

GCC MLI Update

January 2019

Signing of MLIs - Another step by GCC in the BEPS land

Introduction

As BEPS¹ implementation has gathered momentum globally, the GCC countries have also been actively supporting/ participating in this initiative. In the GCC, we now have:

- 5 out of 6 countries (except Kuwait) that have joined the BEPS inclusive framework;
- 4 out of 6 GCC countries (Kuwait, UAE, Saudi Arabia and Qatar) that have signed the multilateral convention ('multilateral instrument' or 'the MLI') to implement tax treaty measures relating to BEPS (in relation to harmful tax practices, treaty abuse, transfer pricing documentation and making dispute resolution mechanisms more effective).

As of date, 85 countries have signed the MLI. We are pleased to provide a summary of the MLI positions of the GCC countries and key implications of the same.

MLI - A quick recap

MLI is a medium for updating bilateral double tax avoidance agreements ('DTAAs') swiftly (currently covering nearly 1,500 of them). It was devised under Action Point 15 of the BEPS project of the OECD² commissioned to assist governments to reduce opportunities for tax avoidance by multinational enterprises ('MNEs'). The measures specifically target:

- Hybrid mismatches (BEPS action point 2)
- Treaty abuse (BEPS action point 6)
- Avoidance of permanent establishment ('PE') status (BEPS action point 7)
- Improving dispute resolution (BEPS action point 14)

¹ Base erosion and profit shifting

² Organisation for Economic Co-operation and Development



Each of the MLI signatories is required to provide a list of DTAA's wished to be covered and its positions and reservations in respect of each provision covered under the MLI. The signatories can amend their MLI positions until ratification through their domestic legislations. Even after ratification, countries can choose to opt in with respect to optional provisions or to withdraw reservations.

The modified DTAA comprises the original DTAA provisions and the modified/ newly added provisions i.e. the commonly accepted features of the MLI by both the contracting parties.

Qatar has been the latest addition to the list of MLI signatories (signed on 4 December 2018). It recognises 84 DTAA's to be covered by the convention and has adopted only the minimum mandatory standards pertaining to inclusion of the principal purpose test to prevent treaty abuse and provision of Mutual Agreement Procedure ('MAP') remedy to taxpayers. It has expressed reservations on all the other MLI provisions.

Summary of key MLI positions of GCC countries

Following is a comparative summary of the key MLI positions adopted by the four GCC countries which have signed the MLI.

Particulars/ Provisions relating to	MLI Article ref	Kuwait	UAE	Saudi Arabia	Qatar
Number of DTAA's covered ³	2	45	114	53	84
<u>Hybrid Mismatches</u>					
Transparent and Dual resident entities	3 and 4	Expressed reservation	Expressed reservation	Expressed reservation	Expressed reservation
Application of methods for elimination of double taxation	5	Not adopted	Not adopted	Adopted the credit method for elimination of double taxation	Expressed reservation
<u>Treaty Abuse</u>					
Purpose of a covered tax agreement	6	Adopted the suggested preamble language ⁴ to counter tax avoidance (BEPS minimum standard) and included intent to develop economic relationship/ enhance co-operation in tax matters			
Prevention of treaty abuse	7	Adopted the principal purpose test ⁵ to deny grant of treaty benefits in cases where it is established that obtaining such benefit was one of the principal purposes of any transaction/ arrangement (BEPS minimum standard)			

³ Includes treaties signed but not yet in force

⁴ "Intending to eliminate double taxation with respect to the taxes covered by this agreement without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of third jurisdictions)."

⁵ Kuwait has expressed an intention to adopt limitation on benefits provision through bilateral negotiations.



Particulars/ Provisions relating to	Article ref	Kuwait	UAE	Saudi Arabia	Qatar
Dividend Transfer Transactions	8	Expressed reservation	Expressed reservation	Expressed reservation	Expressed reservation
Capital Gains from alienation of shares or interests of entities deriving their value principally from immovable property	9	Expressed reservation	Expressed reservation	Such gains may be taxed in the state in which immovable property is situated where the shares derive more than 50% value therefrom at any time during the 365 days preceding the alienation	Expressed reservation
<u>Avoidance of permanent establishment status</u>					
Through commissionaire arrangements and similar strategies	12	Expressed reservation	Expressed reservation	Expanded scope of agency PE to include cases where agent plays principal role in conclusion of contracts; Also, Independent agent not to include a person acting exclusively on behalf of a closely related enterprise	Expressed reservation
Through specific activity exemptions	13	Fixed place PE exemptions to only include activities of a preparatory or auxiliary character; also, no reservation against application of anti-fragmentation rule ⁶	Expressed reservation	Fixed place PE exemptions to only include activities of a preparatory or auxiliary character; also, no reservation against application of anti-fragmentation rule ⁶	Expressed reservation
Splitting-up of contracts	14	No reservation i.e. time periods for determination of existence of PE by related parties are to be aggregated ⁷	Expressed reservation	No reservation i.e. time periods for determination of existence of PE by related parties are to be aggregated ⁷	Expressed reservation

⁶ Exemption not to apply if business activities constitute complementary functions that are part of cohesive business operations

⁷ Specifically for building sites, construction or installation projects etc.



Particulars/ Provisions relating to	Article ref	Kuwait	UAE	Saudi Arabia	Qatar
<u>Improving Dispute Resolution</u>					
Mutual Agreement Procedure	16	Minimum standard under BEPS; Following remedy has been provided: <ul style="list-style-type: none"> • A person could approach either Competent Authority to initiate MAP proceedings • This case must be brought within three years/ specified due date of the first notification of the action resulting in taxation contrary to the provisions of the covered tax agreement • The competent authority shall, in genuine cases, endeavour to resolve the matter by mutual agreement with the competent authority of the other contracting jurisdiction. 			

Oman has already expressed its intent to sign the convention. **Bahrain** was a member of the ad-hoc group responsible for finalising the MLI and accordingly, can be expected to sign the MLI in future.

Our Comments

The MLI positions of the GCC countries highlights that the current focus lies mainly on inclusion of the minimum BEPS standards as reservations have been made in respect of the other provisions. This would have the effect of not modifying its bilateral treaties to a large extent (except the minimum required MLI provisions) even where the other contracting jurisdiction may have adopted a given provision.

It is interesting to note that some of the recent DTAA's signed by the GCC countries, for instance, the Qatar-Argentina DTAA and the UAE-Brazil DTAA incorporate certain provisions which are not accepted by Qatar and UAE in their respective MLI positions, for instance, provisions relating to avoidance of PE status through specific activity exemptions, commissionaire structures and splitting up of contracts. Also, these DTAA's are not covered tax agreement as per the MLI positions of Qatar and UAE. One may expect the new tax treaties of GCC countries to incorporate the BEPS MLI provisions, based on bilateral negotiations.

GCC countries' commitment to BEPS minimum standards and other information exchange mechanisms is further embodied in the following:

- Recently issued three-tiered transfer pricing documentation requirements (including country by country reporting, master file and local file) of the draft transfer pricing bylaws of Saudi Arabia;
- Country-by-country ('CbC') reporting legislation introduced by Qatar (covering the recommendations of the minimum BEPS standard pertaining to action point 13);
- Multilateral competent authority agreement on the exchange of CbC reports signed by Qatar and UAE



- Multilateral competent authority agreement on automatic exchange of financial account information signed by 5 out of six 6 countries (other than Oman).

With the GCC's commitment to BEPS and the aforementioned developments, it is imperative that GCC headquartered companies and MNEs having business presence in the GCC review their tax/ transfer pricing structures. Also, MNEs entering into transactions with residents of GCC countries that have signed the MLI will need to note such MLI positions and whether the same will have any impact on the bilateral treaties in order to ascertain treaty benefit entitlements.

Contact us

While this Alert summarises the key aspects of the MLI positions of GCC countries, if you would like our assistance in understanding the specific implications of the same to your business, please feel free to get in touch with us at nilesh.ashar@dhruvaadvisors.com or wartika.jain@dhruvaadvisors.com.



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