services get cut."[57] The revelation that Google avoided significant amounts of tax prompted audits in France and Italy.[58] Germany, France, and other countries "want the [tax] revenue, and their taxpayers are disgusted by the constant stories of multinational companies paying low (and even nonexistent) taxes."[59]

As the Double Dutch Irish Sandwich transaction shows, particularly in regard to the mobility of intellectual property rights, the current international tax rules were not designed for the modern digital economy. International standards (such as those by the OECD, the UN, or even the United States) have not adapted to the international and technology-driven modern business environment.[60] The changing nature of international business and commerce, increasing in pace and technological sophistication, challenged the ability of national tax administrations to adapt the international tax regime accordingly.[61]

The instances of digital giants Apple, Google, and Microsoft were the

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[53] Marie Sapirie, *As American As Apple*, 139 TAX NOTES 1095 (June 3, 2013); Lee A. Sheppard, *Apple's Tax Magic*, 139 TAX NOTES 967 (May 27, 2013).

[54] Jesse Drucker, *Google Revenues Sheltered in No-Tax Bermuda Soar to $10 Billion*, BLOOMBERG, December, 2012.

[55] Richard Waters, *Microsoft's Foreign Tax Planning Under Scrutiny*, FIN. TIMES, June 7, 2011; *see also* Kaye, *supra* note 52; *Offshore Profit Shifting and the U.S. Tax Code—Part 1 (Microsoft and Hewlett Packard): Hearing Before the Permanent S. Comm. on Investigations of the Committee on Homeland Sec. & Governmental Affairs*, 112th Cong. 64 (2012) (statement of Sen. Carl Levin, Chairman, Permanent S. Comm. on Investigations).

[56] Edward D. Kleinbard, *Through a Latte Darkly: Starbucks's Stateless Income Planning*, 139 TAX NOTES 1515, 1516 (June 24, 2013).

[57] Drucker, *supra* note 54.

[58] *Id.*

[59] Jeremy Scott, *Can The United States Kill BEPS?*, FORBES, June 16, 2015.

[60] OECD, INFORMATION BRIEF: OECD/G20 BASE EROSION AND PROFIT SHIFTING PROJECT (2015).

[61] *Building a Competitive US International Tax System: Hearing Before the S. Fin. Comm.*, 114th Cong. 1–2 (2015) (Statement of the Pamela F. Olson, Partner, Skadden, Arps, Slate, Meagher & Flom, Former Assistant Secretary of the Treasury for Tax Policy).

"triggering cases" for the BEPS project. Media attention revealing the extent of their tax avoidance gave rise to public hostility that served as the impetus for the BEPS.[62] That the United States is the origin and host of many of the largest technology companies (Google, Microsoft, Apple) makes it particularly interested in the taxation of intangible products (technology-related IP and support). While treaty shopping can be problematic generally, the mobility of intellectual property rights makes them particularly easy to shift across jurisdictions.[63] Perhaps for that reason, "[i]t is not surprising that U.S. multinationals shift profits to low tax countries, as the U.S. maximum statutory corporate income tax rate of 35% is among the highest in developed countries."[64]

## IV. ACTION ITEM 6, OECD BEPS PROJECT: ELIMINATE TREATY ABUSE

The principal insight of the OECD BEPS project is to develop a more uniform and coordinated international tax regime. The BEPS project is based on the idea that coordination of national efforts is necessary to reduce and eliminate double nontaxation, as well as to protect against double taxation.[65] By targeting harmful tax practices, the BEPS project asks corporate taxpayers to disclose assiduous tax planning arrangements, as well as adhere to reporting requirements that disclose the income, economic activity, and taxes paid to tax administrations on a country-by-country basis.[66]

The BEPS Action Plan seeks to align taxation with economic activity and ensure that taxable profits cannot be artificially shifted.[67] Action Item 6 of the Action Plan identifies treaty abuse (particularly, treaty shopping) as a principal source of concern in this regard.[68] This Action Item offers model treaty provisions and recommendations for tax laws to prevent corporate taxpayers from accessing treaty benefits inappropriately.[69]

Treaty shopping is a primary driver of BEPS concerns. "Treaty shopping" refers to a circumstance where a taxpayer seeks to obtain benefits under a tax treaty despite not being a resident of a state included in the treaty (benefits are generally reserved for residents, or other qualified entities, of the two states of a bilateral treaty). Taxpayers pursue these strategies by

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[62] Yariv Brauner, *What the BEPS?*, 16 FLA. TAX REV. 55, 71 (2014); Brauner, *supra* note 11, at 27.

[63] Yariv Brauner, *Value in the Eye of the Beholder: The Valuation of Intangibles for Transfer Pricing Purposes*, 28 VA. TAX REV. 1 (2008).

[64] Ting, *supra* note 7, at 54.

[65] Ault, Schon, & Shay, *supra* note 16, at 276.

[66] OECD, *supra* note 30.

[67] *Id.*

[68] OECD, PREVENTING THE GRANTING OF TREATY BENEFITS IN INAPPROPRIATE CIRCUMSTANCES, ACTION 6: 2015 FINAL REPORT (2015).

[69] *Id.*

establishing a "shell company" (also referred to as letterbox companies or conduits) in a state with a desirable tax treaty, through which taxpayers avail themselves of the beneficial treaty provisions.[70]

Treaty shopping enables taxpayers to gain access to treaty benefits in situations where the benefits were not intended. This undermines tax sovereignty and deprives states of tax revenue.[71] Tax sovereignty refers to the ability of governments to raise revenue through taxation to support themselves, provide public goods, and protect their population from physical or economic harm.[72] That is, "taxation is an inherent or essential component" of sovereignty, and the ability to levy taxes and collect the resulting revenue is plausibly "an inherent right or entitlement attaching to sovereign status" to such an extent that "infringing on the right of taxation is an infringement on sovereignty itself."[73]

The crux of the challenge addressed by the OECD, however, is that "[m]ajor theoretical developments in tax policy are now arising . . . through the interactions of nongovernmental actors in transnational settings."[74] As a result, even the largest countries cannot independently enforce their tax laws under the status quo.[75] As Steven Bank observes,

> [T]he ease in moving corporate assets [(particularly intellectual property rights in the high tech industry[76])] and the malleability in the definition of legal home, combined with a few tax-friendly jurisdictions, makes it increasingly difficult for countries to unilaterally maintain the integrity of their separate corporate tax systems except in the case of purely domestic corporations.[77]

The "Limitations on Benefits" (LOB) provision included in the final BEPS report addresses this problem specifically. LOB provisions consist of treaty provisions and domestic rules to prevent usage of tax treaties (and access to the corresponding benefits) in inappropriate circumstances. LOB provisions provide a means through which treaty shopping and inappropriate tax avoidance can be prevented.

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[70] OECD, OECD/G20 BASE EROSION AND PROFIT SHIFTING PROJECT 2015 FINAL REPORTS: FREQUENTLY ASKED QUESTIONS 12 (2015), http://www.oecd.org/ctp/beps-frequently-asked-questions.pdf (last visited Apr. 6, 2017).

[71] OECD, *supra* note 68.

[72] Allison Christians, *Sovereignty, Taxation and Social Contract*, 18 MINN. J. INT'L L. 99, 104 (2009).

[73] *See id.* at 104–06; Jinyan Li, *Tax Sovereignty and International Tax Reform: The Author's Response*, 52 CAN. TAX J. 141, 141 (2004).

[74] Christians, *supra* note 72, at 99.

[75] Brauner, *supra* note 11, at 59.

[76] A key component of the tax strategy used by Apple, Inc. is the transfer of Apple's intellectual property rights to an Irish subsidiary under a cost-sharing agreement. U.S. multinationals have employed the technique to shift profits to low-tax countries since the 1970s. Ting, *supra* note 7, at 47.

[77] Bank, *supra* note 45, at 1312.

The United States has long recognized the problem of treaty shopping. However, only in May 2015 did the U.S. Treasury propose language addressing the issue to be included in the U.S. Model Tax Treaty. In May 2015, the U.S. Treasury Department released proposed revisions to the U.S. Model Income Tax Convention ("U.S. Model"),[78] among which included an article dedicated to limitation on benefits.[79]

Few countries other than the United States use a LOB measure to address cases where a corporate taxpayer attempts to circumvent limitations imposed by a tax treaty.[80] Parillo characterizes the impact of these changes as preventing residents of third countries from inappropriately obtaining the benefits of a bilateral tax treaty and enabling the U.S. Treasury or its treaty partner to curtail benefits if a change in domestic tax rates are made after a treaty is signed.[81]

The U.S. delegation to the OECD advocated for the BEPS project to address treaty shopping with a U.S.-style LOB provision.[82] The release of the U.S. provision was intended to influence the BEPS initiative.[83] The Final BEPS Report includes a LOB provision similar to those included in the U.S. Model. As such, the U.S. LOB provision served as the prototype for the OECD.[84]

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[78] Four of these provisions concern treaty shopping; the other (concerning expatriated entities) is specific to the United States—it seeks to deter inversions (where a corporation becomes a subsidiary of a company in another country in order to avail itself of favorable tax laws) by denying treaty benefits for expatriated companies. No similar provisions appear in the BEPS package; as a result, it will not be discussed in this paper. U.S. DEP'T OF THE TREASURY, *Treasure Releases Select Draft Provisions for Next U.S. Model Income Tax Treaty* (May, 20 2015), http://www.treasury.gov/press-center/press-releases/Pages/jl10057.aspx (last visited Apr. 7, 2017) (describing the proposals). U.S. DEP'T OF THE TREASURY, U.S. MODEL INCOME TAX CONVENTION (2016), https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/treaties.aspx.

[79] U.S. DEP'T OF THE TREASURY, SELECT DRAFT PROVISIONS OF THE U.S. MODEL INCOME TAX CONVENTION: NEW ARTICLE 28 (2015), https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-Subsequent-Changes-in-Law-5-20-2015.pdf; U.S. DEP'T OF THE TREASURY, SELECT DRAFT PROVISIONS OF THE U.S. MODEL INCOME TAX CONVENTION: NEW ARTICLE 1 (2015), https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-Exempt-Permanent-Establishments-5-20-2015.pdf; U.S. DEP'T OF THE TREASURY, SELECT DRAFT PROVISIONS OF THE U.S. MODEL INCOME TAX CONVENTION: NEW ARTICLE 3 (2015), https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-Special-Tax-Regimes-5-20-2015.pdf; U.S. DEP'T OF THE TREASURY, SELECT DRAFT PROVISIONS OF THE U.S. MODEL INCOME TAX CONVENTION: NEW ARTICLE 22 (2015), https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-Limitation-on-Benefits-5-20-2015.pdf.

[80] Japan and India also use LOB measures. *See* OECD, *supra* note 68, at 20.

[81] *See* Kristen A. Parillo, *Model Treaty Proposals Reflect Dramatic Change in U.S. Policy*, 147 TAX NOTES 868 (May 25, 2015).

[82] *See* Kristen A. Parillo & Lee A. Sheppard, *OECD Panel Explores Treaty Abuse*, 143 TAX NOTES 1118 (June 9, 2014).

[83] Sapirie, *supra* note 9, at 594.

[84] David D. Stewart & Kristen A. Parillo, *OECD's LOB Approach Needs Refinement, Practitioners Say*, 143 TAX NOTES 313 (Apr. 21, 2014).

The Final BEPS Report reflects agreement among the participating states that interested countries must meet a minimum OECD standard to prevent treaty shopping.[85] While acknowledging the need for flexibility for each country, and the circumstances of the bilateral treaty negotiations,[86] the minimum standard requires countries to include in their bilateral tax treaties a principal purpose test, a limitation on benefits provision (supplemented with domestic anti-abuse rules), or both.

The minimum standard seeks to ensure that treaty benefits are available only to entities entitled to them.[87] The standard requires that only true residents qualify for treaty benefits (implemented through limitation on benefits rules, as well as principal purpose test (PPT) rules).[88] The OECD proposed a three-pronged approach. It recommends (1) including a statement in tax treaties that the States (parties to a treaty) wish to prevent tax avoidance, (2) including an LOB rule in the model treaty, and (3) incorporating a general rule that uses the principal purpose test.[89]

The Final BEPS Report included a draft LOB and principal purpose provisions (with accompanying commentary). However, the LOB in the Final Report departs from a U.S.-style LOB by including a general anti-avoidance rule based on a main purpose test.[90] The following is a summary of the OECD recommendation:

> First, a clear statement that the States that enter into a tax treaty intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements will be included in tax treaties . . . .
> Second, a specific anti-abuse rule, the limitation-on-benefits (LOB) rule, that limits the availability of treaty benefits to entities that meet certain conditions will be included in the OECD Model Tax Convention. These conditions, which are based on the legal nature, ownership in, and general activities of the entity, seek to ensure that there is a sufficient link between the entity and its State of residence. . . .
> Third, in order to address other forms of treaty abuse, including treaty shopping situations that would not be covered by the LOB rule described above, a more general anti-abuse rule based on the principal purposes of transactions or arrangements (the principal purposes test or "PPT" rule) will be included in the OECD Model Tax Convention.

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85 OECD, *supra* note 68, at 9.
86 *Id.*
87 *Id.*
88 OECD, *Videos:Multimedia Examples of How the OECD/G20 BEPS Project will Revise International Tax Rules*, http://www.oecd.org/ctp/beps-2015-final-reports.htm (last visited Mar. 16, 2017).
89 J.P. Finet, *BEPS Treaty Provisions Need More Work, Treasury Official Says*, 149 TAX NOTES 502 (Oct. 26, 2015).
90 Stewart & Parillo, *supra* note 84.

> Under that rule, if one of the principal purposes of transactions or arrangements is to obtain treaty benefits, these benefits would be denied unless it is established that granting these benefits would be in accordance with the object and purpose of the provisions of the treaty.[91]

The Final Report recommends language to clarify that tax treaties do not intend to create opportunities for double nontaxation. Since 1977, Article 1 of the OECD Model Treaty has included a statement that tax treaties should not help tax avoidance or evasion.[92] Here, the OECD provides further clarification, and it encourages a clear statement in the title of a treaty that the prevention of tax avoidance is a purpose of tax treaties. It also recommends that a preamble expressly indicate that the treaty intends to "eliminate double taxation without creating opportunities for non-taxation or reduced taxation . . . ."[93]

Article 10 of the Final Report provides language for the LOB rule, which tests whether a taxpayer is eligible for treaty benefits.[94] This test evaluates factors such as legal structure, ownership, or business activity to ensure a legitimate connection between the taxpayer and the state of residence.[95] The Final BEPS Report indicates that further work is needed to refine the LOB rule (final versions of the rule will be completed in 2016).[96]

As noted above, the treaty abuse effort includes two approaches. The first reflects U.S. desire to ensure that the principal purpose test sought by the Europeans was not the only solution to treaty shopping. The United States succeeded in having a scaled-down LOB provision included, although no countries subscribe to it other than in the context of a U.S. treaty.[97]

Seemingly as a compromise between insistence on an LOB provision and the concern that this model is too complicated,[98] the Final BEPS Report also contains provisions for a simplified LOB rule (which provides a mechanism to evaluate standard cases of treaty shopping); however, it is complemented by the PPT to address cases not covered by the simplified rule. Thus, the treaty abuse measure in the Final BEPS Report consists of a

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91 OECD, *supra* note 68, at 9.

92 U.S. DEP'T OF THE TREASURY, OECD MODEL INCOME TAX TREATY CONVENTION (1977).

93 OECD, *supra* note 68, at 19. The Commentary to the OECD Model includes language referring to the BEPS project and the intent to address BEPS concerns arising from treaty shopping arrangements. *Id.* at 13.

94 *Id.* at 55. The 2015 Final BEPS Report defines "qualified persons" entitled to treaty benefits. *Id.* at 23.

95 *Id.*

96 *Id.* at 3. For this reason, the LOB rule, and related Commentary, in the Final Report is subject to change pending further review.

97 Lee A. Sheppard, *Barking At The Moon and Battling Treaty Abuse*, 147 TAX NOTES 1248 (June 15, 2015).

98 Parillo & Sheppard, *supra* note 82, at 1118.

simplified LOB clause with a backstop to allow tax authorities to prevent treaty benefits for a transaction with a "main purpose" of (inappropriately) taking advantage of the treaty.[99]

## V. ANALYSIS

### A. Diverging Views on the Principal Purpose Test

That the OECD included an anti-abuse provision modeled on the U.S. LOB measure, and that the provision should also include a general anti-abuse rule based on a main purpose test, generated controversy.[100] Attendees at a public consultation held by the OECD voiced a variety of concerns.

U.S. participants feared that an LOB provision with a main purpose test would "cause uncertainty, discourage cross-border investment, undermine the purpose of tax treaties, and reverse much of the work that the OECD has done to reduce trade barriers."[101] Several speakers suggested that "the advantages of a clear set of objective, mechanical tests like those offered under a U.S.-style LOB provision would be completely undone by a main purpose clause."[102]

A clear set of objective, mechanical tests like those in a U.S.-style LOB provision offers clarity on how the treaty provisions apply and whether treaty benefits will be available.[103] While a U.S.-style LOB can be complex to negotiate and draft, it provides predictability; a main purpose test requires fewer words, but it does not provide as much certainty.[104]

### B. Potential Conflict with European Union Law

Further, some experts raised serious concern that the OECD BEPS anti-treaty shopping measures could violate the right to freedom of establishment (regardless of motive) and restrict the free movement of capital in the European Union.[105] European Union law neither requires member states to impose corporate income tax nor does it require those states that do to do so at any specific level, regardless of whether it results in double non-taxation.[106] Member states are not required to adapt their tax systems to

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[99] Kristen A. Parillo, *U.S Views on Treaty LOB and Main Purpose Test Draw Skepticism*, 143 TAX NOTES 426 (Apr. 28, 2014).

[100] *Id*.

[101] *Id.*

[102] *Id*.

[103] Parillo & Sheppard, *supra* note 82, at 1118.

[104] *Id*.

[105] Christiana HJI Panayi, *The Compatibility of the OECD/G20 Base Erosion and Profit Shifting Proposals with EU Law*, 70 BULL. INT'L TAX'N 1 (2015).

[106] *Id.*

eliminate juridical double taxation (as opposed to economic double taxation).[107] Under the same reasoning, if double nontaxation is the result of parallel and nondiscriminatory taxation by member states, European Law does not prohibit it, no matter whether tax advantages accrue to the taxpayer.[108]

Moreover, the loss of tax revenue that results from double nontaxation has not yet been allowed as a justification to restrict fundamental freedoms of the European Union, such as freedom of establishment and the free movement of capital.[109] Neither has the European Court of Justice (ECJ) equated a tax saving that results from disharmony of tax rules among member states as tax avoidance or evasion.[110] Only to the extent that the activity would be viewed as abusive is there a legal basis for action by the European Union.[111]

Simple tax forum shopping is not considered abusive under the case law of the ECJ.[112] For abusive structures, where the intermediary is a sham (if there is no genuine exercise of establishment in the jurisdiction, nor movement of capital), the protection afforded by the fundamental freedoms does not hold.[113] However, the more economic substance to the activity, the more likely the intermediary can avail itself of the right to freedom of establishment, and its investment activity will be protected under the right to free movement of capital.[114]

### C. International Cooperation: How Much is Enough?

Other experts criticized the BEPS project and its outcome more fundamentally, noting that "upholding [BEPS] requires cooperation by too many jurisdictions."[115] The BEPS project attempts to improve the system of taxation remain rooted in the idea that income is earned in the country where the business activity takes place.[116] This perspective is increasingly difficult to reconcile with globally integrated supply chains for products that draw

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[107] *Id.*
[108] *Id.*
[109] *Id.* The author cites a variety of cases in this article to support this claim.
[110] *Id.*; *see also* Filip Debelva et al., *LOB Clauses and EU-Law Compatibility: A Debate Revived by BEPS?*, 24 EC TAX REV. 132–43 (2015).
[111] Panayi, *supra* note 105.
[112] *See Id.* (citing Case C-196/04, Cadbury Schweppes plc v. Comm'rs of Inland Revenue, 2006 E.C.R. 1-7995).
[113] *Id.*
[114] *Id.*
[115] Reuven S. Avi-Yonah & Haiyan Xu, *Global Taxation After The Crisis: Why BEPS And MAATM Are Inadequate Responses, And What Can Be Done About It* 1, 3 (Mich. Law Sch. Pub. Law & Legal Theory Research Paper Series, Paper No. 494, 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2716124. This is known as the "benefit principle." *See id.* at 32.
[116] *Id.* at 2.

value from intellectual property registered in locations other than where it is created, while individual components are manufactured or assembled in countries other than where they are sold, by corporations that lack physical presence in any of them.

The BEPS project does not elaborate on the concepts of residence and source or directly address the issue of where profit is earned.[117] Even using the independent entity theory (used in the BEPS project), where international tax works from the assumption that constituent entities of a multinational corporation are independent and transact with each other at arm's length,[118] the difficulty in assigning value to the income earned at any point along a globally integrated process quickly becomes evident.

Moreover, the perspective of taxing corporate income in the country where the business activity takes place has served as the basis for the modern international tax regime for nearly a century, and consequently it is embedded in several thousand bilateral tax treaties as well as the domestic law of most countries.[119]

Should a system or methodology be created to perform the task (such one based on single-entity perspective), it is equally understandable that it will require extensive multilateral coordination to develop and a strong commitment to enforce the regime to succeed. As dysfunctional and under-equipped as the current regime might be, even gradual replacement will likely meet resistance from countries and multinationals who favor it.[120]

At the same time, the guidelines developed in the BEPS project only apply to members of the OECD and G20.[121] To the extent that income is sourced in countries that are not members of these organizations (and chose not to adopt the rules), multinationals can seemingly avoid the outcome of the BEPS project.[122]

In that respect, for the project to succeed, it would need to have been more inclusive. That 60 nations participated in the BEPS project and contributed to the development of the international tax environment is an achievement. While this is a step toward increased multilateralism and inclusiveness for international tax law, participating countries represented less than a third of the 193 members of the United Nations.

As a result, the possibility remains for tax competition between the nations who participated in the BEPS project, and those that did not.[123]

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[117] *Id.* at 5.

[118] *Id.* at 6; *see also* The BEPS Monitoring Group, *Overall Evaluation of the G20/OECD Base Erosion and Profit Shifting (BEPS) Project* (Oct. 5, 2015), https://bepsmonitoringgroup.wordpress.com/2015/10/05/overall-evaluation.

[119] Avi-Yonah & Xu, *supra* note 115, at 3.

[120] *Id.* at 4.

[121] *Id*.

[122] *Id*.

[123] *Id.* at 8.

Additionally, the two-year time horizon under which the BEPS project was conducted was insufficient for anything but the first step in the intended evolution of global tax governance.[124]

### D. Unfinished Business & Enforcement

For the moment, however, Article 10 in the Final BEPS Report is placeholder text, with explanatory commentary to give an indication of the principles. The actual provision in the BEPS report is undrafted, reading "The drafting of this Article will depend on how the Contracting States decide to do so."[125] The timeline for drafting a new OECD Model is not clear. Given the number of participants involved, it could be several years before the final version is ready. Moreover, another drawback to an LOB approach is that it would likely take "decades for countries to update their treaties through renegotiations."[126]

For these reasons, the ultimate effect of this is uncertain, given that the Article is not drafted, and that provisions also often require implementing action by member states.[127] Thus, the provisions created by the OECD are not automatically effective, and for that reason the BEPS project cannot result in perfect harmonization of global tax systems.[128] Indeed, a proliferation of LOB articles of different varieties could result in "over complexity in the treaties or domestic legislation,"[129] as well as inconsistency among nations.

One potential problem in a multilateral system is that there is no supranational authority to validate that countries abide by the spirit of the agreement. As a result, implementation and enforcement could be uneven and potentially arbitrary. Moreover, even if the recommendations of the BEPS project are implemented as outlined in the Final Report, nothing prevents multinationals from creating or identifying new techniques to evade tax.

## VI. CONCLUSIONS

The OECD BEPS project seeks to bring coherence to domestic tax rules that affect cross-border activities.[130] While the BEPS project was an impressive effort, the 2015 Final BEPS Report does not rise to this level of

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[124] Avi-Yonah & Xu, *supra* note 115, at 4–5.
[125] OECD, *supra* note 68, at 21.
[126] Stewart & Parillo, *supra* note 84, at 313.
[127] Ajay Gupta, *United States and Business Remain Unsure About BEPS*, 148 TAX NOTES 1054 (Sept. 7, 2015).
[128] Plowgian, *supra* note 15, at 257.
[129] Avi-Yonah & Xu, *supra* note 5, at 13.
[130] OECD, *supra* note 68, at 3.

ambition. The Final BEPS Report is an achievement in the sense that it reflects agreement among participating countries (a larger body of membership than previous OECD initiatives) to ensure treaties include the means to prevent treaty shopping. It reflects a desire among these states to have a minimum standard to protect against treaty abuse.[131]

The achievement in this respect is that an LOB provision was included in the first place, rather than the actual content of a provision. However, the BEPS project nonetheless increased concerns of uncertainty across the international tax landscape, "because it may lead to modifications to the long-standing international tax standards established by the OECD."[132]

The United States plays a pivotal role in the international tax arena as a result of its historic economic influence and that many of the largest multinational corporations are of U.S. origin. The effectiveness of the BEPS provisions, and how they impact U.S. corporations are two of the most salient explanatory factors in understanding how much support the United States will ultimately provide to the OECD in the context of the BEPS project. Though its influence is potentially weaker now than at any point in several decades, the participation and support of the United States is critical to the ultimate success of the BEPS initiative.

### A. Impact for U.S. Multinationals: Indications

While some experts suggest that the OECD BEPS project likely will not directly affect U.S. tax treaty policy or its interpretation,[133] others note that even if the new OECD Model Convention does not grow into a multilateral tax treaty, it will have a significant impact. Some accounts indicate that the draft BEPS reports shifted the international tax landscape. Citing a 2014 report from PricewaterhouseCoopers, the Peterson Institute for International Economics indicated that more than 30 unilateral measures had been taken in the wake of draft BEPS reports, mostly to the disadvantage of U.S. multinationals operating in low-tax jurisdictions.[134] The Peterson Institute also predicted in 2015 that if the United States were to implement the BEPS actions, many U.S. multinationals would relocate their headquarters to tax-friendly jurisdictions (as well as to move their R&D activity offshore).[135]

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[131] Global Tax Alert, Ernst & Young, OECD Releases Final Report Under BEPS Action 6 on Preventing Treaty Abuse (Oct. 20, 2015) (All tax work at the OECD takes place on the basis of consensus; if one member objects, no action can take place), http://www.ey.com/gl/en/services/tax/international-tax/alert—oecd-releases-final-report-under-beps-action-6-on-preventing-treaty-abuse.

[132] Plowgian, *supra* note 15, at 255.

[133] Sapirie, *supra* note 9, at 594.

[134] Hufbauer et al., *supra* note 40, at 1.

[135] *Id.* at 19, 29.

B. Will the United States Sign-On?

One further point of concern is that the United States indicated in 2014 that it will not sign a treaty that combines a simplified LOB clause with a principal purpose clause.[136] Action Item 6 of the BEPS project establishes a minimum standard to prevent treaty abuse, in particular treaty shopping. The Final Report includes recommendations to meet the standard, recognizing that model provisions must be adapted for individual countries. The minimum standard requires that countries include in their treaties a PPT, a PPT in combination with a LOB provision, or a LOB provision along with rules targeting conduit financing arrangements.[137] The simplified rule is intended for countries that employ an approach that combines a LOB rule and a PPT.[138]

While the United States does not like the main purpose approach, it nevertheless uses one to deny treaty benefits using doctrines such as developed in *Aiken Industries v. Commissioner*, 56 T.C. 925 (1971).[139] Moreover, the effectiveness of the PPT depends heavily on the decisions of tax authorities and courts; to the extent that developing countries lack the institutional capacity and other resources to employ it effectively, or appreciate the original intent and perspective, it could be problematic.[140]

C. U.S. Influence in International Tax

The international context that shapes the posture of U.S. international tax policy has changed throughout the past decade. Economic growth in the developing world, and in China, has altered the stature of the United States in the global economy. Forces at play in the international tax regime are likely to change as a result. An international tax expert testified to Congress that

> [w]hen the United States had a dominant role in the global economy, we were free to make decisions about our tax system with little regard to what the rest of the world did. As a practical matter, our trade partners generally followed our lead in tax policy. That is no longer the case.[141]

By virtue of economic influence, the current international tax regime

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[136] Sheppard, *supra* note 97, at 1248.
[137] OECD, *supra* note 68, at 10.
[138] *Id.* at 22.
[139] Kristen A. Parillo, *ABA Section of Taxation Meeting: Stack Previews Final BEPS Reports*, 74 TAX NOTES INT'L 585 (May 19, 2014).
[140] Avi-Yonah and Xu, *supra* note 115, at 14.
[141] *Building a Competitive US International Tax System: Hearing Before the Senate Finance Committee*, *supra* note 61.

was created and maintained by the largest economies of the past century. The United States was the center of the global economy during that period; for that very reason, the United States was the most influential in the international tax landscape. While previously the European countries might have acquiesced to American leadership (demands) on tax issues, the fallout of the most recent financial crisis suggests that they are less willing to do so now. Indeed, Pascal Saint-Amans, the OECD official who led the effort, described the Final BEPS Reports as an "end run around the United States."[142]

Moreover, China is increasingly influential.[143] The nature of economic cooperation with China is likely to be an increasingly significant factor for many OECD member states. The diverging perspective on related issues has the potential to create a fissure, and this fissure is dangerous for OECD governments because the lack of uniformity allows an opportunity for multinational corporations to exploit the rules in ways that can result in double non-taxation.

### D. Concluding Thoughts

Many criticized the Final BEPS Report for failing to deliver on its level of ambition, and being "mainly aimed at patching up the existing system."[144] Independent commentators noted the influence of tax advisers and representatives of multinational corporations,[145] and lamented that the desire to preserve tax breaks to support national "competitiveness" and the need for consensus among participating countries produced a report that represents only the lowest common denominator of their collective interests.[146] By at least one account, the BEPS project achieved very little:

> The result is that the proposals will make international tax rules even more complex, and largely retain the scope for countries to offer tax breaks, while raising compliance costs for MNEs, yet preserving the systemic incentives for them to devise avoidance structures. The consequence of weak coordination will be an acceleration of unilateral measures: some have already been initiated by countries such as the UK and Australia, and other countries are likely to follow, to protect their tax base.[147]

Nonetheless, the BEPS project is not the final destination in international tax reform but only the opening salvo in the process of

[142] Lee A. Sheppard, *OECD Head Takes a BEPS Victory Lap*, 149 TAX NOTES 340 (Oct. 19, 2015).
[143] *See* Brauner, *supra* note 62, at 63.
[144] The BEPS Monitoring Group, *supra* note 118, at 10.
[145] *Id.* at 1.
[146] *Id.* at 3.
[147] *Id.* at 4.

modernizing global tax governance.[148] It made remarkable progress considering the scope and complexity of the undertaking, as well as the political and corporate interests involved.

The road ahead for BEPS looks like a bumpy one, and it is unclear how much will be achieved. However, international cooperation through the OECD BEPS project offers the most promise for the "survival of international standards to prevent double taxation of cross border income, and to provide the certainty businesses need to invest."[149] The lack of coherence in the international tax system has allowed for tax avoidance over the past century. While the impact of BEPS-related changes on taxpayers remains dependent on consistency in implementation,[150] if brought to a successful conclusion, the BEPS project remains the most promising initiative to bring greater coherence to the international tax regime.

## VII. POSTSCRIPT

This paper was conceived in mid-2015, in the months preceding the October 2015 meeting when G20 Finance Ministers endorsed the OECD BEPS package. The OECD moved forward on the BEPS project since that point, with apparent success. On 7 June 2017, the OECD hosted a signing ceremony for the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS). During the ceremony, 67 countries signed the Multilateral Instrument (MLI). As of 17 August 2017, 71 countries had signed.

The MLI provides a mechanism to implement the tax treaty-related measures under Actions 2 (hybrid mismatches), 6 (treaty abuse), 7 (permanent establishments), and 14 (mutual agreement procedures) of the BEPS project. For Action 6 of the BEPS Action Plan, the minimum standard requires that countries:

- Include in their tax treaties a statement that their common intent is to eliminate double taxation without creating opportunity for non-taxation or reduced taxation via tax evasion or avoidance, including through treaty-shopping; and
- Address treaty shopping by, at a minimum, implementing (i) a Principal purpose test (PPT), (ii) a PPT and a simplified or detailed limitation on benefits provision (LOB), or (iii) a detailed LOB, supplemented by a mechanism (treaty-based or otherwise) to address conduit arrangements not already covered in the tax treaty.

[148] Avi-Yonah & Xu, *supra* note 115, at 4.
[149] Plowgian, *supra* note 15, at 255.
[150] Sapirie, *supra* note 9, at 594.

To determine how the MLI affects a bilateral treaty between two signatory countries requires an examination of the provisions 'reserved' (opt-out) by those two countries. Where either country opted out of a provision, it doesn't apply.

The United States did not sign the Multilateral Instrument. The United States has pre-existing anti-abuse measures in its treaties; thus, the lack of signature is not anticipated to undermine the MLI. Countries that signed the MLI must ratify the instrument through their domestic processes. The MLI will take effect once ratified by five countries.