Università
Ca'Foscari
Venezia

Master's Degree programme
Second Cycle (*D.M. 270/2004*)

in Accounting and Finance

(Amministrazione, Finanza e Controllo)

Final Thesis

Ca' Foscari
Dorsoduro 3246
30123 Venezia

Anti-Avoidance Measures against Treaty Shopping and the Employment of Base Companies

Supervisor
Ch. Prof. Antonio Viotto

Graduand
Paolo Burattin
Matriculation Number 837537

Academic Year
2015 / 2016

INDEX OF CONTENTS

7. Bibliography;
8. Cases;
9. Foreign Reviews;
10. Italian Reviews;
11. Legal Acts;
12. Online Resources;
13. Other Resources.

1 International Tax Planning

SUMMARY: 1.1 Abstract; **1.2** The Approach in Tax Planning; **1.3** Some of the Most Commonly Used Tax Planning Tools.

1.1 Abstract

The globalisation process and, within the European framework, the implementation of the EU Single Market have led numerous corporations to overstep the national boundaries either to conduct phases of their economic process where it is more convenient or to expand their business abroad. Hence, the involvement of the diverse tax regulations of the countries, whose territories host such businesses, cannot be avoided. Thus, the lack of neutrality of taxation[1] has brought the managers of big corporations to take more and more into consideration tax issues in their decision-making process, especially during periods of crisis.

Therefore, multinationals can pursue the aim of optimizing their fiscal burden by exploiting the legal options that the countries involved have given to their taxpayers, which constitute, *de facto*, the tax competition among the governments.
Such planning of the cross-border activities of a business, taking into consideration the different tax laws of the concerned states, is known as tax planning.

This phenomenon is becoming increasingly concrete even within the European borders, as companies located in one of the Member States of the European Union are entitled to take advantage of the numerous European directives issued in order to guarantee the European freedoms[2].

1 The neutrality of taxation would ideally require: financing neutrality (i.e. the same tax treatment of equity and debt), neutrality towards the tax treatment of profits (distributed or retained), neutrality towards the legal form and for the location of the business. (ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, p. 203).
2 The free movement of goods (articles 28–37) and of workers (articles 45-48), the freedom of

Academic writings about tax planning encompass a great variety of legal matters concerning those operations that may be implemented by corporations to reduce their tax burden.

Conversely, the aim of this research is to point out the most common tax planning schemes, highlighting what are the limitation on benefits (LOB) provisions that are used in the *Model Tax Convention on Income and on Capital* by the OECD and in the *US Model Income Tax Convention* and describing how they work with reference to the treaty shopping practice and to the employment of the so-called base companies.

In addition, the work by the OECD in *BEPS 2015 Final Reports* is taken into account with reference to the above-mentioned fields and the relevant innovations provided by the document are presented and inspected: those supplementary anti-avoidance provisions are critically analysed in order to provide solutions to their weaknesses and to develop other solutions that enable tax administrations to achieve the same goal.

Furthermore, attention is paid to Action 12 in *BEPS 2015 Final Reports*, whose mandatory disclosure regime can be seen as a means to bypass the need of the anti-avoidance provisions exposed in the research, since the disclosure of the relevant information is set as a legal obligation in such system.

Under this perspective, the most suitable implementation of the mandatory disclosure regime is presented by making reference to the main characteristics that distinguish each tax jurisdiction.

establishment (articles 49-55) and the free movement of services (articles 56-62) and of capital (articles 63-66) have been implemented in the *Treaty on the Functioning of the European Union*, which is considered the primary European law and, as such, overrides national laws.

1.2 The Approach in Tax Planning

For an international group of companies, international tax planning represents a strategic field of its general corporate strategy. The goal of such activity consists in minimising the overall tax burden by means of the legitimate use of the existing tax provisions.
The tax savings may be achieved on a temporary or permanent basis. In the first case, the postponement of the tax payments allows the company to benefit from the lower interests paid and from the higher liquidity retained. In the latter, the tax payments are reduced or completely avoided[3].

As tax planning techniques require an interdisciplinary approach, such activity does not merely involve the tax provisions analysis, the understanding of their application by the jurisprudence, and the comparison of the results found in the different countries.
The particular characteristics of the business model of the firm that opts for the implementation of a tax planning pattern must also be taken into account.

As professionals are asked to develop a tax planning strategy that is appropriate for the features of a specific corporation, they use a bottom-up approach.
Simplifying the issue, tax planners attempt to tackle the problem that the country where the taxable event occurs imposes a high tax rate. To reduce the tax burden, they try to shift the income to other jurisdictions that offer lower taxation.

From the perspective of a domestic enterprise determined to expand its business abroad, the tax planners' activity can be divided into five steps:

I. Business model analysis;
II. Analysis of the domestic, European and conventional anti-avoidance provisions;

3 ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, p. 95.

III. Analysis of the tax provisions of foreign countries concerning the income streams that match the specific needs of the business;
IV. Division of the sole corporation into business lines, allocating these new companies into different foreign countries in order to exploit the tax opportunities offered;
V. Development of methods to shift the income from one firm to the other;
VI. Constant updating of the tax planning scheme.

To achieve the goal of shifting income to a low tax jurisdiction, there is a great variety of tools at disposal, and the combination of them on the multiple levels of a group gives rise to countless models.
In other words, the same result can be obtained through many legal patterns but the most challenging activity deals with the comparative evaluation of the cost-efficiency and of the inherent risk of the application of a general anti-avoidance principle to the detected models by the courts[4].

4 ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, p. 391.

1.3 Some of the Most Commonly Used Tax Planning Tools

Within this paragraph the most commonly used structures for tax planning purposes are presented to give an insight into its underlying mechanisms. Hence, the following cases are merely illustrative[5].

- The selection of the holding company location

  The best location for the holding company of a multinational group should allow both a strong network of double tax conventions and guarantee access to the European directives. In addition, the residence country should, ideally, not tax dividends, capital gains, royalty and interest income and no withholding tax should be levied on the outflow of royalties, interests and dividends.

  As there is no country that meets all these criteria, it is advisable that the multinational group focuses its strategy only taking into account a few of them;

- Financing a company with debt

  Taking into account the fact that interests are considered deductible expenses in a great many of the jurisdictions around the globe, financing a subsidiary with debt instead of using equity entails a lower tax base, as dividends are not usually deductible. Nonetheless, attention should be paid to a set of provisions called thin capitalization rules, whose aim is to hinder this kind of tax planning.

  In addition, such a scheme has to be matched with either the lack of withholding tax on the outbound interests or with a network of double tax treaties that allows a double tax relief on the withholding tax applied. The most sophisticated strategies include the location of the financing company in a country that provides a tax exemption on the interest income (e.g. Hong Kong);

- Arbitrage and qualification conflicts

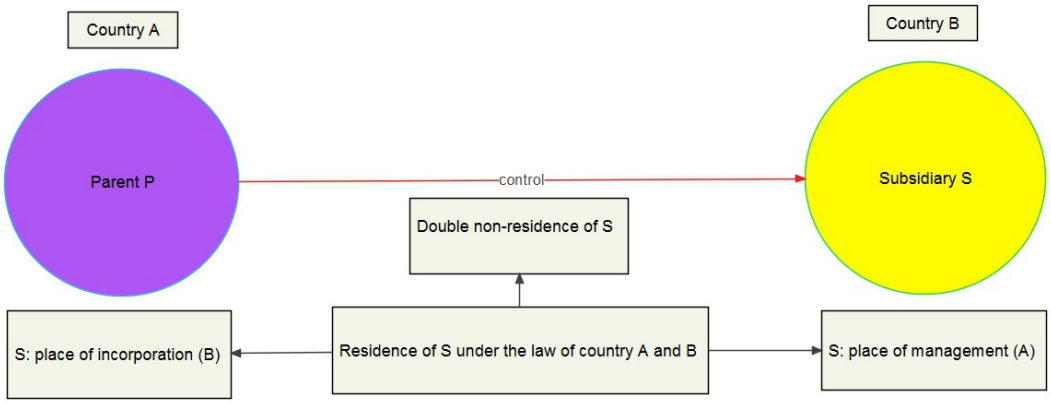
  A qualification conflict relies on the fact that two or more jurisdictions take into

5 ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, p. 392.

account different parameters to define a taxable income and deductible expenses. In this case, derivative instruments are one of the most wide spread tools to implement such a scheme, since there is a number of different approaches used to determine their taxation. Nonetheless, even the characterisation of crucial aspects, such as the residence, shows these kind of inconsistencies.

For instance, whenever a company (P) resident in country A, which applies the place of incorporation to determine the residence of legal persons, incorporates its subsidiary (S) in country B, which applies the place of effective management as the criterion to determine the residence of legal persons, the subsidiary (S) would not be considered to be resident either in country A or in B. This happens because:

1. The place of incorporation of S is country B, therefore it is considered to be resident in B under the law of country A;
2. The place of effective management of S is country A, where P is located, hence the subsidiary is considered to be resident in A under the law of country B.



Nonetheless, the exchange of information among the tax authorities involved may affect this kind of tax planning;

- <u>Intellectual properties</u>

  Since intangible assets play a key role in the value added chain, their location may entail substantial tax savings, whenever either no withholding tax is applied or a double tax treaty grants a tax relief for the withholding tax applied.

The intra-group transaction are usually ruled by the transfer pricing legislation. Nevertheless, the contribution of an intangible asset to the value creation is very difficult to assess. Therefore, most of the time the application of the rule is challenging.

As this paper mainly focuses on the treaty shopping practice and on the employment of base companies, the discussion cannot exclude the introduction of the most commonly used double tax treaty models, which are presented in the following chapter.

2 Double Tax Treaties and International Tax Planning

SUMMARY: 2.1 International Tax Avoidance and Double Tax Treaties; **2.2** The OECD Model and its Function; **2.3** The United States Income Tax Convention.

2.1 International Tax Avoidance and Double Tax Treaties

When assessing the means through which a legal system hinders the illegal tax saving, it is essential to distinguish between domestic and international tax avoidance.
The first can be tackled through anti-avoidance rules which may be:

- general codified or court-based anti-avoidance rules;
- specific and codified anti-avoidance rules, which usually result in legal presumptions;
- anti-avoidance interpretation of the tax provisions by the courts, using the *analogia legis* and *analogia iuris* techniques[6].

Whenever international transactions take place and, therefore, the risk of international tax-avoidance arises, the two countries involved may have signed a double tax treaty.
The main aim of a tax convention is to eliminate the double taxation of an income[7],

6 ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, p. 274.

7 The double taxation of the cross-border income may occur whenever the same income is taxed in the hands of the same taxpayer both in the country where the source of that income is located and in the country of residence of the recipient (juridical double taxation).
A list of typical cases is presented within the OECD Commentaries:
"3. International juridical double taxation may arise in three cases:
a) where each Contracting State subjects the same person to tax on his worldwide income or capital [...];
b) where a person is a resident of a Contracting State (R) and derives income from, or owns capital in, the other Contracting State (S or E) and both States impose tax on that income or capital [..];
c) where each Contracting State subjects the same person, not being a resident of either Contracting State to tax on income derived from, or capital owned in, a Contracting State; this may result, for instance, in the case where a non-resident person has a permanent establishment in one Contracting State (E) through which he derives income from, or owns capital in, the other Contracting State [...]" (Commentary on Articles 23 A and 23 B Concerning the Methods for Elimination of Double Taxation, *Commentaries on the Articles of the Model Tax Convention 2014*, OECD).

which may occur in case of disharmonies amongst the respective national tax systems. In other words, the two contracting states have to agree on the allocation of their tax rights with respect to cross-border investments.
Nonetheless, such a tool is used even to counteract tax evasion, fraud, and double non-taxation cases, since within the models are contained procedures, directed to ease the exchange of information and administrative assistance, that may help the audit process of the tax administrations.

Tax avoidance can be pursued through the abusive use of the tax conventions since they limit the tax right of one of the two contracting states in order to achieve the goal of eliminating the double taxation.
Conversely, tax avoidance can be achieved even without trying to enter into a tax treaty that otherwise would not be available. Nonetheless, in this case, tax treaties and domestic laws can be useful means to counteract this phenomenon[8].

Conversely, the economic double taxation takes place whenever two different taxpaying entities are taxed on the same income that is transferred from one of them to the other. (RUST A. et al, *Double Taxation within the European Union,* 2011, Wolter Kluwer, pp. 19-20).

8 ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, p. 274.

2.2 The OECD Model and its Function

The Organisation for Economic Co-operation and Development (OECD), an international organisation of the most advanced countries whose aim is, in broad terms, to coordinate domestic and international policies[9], has released the so-called *Model Tax Convention on Income and on Capital* (2014), which strives to provide a means to solve the double taxation of the cross-border income.
Such a model can be considered to belong to the *genus* of the soft laws, since it is a quasi-legal instrument which does not have any legally binding force.

In addition to the *Model Tax Convention on Income and on Capital*, which is the most commonly used model by the governments, the OECD has published the *Commentaries on the Articles of the Model Tax Convention*. Such document provides explanations and considerations on various provisions contained in the 2014 OECD Model and it therefore gains relevance whenever the anti-avoidance rules codified within the model have to be applied[10].

Given the fact that the aim of tax treaties is to avoid double taxation, in practical terms, the issue results in the restriction of the tax rights of the contracting countries, as tax rights can only rise through domestic law and not through these treaties.
Hence, whether a double tax treaty is in force, it prevails on the domestic legislation, even if the latter has been issued at a later time. In case of conflict, the internal law takes precedence only if it explicitly overrides the treaty provision and the constitutional law

9 The OECD runs a number of programmes whose aim is providing effective solutions to tackle the problems that have arisen for the globalisation. Within the tax planning field, special consideration shall be given to the Base Eroding and Profit Shifting Programme (BEPS), which contains measures ranging from the new minimum standards to the revision of existing standards, and common approaches that will ease the convergence of the national practices, and offers guidance on the best practices (http://www.oecd.org/tax/ Access: 22 January 2016).

10 The majority of the scholars agrees that, as the OECD Commentaries can be properly define as preparatory work of the treaty, it appears to be a supplementary means of interpretation (art. 32 VCLT), although other authoritative researchers claim that it has to be considered an agreements concerning the conclusion of a double tax convention (art. 31 VCLT). (FINNERTY C. J., MERKS P. et al, *Fundamentals of International Tax Planning,* 2007, IBFD, pp. 18-19.)

allows it[11] [12].

Within the Italian legal system, the ratification of a tax treaty by the Italian President, under mandate of the Italian Parliament (art. 80 of the Italian Constitution), allocates the tax conventions in a lower ranking with respect to the Italian Constitution but in a higher position than the ordinary law. This happens because art. 117 of the Italian Constitution imposes the compliance to the international obligations. Therefore, in case of contrast between the ordinary law and a convention, the latter prevails.

The functioning of a double tax treaty relies on the adoption of a common double tax relief system[13] by the contracting states. The most commonly used double tax relief methods are the exemption method[14] and the foreign tax credit[15], which reflect the tax

11 FINNERTY C. J., MERKS P. et al, *Fundamentals of International Tax Planning,* 2007, IBFD, pp. 12-13.

12 Nevertheless, a country can establish that the provisions of an international treaty shall not applied if the domestic rule is more advantageous for the taxpayer.
This is the case of art. 169 of the Italian Presidential Decree no. 917 of 22 December 1986:
"*Le disposizioni del presente testo unico si applicano, se più favorevoli al contribuente, anche in deroga agli accordi internazionali contro la doppia imposizione.*"
The legal basis supporting such provision lies in the fact that the Italian State, through this rule, is actually waiving its own tax right and this does not interfere with the tax rights of the other contracting country. In other words, the result of its application is a lower tax revenue for Italy, which does not affect the financial resources of the other country.

13 Double tax relief methods are essentially based on the principles of the capital export neutrality and capital import neutrality. In the first, a resident firm investing abroad should bear the same tax burden applied to companies investing at home whereas the second requires that the same taxation should be levied both on foreign corporations and on resident companies.
Those principles are relevant for tax purposes because they are means through which the adequacy of the double tax relief methods can be assessed, each one highlighting a different perspective of their efficiency. (ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, pp. 203 – 210).

14 In the exemption method, the residence country does not impose taxation on the income generated and taxed in a foreign country.
In the "tax exemption", the country of residence considers the world-wide income and then it grants a tax exemption for the foreign income. In other words, in case of progressive tax rate systems, the foreign income is used to determine the tax rate to be applied on the domestic income, thus enhancing the tax rate if the add of the foreign income is sufficient to cross the subsequent threshold.
Conversely, in the "income exemption" method, the state of residence simply does not consider the foreign income and therefore there is no progression in the tax rate. (ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, pp. 197 – 199).

15 In the foreign tax credit method, the residence state recognises a credit for the taxation levied by the tax authority in the other country. Such credit may be entirely deducted from the tax established on the basis of the world-wide income (full credit), in this case the progression of the tax rate may take place, or up to the levy the resident state would have applied on that investment if it had been made within its territory (ordinary credit). In the ordinary credit method, the foreign tax credit consists in the lowest between the foreign tax paid and the domestic tax.
To sum up, in the unlimited credit method (full), the overall tax burden is always the one determined

policy of the countries involved in the international trade[16].

Other minor methods that may be used to eliminate the double taxation are the deduction, the lump-sum and the remission methods.

Actually, as governments attempt to tackle the double taxation cases that may arise whenever no double tax treaty is in force with the other country involved, double tax relief methods are usually codified even within the domestic tax law of a country, otherwise there might be negative effects on cross-border investments and distortions regarding business competition[17]. Nevertheless, it is worth pointing out that the aim of eliminating the double taxation may not be achieved if the two countries involved in the transaction apply different double tax relief methods, which does not happen in case of

in the resident state, without regard to the foreign tax rate.
On the contrary, in the limited credit method (ordinary), the overall tax burden is equal to the one determined in the residence country, whenever the foreign tax rate is equal or minor to the domestic tax rate because the tax paid abroad is fully recognised. Conversely, when the foreign tax rate is higher than the domestic one, the overall tax burden is greater, since the foreign tax is not entirely recognised. Therefore, that difference between the higher foreign tax and the lower domestic tax on the income cannot be deducted against the domestic tax on the world-wide income, thus enhancing the overall tax burden.
The overall limitation, per-country limitation and per-item-of-income limitation are variations of the limited tax credit method that may be applied when the cross-border transactions involve different countries.
The overall limitation consists in granting a credit for the tax paid abroad to the extent of a threshold determined applying the domestic tax rate to the foreign income considered as a whole.
The per-country limitation entails that the maximum credit granted in each country is established considering the income generated in each single country. Hence, there is no compensation between the excess of the tax paid in a high tax jurisdiction with respect to its threshold and the tax credit that cannot be used due to the lower tax paid in another country. Thus, the tax paid in low tax jurisdictions can be credited in full whereas the credit for the taxation paid in high tax jurisdiction is limited.
In the per-item-of-income limitation, the tax credit is limited as the classes of income are considered separately. (ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, pp. 199 – 203).

16 In the income exemption, the result is that the substantial tax rate levied on the foreign income is the one established by the source country. On the contrary, in the limited tax credit method, since the foreign income is used to determine the tax burden in the residence state first, and then the limited tax credit is deducted from the total amount, it entails that the substantial tax rate is the higher.

17 The domestic Italian law has opted for a limited tax credit method with per-country and per-item-of-income limitations. Within the meaning of art. 165 (DPR 22/12/1986 no. 917), the foreign income is included in world-wide tax base and the tax paid abroad for that foreign income on a permanent basis can be deducted up to a limit determined as the ratio between the foreign income and the world-wide income. The difference between the tax paid abroad and the tax credit computed as described can be carried backward up to the eighth preceding year and deducted from the tax debt up to the threshold for the tax credit recognised each year. In case the excess of the threshold for the tax credit compared to the tax paid abroad does not occur in the eight preceding years, it can be carried forward up to the following eighth year. The loss carry-back and forward of the excess can be used only within the same class of income that has generated such excess. Moreover, whenever the foreign income is used only partially to determine the world-wide tax base, the tax paid abroad has to be reduced proportionally.

double tax treaty contexts.

The relevance of the exemption method (art. 23 A[18]) and of the tax credit method (art. 23 B[19]) is confirmed in the OECD Model, which suggests to the contracting countries these two options.
Nonetheless, it is necessary to take into account the Commentaries to the 2014 OECD Model to get an insight of the two ways in which each of these methods may be implemented.

From the tax planning perspective, the adoption of the *2014 Model Tax Convention on Income and on Capital* by the OECD leads to both pros and cons.
Such models definitely simplify the legal framework within which professionals have to implement their strategy and ensure a higher level of certainty of its legal effects.
Nonetheless, it is important to highlight that the existing conventions based on this model are generally dated, therefore the several recent amendments to the Model may not actually be in force.

In addition, the domestic anti-avoidance rules that prevents the tax convention abuse are simply safeguarding the tax rights of a country which rise through the domestic law and, only subsequently, are restricted by the provisions of tax conventions. Hence, the relation between domestic anti-avoidance rules and tax treaties results in the fact that

18 The first form is called "full exemption". In this case, the residence state is not entitled to take the income so exempted into consideration when determining the tax to be imposed on the rest of the income. So, no progression at the level of the tax rate may occur in progressive tax rate systems, as the income cannot be considered for such purpose. Hence, the full exemption method by OECD coincides with the income exemption method as it has been defined above.
In the so-called "exemption with progression" method by OECD, the income which may be taxed in the source country is not taxed by the residence country but it retains the right to take that income into consideration when determining the tax rate to be imposed on the rest of the income. (Commentary on Articles 23 A and 23 B Concerning the Methods for Elimination of Double Taxation, *Commentaries on the Articles of the Model Tax Convention*, OECD).
Therefore, the exemption with progression method by OECD reflects the above-mentioned tax exemption method.

19 In the "full credit" method, the residence state determines its tax on the basis of the taxpayer's total income including the income from the source country. It, then, allows a deduction against its own tax for the total amount of the tax paid in the source country.
Conversely, the "ordinary credit" method consists in the fact that the deduction given by residence state for the tax paid in the source country is restricted to the tax that would have been paid to the residence country. (Commentary on Articles 23 A and 23 B Concerning the Methods for Elimination of Double Taxation, *Commentaries on the Articles of the Model Tax Convention*, OECD).

any abuse of the provisions of a tax convention could also be characterised as an abuse of the provisions of domestic tax laws[20].

This is to say that anti-avoidance rules are set by domestic tax laws for determining which facts give rise to a tax liability, therefore provisions in tax conventions do not prevent the application of domestic anti-abuse rules, as there is no conflict between such rules and the provisions within tax conventions.

20 Paragraph 9.2, Commentary on Article 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.

2.3 The United States Income Tax Convention

Other tax treaty models are the United Nation Model Convention, specifically designed for developing countries, and the United States Model Convention, whose hallmark is containing several anti-avoidance rules[21].
The newest version of the latter, which is very widespread due to the strong network of commercial and diplomatic relations of the United States, was released in February 2016 by the US Treasury Department[22].

In recent times, the US has intensely contributed to the development of the 2014 OECD Model, therefore the US Model shows a number of analogies due to this cooperation[23].
The 2016 revised model presents some technical improvement but it does not show substantial changes compared to the 2006 version. Nonetheless, it introduces new provisions intended to hinder the opportunities for double non-taxation. For instance, it has introduced a new rule whereby it denies treaty benefits on deductible payments of highly mobile income (generated from intangible properties) made to related persons

21 The provisions regarding the interpretation of all the international treaties can be found in the *Vienna Convention on the Law of Treaties* (VCLT), signed in 1969 to establish a shared set of rules for the implementation of international agreements among states.
Art. 31 of the VCLT gains relevance in the field of double tax treaties since it contains the general rules for their interpretation:
"1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
(a) Any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty;
(b) Any instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
3. There shall be taken into account, together with the context:
(a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
b) Any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
(c) Any relevant rules of international law applicable in the relations between the parties.
4. A special meaning shall be given to a term if it is established that the parties so intended.".
(Art. 31, *Vienna Convention on the Law of Treaties*, 1969)

22 The Technical Explanation of the 2016 Model will be released later this year.

23 Doernberg R. L. and Van Raad K., *The 1996 United States Model Income Tax Convention*, 1997, Kluwer Law International, p. 1.

that enjoy a privileged tax regime allowing low or no tax on that income[24].

The first significant peculiarity in the US Model concerns the decisive criterion to solve the cases of dual resident companies. Whilst the OECD Model considers the place of effective management to determine the residence of a company that, due to the domestic laws, is considered resident in both countries, the 2006 US Model requires, first, to deem that company as resident of that contracting state whose law has been used to incorporate or organise the entity. In case the entity has been incorporated or organised in a third country that is not party of the convention, the competent authorities have to determine the mode of application of the convention and, if no agreement is reached, the company is not treated as resident of either contracting states for the purpose of claiming the benefits provided[25].
In the newest version, this procedure has been radically wiped out but it is still relevant because the conventions signed between 2006 and 2016 may have included this kind of provision.
In the 2016 US Model, paragraph 4 of art. 4 simply claims that whenever a company is a resident of both contracting states, it is not considered to be a resident of either countries.

Contrary to the OECD Model, art. 22 of the US Model is completely devoted to the limitation on benefit provisions whose aim is to limit the treaty shopping phenomenon. The so-called LOB clause is directed to prevent the incorporation of entities by residents of a third state that is not party of the treaty in order to take advantage of the conventional regulation.
The analysis of such provision is deferred to the following chapter.

For the relief of the double taxation, art. 23 of the US Model clearly states that the US uses the foreign tax credit methods. Hence, it allows a credit to its residents against the US tax for the taxes paid or accrued in the other country, if such taxes can be considered income taxes under the US law. Such credit is determined by the US domestic law and

24 *Preamble to 2016 US Model Income Tax Convention.*
25 *United States Model Convention of November 15 2006*, art. 4, paragraph 4.

therefore it is an ordinary credit with a per-item-of-income limitation. In addition, for the carry forward of the excess of such credit, reference should be made to the US law[26]. Conversely, the other contracting country is entitled to adopt either the exemption method, the credit method or a mixture of them both.
So, differently from the OECD Model, the US Model identifies *ex ante* the double tax relief method for its residents, leaving the decision of what method is the most suitable to the other contracting state for its residents.

In the 2016 US Model a new art. 28 has been added to hinder those cases in which a treaty partner radically changes its corporate tax system, imposing a low taxation on the cross-border income of its residents. Whenever it happens, since the negotiated benefits do not reflect the original equilibrium, the contracting countries should consult each other to determine if new amendments are required.

26 *United States Model Technical Explanation Accompanying the United States Model Income Tax Convention of November 15 2006,* art. 23 (Relief from Double Taxation).

3 Treaty Shopping

SUMMARY: 3.1 Treaty Shopping and Conduit Companies; **3.2** The Beneficial Owner Concept in the OECD Model; **3.3** Pros and Cons of the Procedural Approaches for the Identification of the Beneficial Owner Contained in the OECD Commentaries; **3.4** *Bona Fide* Provisions in the Beneficial Owner Concept Contained in the OECD Model; **3.5** The Limitation on Benefits in the US Model; **3.6** The Beneficial Owner in the US Model; **3.7** Actions against Treaty Shopping in *BEPS 2015 Final Reports*; **3.8** Conclusion.

3.1 Treaty Shopping and Conduit Companies

Treaty shopping can be defined as the artificial arrangement implemented by an economic operator in order to secure the benefits of a double tax treaty which were not intended by the contracting states in their negotiation. This activity may result in very sophisticated schemes, which are mainly put in place through the practice of using conduit companies[27] [28].

Such legal entities are used for channelling the income to those taxpayers whose residence is deemed to be in a country outside the treaty, which otherwise would not be able to benefit from the convention provisions[29].

The two basic strategies identified by the OECD Commentaries are the method of direct conduit structure and the method of the stepping stone conduit structure, which are implemented in practice by corporations using significant variations.

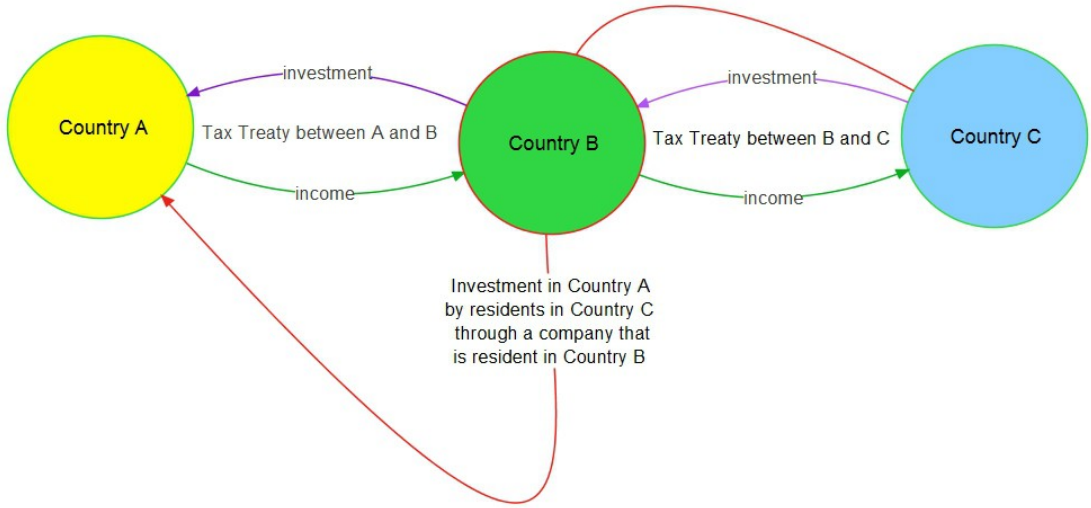
In the first, an interposed corporation, taking advantage of a tax treaty, is used to shift income to another country whose residents cannot benefit directly from the treaty provisions.

27 Even individuals may be used for such purpose (VAN WEEGHEL S., *The Improper Use of Tax Treaties*, 1998, Kluwer Law International, p. 119).

28 Paragraph 11, Commentary on Article 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.

29 Paragraph 1, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.

In other words, whenever two countries, say A and B, have entered a tax treaty whereas a third country, say C, has signed a tax treaty just with country B, the taxpayers in country C may take advantage of the tax treaty between A and B by incorporating a company in country B. Therefore, if the residents in country C want to invest in country



A, by interposing a company resident in country B, they take advantage, firstly, of the tax treaty between countries A and B, avoiding the withholding tax on the income transferred from country A to country B, and, secondly, benefit from the treaty provisions in force between countries B and C[30] with reference to the withholding tax on the dividends distributed from the company in country B to the residents of country C. Alternatively, the income may be tax-exempted in country B because of the application of a parent-subsidiary regime.

In other words, assets and rights giving rise to passive income are transferred to the company in country B to take advantage of the full or partial exemption from the withholding tax that country A would have levied in case the investment had been made directly by using a company incorporated in country C[31].

The stepping stone structure relies on the erosion of the income produced through the investment in country A by the company incorporated in country B, under the assumption that country B is a high tax jurisdiction. In this case, the corporation in

30 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, p. 205.

31 Paragraph 4, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.

country B pays another company in country D, a low tax jurisdiction, deductible expenses so that the net income in country B is lower[32]. Therefore the income arrives to the residents of country C from the company in country D, which enjoys a privileged tax regime, and not directly from the company in country B[33].

In general terms, the essence of the treaty shopping phenomenon consists in interposing a company that is entitled to claim the treaty benefit between the payer of the income and the recipient.

Nonetheless, the use of conduit companies may be led by different assumptions. If a tax treaty is in force even between countries A and C, these schemes may be used either because the treaty between countries A and B allows higher protection than the other, it can avoid the disclosure of information, or it can be used to avoid taxation in country C[34].

32 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, p. 206.
33 Paragraph 4, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.
34 Paragraph 10, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.

3.2 The Beneficial Owner Concept in the OECD Model

With reference to the treaty shopping phenomenon, there are several approaches that may be implemented by the contracting states in their double tax treaties, each of which implicates testing the genuineness of the alleged conduit company.

The legal basis of the treaty shopping practices relies on the fact that residents of the two contracting countries are entitled to claim the right to the application of the treaty provisions[35]. Therefore, the statutory definition of the criterion on which a legal or a natural person is considered to be resident is crucial, as the interposed legal structure demands the application of the double tax convention on the basis of its residence.

The OECD Model faces the matter in art. 4 and the criteria explicitly used to define the resident entity are just exemplifying cases. They are the domicile, residence, and place of management. Hence, it devolves to the domestic laws of the contracting states the identification of such criterion[36].

35 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, p. 223.

36 *"The definition refers to the concept of residence adopted in the domestic laws"* (Commentary on Articles 4 Concerning the Definition of Resident, *Commentaries on the Articles of the Model Tax Convention*, OECD).
Nevertheless, the OECD Model identifies decisive elements in order to solve the cases of the dual residence of natural persons due to disharmonies in the tax laws of the two contracting countries:
"2. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:
a) he shall be deemed to be a resident only of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests);
b) if the State in which he has his centre of vital interests cannot be determined, or
if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode;
c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national;
d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.
3. Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated."
With reference to the case of double residence of legal persons, it is established that the place of the effective management is the decisive criterion for the issue, also known as the tie breaker rule.

However, within the meaning of the OECD Model, persons are not considered to be resident of a contracting state in the sense of the convention and, thus, are not entitled to claim the application of such benefits, whenever they are considered to be resident according to the domestic laws but the only taxation levied is on the income deriving from sources or capital located in the country in which the persons are resident. This happens in case of diplomatic and consolar staff but also when foreign-held companies are exempted from taxation on the income generated abroad due to the application of special provisions.

As one of the main advantages gained through a tax convention is the reduction on the withholding tax on interests, royalties, and dividends paid to the other contracting state, the beneficial owner concept prevents the application of such reduction to those legal structures which are just the legal but not the economic beneficiary of that income[37].
On the basis of these premises, the conduit entity is not entitled to qualify as the beneficial owner of the income, hence the legal definition of beneficial owner becomes paramount. Though there is no characterisation within the OECD model of the beneficial owner, the Commentaries clarify that such term has to be interpreted in the sense that the source country is not obliged to waive its tax right whenever an intermediary is interposed between the economic beneficiary and the payer[38]. Therefore, the relief gained through the treaty is not available for the members of the conduit company that are not entitled to benefit from it directly because they are not considered to be resident within the meaning of the convention[39], despite the fact that they use an interposed entity.

The need of further specific explanations of the beneficial owner concept has been acknowledged by the Fiscal Committee of the OECD which released in 2011 the public

(Art. 4, *Model Tax Convention on Income and on Capital*, OECD).

37 Articles 10, 11, and 12, *Model Tax Convention on Income and on Capital*, OECD.

38 Paragraphs 12, 12.1, and 12.2, Commentary on Articles 10 Concerning the Taxation of Dividends.
Paragraphs 8, 9, and 10, Commentary on Articles 11 Concerning the Taxation of Interests.
Paragraphs 4, 4.1, and 4.2, Commentary on Articles 12 Concerning the Taxation of Royalties, *Commentaries on the Articles of the Model Tax Convention*, OECD.

39 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, p. 224.

discussion draft known as "*Clarification of the Meaning of the "Beneficial Owner" in the OECD Model Tax Convention*".
Since the term has given rise to different interpretations by courts and tax administrations, the discussion draft proposes a clarifying interpretation of its meaning, inviting comments from interested parties. The result of such comments has been published in the "*Revised Proposal Concerning The Meaning of Beneficial Owner in Articles 10, 11 and 12 of the OECD Model Tax Convention*".

The reports mainly debate the introduction of additional clauses to the OECD Commentaries with reference to dividends, interests and royalties.
The first issue concerns the introduction of the concept that either has an autonomous meaning within the treaty or takes into account the domestic law meaning of the term.
The discussion on the matter has led the Fiscal Committee not to take into account the national concept of the beneficial owner, not even as a secondary meaning, as this is potentially confusing.

It then discusses the characterisation of the beneficial owner, identifying the key elements of the concept as it follows. The full right to use and enjoy the income received has to be constrained because the recipient has a legal or contractual obligation to pass the payment to another person. On the basis of the contribution of the commentators, a following requirement has been added, namely that such an obligation has to be related to the payment received, so that it does not encompass the situation in which the recipient voluntarily uses the payment to satisfy other obligations that are not connected to the received income. Otherwise, the rule would have been overly broad and would have caught even legitimate situations.
The existence of such legal or contractual obligations can be proved on the basis of facts and circumstances or may be detected from relevant legal documents.

3.3 Pros and Cons of the Procedural Approaches for the Identification of the Beneficial Owner Contained in the OECD Commentaries

As the Fiscal Committee of the OECD recognised that the definition of the beneficial owner may be challenging to apply, several procedural approaches are described within the Commentaries.

The look-through approach[40] consists in denying the treaty benefits whenever a corporation is owned by non-residents of the contracting countries. In order to prevent misunderstandings, it is advisable that the two contracting states agree on which criteria a company is considered to be owned by non-residents, as the Commentaries suggest.
Such provision appears to be suitable in case of a treaty signed with a country that levies little or no taxation, where, usually, there is little substantive business activity[41]. In this case, a company incorporated in such a country is probably used as a conduit entity.
Nonetheless, the weakness of such provision relies on the fact that it merely focuses on the ownership. Hence, it can be easily bypassed by incorporating a company with little equity owned by residents and financing the entity with debt. In this case, besides the fact that the company allows to benefit from the treaty, the interest paid to the non-resident financier would erode the tax base, allowing the shifting of a considerable fraction of the income[42].

One of the most efficient approaches is the so-called base-erosion or channel approach[43]. It focuses on the amount of the tax deductible expenses paid to countries that are not encompassed in the treaty whose benefits are claimed. If that amount

40 Paragraphs 13 and 14, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.
41 Paragraph 25, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.
42 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, pp. 225 - 226.
43 Paragraphs 17 and 18, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.

exceeds a certain threshold (usually 50%), the company is not entitled to take advantage of the treaty benefits with the other contracting state[44].

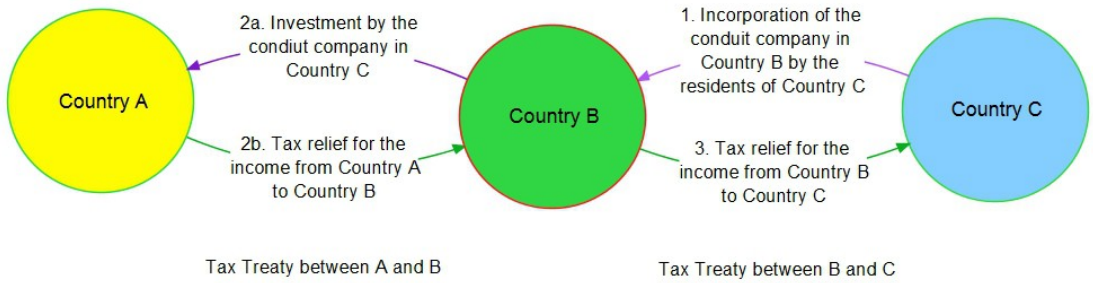
With reference to the exclusion approach[45], the key element taken into account to single out the companies that are used to benefit indirectly from a treaty is the fact that tax privileges are granted to them in their residence country, allowing little or no taxation. As these tax-exempted companies play the role of conduit companies, the benefits from the treaty between the source country and the residence country of the tax-exempted entities are denied[46].
Therefore, the treaty provision results in identifying the type of companies enjoying such a regime and denying them the treaty benefits, leading to a simple and clear application of the rule[47].

The subject-to-tax approach[48] has been developed on the idea that tax treaties should prevent double taxation and should not provide double tax exemption. Therefore, this approach relies on denying the application of the treaty benefits on the income in case the recipient does not pay taxes on that income in the country of residence.
Several scholars highlight that the differences in the tax environments lead to difficulties in assessing whether the income has been taxed and that such provision encompasses even those entities that are exempted for social reasons[49].

All the afore-mentioned approaches identify one specific trait of the treaty shopping schemes and use that element as the condition for the denial of the treaty benefits.
Effectively, it is possible to retrace the basic scheme of the treaty shopping phenomenon by using the afore-mentioned approaches:

44 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, p. 227.
45 Paragraphs 21, 21.1, and 21.2, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.
46 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, pp. 227 - 228.
47 Paragraph 28, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.
48 Paragraphs 15 and 16, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.
49 HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, p. 228.

1. The issue regarding the incorporation of the conduit company by the residents of a country that are not entitled to take advantage of the tax treaty between countries A and B is taken into account by the look-through approach;
2. Provisions affecting the investment of the conduit company in country A and the tax relief for the income deriving from such investment is not taken into account



by any of the above-mentioned approaches as the operation is in line with the aim of the treaty;
3. The transfer of the income from country B to country C is hindered through the base-erosion approach;
4. The potential circumstance that little or no taxation is levied by country B is obstructed by considering the overall taxation of the conduit entity in its residence country in the exclusion approach, whereas the subject-to-tax approach inspects only the tax treatment of the shifted income from country A to country B.

From this perspective, such provisions are implicitly implementing the beneficial owner principle, focusing on conditions that lead to the assumption that the operation is not in line with it. Nonetheless, it is advisable to insert all these provisions into a tax treaty in order to hinder more complex schemes but, at the same time, to add exceptions to the exclusion and subject-to-tax approaches, as they may encompass even entities that benefit from privileged tax regimes since they pursue public interests.

3.4 *Bona Fide* Provisions in the Beneficial Owner Concept Contained in the OECD Model

Effectively, the afore-mentioned approaches may restrict the application of the treaty even to those entities that have not been created for treaty shopping purposes, though fail to pass the tests implemented to identify the beneficial owner. Actually, such a situation often occurs in international transactions between members of the same group. With reference to this issue, the Commentaries suggest to implement *bona fide* provisions in order to exclude from the limitation of the benefits the cases that do not involve the improper use of a tax treaty[50].

The general *bona fide* provision stated by the Commentaries[51] refers to the rather vague concept of the sound business reason of the alleged conduit company. Hence, it appears not in line with the need for legal certainty because, in other words, it has to be assessed whether the purpose of the company is conducting its business.

The activity provision[52] requires that the tax relief is applied, disregarding the results of the afore-mentioned tests, only to the income generated by the resident of a contracting state that is strictly connected with the business operations. This rule seems to be in line with the aims of the tax treaties but such connection may be difficult to verify and it does not provide a means to qualify non-conduit companies and conduit entities, as the latter may conduct substantive business operations as well.

The amount of tax provision[53] denies the presumption generated through the tests whenever the amount of tax relief claimed in the source country is lower than the tax

50 Paragraph 9, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital* (full version), 2014, OECD.
51 Paragraphs 19 A, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.
52 Paragraphs 19 B, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.
53 Paragraphs 19 C, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.

paid in the residence country of the alleged conduit company. This provision basically relies on the fact that the taxes that have actually been paid are higher than the tax benefit provided by the treaty, thus, encompassing even the case of the stepping-stone structures. It therefore appears to be apt to distinguish substantive companies from conduit entities, although it is not sufficient for those cases in which genuine companies claim a higher tax relief than the tax paid in the residence country, and do not pass the tests implemented by the approaches.

Another interesting rule, the stock-exchange provision[54], requires that the shares of the company are registered on an approved stock-exchange or that they are owned directly or indirectly by residents in the country where the company itself is resident. With regards to the first option, the registration of the shares appears to be a convincing indicator of the vitality of the company, though this does not allow those companies that do not have the resources to list their share to benefit from this safeguarding provisions. On the other hand, the ownership requirement certainly distinguishes conduit entities from substantive companies but it does not consider the genuine companies, owned by non-resident, that do not pass the tests, even though they run a substantial economic activity.

The alternative relief provision[55] focuses on the fact that the owners of the conduit company have their residence in a country that has a no less advantageous tax treaty with the source country. In this case, using a conduit entity would be nonsensical. Therefore, *a contrario*, the genuineness of the company is proven. Even this rule, though, cannot redeem substantive businesses owned by non-residents that have no tax treaty in force with the source country.

In addition, the Commentaries suggest including an additional clause whereby the tax authority of the source state is entitled to ensure the treaty benefits, despite the fact that

54 Paragraphs 19 D, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.
55 Paragraphs 19 E, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.

the entity has failed to pass the tests described within the approaches[56].

The need of *bona fide* provisions basically relies on the fact that the afore-mentioned approaches are unsuitable to truly identify conduit companies. Therefore, the safeguarding rules should be developed to ensure that no substantive company can fall within the presumptions generated by the approaches. As these provisions are able to redeem just a few cases, all of these should be adopted together, despite the fact that, even intersecting all the rules, ideally, genuine businesses could be likewise affected by the presumptions, if they do not fall within the cases identified by the *bona fide* provisions.

56 Paragraphs 19, Commentary on Articles 1 Concerning the Persons Covered by the Convention, *Commentaries on the Articles of the Model Tax Convention*, OECD.

3.5 The Limitation on Benefits in the US Model

The US approach to grant the treaty benefits relies on the distinction of the residents into two categories: qualified and non-qualified persons. According to art. 22, only the first group is entitled to benefit from the treaty provisions. Hence, once a resident has satisfied one of the following tests and, for this, is a qualified person, the treaty benefits are granted regardless of the underlying motivation for choosing a particular business structure.

With reference to companies, they are considered to be qualified person if:

I. The principal class of their shares is regularly traded on one or more recognised stock-exchanges and either such stock-exchange is located in the same contracting state where the company is resident or the place of management of the company is in its residence country. The rationale of this "publicly traded test" consists in the fact that, in case of a dispersed stock ownership, it is difficult to identify the residence of the members;

II. At least 50% of the voting rights and value of the shares are owned by five or fewer companies considered as qualified persons. In other words, this rule allows the subsidiaries of a publicly traded company to qualify for treaty benefits;

III. Less than 50% of the company's gross income is paid or accrued in the form of deductible payments in the company's residence country to either non-residents or to persons related to the company that enjoy a privileged tax regime with respect to such deductible payments. This rule is known as the base-erosion test;

IV. At least 50% of the voting rights and value are owned by resident qualified persons (not only five) and less than 50% of the company's gross income is paid or accrued in the form of deductible payments to either non-residents, or to persons related to the company that enjoy a privileged tax regime with respect to such deductible payments. In this case, the residence of the member is taken into account, without establishing a maximum number, but it is matched with the base-erosion test.

The active-trade-or-business is an alternative test whose aim is granting the treaty benefits for certain items of income that are connected to the businesses activity in the residence country but are generated in the other contracting state, regardless of whether the resident is a qualified person.
According to this provision, three conditions have to be met: the person is actively conducting the trade or business in the country of residence, the income is generated in the other contracting state and that income emanates from or is incidental to that trade or business.
Nonetheless, the term "trade or business" is not defined in the US Model. Therefore, in case of an item of income derived from sources within the United States, the meaning of the term has to be found in accordance to the US law and, symmetrically, in the other contracting state.
The Technical Explanation claims that an item of income is considered to be derived in connection with a trade or business whenever the income-producing activity in the source country forms a part or is complementary to the activity carried out by the recipient of that income in its residence country. Conversely, the income from the source country is considered to be incidental to the trade or business carried out in the residence state if such productive activity eases the trade or business in the residence country.

In addition, the 2016 version excludes from the concept of active trade or business the typical activities of the holding companies, the supply of supervision or administration of a group of companies, the activity of financing the group and the making or managing investments (unless they are carried out by banks, insurance companies or by registered securities dealers). The rationale of this new provision relies on the need for counteracting the most common tax planning schemes, such as locating the holding company within a country with a strong network of treaties to avoid the withholding tax on dividends, financing the subsidiaries or supplying administrative consultancies in order to obtain deductible expenses on which no withholding tax is levied.

In case the income generating activity in the source country is carried out by a related

person or by a related enterprise[57], there must be a substantial relation between the trade or business in the residence and source states. The underlying reason of such provision consists in avoiding the fact that a conduit company, although not being considered as a qualified person[58], claims the treaty benefits for the income shifted by a related company that is resident in the other country, which conducts a business that is very weakly connected to the activity carried out by the conduit company. For this reason, a substantial connection is required.

In the 2016 US Model, it has been added the derivative beneficiary test[59] according to which a company, regardless of whether it is considered to be a qualified person, is entitled to benefit from the convention in case at least 95% of voting rights and value of its share is owned by equivalent beneficiaries, i.e. by persons who would be entitled to similar benefits, and less than 50% of the company's gross income is paid or accrued in the form of deductible payments to non-equivalent beneficiaries or to equivalent beneficiaries that enjoy a privileged tax regime with respect to such deductible payments. Such a rule has been included basically to grant the treaty benefits to those companies that, besides not being owned by residents in the two contracting countries and therefore not being considered to be qualified persons, have no reason to implement a treaty shopping structure, since the members profit from similar benefits.

The headquarter company rule[60] has been introduced in the 2016 US Model in order to entitle the active headquarter of an international group, that is resident in one of the contracting states, to benefit from the treaty provisions for the dividends and interest received by its subsidiaries. For this purpose, the company is considered to be the headquarter if its primary place of management and control is located in its residence country. In addition, to be classified as a multinational group, the structure has to be composed of companies that are resident in at least four countries not including the residence state, whose active trade or business generates at least 10% but no more than 50% of the gross income of the group. Further conditions that have to be met are that no

57 In other words, outside the case in which a permanent establishment is employed.
58 Otherwise, the benefits would be granted.
59 Art. 22, paragraph 4, *United States Model Convention 2016.*
60 Art. 22, paragraph 5, *United States Model Convention 2016.*

more than 25% of the company's gross income is derived from the other contracting country and that less than 50% of the company's gross income is paid or accrued in the form of deductible payments in the company's residence country to either non-residents, or to persons related to the company that enjoy a privileged tax regime with respect to such deductible payments.
Such a rule has been issued to promote the location of strategic headquarters within the territories of the two contracting states and such conditions are considered to be a sufficient nexus to the residence country to grant the treaty benefits with respect to interests and dividends.

The technique used by the US Model is substantially different to the one used in the OECD Model. It does not focus on the concept of the beneficial owner but instead uses an additional characteristic that the residents of the contracting countries have to meet.
Nonetheless, it considers the fact that such conditions may be too strict and therefore includes further situations that may entitle the company for the treaty benefits even if they are not considered to be qualified persons, namely the active-trade-or-business test, the derivative test, and the headquarter test.

Besides the headquarter test, which extends the treaty benefit even to those subsidiaries located outside the territories of the treaty partners, the active-trade-or-business test aims to render ineffective the practice of locating a conduit company that conducts not only a fictitious business but also an activity that is not related to the one in the source country for which the tax relief is claimed. Thus, a multinational group, whose headquarter is not located in either the two contracting states, cannot exploit the activity conducted in one contracting country for channelling the income generated in the other without paying the withholding taxes, unless the two activities are strictly connected.

Conversely, the derivative test extends the treaty benefits to those companies that are neither listed in the recognised stock-exchanges nor owned by qualified persons. In this case, the combination of the concept of the equivalent beneficiary and of the base-erosion test appears to be consistent with the general aim of preventing the treaty shopping which characterises the LOBs.

3.6 The Beneficial Owner in the US Model

The beneficial owner concept is used as an anti-treaty-shopping measure in articles 10, 11, and 12, since the aim of such practice is preventing the application of withholding taxes on dividends, interests, and royalties.

According to article 10, the taxation of dividends paid by a company that is resident in one contracting state to a beneficial owner that is a resident of the other contracting state results in a full taxation in the residence country of the recipient and a in limited right to tax for the source country.

On the other hand, art. 11 grants only to the residence country of the beneficial owner the right to tax the interests paid by a resident in the other contracting state.

Symmetrically, with respect to royalties, art. 12 claims that the residence country of the beneficial owner has a full right to tax the incoming royalties generated in the other state, denying the right to tax to the source country.

Despite the fact that the meaning of "beneficial owner" is not explained in the convention, the Technical Explanation suggests that reference should be made to the internal law of the source country. In other words, the beneficial owner of the payment is the subject to which the income is attributable under the laws of the source state.
It has to be noted that whenever the cash flow is paid by the residents in one of the contracting states to a nominee or agent that is resident in the other contracting country but on behalf of a person that is not a resident in either the two contracting parties, the income cannot benefit from the tax relief[61].

It is interesting to underline that the Technical Explanation makes reference to the

61 *United States Model Technical Explanation Accompanying the United States Model Income Tax Convention of November 15 2006*, Article 11 (Interest) and Article 12 (Royalties).

OECD Commentaries every time it deals with the meaning of the term "beneficial owner". Hence, it is possible to claim that, in case the domestic law of a contracting state does not include a definition of the beneficial owner, reference should be made to the above-mentioned OECD approaches.

For instance, within the Italian system, scholars and the Italian Courts have remarked that the key identifying element of the beneficial owner is the power of disposal of the income. To verify the presence of such element, further aspects have to be inspected, namely that the recipient has adequately contributed to the generation of the income, it bears the business risk, and that the shorter the time between the reception of the income and the subsequent payment is, the more it is likely that the foreign recipient is not the beneficial owner[62].

Circulars no. 47/E of 2 November 2005 and no. 41/E of 5 August 2011 issued by the Italian Tax Authority seem to confirm this approach. Effectively, they have closed the gap by specifying that the recipient entity of an income may be qualified as the beneficial owner only in case that, through the underlying operation, it is pursuing an economic benefit regarding its own business and this determines the ownership and the availability of that income for its purposes. Therefore, Italian taxpayers that transfer an income to a foreign entity bear the burden of proving that the foreign recipient is the beneficial owner through documentary evidence of the substantial ownership of the income by the foreign entity, since it may be a conduit company[63].

62 GIACONIA M. and PREGAGLIA A., *Interessi e dividendi infragruppo: "beneficiario effettivo" e "costruzione di puro artificio",* Fiscalità & Commercio Internazionale no. 10/2011, pp. 15 – 16.
63 FURLAN A. and COLUCCI B., *Il principio di «sufficienza probatoria» a servizio del beneficiario effettivo,* Fiscalità & Commercio Internazionale no. 12/2012, p, 30.

3.7 Actions against Treaty Shopping in *BEPS 2015 Final Reports*

Action 6 in *BEPS 2015 Final Reports* (*Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*) basically reviews the existing provisions in the OECD Model addressing the practice of treaty shopping.

In the first part of the work, it introduces a series of limitation on benefit provisions on the basis of the tax treaties concluded by the United States.
Since new amendments to US LOBs, discussed in chapter 3.5, have been added in the 2016 US Model, the OECD Fiscal Committee underlines that the regulation presented in *BEPS 2015 Final Reports*, reflecting the provisions that were contained in the US Model before the 2016 update, should be considered as a draft which will be subject to change in order to benefit from the new elements of the 2016 US Model[64].

The most innovative tool that has been provided by Action 6 is the principal purposes test (PPT). The rationale behind such provision relies on the fact that there may be treaty shopping cases that are not encompassed by the specific LOBs[65].

According to the PPT rule, a benefit arising from the convention is not granted whenever, on the basis of the results achieved through an analysis of the relevant facts and circumstances, it is reasonable to deduce that one of the main purposes of the transaction is obtaining that benefit[66].
Pursuant to PPT, the characterisation of a treaty shopping practice relies on the general element of the intention of the taxpayer, avoiding the need to identify the specific details of a scheme.

64 OECD, *Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*, in *BEPS 2015 Final Reports*, paragraph 25.
65 OECD, *Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*, in *BEPS 2015 Final Reports*, page 54.
66 OECD, *Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*, in *BEPS 2015 Final Reports*, page 55.

Nonetheless, in case the competent tax authority determines, upon the request of the person and by taking into account relevant facts and circumstances, that the same benefit would have been granted to the person, even if the contested transaction was not undertaken, the benefit should be granted. In addition, before denying the request, the competent authority has to consult its counterpart in the other contracting state[67].

Such provision, in order to hinder all the possible forms of treaty shopping, have been voluntarily designed broad enough to encompass even unpredictable situations.
Under this perspective, it is possible to understand the rationale of granting the benefit that the person would have obtained it even without the debated transaction. Having the person no reason to implement the transaction since the benefit can be claimed directly, the tax benefit cannot be considered to be the main purpose of the transaction.

67 OECD, *Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*, in *BEPS 2015 Final Reports*, pages 65 and 66.

3.8 Conclusion

The two models analysed in the preceding lines present different approaches that may be caused by the different perspective of the US Treasury Department and of the OECD. Such positions can be easily identified by making reference to the explanation of the beneficial owner concept. On one hand, massive efforts have been made by the OECD in order to provide its member countries with reliable methods to identify the beneficial owner. On the other, the US Treasury Department refers to the domestic law of the countries for the identification of such meaning.

The reason may rely on the fact that the US Treasury Department's aim is implementing a model that is in line with the US tax policy but, at the same time, does not lead to strenuous diplomatic efforts. Thus, the choice of the domestic definition certainly decreases the issues that have to be faced by the contracting countries during the negotiations.

On the contrary, since the purpose of the OECD Model is implementing effective solutions to the international trade matters, such issues have not been omitted.

Another remark concerns the function of the beneficial owner concept. In the OECD Model, it is the main means through which the treaty shopping practice is hindered. This happens because no strict LOB provision, as art. 22 in the US Model, has been included. The reason of this absence may derive from the fact that it may be not in line with the international trade agreements that a country, inclined to use the OECD Model as a guideline, may have already signed, e.g. the EU laws.

Conversely, in the US Model, the beneficial owner concept is just a secondary means to prevent the treaty shopping, as more specific provisions are contained in art. 22.

Nonetheless, Action 6 in *BEPS 2015 Final Reports* has recognised the usefulness and strength of the US LOBs by the proposal of introducing a LOBs draft on the basis of the US experience. Consequently, by the time the work of the OECD is finished, the two models will have anti-treaty-shopping sets of rules basically overlapping.

On the side of the effectiveness of the two approaches in the models, the US LOBs certainly provide rules that are in line with the need for legal certainty for a tax environment to be competitive. Nonetheless, further efforts should be made in order to balance the will of counteracting the treaty shopping with the necessity of clear tax rules, as the outcome of the US Treasury Department is a set of rules that is very challenging to grasp, verify, and prove.

Conversely, the attempt by the OECD Fiscal Committee to implement a specific regulation that is not in contrast with all the laws that may be in force in any of its members countries has lead to a series of provisions that are rather vague, providing the tax authorities with considerable discretionary powers, and, therefore, this does not comply with the need for legal certainty.

4 The Employment of Base Companies

SUMMARY: 4.1 Base Companies and Tax Avoidance; **4.2** Conventional Counteracting Measures to the Relation between the Base Company and the Source of its Income in the OECD and US Models; **4.3** The Approach to Risk Allocation in BEPS 2015 by the OECD; **4.4** The Italian Domestic Transfer Pricing Regulation; **4.5** Controlled Foreign Companies Rules; **4.6** Critics and Solutions to the Actions against the Employment of the Base Companies.

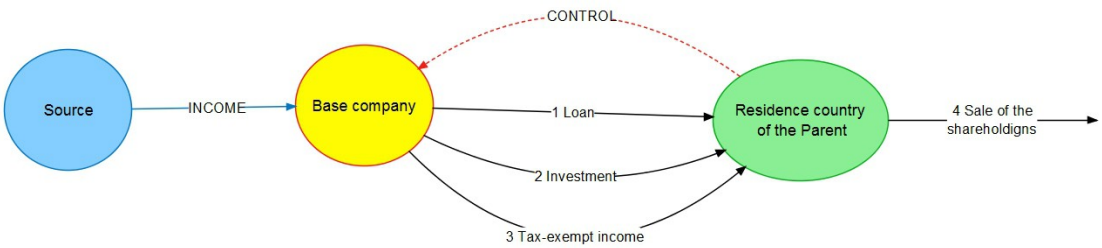
4.1 Base Companies and Tax Avoidance

The distinction between base companies and conduit companies relies on the different purposes pursued with the entity. Effectively, the use of base companies aims at minimising the tax levied on the income in residence country of the taxpayer that controls such an entity.

Notwithstanding the residence of base companies is often located in a tax haven, it may be established even in high tax jurisdictions, either because the tax rate is adequate or for privileged tax regimes granted to the company[68].

In other words, a base company is an interposed entity between the source country and the residence country of its members. The tax advantage gained through such scheme results in a mere tax deferral as long as the income is not distributed to the shareholders of the base company[69].

The final tax levy can be avoided or reduced by redirecting the income in the form of a



loan, by reinvesting the income, by distributing a tax-exempted type of income, or by

68 Paragraph 7, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital 2014* (full version), OECD.

69 Paragraph 11, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital 2014* (full version), OECD.

the sale of the shareholdings in the base company, realising a tax-exempted capital gain[70].

After having discussed the basic ways through which the tax deferral can be transformed into a tax advantage for the controlling taxpayers, it is useful to underline how the income generated through the source can be shifted to the base company.

The most common strategy consists in transferring an asset to the base company, so that the passive income generated through it is attributed to the entity for tax purpose[71].

Other secondary ways use the base company as the financing centre of the group or allocate business or professional activities within it.

70 Paragraph 12, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital 2014* (full version), OECD.

71 Paragraph 14, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital 2014* (full version), OECD.

4.2 Conventional Counteracting Measures to the Relation between the Base Company and the Source of its Income in the OECD and US Models

The transfer of the income from the source country to the base company that actually carries out little economic activity is hindered through a special *genus* of anti-avoidance provisions, known as transfer pricing rules.
Since the goal of using base companies is sheltering the collected income, such transfer pricing rules are suggested to be included in the double tax conventions by the OECD but can be found in the domestic tax law of many countries as well, as this strategy does not require a tax treaty to be in force between the two countries involved.

Art. 9 of the OECD Model, designed to counteract the use of base companies, is essentially the same as its counterpart in the US Model.
This provision basically addresses the situation wherein an enterprise of a contracting state is related to another enterprise that is resident in the other contracting country because, in this case, the likelihood of a manipulation of the price charged to international transactions is higher.
Such connection is identified by two alternative conditions. Firstly, a participation of a resident enterprise in one contracting state in the management, control or capital of an enterprise that is resident in the other contracting country is considered to be a symptom of the fact that the two parties are related. Secondly, the participation of a third person in the management, control and capital of two enterprises each of which is resident in one of the two contracting state is regarded to be sufficient evidence that the two companies are subject to the same overall strategy.
Despite the fact that art. 9 of the OECD Model focuses on the above-mentioned legal conditions, the control over an enterprise may be exercised and identified even on an economic basis, such as the right to choose the member of the management body of the related company, the control over the supply chain of the enterprise, contractual control, and all the other means through which the control is exercised over the entrepreneurial

decisions of the entity.
Whenever the arrangements or conditions applied to the commercial or financial relations between these enterprises are different from those that would have existed in the absence of the relationship, the contracting countries are entitled to adjust the income generated by following the transfer pricing rules, in order to reflect what it would have been in the absence of such a relationship.

The arm's length principle, outlined by the OECD, is a general concept according to which the international transactions between related parties should be assessed as if such companies were independent traders for tax purposes.
The reasoning behind such principle lies in the fact that the intra-group exchange of goods and services can be used in an international group to shift income from a high tax jurisdiction to a low one. In other words, it is used to avoid the fictitious tax deductible cost increase in the company located in the high tax jurisdiction and to determine the real income that has to be attributed to the entity in the low tax country.
Such a method, reflecting the functionally separate entity approach, has been sharply criticised, as it does not actually take into account the underlying economic substance. Thus, in the process of pricing the transactions, although it uses parameters such as functions performed, assets used and risks assumed, it does not consider that *"[...] intra-group contracts [...] do not transfer any functions, assets or risks outside the group [...]"*[72]. This happens because the method just recognises that, from a legal point of view, the companies are separate legal entities whereas, from an economic point of view, which is more consistent to the reality, they are always pursuing the same goal.
In addition, even the OECD has recognised that:

"*[...] the normal conflict of interests which would exist between independent parties is often absent [...] Moreover, contracts within an MNE could be quite easily altered, suspended, extended, or terminated according to the overall strategies of the MNE as a whole, and such alterations may even be made retroactively*"[73]

72 A. TING, *iTax – Apple's International Tax Structure and the Double Non-Taxation Issue*, British Tax Review, no. 1 2014, p. 56.
73 OECD, *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*.

The United States, as clarified in the Technical Explanation, generally interprets the arm's length standard in a manner that is consistent with the OECD Transfer Pricing Guidelines. For this reason, the analysis of the transfer pricing regulation can be carried out jointly.

The transfer pricing rules not only apply to the case of related enterprises but they are also used to determine the income that is attributable to an offshore permanent establishment of an enterprise located in the other contracting country.

Nonetheless, the essential procedural elements to determine the fair value of such transactions are not contained in either the OECD and US models but in the Commentaries to OECD Model, which are cited by the US Technical Explanation.

Commentary to art. 7 clearly states that the profits that would have been realised if the permanent establishment had been a separate and distinct enterprise, engaged in the same or similar activities, under the same or similar conditions and dealing entirely independently with the rest of the enterprise, should be assessed and measured as it is described in "*Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations"* (2010, OECD). The same document is recalled as a milestone even by the commentary to art. 9 concerning the taxation of associated enterprises.
Such a report offers five major relevant methods to determine the fair value of a transactions, which are briefly set out below:

The "comparable uncontrolled transfer price" method simply requires the juxtaposition of the price of the controlled transaction to the price of a comparable transaction between independent agents in similar circumstances. If there is any difference between the two prices, this may be evidence that the conditions of the commercial and financial transaction between the related companies are not at the arm's length.
The limit of such a method consists in the fact that it may be not easy to identify a transaction between independent enterprises that is similar enough to the specific case

under analysis[74].

The "resale price" method takes into account the price at which the same asset can be resold to an independent agent and sets a gross margin that has to be deducted from the resale price in order to determine the fair value of the transaction. In this case, reference can be made either to the price applied by the same intra-group seller in an uncontrolled transaction (internal comparison) or to the margin that a company outside the group earns for the same item in an uncontrolled transaction (external comparison).
When assessing an uncontrolled transaction, the more the two products sold are comparable, the more likely it is to identify the arm's length price. In other words, this method becomes less reliable whenever there are differences between the controlled and uncontrolled transaction and between the parties involved.
Another element that has to be taken into account is the time at which the comparable transactions took place. It is evident that the prices may be different not only because the one charged in the controlled transaction is not at the arm's length but it also may be due to evolutions of the conditions in the market[75].

On the other hand, the "cost plus" method sets a mark-up that represents the profit margin of a supplier that has to be added to the price at which the first company has bought the asset. Even in this case, the mark up of the supplier in the controlled transaction, ideally, should be identified by taking into account the mark up that the same intra-group supplier applies in a comparable uncontrolled transaction (internal comparison). In case this data is not available, the mark-up can be established by making reference to the mark up applied to comparable transactions between enterprises outside the group (external comparison). The considerations referred both to the comparability of the controlled and uncontrolled transactions and to the time at which they took place, stated for the resale price method, are relevant.
Moreover, in the cost plus method, additional attention should be paid to the determination of the cost, as it may vary, for instance, for the economies of scale of the

74 OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, paragraphs 2.13 – 2.16.
75 OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, paragraphs 2.21 – 2.35.

supplier and by reason of other characteristics either of the market or of the uncontrolled supplier[76].

The "transactional net margin" method is an analytical procedure which inspects a net profit indicator, i.e. a ratio of net profit relative to an appropriate base (e.g. costs, sales, assets), that a taxpayer realises from a controlled transaction with the net profit earned in comparable uncontrolled transactions. In practise, the application procedure of the transactional net margin method is very similar to the one of the method of the market multiples, used to assess the value of enterprises.
The arm's length net profit indicator observed in the controlled transaction may be determined by making reference to the net profit indicator that the same taxpayer earns in comparable uncontrolled transactions (internal comparison), or by reference to the net profit indicator earned in comparable transactions by an independent enterprise (external comparison).
According to this method, the selection of the most suitable profit indicator should be conducted considering the circumstances of the specific case and attention should be paid to the fact that the indicator may be influenced by non-relevant factors[77].

Finally, the "profit split" method aims at identifying the combined profits of the related enterprises generated from the controlled transaction and then attributes such a combined profit to the two entities on a valid economic basis, as if they were independent agents.
The economic basis may be supported either by market data or by internal data, which becomes relevant depending on the specific facts and circumstances of the case.
The result of the income splitting procedure should ideally reflect the respective contribution of the related companies to the creation of the income[78].

The selection of a transfer pricing method should aim at finding the most suitable

76 OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, paragraphs 2.39 – 2.51.
77 OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, paragraphs 2.58 – 2.67.
78 OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, paragraphs 2.108 – 2.114.

procedure for the specific case because none of them is appropriate for every possible situation. Such selection process should be conducted by taking into account the strengths and weaknesses of each method and the availability of the required data.

Both the US and the OECD models state that whenever one of the two contracting states adjusts the income of a related company that is resident within its territory, and the other country agrees on the fact that such adjustment properly reflects the arm's-length conditions, the latter tax jurisdiction shall grant a corresponding adjustment to the tax liability of company that is resident therein[79].

In case the competent authorities disagree with the adjustment, they can consult each other following the mutual agreement procedure of art. 25.

Whenever an adjustment has been made, one of the two related parties has its possession funds that it would not have had at arm's length and, according to the OECD Commentaries and to the Technical Explanation to the US Model, for the treatment of such funds reference should be made to the domestic law of the contracting country involved[80].

In the United States the general practice is to treat such funds as dividends or contributions to capital, depending on the relationship between the parties. Under certain circumstances, the parties may be permitted to restore the funds to the party that would have owned them if the transaction had been at the arm's length[81].

79 OECD, *2014 Model Tax Convention on Income and on Capital,* art. 9 paragraph 2.
United States Model Convention (2016), art. 9 paragraph 2.

80 *United States Model Technical Explanation Accompanying the United States Model Income Tax Convention of November 15 2006*, Article 9 (Associated Enterprises) paragraph 2.
OECD, *Commentaries on the Articles of the Model Tax Convention,* 2014, Commentary on Article 9 Concerning the Taxation of Associated Enterprises, paragraph 2, points 8 – 11.

81 *United States Model Technical Explanation Accompanying the United States Model Income Tax Convention of November 15 2006*, Article 9 (Associated Enterprises) paragraph 2.

4.3 The Approach to Risk Allocation in BEPS 2015 by the OECD

In *BEPS 2015 Final Reports*, a section of the work (Actions 8 – 10, *Aligning Transfer Pricing to Value Creation*) is devoted to the update of the transfer pricing rules in order to better reflect the global value creation of a multinational group.

One of the major topics faced in Action 8 concerns the risk allocation among the group companies and tries to determine its influence over the price determination in a controlled transaction.
In other words, the OECD has tried to answer the critiques presented in the previous chapter, according to which intra-group contracts do not transfer any risk outside the group considered as a whole and that there is no conflict of interests amongst related parties.
To do so, a detailed procedure, aiming at identifying the risk allocation in a controlled transaction, has been outlined together with a specific technical terminology which is exposed in the following lines.

Since the transfer price methods rely on the comparison between controlled and uncontrolled transaction, a correct approach should start first with a deep understanding of the industry sector within which the multinational group operates. In addition, the functions carried out by each group member along with the commercial and financial relations amongst them should be inspected through the analysis of the controlled transactions within the multinational group[82].

Once a controlled transaction is examined for transfer price purposes, its relevant characteristics (such as functions performed, risk assumed and assets used by each party as well as contractual terms, economic circumstances, business strategies pursued, and

82 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraph 1.35.

features of property transferred or services provided) have to be seen as the comparability factors that should ideally coincide with those in the uncontrolled transaction. In fact, since the price of the uncontrolled transaction is considered the arm's-length price, if any differences in the comparability factors are found, the adjustment of the uncontrolled price is required to reflect this diversity[83].

Despite the fact that a contract should reveal the obligation and rights, price arrangements and risk assumed by the contracting parties, in case the associated enterprises enter into a transaction, attention should be paid even to the real conduct of the entities, since the goal they are actually pursuing can be found at the level of the group as a whole. This happens because the control of the parent company can influence the relations between contracting parties, so the controlled companies can ignore or modify the terms of the contract after it has been concluded without any legal consequence[84].

Given the fact that the price of a transaction is influenced by the functions that each party performs, a functional analysis is required to define the activities and responsibilities, risk assumed and assets used according to the agreement. Nonetheless, in a controlled transaction, it should be inspected if the management bodies of the parties are free to define their own strategy or are directed by another group member.
For this purpose, in case of a highly fragmented value chain, scattered amongst the group members, it is likely that the group companies are co-ordinated by the parent, so it is essential to determine how the decision making process is structured[85].

Since the risk taken on by each enterprise influences the price of the transaction, it is crucial to identify which kind of risk has been assumed and what party bears the specific risk. Considering the fact that risk is inherent to economic activities, the risk assumed by each enterprise can be identified through the analysis of the commercial and

83 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.36 and 1.38.
84 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.42 and 1.45.
85 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.51.

financial relation between the contracting parties.
For the identification of the economically relevant risk assumed through a contract, it is fundamental to determine what are the sources of uncertainty, since the risk is the effect of the uncertainty in reaching the objectives of a business.
The kind of risk varies a lot depending on how the transaction is structured. For instance, the uncertainty about the productive process gives rise to operational risk, whereas marketplace risk is caused by the underlying uncertainty in the identification of the trends of the market[86].

Conversely, risk management is the activity through which the risk of an enterprise is administrated. According to Action 8, risk management can be divided into three elements, namely the decision making process of accepting or refusing a risk associated with an opportunity, the definition of the strategy to manage a risk that has already been assumed, and the activity of monitoring the evolution of the risk.
Nonetheless, it is essential to understand that the party that bears the risk may not perform the risk management of that specific risk.
To assess whether a company performs the risk management, it should be understood if the entity has the competence to manage the risk, has access to the relevant information, and analyses the information gathered. Such aspects have to be taken into account because a mere formalisation of the decision is not sufficient to prove control over a specific risk.
Once a specific risk and a comparable uncontrolled transaction have been identified, it should be determined whether the uncontrolled agreement includes the same level of risk and management risk in order to interpret the differences in the prices charged[87].

Another element to be inspected is the capacity of an entity to have access to funds to assume or lay off the risk and to respond to its consequences (financial capacity).
Such assessment should be made by making reference to independent parties, taking into account all the assets at disposal of the enterprise. Nonetheless, the fact that a group

86 OECD, *Action 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.56 – 1.58, and 1.72.
87 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.61, 1.63, 1.66, and 1.73.

member provides the funds related to the risk, it does not mean that the providing company bears that specific risk. It just bears the financial risk associated with the specific risk[88].

Further evidence of the intention of the parties is the written contract, which can be used to understand what risks have been assumed by each enterprise. Nevertheless, it can be interpreted to set out the risks that have been implicitly taken on.
Despite the fact that the contractual risk allocation influences the arm's-length price charged to the transaction, it is the real assumption of the risk, which can be determined by making reference to the risk management and to the distribution of the risk outcomes, that guides the selection of the transfer pricing method[89].

Once it has been established what party assumes and manages the risk, bears the risk consequences, and has the financial capacity related to the risk, the results have to be interpreted. It has to be inspected whether the conduct of the party reflects the contractual terms, whether the contract is followed as if they were independent agents, and whether the risk assuming party performs the risk management and has the necessary financial capacity.
In case the conduct of the parties is not in line with the agreement, the conduct should be considered to be the evidence of the enterprises' intention with reference to the assumption of the risk.
Whenever the risk assuming company does not perform the risk management, a comparison should be made with a comparable uncontrolled transaction in order to determine the level of control over the risk that an independent agent would have performed[90].

After having verified that the risk is not allocated to the same party that performs the risk management and/or has the financial capacity to assume the risk, the risk should be

88 OECD, *Action 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraph 1.64.
89 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.77 and 1.81.
90 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraphs 1.86, 1.88, and 1.97.

shifted to the party that exercises the control or has the financial capacity. Therefore, the price charged to the transaction should be redefined to assign the right remuneration to the risk controlling and financing party.
In other words, the risk re-location influences the selection of the comparable uncontrolled transaction, on the basis of which the price comparison should be made[91].

In evaluating whether the *BEPS 2015 Final Reports* have properly made adjustments to the prior transfer pricing regime, a number of considerations have to be presented.

With reference to the critique according to which related parties can modify the contract after it has been concluded, it should be noted that this is just a possibility. Therefore, it is not acceptable to deny the worthiness of the transfer pricing rules just on this basis, since, in case the contract eventually does not reflect the conduct of the parties, the tax authorities prioritise the real behaviours of the parties to determine the relevant characteristics for transfer pricing purposes.

On the other hand, in case of a controlled transaction, it is true that the risk is not shifted outside the group. Nonetheless, considering that the aim of the transfer pricing rules is to distribute the income amongst the group companies, even the risk inherent to any transaction amongst related parties has to be taken into account to determine the arm's-length price.
Therefore, the choice of attributing the risk to the risk controlling or funds providing group member appears to be in line to the arm's-length principle, despite the fact that it can be difficult to assess in some cases and that other cost-efficient methods, presented in chapter number 4.6, are available.

91 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* paragraph 1.98.

4.4 The Italian Domestic Transfer Pricing Regulation

Despite the recommendations by the OECD for the implementation of the transfer pricing rules in a double tax treaty, it is essential to understand what is the approach followed by the Italian domestic law with reference to the base companies.

From the Italian perspective, the provision through which the arm's length principle is introduced in the domestic framework is paragraph 7 of art. 110 of Presidential Decree no. 917 of 22 December 1986, whereby international transactions between related parties has to be priced, for tax purposes, by making reference to normal value concept.
Specifically, art. 110 states that transactions between a resident and a non-resident company that, directly or indirectly, is controlled[92] by the resident entity, controls it, or both are controlled[93] by a third entity shall be assessed according to the normal value concept of art. 9.
If the above-mentioned conditions are met, the income rising from those transactions has to be assessed at its normal value for tax purposes only if it entails an increase of the tax base. If the application of the provision leads to a decrease of the tax base, the normal value of the transaction is admitted only if there is an agreement with the tax authority of the other state which consequently taxes the income that is not taxed in Italy due to the reduction of the tax base.

The normal value[94] has to be identified, in accordance to art. 9, primarily, by reference to the price catalogue of the supplier or, missing it, by reference to the price catalogue

92 Within the meaning of art. 2359 of the Italian Civil Code, an entity is deem to be controlled if:
1 a person holds, directly or indirectly, the majority of the votes at the shareholders' meeting;
2 a person holds, directly or indirectly, sufficient votes to exert a decisive influence in the shareholders' meeting;
3 the entity is under the dominant influence of another person due to a special contractual relationship.

93 In this case, the Ministerial Circular no. 32 of 22 September 1980 claims that this concept of control is wider than the one provided in art. 2359 of the Italian Civil Code, including all the cases in which an existing or potential economic influence may be inferred from the factual circumstances.

94 The normal value is a concept that has more than one function under the Italian law.
Not only it is used for the application of the domestic legislation on the transfer price but also to assess the income rising from a *datio in solutum*.

of the Italian Chamber of Commerce and to the professional fees. Whenever it is not possible to asses the normal value by taking into account such parameters, it has to be set as the payment ordinarily exchanged for that specific type of goods and services or similar, between independent agents at the same phase of the trade, in the same place and at the same time in which such goods and services have been exchanged or, in absence of them, in the closest place and at the closest time[95].

Although such definition appears to be in line with the arm's length principle, further explanation of the normal value can be found in the Ministerial Circular no. 32 of 22 September 1980 and no. 42 of 12 December 1981. Basically, the circulars conclude that for the interpretation of the normal value reference should be made to the principles set out by the "*Transfer Pricing and Multinational Enterprises*" report published in 1979 by the OECD. Consequently, even the Italian Tax Authority indicated that the term normal value used in the Italian Tax Code has to be considered as having the same meaning as the arm's length principle by the OECD.
Despite the fact that the 1979 report by the OECD has been repeatedly substituted with more recent versions but no changes in the circulars have been made, scholars agree that reference should be made to the latest version of the document[96].

Therefore, even the Actions 8 - 10 in *BEPS 2015 Final Reports*, that are considered to be amendments to the Transfer Pricing Guidelines[97], apply to the Italian legal system.

95 The price of shares, bonds and other types of stock is determined following other methods (see art. 9, paragraph 4 of Presidential Decree no. 917 of 22 December 1986).
96 INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *Transfer Pricing and Intangibles*, Vol. 92 A, 2007, Sdu The Netherlands, pp. 359 – 362.
97 OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports,* page 10.

4.5 Controlled Foreign Companies Rules

A number of countries have developed specific provisions, known as Controlled Foreign Companies (CFC) rules, within their tax system to counteract the sheltering of income into a base company, put into practice to shrink the tax base of the controlling shareholders in their residence country.

Under certain conditions, the sheltered income is taxed in the hands of its shareholders to ensure that profits generated through the CFC are included in the tax base of the parent.

Such provisions basically apply on the assumptions that the income is distributed as a fictive dividend, since there is no real economic activity carried out by the base company, that the activity of the company is not autonomous and it therefore has to be attributed to the shareholder, and that the ability to pay of the taxpayer has actually increased, as the taxpayer has the income at his disposal[98].

It is worth saying that the EU law imposes limitations on the development of a CFC regime. The European Court of Justice[99] has set out the principle whereby such anti-avoidance provisions do not contrast with the European regulation (freedom of establishment and non-discrimination) only in case they apply to wholly artificial arrangements that do not reflect economic reality, having the sole purpose of obtaining a tax advantage.

Therefore, EU Member States should include in their CFC system a substance analysis so that such rules do not apply to genuine economic activities. In addition, to avoid discriminations against non-residents, the regime should applied both to domestic and cross-border subsidiaries.

Wittily, Action 3 in *BEPS 2015 Final Reports* (*Designing Effective Controlled Foreign Companies Rules*) suggests that justifying the application of the CFC regime with the need of preventing tax avoidance and maintaining a balanced allocation of the tax rights

98 Paragraph 24, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital 2014* (full version), OECD.

99 In Cadbury Schweppers (ECJ, C – 196/04) and subsequent cases.

would allow EU Member States to counteract even those arrangements that are not wholly artificial.

The issue concerning the use of base companies relies on the fact that the residence country of the controlling taxpayer is not able to tax the income since it is sheltered in the base entity, though it is economically attributable to its resident taxpayer.
The purpose of providing governments with effective CFC rules has led the OECD to devote Action 3 in *BEPS 2015 Final Reports* to the definition of a CFC regime that can be easily adapted to suit the diverse policies of the countries.
In this section of the work, the experiences of those countries having domestic CFC rules in force are taken into account and updated in order to face the new challenges of tax engineering.

According to Action 3, to avoid the parent company circumventing the system simply by changing the legal form of it subsidiaries, CFC rules should apply even to trusts and partnerships, whenever the income generated is not taxed in the parent jurisdiction.
In addition, related parties can be treated as the same entity in the CFC regime so that deductible payments among them are not taken into account in the parent jurisdiction[100].

The employment of a permanent establishment (PE) by the base company becomes relevant in the CFC system whenever the CFC establishes a PE in the same residence country of its controlling shareholders and when the PE is located in a third jurisdiction.
A permanent establishment (PE), also called branch, is a concept that is used by many jurisdictions in order to define a minimum presence to tax a non-resident[101].
It is described as *"a fixed place of business through which the business of an enterprise is wholly or partly carried on"* by art. 5 of the OECD Model, which cosiders to be a PE

100OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 24.

101This approach is not uniformly followed world-wide. For instance, the United Kingdom tax policy imposes the taxation of the income without regard to how small the part of business that took place in the UK territory is. This approach is known as carrying on a business or trade concept and it is typical of the Anglo-Saxon countries. It is not defined by law but rather in case law and it extends the tax rights of the state to non-fixed businesses when contracts are regularly concluded with local customers or the key activities of the economic process are carried out within the territory. (ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning*, 2015,Kluwer Law International BV, p. 309).

even the case of a dependent agent that acts *"on behalf of an enterprise and has, and habitually exercises, in a Contracting State an authority to conclude contracts in the name of the enterprise"* (agency permanent establishment)[102].

In case of a base company having a PE in the residence country of its members, since only the income generated therein is taxable, CFC rules should apply only to the CFC income that has not been generated through the PE.
On the contrary, whenever the branch is established in a third country and there is concern that the PE is used to shelter the income, the CFC regime should encompass even the branch income.

On the side of the control, the typical tools used are: setting the minimum holding percentage of the shares in the subsidiaries (usually 50%), inspecting the economic control on the company, which can be summed up with the entitlement to the underlying value of the CFC, identifying the person that *de facto* controls the CFC (the top-level decision maker), or through the inclusion of the CFC in the consolidated financial account of the parent based on the IFRS.
In the above-mentioned control definition even the indirect control should be included, otherwise the CFC regime could be easily circumvented by interposing other companies[103].

Since the control can be exercised by the minority shareholders jointly, Action 3 suggests applying a fact-based test whereby, in case the shareholders are actually acting together to influence the base company, their percentage of control is summed up to

102From the perspective of the domestic law, the permanent establishment concept is used to establish that nexus that entails the limited tax liability of a non-resident in the country of the source.
On the contrary, in the OECD Model, the branch is used to waive the tax right of the residence country on the profits generated through a PE in the other contracting state. Whenever the foreign investor's activity does not fall within the PE statutory definition, the provisions of the tax treaty do not apply.
Since tax rights do not arise through the double tax treaties, the dis-application of the provisions contained within it does not entail that a country cannot tax a taxable event under its domestic law. Therefore, the domestic characterisation of the PE becomes relevant. In case such activity does not even fall within the domestic PE definition, the profits generated through the branch are taxed only by the residence state, if it applies the world-wide system.

103OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 35.

determine whether the controlling threshold has been met[104].

Another method consists in taking into account the relationships among the minority shareholders in order to understand if they are influencing the CFC.

The third approach requires the aggregation of the controlling interests only in case they exceed a certain threshold (usually 10%).

Alternatively, the threshold requirement (50%) can be considered to be met whenever a given number of shareholders (for e.g. 5) jointly reach that percentage.

Since even unrelated parties could act together to influence a CFC's policy, CFC rules can be designed taking into account even the economic interests of foreign taxpayers, depending on the country's policy[105].

The inclusion of the exemption and threshold requirement in a CFC system is suggested by Action 3 in *BEPS 2015 Final Reports* to exclude from the CFC regime those companies that are subject to an effective tax rate that is basically at a similar level to the one applied in the parent country and to reduce the administrative burden.

The exclusion of a company may be caused by the fact that the CFC income is lower than a predetermined amount, so that insignificant situations are not considered.

Nonetheless, since the fragmentation of the income into several CFCs allows the avoidance of the rule, it is recommended to include an anti-avoidance rule whereby, in case the purpose of separating of the activities into more companies is avoiding surpassing the threshold, the CFCs are considered to be a single entity.

Conversely, the threshold can be considered to be exceeded by making reference to the overall income of the CFCs that are controlled by the same shareholder[106].

On the other hand, by classifying either those countries applying a tax rate above a certain level (white lists) or tax havens (black lists), it is possible to define which CFCs should be exempted or included into the CFC regime[107].

The employment of the solution of listing the countries appears to be more advisable in

104OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraphs 37 - 39.

105OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraphs 41, 43 and 45.

106OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraphs 51, 53 and 54.

107OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 62.

comparison to the first, since it makes the application of the rule easier and more cost-efficient.

With reference to the attribution of the income of a CFC to the controlling shareholders, the attributable income may be identified through its legal characterisation. In this way, only the income category that is considered to be at risk is attributed to the parent (for e.g. royalties)[108].

Alternatively, only the income generated through transactions amongst related parties can be attributed to the controlling shareholders, under the assumption that in a controlled transaction the risk of shifting income is higher.

Nonetheless, several countries attribute only the income that a CFC has earned through cross-border transactions to the parent because they consider that the domestic trade in the CFC residence country cannot be used to shift the profits to other jurisdictions.

Instead, other countries have opted for a substance analysis on the basis of the workers, assets and risks allocated in the CFC in order to assess whether the company has conducted an economic activity that is consistent to the income earned[109].

Alternatively, the excess profit analysis can be used to inspect whether the income earned by the CFC exceeds the normal return an investor would expect with respect to an equity investment in that same country. Whenever the income is grater, it is likely that the company is pursuing the goal of sheltering the income[110].

Furthermore, Action 3 suggests determining the CFC income according to the principles in the parent country, to avoid the application of more favourable standards of the CFC jurisdiction, and to use the CFC losses only to offset the income of other CFCs that are resident in the same country, in order to prevent that the CFCs losses are used to lower the tax base of the parent[111].

After having determined the CFC income, it should be attributed to the controlling

108OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 77 and 78.

109OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraphs 79 – 81.

110OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 89.

111OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 99.

persons proportionally to their controlling interests and period of ownership or influence[112].

With reference to the double taxation that may arise in case the CFC is taxed in its residence country or when more jurisdictions apply the CFC rules to the same income, a tax credit should be granted for the taxes paid abroad.
Conversely, the residence country of the shareholders should allow an exemption for the dividends distributed by the CFC, in case the same income has already been taxed in their hands because of the CFC regime[113].

The presence of the CFC Rules in a double tax treaty context have been criticised on the basis that the country of residence of the base company members is basically disregarding the base company as a person and that this is contrary to the conventional provisions. Nonetheless, through the use of such a scheme, the effect results in an indefinite tax deferral, which is not in line with the general aims of double tax treaties[114]. Therefore, the issue of using CFC Rules should be reinterpreted as the activity through which a country pursues the goal of safeguarding its own tax rights on the taxable events determined by the law.

112OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 111.
113OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 123.
114Paragraphs 44 and 45, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital 2014* (full version), OECD.

4.6 Critics and Solutions to the Actions against the Employment of the Base Companies

The commonly adopted method of separately taxing a corporate entity consists in determining its tax base, including those transactions that took place amongst its related parties (separate entity approach). The price of those transactions, for tax purposes, is determined consistently with the arm's length principle and, therefore, such price influences the tax base of the corporations involved. Nonetheless, despite the numerous methods outlined to implement the arm's length principle, none of them seems to be suitable to take into consideration that, whenever the parties involved in a contract pursue the same goal, the traditional conflict of interest between the contracting parties is missing. Therefore, albeit these techniques assess the transactions as if they were concluded amongst independent agents, the result is unsatisfactory, as it does not recognise that the parties could rescind the contract whenever they wish, without any legal consequence.
For these reasons, in the following lines the transparent and the consolidated taxation are analysed as they may tackle the shortcomings of the transfer pricing rules.

The aforementioned separate entity approach is the most wide spread and consists in the fact that a business, legally organised as a corporation, is subject to corporate income tax. In this case, two levels of taxation can be identified: the level of the corporation and the level of the shareholders. In the latter, the income is taken into account to determine their tax base either for the personal income tax[115], if the members are natural persons, or for the corporate income tax, whenever they are legal persons[116].
On the contrary, another method, known as “transparent taxation”, consists in having just one level of taxation, as the income generated through the business organised in the legal form of a corporation is passed through to the shareholders and taxed in their

115Such income is generally qualified as capital income but, if the shareholdings are held within a business owned by the natural person, it may be classify as business income.
116Nontheless, many tax environments, such as Italy, grant a partial exemption on such income since it has already been taxed at the level of the company.

hands. As a result, in case of natural persons, it is taxed with the personal income tax, whereas, in case of legal persons, it is taxed with the corporate income tax (pass-through approach)[117].

The rationale behind the transfer pricing rules can be summarised, broadly speaking, in avoiding that the income retained in the base company is shifted to its member not in the form of dividends but as a different kind of income through unequal contracts that generate deductible expenses. In this way, the deductible expenses erode the tax base of the base company, leading to the lowest possible taxation, and, at the same time, the cash is transferred to its members.
The transparent taxation appears to be a good solution to bypass the problem of assessing such transactions at their fair value and for this reason it has been chosen by the governments as the mechanism behind the CFC rules.
So, since the aim of using the base company is to retain the income into such entity, in case it is subject to the transparent taxation, this effect is missing because the income is taxed in the hands of the final shareholders.
Therefore, with the transparent taxation, the value assigned to the transactions among related parties becomes irrelevant, once the base company has been identified and is subject to the CFC rules since it is used as a storage device for the income.

In addition, the transparent taxation allows an easier computation of the overall tax burden. The total taxation in the separate entity approach depends on three variables: the tax rate at the level of the corporation, the exemption rate of the dividends, and the tax rate in the country of the shareholders, which may apply a progressive tax rate system.
On the other hand, whenever a company is taxed as transparent, just the tax rate applied to the shareholders is critical, as its income is added to the tax base of the shareholders and then taxed.

Another issue to take into consideration is the determination of the tax base. An income generated within a business of a corporation, for corporate income tax, is always

117ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, page 130.

considered to be as a business income whereas, for personal income purpose, the income generated through a business may fall within different class of income, depending on the domestic provisions, if it is not generated through a business which is owned by the natural person as a sole proprietorship. Therefore, attention should be paid when the income of a corporation is taxed in the hands of its members as a result of the transparent taxation, since special provisions may be applicable for the determination of the tax base[118].

Conversely, the opportunity to consolidate the overall income of a group for tax purposes, known as tax consolidation, entails that the group is taxed as if it was a single entity. From this perspective, it is evident that transactions amongst group members are not considered in the consolidated tax base, as they offset each other.
In other words, even tax consolidation can be used to counteract the weaknesses of the transfer pricing rules since it considers just the transactions concluded with parties that are outside the group, which are priced consistently with the arm's length principle.

However, in a progressive tax rate system, the tax consolidation can lead to disadvantages whenever the sum of all the incomes both of the parent and of the subsidiaries cause the advance to a higher tax rate.

Nonetheless, the separate entity approach has another weak point that can be bypassed with tax consolidation, namely that the losses generated in a subsidiary cannot offset the profits of the parent[119].
Therefore, in tax consolidation, whenever the profits offsets the losses, the benefit may be higher in a progressive tax rate system, as it may cause the application of a lower tax rate. All this is to say that, whenever a progressive tax rate applies to the corporate income tax, the tax consolidation is convenient for the taxpayer only if the generation of losses is expected at some level of the group.

118OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports,* paragraph 73.
119Symmetrically, as the participation exemption consists in exempting (partially or fully) the capital gain from the sale of shareholdings and divides, it consequently entails that neither unrealised losses nor capital losses can be deducted against the tax base.

At the European level, the European Commission, aware of the weakness of the transfer pricing methods, has released the Draft Council Directive on a Common Consolidated Corporate Tax Base (COM 121/4, 2011).

The unfinished project seeks to introduce an optional regime for the European multinational groups, which consists in a common set of accounting principles for the determination of the tax base of the member companies, the consolidation of each tax base computed at the level of the group members and the allocation of the overall tax base in those countries where the member companies are located. To do so, it has developed a formula apportionment to proportionally distribute the consolidated tax base amongst European jurisdictions on the basis of the profit generating activities that took place in each country with respect to the overall business that has been conducted at the European level. The parameters taken into account in the Draft Council Directive are: sales, payroll, number of employees and assets.

This sharing mechanism becomes relevant with reference to the above-mentioned shortcomings of the transfer pricing rules as it bypasses the limits of the separate entity approach, which necessarily requires the application of the arm's length principle.

Thus, the apportionment formula allows the distribution of the income among the involved countries, regardless to the assessment of the intra-group transactions[120].

Nonetheless, there is a significant procedural difference between tax consolidation and the European common consolidated tax base.

Firstly, in tax consolidation, earnings and costs offset each other, as the accounting data of the company members are gathered together to determine the tax base. Conversely, in the European common consolidated tax base, every group member separately determines its profits, so the earnings and costs of the intra-group transactions are taken into account to determine the income pf each single company. Then, the profits are gathered together and only subsequently are distributed to each entity by means of the formula apportionment.

In addition, in tax consolidation, a single tax rate applies to the consolidated tax base

120D. ENDRES and C. SPENGEL, *International Company Taxation and Tax Planning*, Kluwer Law International BV, 2015, pp. 373 - 379.

whereas, in the European common consolidated tax base, the overall tax base, shifted to the various countries, is subject to different domestic tax rates.
Moreover, despite tax consolidation and the European common consolidated tax base appears to be similar, they show another substantial difference even on the procedural issue.
On one hand, the European common consolidated tax base requires a high level of cooperation amongst the European countries involved in the tax base sharing process. Whereas, tax consolidation entails that just one tax authority has to take into account different economic activities that took place in different countries[121].

Finally, it has to be remarked that, in many jurisdictions, tax consolidation is not mandatory, as it is not the European common consolidated tax base. Hence, being the management body of a multinational group aware that this regime is able to frustrate the effect of their strategies of income retention, it is very unlikely that they choose to implement this option.
Effectively, opting for tax consolidation and for the European common consolidated tax base entails waiving the majority of a company's tax planning opportunities.

Nonetheless, since the European common consolidated tax base applies the formula apportionment, this fact gives rise to new methods of tax planning, as it is possible for the company to relocate its profit generating activities in low tax jurisdictions, so that the distribution of the consolidated income through the formula apportionment leads to the allocation of the largest part of the tax base in such countries[122].

On the other hand, it is particularly interesting to note that the formula apportionment does not consider the intangible assets as profit generating activities. The rationale of this loophole basically relies on the fact that intangible assets are difficult to assess. Hence, if such an approach was extended to intangibles, further tax planning schemes would be available through the intellectual properties management. Thus, they would

121L. BUCCI, V. CAPOZZI, and M. GALLUCCI, *La disciplina IRES dei gruppi di imprese*, Giuffrè Editore, 2006, p. 124.
122D. ENDRES and C. SPENGEL, *International Company Taxation and Tax Planning*, Kluwer Law International BV, 2015, p. 382.

give an additional lever for the manipulation of the income sharing mechanism, if they were included in the formula apportionment. In other words, intellectual properties could be relocated, in order to obtain the income shifting to low tax jurisdictions, and overestimated, so that a higher portion of the overall tax base is directed to such countries[123].

123ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV, pages 382 and 383.

5 The Mandatory Disclosure Regime in *BEPS 2015 Final Reports*

SUMMARY: 5.1 The Working Principles of the Mandatory Disclosure Regime; **5.2** Mandatory Disclosure Regime Applied to International Tax Planning.

5.1 The Working Principles of the Mandatory Disclosure Regime

In Action no. 12, part of the BEPS project concluded in 2015 by the OECD, basic rules and principles are set out for the design of a mandatory disclosure regime, whose aim is to provide the tax administrations with timely, relevant, and comprehensive information about aggressive tax planning[124].

In order not to increase the compliance costs for the taxpayer and not to provide tax administrations with unnecessary information, thresholds and hallmarks have to be outlined to identify the features of the tax planning schemes that tax administrations consider to be relevant.
In other words, the government should define what strategies have to be disclosed, called reportable transactions, by defining the elements that characterise them and that are relevant for the specific jurisdiction (the hallmarks). Under this perspective, the tax administration's resources needed to carry out the analysis of the collected data can be minimised, with lower expenses for the administrative apparatus[125].

The rationale behind the generic hallmarks identified by the OECD Report, focusing on the relation between the tax advisor and the taxpayer, is recognising new tax planning methods, whose characteristics cannot be singled out because no similar strategy is known by the tax administration[126].

124OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 5.
125OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 12.
126OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 91.

The confidentiality obligation owed by the client to the promoter[127] consists in the fact that the taxpayer is not entitled to reveal the scheme designed by the tax advisor[128].
Such contractual clause is considered by the OECD to be relevant as it may indicate that the tax scheme is innovative and that it is suitable to be marketed.

Another generic element used in countries such as UK, US, Ireland and Canada is the premium fee.
A premium fee is a reward for the tax advice that is considerably higher in comparison to the one usually charged by the tax consultant. Its presence is interpreted as evidence that the tax advice has been specifically tailored for the taxpayer and that it leads to significant tax savings for the enterprise[129].

A further hallmark that calls attention to the fact that a revolutionary tax strategy may have been developed is the contractual protection that the taxpayer and the advisor may obtain due to any form of insurance for the failure of the tax scheme and for the covering of taxpayer's legal expenses in case of a dispute regarding the tax benefits arising from the transaction[130].

Conversely, specific hallmarks encompass those arrangements that are considered to be at risk by the tax administration, identifying the relevant transactions by the employment particular elements.
The most widespread elements are the transfer of losses, leasing agreements, the transformation of income into capital or gifts, those transactions involving a listed tax haven jurisdiction, and the use of convertible loans or tax driven financial instruments.
Another way of developing specific hallmarks consists in listing the agreements that, in the opinion of the tax administration, can be potentially used to pursue tax avoidance purposes. For this intent, governments have access to the Aggressive Tax Planning

127The promoter definition in Action no. 12 (BEPS Project) encompasses both tax advisers promoting aggressive tax planning schemes and intermediaries that ease the implementation of a reportable scheme.
128OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 95.
129OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 98.
130OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 101.

Directory of the OECD, a secure database of aggressive tax planning trends which even provides procedures to detect and counteract those strategies[131].

Once the reportable transactions have been defined, the governments have to choose how to implement the duty of revealing the full details of the agreement.

The information disclosure is a legal obligation that the countries may impose either only on the promoter or both on the promoter and on the taxpayer.

The disclosure obligation on the promoter is triggered at the moment at which the scheme is sufficiently well-developed and, for this reason, it is available to users for implementation[132]. The deadline by which the promoter has to comply with the disclosure obligation may vary depending on the countries' policies (in UK only five working days are left to the promoter)[133].

In case the legal obligation of disclosure is imposed on the taxpayer, the triggering event may be identified either by the implementation of the scheme, or by the payment or receipt of money with reference to the reportable arrangement[134].

Such legal obligation can be set either equally on the promoter and on the taxpayer, so both are subject to the disclosure regardless to the behaviour of the other, or by designing a primary obligation on the promoter that, once it has revealed the details of the scheme, removes the obligation on the taxpayer.
The imposition of the disclosure obligation not only on the taxpayer but also on the promoter offers both the opportunity to verify the compliance of a taxpayer to the disclosure duty and has a deterrence effect on the taxpayer with reference to the employment of tax planning strategies[135].

131OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 119 – 130.
132In the US mandatory disclosure regime, the triggering event arises when the tax consultant provides material aid with reference to a reportable transaction and directly or indirectly receives a fee for the consultancy.
133OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 141.
134OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 145.
135OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 66 – 67.

Whenever the primary obligation is imposed on the promoter, the secondary obligation on the taxpayer becomes effective in the cases in which the promoter is offshore, as the compliance to the rule may not be fulfilled since the government has no tools at disposal to enforce it, when there is no promoter because the scheme has been internally developed, or when the legal system grants to the promoter professional secrecy[136].
Many countries that have already designed a mandatory disclosure regime require that the obligation on the taxpayer fails only if it has obtained a written confirmation of the compliance to the disclosure obligation by the promoter or by another participant[137].

Once the promoter has satisfied the disclosure obligation, an identification number for the tax planning scheme is assigned by the tax authority. The reference number is then communicated by the promoter to the taxpayer because the latter has to attach it to the tax return referred to the tax period in which the scheme has been used.
The employment of the reference number not only enables the tax authority to easily identify a taxpayer that has used the reportable transaction but it also helps to single out the other taxpayers that are part of a given agreement[138].

An additional obligation weighing only on the promoter consists in establishing a rule whereby the promoter has to reveal to the tax authority the list of those clients that have used a given strategy. This obligation can be used either to enforce the audit process of verifying whether the taxpayers have complied with the disclosure duty or, less frequently, to avoid the employment of the identification number.
The co-existence of the identification number practice and of the communication of the client list by the promoter allows the tax authority to assess if there has been a full disclosure of the details of the agreement and to evaluate the spread of the phenomenon amongst taxpayers[139].

136OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 68 – 70.
137OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 66.
138OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraph 160, 168 – 170.
139OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 163 – 166, 171.

The information required to be disclosed regards not only the reference number of the transaction, the list of the clients, and the identification data both of the promoter and of the taxpayer.

The details concerning the transaction have to enable the tax administration to understand how the strategy works and on what legal basis the tax advantages are claimed.

The disclosure of such information allows the governments to detect vulnerabilities in their tax system, which are highlighted by the tax advisor when the tax scheme is available, much earlier before the implementation of the transaction, enhancing the opportunities to counteract such practice through circulars by the tax administration or by means of a modification of the tax law. Therefore, the incentive to develop new strategies is cut down, as the time within which the scheme can be used is reduced[140].

At the beginning, this system requires an increase of the up-front costs for the tax administration but, once it has been set, the on-going costs are very low.

Another aspect that has to be taken into account relies on the fact that lots of resources employed in the detection of tax avoidance by the tax authorities can be directed to other activities, since, if the system is implemented in the right way, there is less need to inspect the taxpayers' behaviours. Such resources, for instance, can be used to develop more suitable responses to the tax avoidance schemes.

In addition, the tax authority could also contact the taxpayers in the list provided by the promoter in order to communicate to them its position on the reportable transaction which is to be undertaken, altering the market equilibrium between the tax planning demand and the supply by the tax advisers. In this case, the benefit consists in a lower number of trials for the courts because of the deterrent effect on the taxpayers.

The UK Tax Administration, after having issued a mandatory disclosure regime, has registered a decrease in the number of the schemes disclosed over the years and this fact has been interpreted as the shrinking effect on the market. Hence, it can be assumed that the resources employed for the mandatory disclosure system can be further reduced over time[141].

140OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 22, 39, and 201

141OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 39, and 48

The key element for the mandatory disclosure regime to be working are the consequences of non-compliance.

Monetary penalties may apply for the non-disclosure of a scheme, for the non-compliance to the obligation of providing the client list by the promoter, for the failure by the promoter to provide the identification number to the taxpayer, and for the lack of the reference number on the tax return of the taxpayer.

Both the Canadian and the US experiences suggest that even non-monetary penalties may be effective. Within the Canadian context, the failure to comply with the disclosure obligation entails the denial of the tax benefit gained through the scheme for the taxpayer.

On the other hand, in the United States, the non-compliance is considered to be evidence of the lack of *bona fide* in the taxpayer[142].

– 51.

142OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 180, 182, 195, and 196.

5.2 Mandatory Disclosure Regime Applied to International Tax Planning

In an international context, additional rules can be added to make the system more effective, given the fact that the means of the tax administrations may be insufficient to reach the goal of obtaining the information desired and gaining a comprehensive overview when the transaction involves different jurisdictions.
In other words, a mandatory disclosure regime should impose the legal obligation to disclose the information only on the persons on which the country has the power to enforce its compliance, leaving aside foreign taxpayers and advisers, and should focus only on those transactions whose consequences impact on the country's financial resources.

The first step to broaden the coverage of the system is to include in the list of the reportable transactions all those arrangements involving a domestic taxpayer giving rise to a cross-border income.
As this characteristic is overly wide, further efforts have to be undertaken by the tax administrations to identify specific hallmarks reflecting those base eroding and profit shifting transactions that the jurisdictions want to hinder, avoiding over disclosures[143].
For instance, tax administrations could require that only those schemes in which the cross-border income is one of the main purpose of the transaction are disclosed.

The main issue that has to be taken into account is that when an international tax scheme has been implemented, frequently the taxpayers involved are related parties.
Under this condition, the offshore parent company, aware that, in the residence country of its subsidiary, a mandatory disclosure regime is in force, may not communicate the overall strategy to the management body of the subsidiary. Therefore, the tax jurisdiction has to make it crystal clear that its taxpayer has to reveal any information on

143OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*, paragraphs 239 and 240.

its possession.

To bypass the problem of information asymmetry between the tax administration and the multinational group unwilling to disclose its strategy since the parent company is resident in an offshore country, existing information exchange agreements can be used to communicate with the other government.

The main existing procedures to exchange the information are art. 26 of the OECD Model Tax Convention and the Convention on Mutual Administrative Assistance in Tax Matter, a multilateral treaty signed by 87 countries that has entered into force in Italy since 2006.

Nonetheless, Action 5 in *BEPS 2015 Final Reports* (*Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance*) suggests implementing a mechanism whereby a jurisdiction states its opinion about a specific ruling decision and then the tax authority that is interested on the matter is entitled to ask further information in case it is considered to be relevant for its taxpayers[144].

Another notable mechanism, based on the understanding of the global approach of multinationals with reference to the tax field, is presented in Action 13 in *BEPS 2015 Final Reports* (*Transfer Pricing Documentation and Country-by-Country Reporting*), whereby multinationals should provide, firstly, a master file containing the information that are relevant for all the group members, secondly, a local file referred to the transactions of local group members, and, thirdly, a country-by-country report containing the global allocation of the group's income and the taxes paid, revealing indicators concerning the location of the economic activities of the group.

In details, the master file should provide an overview of the overall business of the group, describing its organisational structure and business conducted, the ownership and the exploitation scheme of the intangible properties, and the inter-company financial

144 Within the European context, the 2015 modification of Council Directive 2011/16/EU has basically implemented the same mechanism of information sharing with reference to domestic rulings outlined by the OECD.

activities. In addition, the consolidated financial statement of the group should be attached together with the disclosure of the group's existing unilateral advanced pricing agreements and other tax rulings[145].

Conversely, the local file should show the position of each related party, highlighting the controlled transactions in which it has entered into. For this purpose, an accurate description of the transactions together with the consequent intra-group payments should be provided. In this case, specific information about the transfer pricing method adopted and the reasons for selecting such a method should be stated, including the financial statement of the related entity and the copies of its advanced pricing agreements and other tax rulings[146].

Finally, the country-by-country report requires the aggregation of the relevant data for each jurisdiction in which the group members operate.
For each country, information about the revenues from controlled or uncontrolled transactions, the profits, the income paid or accrued should be provided.
In addition, the sum of capital and earnings of all the resident group parties, the number of their employees, their intangible assets, and the nature of the business conducted should be disclosed for each jurisdiction involved.
In other words, the information is not provided on the basis of the entity. All the resident companies in a country have to consolidate their data together, so that the information can be read with reference to each jurisdiction[147].

In case the information is disclosed according to Action 13 in *BEPS 2015 Final Reports*, the tax authorities would have little difficulties in assessing their taxpayers' international transactions. Therefore, it is advisable that this kind of information is included in the legal obligation of disclosure in the mandatory disclosure regime.
If all the OECD member countries adopted such system there would be no need of using

145OECD, *Action 13: Transfer Pricing Documentation and Country-by-Country Reporting*, in *BEPS 2015 Final Reports,* Annex I to Chapter 5.
146OECD, *Action 13: Transfer Pricing Documentation and Country-by-Country Reporting*, in *BEPS 2015 Final Reports,* Annex II to Chapter 5.
147OECD, *Action 13: Transfer Pricing Documentation and Country-by-Country Reporting*, in *BEPS 2015 Final Reports,* Annex III to Chapter 5.

the sharing information mechanism and the other procedures to exchange information.

6 Effective Practices against the Treaty Shopping Phenomenon and the Employment of Base Companies

The analysis of the US and OECD models has revealed that two different approaches that have been followed for the purpose of hindering the treaty shopping practice.

On one hand, the OECD has been focusing on developing a general rule, the beneficial owner concept, whose practical application requires the selection of one procedural approach among those identified in the *Commentaries on the Articles of the Model Tax Convention.*
The coverage of such rule has been recognised to be overly broad. Hence, additional clauses, the *bona fide* provisions, have been provided to the governments in order to exclude substantial businesses not passing the tests from the limitation on the benefits claimed.
The result achieved, in some cases, leads to a shortage of legal certainty because of the different positions the tax authorities may take on a specific case.

On the other, the US Model has chosen to adopt a more specific regulation and the OECD has recently shown interest in this kind of lawmaking.
The US LOBs differentiate the taxpayers into qualified and non-qualified persons in order to determine the entitlement to treaty benefits.
The outcome is a set of rules very difficult to interpret and assess, that requires a huge amount of information.

With respect to the employment of base companies, efforts have been made by the OECD and by the European Commission to counteract this phenomenon.

The main disadvantage of transfer pricing regulation is the high degree of complexity inherent to its implementation. Another weak point consists in the fact that it does not

consider that the parties are able to rescind the contract without any legal consequences, with them being a single economic entity.

The transparent taxation is the mechanism on which CFC rules are based. Despite the fact that it may be challenging to apply in case of a great number of shareholders, it appears a good solution to prevent the effect of income retention that characterises the activities of base companies.

Another solution is tax consolidation and the European common consolidated tax base. Nonetheless, being non-mandatory tax procedures, tax administrations cannot rely on them to contrast the employment of base companies.

After having presented the most commonly used methods designed by the governments and by the OECD, the reduction of information asymmetry amongst tax administrations appears to be the most suitable tool to deter from the implementation of such schemes.
For this purpose, two simple additional features to the legal obligation of disclosure in the mandatory disclosure regime are presented.

Chapter 3 (*International Tax Schemes*) of Action 12 (*Mandatory Disclosure Rules*) in *BEPS 2015 Final Reports* does not face the topics previously discussed in the preceding sections of this paper. It just provides general guidelines to the readers, encouraging the countries to implement on their own specific hallmarks concerning the tax planning practices that put at risk their financial revenue. For this reason, in the following lines, efforts are made to identify the relevant elements that may be used to counteract the employment of the base companies in a mandatory disclosure regime.

For such purpose, it is advisable to impose the legal obligation of disclosure on the taxpayer whenever the conditions for the application of the CFC rules are met. In other words, in case a resident taxpayer exercises the economic or legal control over a foreign company as described in paragraph 35 of Action 3 (*Designing Effective Controlled Foreign Company Rules*) by the OECD.
To avoid the over-disclosure, this aspect can be matched with a further requirement,

namely that the country, in which the base company is located, is classified into a black list.

With reference to the treaty shopping practice, it is possible to trigger the disclosure obligation whenever a non-resident claims treaty benefits for an item of income whose source is located within the Italian territory.
In this case, since the aim of treaty shopping is to avoid taxation on the income in the source country, the fact that the non-resident is required to reveal the relevant information about the group structure to which it belongs and their commercial and financial relations could have a deterrent effect on the treaty shopping schemes.

By doing so, tax authorities would have the opportunity to examine *ex ante* and *ex post* each case. Moreover, the obtained data could be registered in the sharing information mechanism, described in Action 5 of *BEPS 2015 Final Reports* (*Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance*).

In order not to enhance the compliance costs of irrelevant taxpayers, the legal obligation may be imposed only on enterprises claiming a treaty benefit above a certain threshold.

In conclusion, the disclosure of relevant information appears to be the most suitable mechanism to counteract such phenomena, not only for its deterrent effect but also because the uncertainty is reduced as no evaluation is left to the taxpayers, avoiding the need to rely on puzzling computations and regulations.

BIBLIOGRAPHY

- BAKER P., *Double Taxation Conventions,* 2001, Sweet & Maxwell, London;
- BORIA P., D*iritto tributario europeo,* 2010, Giuffrè Editore, Milan;
- BUCCI L., CAPOZZI V., and GALLUCCI M., *La disciplina IRES dei gruppi di imprese,* 2006, Giuffrè Editore;
- CHINELLATO G., *Codificazione tributaria e abuso del diritto,* 2007, Cedam, Padua;
- CORDEIRO GUERRA R., *Diritto tributario internazionale: istituzioni,* 2012, Cedam;
- DAMI F., *I rapporti di gruppo nel diritto tributario,* 2011, Giuffrè, Milan;
- DE LA FERIA R. and VOGENAUER S., *Prohibition of Abuse of Law: A New General Principle of EU Law?*, 2011, Hart Publishing;
- DE LUCA A. and BAMPO A., *La stabile organizzazione in Italia,* 2009, IPSOA Gruppo Wolters Kluwer;
- DOERNBERG R. L. and VAN RAAD K., *The 1996 United States Model Income Tax Convention*, 1997, Kluwer Law International;
- ENDRES D. and SPENGEL C., *International Company Taxation and Tax Planning,* 2015, Kluwer Law International BV;
- FALSITTA G., *Corso istituzionale di diritto tributario*, 2014, Cedam;
- FINNERTY C. J., MERKS P. et al, *Fundamentals of International Tax Planning,* 2007, IBFD;
- GAFFURI A. M., *La tassazione dei redditi d'impresa prodotti all'estero,* 2008, Giuffrè Editore, Milan;
- GARBARINO C., *Le Convenzioni dell'Italia in materia di imposte su reddito e patrimonio*, 2002, Egea, Milan;
- GARBARINO C., *Manuale di tassazione internazionale,* 2005, Milan;
- GREGGI M., *Profili fiscali della proprietà intellettuale nelle imposte sui redditi,*

2009, Pacini Editore;

- IANNACONE G. and PERIN L., *Stati Uniti d'America: guida al diritto e alla fiscalità d'impresa*, 2012, IPSOA;
- HELMINEN M., *EU Tax Law. Direct Taxation,* 2015, IBFD;
- LAKATOS I., *La metodologia dei programmi di ricerca scientifici*, 2001, EST, Milan;
- LUPI R., *Compendio di diritto tributario*, 2015, Dike Giuridica Editrice;
- MORO P., *Topica digitale e ricerca del diritto: metodologia e informatica giuridica nell'era dell'infosourcing*, 2015, Giappichelli Editore, Turin;
- HOLMES A. K., *International Tax Policy and Double Tax Treaties. An Introduction to Principles and Application II Edition,* 2014, IBFD, Amsterdam;
- LETTIERI N., MARINI G. and MERONE G., *L'abuso del diritto nel dialogo tra corti nazionali ed internazionali*, 2014, Edizioni Scientifiche Italiane, Naples;
- LOSURDO F., *Il divieto dell'abuso del diritto nell'ordinamento tributario europeo*, 2011, Giappichelli Editore, Turin;
- MAISTO G., *Convenzioni Internazionali per Evitare le Doppie Imposizioni,* 2015, Giuffrè;
- MASS R. W., *Tolley's Anti-Avoidance Provisions,* 1991, Tolley Publishing Company Limited;
- MILLER A. and OATS L., *Principles of International Taxation,* 2016, Bloomsbury Professional;
- NANNETTI F., *La stabile organizzazione quale attività. Profili tributari e giuscommercialistici della stabile organizzazione nei rapporti intersocietari,* 2013, Vetere Severino Editore;
- NIEGEL E. et al., *Intellectual Property Law and Taxation,* 2008, London, Sweet and Maxwell;
- PIANTAVIGNA P., *Abuso del diritto fiscale nell'ordinamento tributario europeo*, 2011, Giappichelli Editore, Turin;
- RUSSO R., FINNERTY C. and MERKS P., *Fundamentals of International Tax Planning,* 2007, IBFD;
- RUST A. et al, *Double Taxation within the European Union,* 2011, Wolter

Kluwer;

- SACHETTO C., *Principi di diritto tributario europeo e internazionale,* 2011, Giappichelli, Turin;
- TESAURO F., *Compendio di diritto tributario*, 2013, Utet Giuridica;
- UCKMAR V. et al, *Diritto tributario internazionale. Manuale,* 2012, Cedam;
- VAN WEEGHEL S., *The Improper Use of Tax Treaties*, 1998, Kluwer Law International;
- VINCENTI U., *L'universo dei giuristi, legislatori, giudici: contro la mitologia giuridica*, 2003, Cedam, Padua;
- VOGEL K., *Klaus Vogel on Double Taxation Conventions,* 1997, Kluwer Law International, London.

CASES

- European Court of Justice, 21/02/2006, Case C-255/02 (Rassegna Tributaria I/2006, pp. 1016 – 1031, n. PICCOLO C.);
- European Court of Justice, 17/01/2008, Case C-105/07 [Lammers Case] (Il Fisco 1 I/2008, pp. 1218 – 1223, n. TURIS P.);
- Cass. Civ., Sez. Trib., 07/03/2002 no. 3367 (GT Rivista di Giurisprudenza Tributaria no. 7/2002, pp. 607 – 635, n. R. SUCCIO);
- Cass. Civ., Sez. Trib., 07/03/2002 no. 3368 (Il Fisco no. 19/2002, pp. 3008 – 3018);
- Cass. Civ., Sez. Trib., 25/05/2002 no. 7682 (Il Fisco no. 38/2002, pp. 6115 – 6121);
- Cass. Civ., Sez. Trib., 25/07/2002 no. 10925 (Massimario Annotato della Cassazione II/2002, p. 1344);
- Cass. Civ, Sez. Trib., 05/05/2006 no. 10353 (Il Fisco 1 III/2006, pp. 3299 – 3301).

FOREIGN REVIEWS

- GOYETTE N., *Tax Treaty Abuse: A Second Look*, Canadian Tax Journal no. 2/2003 vol. 51, pp. 764 – 805;
- HAUG S. M., *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, Vanderbilt Journal of Transnational Law no. 29/1996, pp. 191 - 289;
- INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *Form and Substance in Tax Law*, Vol. 87 A, 2002, Sdu The Netherlands;
- INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *Transfer Pricing and Intangibles*, Vol. 92 A, 2007, Sdu The Netherlands;
- INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *Is There a Permanent Establishment?*, Vol. 94 A, 2009, Sdu The Netherlands;
- INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *Tax Treaties and Tax Avoidance: Application of Anti-Avoidance Provisions*, Vol. 95 A, 2010, Sdu The Netherlands;
- INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *Enterprise Services*, Vol. 97 A, 2012, Sdu The Netherlands;
- INTERNATIONAL FISCAL ASSOCIATION, Cahiers de Droit Fiscal International, *The Taxation of Foreign Passive Income for Groups of Companies*, Vol. 98 A, 2013, Sdu The Netherlands;
- MASON R., *When Derivative Benefit Provisions Don't Apply*, Tax Notes International no. 43/2006 vol. 43, pp. 563 – 567;
- TING A., *iTax – Apple's International Tax Structure and the Double Non-Taxation Issue*, British Tax Review no. 1/2014, pp. 40 – 71.

ITALIAN REVIEWS

- ANDRIOLA M., *La dialettica tra "aggiramento" e valide ragioni economiche, in una serie di ipotesi applicative della norma antielusiva*, Rassegna Tributaria II/2006, pp. 1897 - 1953;
- AVELLA F., *Il beneficiario nelle convenzioni contro le doppie imposizioni: prime pronunce nella giurisprudenza di merito e nuovi spunti di discussione*, 2011, Rivista di Diritto Tributario no. 2/2011, sez. V, pp. 14 – 50;
- AVELLA F., *Nuove pronunce nella giurisprudenza di merito in materia di beneficiario effettivo nelle convenzioni contro le doppie imposizioni*, 2014, Rivista di Diritto Tributario no. 2/2014, sez. V, pp. 18 – 32;
- BEGHIN M., *Esternalizzazione di servizi tra rapporti partecipativi e indeducibilità dei costi* (Cass. Civ, Sez. Trib., 13/05/2009 no. 10981), Corriere Tributario IV/2009, pp. 2143 - 2148;
- BERLIRI C. et al., *Elusione fiscale e abuso di diritto*, ΝΕΩΤΕΡΑ Periodico Ufficiale dell'ANTI no. 1/2009;
- CARINCI A. and DEOTTO D., *Abuso del diritto ed effettiva utilità della novella: Much ado about nothing?*, Il Fisco no. 32-33/2015, pp. 3107 – 3114;
- COMMITTERI G. M. and SCIFONI G., *Tassabili i proventi derivanti dal «dividend washing»*, Corriere Tributario VI/2005, pp. 3729 - 3740;
- CONTRINO A. and MARCHESELLI A., *Luci e ombre nella struttura dell'abuso fiscale "riformato"*, Corriere Tributario no. 37/2015 pp. 3787 – 3795;
- CORASANITI G., *Sul generale divieto di abuso del diritto nell'ordinamento tributario* (Cass. Sez. Un., 23/12/2008 no. 30055 – Cass. Sez. Un. 23/12/2008 no. 30057), Diritto e Pratica Tributaria II/2009, pp. 213 - 249;
- DELLA VALLE E., «*Conduit companies» e beneficiario effettivo dei dividendi in uscita*, 2013, Rivista di Giurisprudenza Tributaria no. 1/2013, pp. 53 – 60;
- FICARI V., *Clausola generale antielusiva, art. 53 della Costituzione e regole giurisprudenziali*, Rassegna Tributaria, I/2009, pp. 390 - 400;

- FURLAN A. and COLUCCI B., *Il principio di «sufficienza probatoria» a servizio del beneficiario effettivo*, Fiscalità & Commercio Internazionale no. 12/2012, pp. 29 – 34;
- GIACONIA M. and PREGAGLIA A., *Interessi e dividendi infragruppo: "beneficiario effettivo" e "costruzione di puro artificio"*, Fiscalità & Commercio Internazionale no. 10/2011, pp. 13 – 19;
- GIULIANI F. M., *Su talune categorie privatistiche, evocate da tre pronunce del Supremo Collegio in tema di elusione-evasione* (Cass. Civ., Sez. Trib., 14/11/2005 no. 22932), Rivista di Diritto Tributario II/2006, pp. 683 - 753;
- LOVECCHIO L., *Divieto di abuso del diritto: l'incognita applicazione futura della giurisprudenza "invasiva"*, Il Fisco no. 35/2015, pp. 3319 – 3323;
- LOVISOLO, A. *Abuso del diritto e clausola generale antielusiva alla ricerca di un principio*, Rivista Diritto Tributario I/2009, pp. 49 - 95;
- LOVISOLO A., *Il principio di matrice comunitaria dell'«abuso» del diritto entra nell'ordinamento giuridico italiano: norma antielusiva di chiusura o clausola generale antielusiva? L'evoluzione della giurisprudenza della Suprema Corte* (Cass. Civ., Sez. Trib., 29/09/2006, no. 21221), Diritto e Pratica Tributaria II-2/2007, pp. 721 - 770;
- LUPI R. and STEVANATO D., *Tecniche interpretative e pretesa immanenza di una norma generale antielusiva* (Cass. Sez. Un. 23/12/2008 no. 30057 - Cass. Sez. Un. 23/12/2008 n. 30056 - Cass. Sez. Un. 23/12/2008 no. 30055), Corriere Tributario I/2009, pp. 403 - 416;
- PICCOLO C., *Abuso del diritto ed Iva: tra interpretazione comunitaria ed applicazione nazionale*, Rassegna Tributaria I/2006, pp. 1016 - 1050;
- POGGIOLI M., *La corte di Giustizia elabora il concetto di "comportamento abusivo" in materia d'Iva e ne tratteggia le conseguenze sul piano impositivo: epifania di una clausola generale antielusiva di matrice comunitaria?*, Rivista di Diritto Tributario III-IV/2006, pp. 122 - 142;
- RENDA A., *L'evoluzione del divieto di abuso del diritto nell'orientamento della Corte di Cassazione (2011 – 2013)*, Diritto e Pratica Tributaria no. 5/2013, pp. 907 – 941.

LEGAL ACTS

- European Commission Recommendation of 6 December 2012 on Aggressive Tax Planning (2012/772/EU);
- European Council Directive 2011/96/EU (EU Parent-Subsidiary Directive);
- European Council Directive 2009/133/EC (EU Merger Directive);
- European Council Directive 2003/49/EC (EU Interest And Royalties Directive);
- European Council Directive of 17 July 1969 Concerning Indirect Taxes On The Raising Of Capital (69/335/EEC);
- Circular no. 41/E of 5 August 2011, Italian Tax Authority;
- Circulars no. 47/E of 2 November 2005, Italian Tax Authority;
- Italian Civil Code;
- Italian Law no. 212 of 27 July 2000;
- Italian Legislative Decree no. 128 of 5 August 2015;
- Italian Legislative Decree no. 358 of 8 October 1997;
- Italian Ministerial Circular no. 32 of 22 September 1980;
- Italian Ministerial Circular no. 42 of 12 December 1981;
- Italian Presidential Decree no. 917 of 22 December 1986;
- Italian Presidential Decree no. 600 of 29 September 1973;
- *Vienna Convention on the Law of Treaties,* 23 May 1969, Vienna.

ONLINE RESOURCES

- http://www.oecd-ilibrary.org/
- http://www.oecd.org/

OTHER RESOURCES

- COSTANTINO F., *L'elusione internazionale tra norma e fatto*, 2010, doctoral thesis, LUISS Guido Carli, Rome;
- COTTANI G., *La disciplina italiana in materia di prezzi di trasferimento: profili di criticità e prospettive evolutive*, 2009, doctoral thesis, LUISS Guido Carli, Rome;
- GARCEA A., *La rilevanza della sostanza economica nel reddito d'impresa,* 2009, doctoral thesis, LUISS Guido Carli, Rome;
- MARCHI M. A., *Elusione fiscale ed abuso del diritto*, Fondazione Franco Bini Congress 3 December 2010, Prato;
- OECD, *Action 3: Designing Effective Controlled Foreign Company Rules*, in *BEPS 2015 Final Reports;*
- OECD, *Action 5: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance*, in *BEPS 2015 Final Reports;*
- OECD, *Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*, in *BEPS 2015 Final Reports;*
- OECD, *Actions 8 - 10: Aligning Transfer Pricing Outcome with Value Creation*, in *BEPS 2015 Final Reports;*
- OECD, *Action 12: Mandatory Disclosure Rules*, in *BEPS 2015 Final Reports*;
- OECD, *Action 13: Transfer Pricing Documentation and Country-by-Country Reporting*, in *BEPS 2015 Final Reports*;
- OECD, *Clarification of the Meaning of the "Beneficial Owner"* in the OECD *Model Tax Convention on Income and on Capital,* 2011;
- OECD, *Commentaries on the Articles of the Model Tax Convention,* 2014;
- OECD, *Double Taxation Conventions and the Use of Base Companies*, R(5) in *Model Tax Convention on Income and on Capital* (full version), 2014;
- OECD, *Double Taxation Conventions and the Use of Conduit Companies*, R(6) in *Model Tax Convention on Income and on Capital,* (full version), 2014;

- OECD, *Model Tax Convention on Income and on Capital,* 2014;
- OECD, *Revised Proposal Concerning The Meaning of Beneficial Owner in Articles 10, 11 and 12 of the OECD Model Tax Convention,* 2012;
- OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*;
- PISTONE P. and ROMANO C., *Report on the 56th IFA Congress*, 25-30 August 2002, Oslo;
- *Preamble to 2016 US Model Income Tax Convention;*
- *United States Model Convention of November 15 2006*;
- *United States Model Convention (2016)*;
- *United States Model Technical Explanation Accompanying the United States Model Income Tax Convention of November 15 2006;*
- VACCA I., Abuso *del diritto ed elusione fiscale*, ANTI Congress, 20 October 2008.