



SOCIEDADE DE ADVOGADOS, SP,RL
ROGÉRIO FERNANDES FERREIRA
& ASSOCIADOS



Nº 18/20

NEWSLETTER

THE NEW MULTILATERAL INSTRUMENT (MLI): RECENT DEVELOPMENTS

This Information is intended for general distribution to clients and colleagues and the information contained herein is provided as a general and abstract overview. It should not be used as a basis on which to make decisions and professional legal advice should be sought for specific cases. The contents of this Information may not be reproduced, in whole or in part, without the express consent of the author. If you should require further information on this topic, please contact contact@rfflawyers.com.

*

This Information is sent in compliance with articles 22 and 23 of Decree-Law no. 7/2004, of 7 January, regarding unsolicited e-mails. If you wish to be removed from our mailing list and avoid similar future communications, please send an email with "Remove" to the email address newsletter@rffadvogados.com.

Legal 500 – Band 1 Tax "Portuguese Law Firm" / Band 1 Tax "RFF Leading Individual" and highlighted in "Hall of Fame", 2013, 2014, 2015, 2016, 2017, 2018, 2019
Chambers & Partners – Band 1 Tax "RFF Ranked Lawyer", 2013, 2014, 2015, 2016, 2017, 2018, 2019 and Band 1 "Private Wealth Law" - HNW "RFF Ranked Lawyer", 2018
International Tax Review – "Best European Newcomer" (shortlisted) 2013 / "Tax Controversy Leaders", 2014, 2015, 2016, 2017, 2018, 2019 / "Indirect Tax Leaders", 2015, 2016, 2017, 2018, 2019 / "Women in Tax Leaders Guide", 2015, 2016, 2017, 2018, 2019 / "European Best Newcomer", 2016 / "Tax Firm of the Year", "European Tax Disputes of the Year" and "European Indirect Tax Firm of the Year", (shortlisted) 2017
Best Lawyers – "RFF Tax Lawyer of the Year", 2014 / "Recommended Lawyers", 2015, 2016, 2017, 2018
Who's Who Legal – "RFF Corporate Tax Adviser of the Year", 2013, 2015, 2016 / "RFF Corporate Tax Controversy Thought Leader", 2017 "Corporate Tax: Advisory and Controversy", 2017, 2018, 2019
Legal Week – RFF was the only Portuguese in the "250 Private Client Global Elite Lawyers" 2018
STEP Private Clients Awards - RFF "Advocate of the Year 2019" (shortlisted)
IBFD Tax Correspondent Angola, Mozambique and East-Timor, 2013, 2014, 2015, 2016, 2017, 2018, 2019

SUMMARY

On February 28th, 2020, Portugal deposited the instrument of ratification of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (the so-called "Multilateral Instrument" or "MLI") after its ratification by the President of the Republic on November 14th, 2019. The Multilateral Convention will enter into force in Portugal as of June, 1st 2020.



www.rfflawyers.com
Praça Marquês de Pombal, 16 – 5th (Reception)/6th
1250-163 Lisboa • Portugal
T: +351 215 915 220 • F: +351 215 915 244
contact@rfflawyers.com



INTRODUCTION

On February 28th, 2020, the instrument of ratification of the Multilateral Convention for the implementation of measures related to tax treaties was deposited with the Secretary General of the OECD.

The Multilateral Convention will enter into force in Portugal as of June 1st, 2020.

Although 94 countries have signed the Convention, up until March 2020 only 44 jurisdictions had deposited the instrument of ratification of the Convention with the OECD, amongst them Portugal.

The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting follows the Project on *Base Erosion and Profit Shifting* (BEPS), implementing some of its conclusions and puts in place several measures which make it a mechanism for joint reaction against practices leading to the erosion of the tax base, transfer of profits and tax treaty abusive practices.

In fact, the MLI is an unprecedented multilateral international instrument,

allowing the automatic and simultaneous modification of previously approved Conventions on Double Taxation.

The MLI offers a high degree of flexibility on what concerns its content, allowing States to pursue their respective tax policies while ensuring that certain minimum BEPS standards are met. In fact, signatories may:

- choose the Conventions to which the MLI will be applied to;
- opt for one of the alternative proposals;
- apply optional, supplementary or alternative provisions; and,
- make reservations, thus excluding the application of part or all of the provisions of the Multilateral Convention.

The Multilateral Convention aims at ensuring the application to tax conventions of the recommendations foreseen in the scope of the BEPS Project, in a synchronized and efficient manner, allowing an update of the network of Conventions of the different States, without making it necessary to trigger bilateral negotiations with each of the signatories States, and thus

avoiding the delays commonly associated with a typical process of negotiations and the conclusion and entry into force of bilateral Conventions.

In the ratification of the MLI, Portugal has formulated several reservations and declarations on what concerns the provisions set forth in the original text of the Convention, also indicating the 79 bilateral Conventions to be impacted by the MLI.

Accordingly, the MLI will only be applicable to certain Double Taxation Agreements entered into by Portugal when the other contracting jurisdiction have also deemed such DTA as covered by the provisions of the MLI.

ACTION 15 OF THE BEPS PROJECT

Acknowledging the BEPS Project aim to combat certain hybrid asymmetries in tax conventions, as well as the artificial avoidance of qualification as a permanent establishment and improving dispute resolution, the OECD published a report on BEPS' Action 15 - Developing a Multilateral Instrument to Modify Bilateral Tax Treaties.

This report analyzed several issues related to the development of a

multilateral instrument which would allow Contracting States to efficiently amend the Conventions to avoid Double Taxation concluded between them, thus implementing the measures identified in the course of the works related with the several BEPS actions.

In fact, the report concluded that the development of a multilateral instrument, equivalent to the simultaneous renegotiation of existing bilateral treaties, would be a desirable and feasible solution.

Following this, the Multilateral Instrument offers objective solutions to overcome gaps in international tax treaties, by transposing the results of the BEPS Project to bilateral tax treaties on a global scale.

Accordingly, the Multilateral Instrument allows governments to implement minimum standards to tackle treaty abuse and develop dispute resolution mechanisms, while also providing flexibility to adapt specific policies at the level of tax treaties.

MLI STANDARDS

The Multilateral Convention provides mandatory rules, enshrining the minimum standards provided for in Action 15

of the BEPS Project, and optional rules, the adoption of which is at the discretion of the signatory States.

In any case, the rules which make up the Multilateral Convention have several variants, allowing the signatory States to choose one of the several alternatives for each standard.

Although there is a set of rules which establishes a minimum standard which all signatory States have to comply with, taking into account the different possibilities allowed for each provision, the Conventions will only be changed automatically when both Contracting States have opted for the same variant of each standard.

In turn, the mandatory norms of the Multilateral Convention take into account the minimum standards which must be adopted by the signatory States.

Amongst those mandatory provisions, we highlight the following:

- the prevention of tax treaty abuse, in the sense that the Double Taxation Conventions should now adopt the general anti-abuse clause, or the so-called *Principle Purpose Test*;

- the dispute resolution mechanism, through the mutual agreement procedure which the signatory States cannot opt out of;
- the application of corresponding adjustments with respect to double taxation arising out of transfer pricing adjustments.

In this context, it should be noted that the signatory States have the option of including, in their Conventions On Double Taxation, a Principle Purpose Test with a simplified limitation clause on the application of benefits (Limitation on Benefits or “LOB”).

As previously mentioned, with regard to optional provisions, such measures will only be automatically added to the Conventions when both signatory States’ choices coincide.

The optional provisions address, in particular:

- hybrid asymmetries (which resulted in double non-taxation situations);
- tax treaty abuse, with a focus on dividends, capital gains arising from the sale of real estate companies and the abuse

- of the concept of permanent establishment; and,
- the mandatory binding arbitration mechanism.

Furthermore, and contrary to the mandatory rules, in this regard, the Signatory States have the possibility to formulate reservations which prevent the application and inclusion of said provisions in their Conventions on Double Taxation.

PREVENTION OF TAX TREATY ABUSE

With regards to Portugal and the so-called mandatory rules, in terms of tax treaty abuse, Portugal considers the Principle Purpose Test, but does not choose to include a simplified limitation clause on the application of benefits, continuing to combat abusive practices through the General Anti-Abuse Clause (whose wording was recently changed following the transposition of the ATAD Directive).

MUTUAL AGREEMENT PROCEDURE

Regarding the improvement of the dispute resolution mechanism, through the mutual agreement procedure, Portugal considered the following measures, as resolution mechanisms, to be included in its Conventions:

- the submission of the request to open the mutual agreement procedure within a period of 3 years, from the date of the first communication of the provision which causes double taxation;
- the submission of the opening request by the taxpayers with the contracting State of residence;
- taxpayers may, in any case, submit a request to open a mutual agreement procedure with the source State, if they consider there has been discrimination based on nationality.

Additionally, Portugal has established that if the competent Authority, before whom the case is presented, is unable to reach a satisfactory resolution, it should make its best efforts to reach a solution through mutual agreement with the competent Authority of the other contracting jurisdiction. Moreover, the competent authorities in the several jurisdictions consult each other in cases not covered by their Conventions to avoid double taxation situations.

CORRESPONDING ADJUSTMENTS

Portugal adopted the corresponding adjustments clause of the MLI, which requires jurisdictions to make compensatory or corresponding adjustments when the observance of transfer pricing rules results in double taxation for the taxable person.

THE OPTIONAL STANDARDS

Under the optional rules regime, and regarding dividend distributions, the withholding tax reduced rate will only apply when the minimum holding period of 365 days is met.

In terms of capital gains arising from the sale of shares in real estate companies, the sale of equity parts or similar rights in companies or in a fiduciary structure, may be taxed in the source State when, at any time during the 365 days prior to the sale, the value of the shares or equity parts results, directly or indirectly, in more than 50% from real estate located in that other contracting jurisdiction.

Finally, it is worth mentioning an anti-fragmentation of activities rule, based on the preparatory or auxiliary character, for the definition of a permanent establishment.

In terms of arbitration, Portugal opted for mandatory and binding arbitration, which, however, is not applicable to cases related to tax crimes and misdemeanors, as well as to cases involving the application of general anti-abuse provisions resulting from national law or anti-abuse provisions resulting from a covered tax Convention.

With regards to the other optional rules, enshrined in the MLI, Portugal chose not to include them in its covered tax Conventions having, for this purpose, formulated a reservation in this regard.

CONCLUSIONS

The impact of the Multilateral Convention is intrinsically connected to the number of jurisdictions which ratify this instrument, given that the greater the number of adherent jurisdictions - which is expected to increase exponentially over time - the greater the impact will be.

In general terms, tax authorities will have more legal and fiscal instruments with which to examine, in detail, international structures, particularly with regard to their economic substance.



Accordingly, the Multilateral Convention establishes significant changes in several articles of the covered Double Taxation Agreements.

Portugal should remain alert to the significant changes operated on the Double Taxation Agreements currently in force, which will entail various consequences in terms of existing 3rd investment structures and income flows.

Lisbon, March 6th 2020

Rogério M. Fernandes Ferreira
Marta Machado de Almeida
Rita Arcanjo Medalho
Catarina Almeida Andrade
Inês Tomé Carvalho
José Oliveira Marcelino
(Corporate & International Tax Team)