IFA Cahiers – The Key Takeaways

- **Anti-avoidance measures of general nature and scope – GAAR and other rules**

The 850+ pages Cahiers on the subject contains General Report, EU report and branch reports from 42 countries on the topic of "Anti-avoidance measures of general nature and scope – GAAR and other rules".

The general report authored by Paulo Rosenblatt (Brazil) and Manuel E. Tron (Mexico) makes an opening remark that *"General anti-avoidance rules (GAARs hereafter) and other anti-avoidance measures of general nature and scope resemble a 'tug of war'".* The report highlights that in a GAAR circumstance, the opposite sides are: (i) the rule of law or the legality principle, and legal certainty; and (ii) tax equality and occasionally the ability to pay.

The analysis of this year's topic refers to general anti-avoidance statutory rules and judge-made doctrines without focusing on the BEPS plan, the changes in the OECD models or the European Union Anti-Tax Avoidance Directive – ATAD but referring to both with a focus on the actual effect these international trends have had on domestic law around the world. The report is also concerned with the potential conflicts between the GAAR and ordinary provisions such as Specific Anti-Avoidance Rules (SAARs), as well as the relationship between domestic anti-avoidance provisions and tax treaties.

The general report observes that *"There is no perfect tax system in the world, and therefore, the risk of abuse of its shortfalls or loopholes is real…and tax authorities will consistently battle the abuse (real or apparent). The combat will exist with or without a formally statutory GAAR; it is not possible to evaluate whether GAARs are better mechanisms than anti-avoidance judicial doctrines or general anti-abuse rules; based upon the branch reports, there are mixed views on the effectiveness of these measures, and on its challenges and limits."* It highlights that based upon the branch reports, there are mixed views on the effectiveness of these measures, and on its challenges and limits. The general report remarks that "GAARs are an inescapable paradox in many senses." It further states that *"avoidance reflects a ruthless relationship between tax authorities and the taxpayer, insofar the boundaries of legitimate and illegitimate tax planning remain blurred."*

The 42 branch reports depict interesting perspectives and evidence that more and more countries have introduced statutory GAARs, have engaged in tax transplants and experienced singular judicial reactions. Hence, there is a higher degree of coincidence among these measures because

they address similar questions and share common elements. The general report states that one country can learn from the other on how to draft GAARs, identify comparable features, solve similar issues and analyse significant judicial responses. The report also discusses the potential conflicts between GAARs with ordinary provisions such as Specific Anti-Avoidance Rules (SAARs).

The cahiers have obtained report from OECD and EU since the OECD Model Convention now recommends the inclusion of a harmonized treaty anti-abuse provision in the Double Tax Treaties (especially in Action 6, with reference to the Principle Purposes Test – PPT and, to some extent, the Limitation on Benefits – LOB) and also the European Union Anti-Tax Avoidance Directive – ATAD, which must be transported by the EU member states into domestic law by 31 December 2018.

The general report states that some countries by adding generic attributes for attracting GAAR such as 'unacceptable' (New Zealand, Israel), 'impermissible' (South Africa, India), 'illegitimate' (Israel), 'aggressive' (EU, OECD), 'unjustified' (Russia) brings more uncertainty as they are a matter of judgment.

The general report states that "*The more broadly a GAAR is designed, the more attractive for the judiciary to adopt an extensive or purposive approach; conversely, a potential limitless GAAR may be judicially limited*." The general report also recognizes that "*It is difficult to determine (or speculate on) the 'appropriate' legal form to be put in place of the disregarded tax avoidance scheme. Most reporters alerted on the uncertainty of a re-characterization in a GAAR context as it might grant limitless powers to tax agents*."

The general report highlights that "Conflict between domestic GAARs and treaty provisions may also rise in the context of BEPS-PPT and EU-ATAD." The General report focuses on matters such as the burden of proof and a comprehensive discussion on safeguards for taxpayers, considering that a GAAR's assessment should be based on reasons, describing its elements and their interconnection, with consistency, fairness and impartiality, so as to provide the taxpayer the fundamental rights of information and defense.

As regards the burden of proof, The General report terms the attribution of the burden of proof as a problematic. Very few GAARs provide for specific rules on this matter. They either leave it to the general rules of judicial evidence or to the courts. The report identifies that in Australia, the burden of proof is on the Commissioner to identify the scheme and the tax benefit. In Canada, the courts decided to divide it: while the Revenue must identify the scheme, the tax advantage and the misuse and abuse of the provision, on a balance of probabilities, the taxpayer has to prove the transaction was entered into for bona fide purpose and 'to refute the Minister's assumptions of fact.' In

Belgium, Denmark, Finland, Luxembourg, Serbia, Singapore, Switzerland, Russia, there is a division of the burden of proof between the tax authority and the taxpayer as well. In Chile, Chinese Taipei, the Republic of Korea, the Netherlands, Sweden and Ukraine, the burden of proof is generally only on the tax authority. Conversely, the burden of proof is generally on the taxpayer in the Czech Republic, India, Israel, Italy and Sri Lanka. The UK general anti-abuse rule allocates the *onus probandi* on the tax officials to show that there are tax arrangements, the tax arrangements are abusive, and the counteraction proposed by HMRC is just and reasonable.

The general report states that *"where a GAAR is in place, it blurs the boundaries of the rule of law since it inevitably confers discretion on tax officials that may enact risks of unfairness, discrimination and arbitrariness on taxpayers."* It states that guidance, rulings and clearances are expected to promote uniform official interpretation and application of GAARs. The report states that aim should not be to replace administrative discretion by judges' subjective assessments but to impartially control ultra vires discretion that does not meet the statutory criteria (unlimited discretionary power or a carte blanche).

The general report concludes that *"There is no perfect tax system in the world; the risk of abuse of its shortfalls or loopholes is real. The risk, on the other hand, of perceiving as abusive conducts which are perfectly valid is equally real or even more so. Tax authorities around the globe will combat the abuse (real or apparent) with or without a statutory GAAR. The first casualty of this fight against the 'legal abuse' of the tax systems is the legal certainty for the taxpayer"*. It further highlights that there is no consensus about how to resolve the conflicts of application between domestic SAARs and GAARs, or between the domestic rules and treaty GAARs. This is a matter of concern, since it aggravates the lack of legal certainty and may lead to a case of authorities going "GAAR shopping".

- **Withholding tax in the era of BEPS, CIVs and digital economy**

The 800+ pages Cahiers on the subject contains General Report, EU report and branch reports from 38 countries on the topic of "Withholding tax in the era of BEPS, CIVs and digital economy". The general report authored by, identifies and compares the frameworks for withholding taxes used in various jurisdictions, taking into account both domestic and international settings. It is divided into 4 parts encompassing basic structures and rules of withholding tax in each jurisdiction, withholding tax as a means of protecting the tax base of the source countries, how withholding tax does and should work in the context of investment activities by CIVs, more serious

challenge of the withholding tax in the digital economy. Part IV of the General Report also assesses whether the proposals of obligating final consumers or intermediary financial institutions to withhold taxes from their payment have yet made any dent in the real world.

The report states that both the new concept of PE with a lowered threshold, and the appropriately expanded use of withholding tax may potentially contribute to overcoming various issues raised by the BEPS phenomenon, but only if they are combined in an optimal way and pursued in a well-coordinated manner.

The report highlights that the BEPS project said very little about withholding tax, and most certainly did not address it at all as an Action despite, as this report tries to show, the long-standing significance of withholding tax in domestic and international tax settings. The report states that if the automatic exchange of information ("AEOI") works well, it may, combined with residence taxation, attain the ideal of taxing every income once.

With respect to withholding for CIVs, the report highlights that CIVs exacerbate the difficulties experienced by withholding agents and national tax authorities, in that they often involve multi-tier entities, many of which raise the issues of beneficial ownership (or possibly substance-over-form) and entity classification (mixed with the thornier issue of hybrid entities). It states that the challenges are compounded by determining who should be the relevant taxpayer – the vehicle which actually receives amounts (which may be transparent or opaque relative to those who hold interests in it) or the persons "behind it" or the ultimate investors and recipients.

The general report highlights that *"it is anticipated that unless combined with a restatement or revised understanding of the PE concept expansion of the withholding tax may be seen to comprise a more radical reallocation of tax revenue to source countries than would result under the current norms."* It states that *"an expanded use of withholding tax will not be of much help in B2C transactions. The most familiar proposal to overcome this difficulty is to obligate financial intermediaries (e.g. credit card companies) instead, which take part in, or control the process of the payment made by the resident end-consumer to the non-resident business".*

With respect to withholding tax on digital contents, the general report states that there is still room for controversy as seen with regard to the downloading of computer software, which might be worse due to the lack of well-established interpretative guidance in this area at the international level, and to certain peculiar wordings of diverse statutory provisions in the domestic law of some countries.

The general report states that "*most branch reporters share the view that the presence of a server can constitute a PE if certain significant business activities are carried out through that server; an opinion ascertained in the branch reports of Austria, Finland, Indonesia, Israel, Italy, Netherlands, Poland, South Africa, Spain, Sweden, Turkey and Uruguay. This development denotes that the previous uncertainty about the necessity of human activity, which was thus deleted from the PE concepts, is now settled, although the geographical location of a physical server is almost meaningless*."

The general report states that the issue of enforcement and collection never goes away as long as one is interested in taxing not only B2B transactions, but also B2C transactions. The optimal way of collecting tax from the latter type of transactions still remains an issue that requires an innovative solution. The general report highlights that the equalization tax is confined to B2B transactions in India so far but, if it survives, it will perhaps make a dent into B2C transactions as well, though future is never for prediction. The general report states that *"Invented for coping with the revenue allocation between residence and source taxation, the equalization tax deserves intellectual and policy discussions around the world."* The report mentions that as early as in 2003, Peru reportedly introduced a 30 per cent withholding tax on certain categories of service supplied via digital means in B2B context in its domestic law. In contrast, it is reported that the US and Finnish governments have indicated that they are not interested in taking any bold actions against the consequences of the digital economy.

The general report concludes that both concept of PE and withholding tax *"are under considerable pressure and there is a known risk which the OECD and others have acknowledged that each jurisdiction may unilaterally proceed to devise and utilise certain new, sometimes creative measures that have not yet been theoretically or practically tested to a reliable extent. In some ways that might return us to the state before the League of Nations embarked on its work after World War I to devise an approach to rationalizing the contemporaneous application of tax systems."* It further states that certain and clear guidelines should be provided so that the withholding agents may escape penalties whenever they are ready to exercise due care.

The general report observes that the Italian idea of combining wider use of withholding tax on business income and lowering the PE threshold appears to deserve due consideration while the Indian equalization levy seems to have both inspired many European countries to consider their positions but, as well, to have caused tax experts at the OECD and elsewhere to advance their consideration in this context of issues as fundamental as what is an "income tax" and what is a suitable indication of a taxable presence in a source country.