



## BEPS ACTION 7: PREVENTING THE ARTIFICIAL AVOIDANCE OF PE STATUS

ICAEW welcomes the opportunity to comment on the Public Discussion Draft [BEPS Action 7: Preventing the artificial avoidance of PE status](#) published by OECD on 31 October 2014.

This response of 9 January 2015 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

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## RESPONSES TO SPECIFIC QUESTIONS

### Section A – Artificial avoidance of PE status through *commissionaire* arrangements and similar strategies

1. We are concerned that the proposals start from the premise, which we do not believe is always true, that commissionaires are inevitably used as part of an avoidance strategy.
2. Whether that is the case, or not, has been thoroughly examined by the highest courts of a number of European countries whose legal systems contain the commissionaire concept (French Conseil d'Etat (Supreme Administrative Court) in *Société Zimmer Ltd v Ministre de l'Économie, des Finances et de l'Industrie*; Norwegian Supreme Administrative Court in *Dell Products(Europe) BV v Skatt Øst*;) All these courts have systematically rejected the argument that this is an abuse.
3. Similarly, in cases where abuse has not been argued, supreme courts have concluded that a commissionaire in itself does not give rise to a permanent establishment (Italian Supreme Court in *Boston Scientific v Italian Revenue Agency*).
4. The example set out at paragraph 7, is the Zimmer case.
5. The statement in paragraph 10 is that in many cases commissionaire structures and similar arrangements are put in place primarily in order to erode the taxable base of the State where sales take place. The assumption is that such arrangements are always for tax avoidance purposes so that some change is necessary to paragraphs 5 and 6 of Article 5 of the OECD Model Convention. There are then four separate proposals for such change, examples A to D.
6. Notwithstanding what we have said above, if there is to be a change in Article 5 (4), then of the proposals put forward we have less objections to proposal A.

#### Proposal A

7. If there is to be a change then we are concerned that the expression "specific persons" is too vague to have any real meaning. Article 5(5) has always and should continue to deal with PEs that arise by reason of contractual relationships. This makes the parties identifiable.
8. We are concerned that the phrase "engages... in a way that results in the conclusion of contracts" is too vague and will give rise to considerable uncertainty.
9. Automatic exclusion of associated enterprises from Article 5(6) as independent agents is bound to result in a proliferation of permanent establishments that runs contrary to the practical allocation of taxing jurisdiction. Article 9 ought to address issues of associated enterprises. Proper application of the arm's-length principle will therefore mean that there will be little profit, if any, for such permanent establishments once the local agent has been properly remunerated, but considerable administrative cost.
10. We are concerned by the automatic exclusion from qualifying as an independent agent under Article 5(6) of persons who act exclusively or almost exclusively for one person. This will have an adverse impact particularly on start-up agents. Any person who sets up an agency in relation to an initial customer will inevitably be a PE under the proposed language until they have managed to secure sufficient work acting for other principals. This will inhibit the activity of start-up agents and will favour established agents thus creating a significant barrier to entry, and will consequently probably be contrary to the TFEU (formerly EC) treaty freedoms

### **Proposal B**

11. Our concern is that if this proposal were adopted, it will be too vague and it will be inherently uncertain making it difficult to administer. This would act as a brake on international trade and would particularly inhibit smaller businesses which might otherwise start to trade in a particular country.
12. In terms of detailed drafting we think that treating an intermediary as constituting a PE when they 'negotiate the material elements of contracts' is again too vague and uncertain to be capable of practical application.

### **Proposals C and D**

13. We are again concerned that the language is very uncertain and wide in scope.
14. A simple solution for countries that do recognise commissionaires in their law would be to include a provision that deems the commissionaire under the relevant law to be a person with authority to conclude contracts and so within Article 5(5).

## **Section B- Artificial avoidance of PE status through the specific activity exemptions**

### **Proposal E**

15. Under the current provision certain activities, such as "the storage, or maintenance of a stock, of goods for delivery" are automatically treated as being activities of a preparatory or auxiliary character which do not create a PE. The proposal is to redefine the test to be whether the activity itself "is of a preparatory or auxiliary character".
16. We believe that introducing a general test, as to whether the activities are of a preparatory or auxiliary character, is the best of the options put forward and we would, therefore, support Proposal E.
17. As an alternative to a general rule which would subject all the listed activities to a "preparatory or auxiliary character" test there are then three alternative suggestions as to how to address BEPS concerns.

### **Proposal F**

18. This option would remove "delivery" as being an activity that could be considered to be "preparatory or auxiliary".

### **Proposals G and H**

19. These proposals would remove the possibility of purchasing goods or merchandise (Option G) from being "preparatory or auxiliary" or in the case of Option G both the purchasing and the collection of information as being "preparatory or auxiliary".
20. We consider that all of these specific proposals (F, G & H) are too draconian. We would favour E ie making these exceptions expressly subject to the requirement that the activity be demonstrated to be auxiliary/ancillary to the other activities of the enterprise.

## **Fragmentation of activities between related parties**

### **Proposals I, J**

21. In new paragraph 4.1 b) we believe there should be a requirement that the enterprises should be acting together rather than merely exercising "complementary functions that are part of a cohesive business operation". We are concerned that the proposed formulation is too vague and would have the result that functions that are genuinely carried on independently could be aggregated whereas the aim is to prevent businesses being artificially split into separate parts.
22. We also note that fragmentation of activities is sometimes occasioned by a particular countries inward investment rules e.g. it is not generally possible for a loss-making foreign parent company to open a branch in certain countries because branch office approval is only given to

companies with a profit-making track record. In such a case the foreign group would have to open a subsidiary which might then be caught by these new rules.

**Section C – Splitting of contracts**

**23.** We have no comments on these proposals.

## APPENDIX 1

### ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see [icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx](http://icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx) )