3. The OECD As The Gravedigger Of The Fun Of International Tax Or "The Spirits That I Summoned Up I Now Can't Get Myself Rid Of"[1)]

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Compared with other developed economies the Swiss marketplace is small. Enterprises that want to grow must reach out to foreign markets. The obvious candidates are the neighboring countries, but also the larger developed countries. The same logic follows the "Convention for the elimination of double taxation with respect to taxes on income and capital" by the OECD ("OECD-MC") as it refers in the preamble first to the development of the economic relationship and then in a second step to tax matters. Therefore, there is strong correlation between the countries with which Switzerland has concluded treaties and the economic development of the bilateral markets. Multinational Companies ("MNC") have a preference to operate in the markets through standalone legal entities. Accordingly, the entities are indicative of the markets that are important to a MNC. In some specific segments of the law, there is a strong trend towards cross-country harmonization. While this might have been true for commercial law, the public laws are still quite dispersed. This is true - or should I say - was, for the domain of taxation, as the tax laws of the different countries around the globe used to vary substantially.

The design of the structure, e.g. which entity owns another entity, is to a certain degree a judgemental decision. There are certain functions, the mobile functions, that could to a large extent be performed anywhere around the globe. Obviously, there were also some ramifications that needed to be considered, such as practicability aspects. But otherwise, MNC's could pick and choose which location appeared to offer the most benefits. MNCs have traditionally taken advantage of the differences in the tax laws. For the mobile functions therefore, the intuition and the technical know-how of the person designing the structure was needed. However, what used to be a creative function has over the last 60 years become a highly regulated environment. In other words, the creative element of the tax function has been replaced by pure compliance. What are the milestones that lead to that development?

1. OECD

The OECD was formed after World War II. Its goal was to help European governments to recognize their economic interdependence. In 1956 the council suggested to form a fiscal committee. The committee was mandated to come up with rules avoiding double taxation. Switzerland was one of the founding members when the prior organization was transformed into the OECD on September 28, 1961. In 1963 the fiscal committee provided a report on the issue of double taxation as well as the first draft OECD-MC.

All the treaties concluded by Switzerland since 1965 followed the OECD-MC 1963. However, it transpired that not all the situations of double taxation could be solved based on the MC 1963. The fiscal committee of the OECD then started a revision of the Model Convention. In 1977 a new version of the OECD-MC including a commentary was approved by the council. On a regular basis new updates of the MC were published on a two-to-three-year basis. Likewise, the commentary was updated and became much more detailed.

2. Anti-Abuse Decree in 1962

The ranking of the goals by the OECD is reflective of the fact that international cooperation also shapes OECD Member's country tax policies. Switzerland became in the 1950s/60s an attractive location for foreign investors to bundle their investments, either by setting up holding companies or by companies with a relatively low level of physical presence to hold securities or intellectual property[2)]. Those companies could avail themselves of the Swiss tax treaty network without any further restriction. Switzerland found itself in a difficult situation as it is a major centre of commerce and industry, and as such needed to be able to participate in the tax treaty network. Some of the countries with which Switzerland had concluded treaties were concerned about specific planning opportunities since those countries considered them to be abusive. Those treaty partners were considering terminating their treaties with Switzerland or to introduce unilateral measures against those schemes that were considered being problematic. Considering these developments Switzerland introduced in 1962 comprehensive unilateral measures[3)] to protect the source states from treaty shopping by using Swiss companies. Switzerland introduced four tests to safeguard that the Swiss entities could not be used for treaty shopping purposes by an early form of a Limitation of Benefits clause. As a result, a Swiss based company needed to perform those tests to determine whether it could avail itself of the treaty network. It should not be last time that treaty partners shaped the Swiss tax law and made the life of Swiss tax practitioners more challenging.

3. Harmful Tax Competition

In May 1996 Ministers mandated the OECD to "develop measures to counter the distorting effects of harmful tax competition on investment and financing decisions and the consequences for national tax bases". In identifying harmful preferential tax regimes, the OECD defined four key factors:

(a) the regime imposes a low or zero effective tax rate on the relevant income;

(b) the regime is "ring-fenced";

(c) the operation of the regime is non-transparent;

(d) the jurisdiction operating the regime does not effectively exchange information with other countries[4)].

The report on Switzerland noted that under certain circumstances, the tax policies of certain cantons do attract mobile tax bases from abroad. Therefore, Switzerland may find itself under continued pressure to provide more complete access to information to foreign tax authorities. The other mobility issue addressed were the special tax regimes for holding, domiciliary and mixed companies.

Switzerland seriously considered the possibility of exercising its veto, but finally decided to abstain. In the statement to the Report[5)], the Swiss side criticized that the scope of the work was restricted to geographically mobile activities, such as financial activities and other services. Further, the Report ignores the reality of the structural diversity of existing tax regimes. For instance, the only solution adopted by the OECD is administrative assistance by means of exchange of information. The OECD ignored the fact that withholding systems could be viable alternatives which entail lower administrative costs. The report did not have immediate consequences for Switzerland. However, it was obviously fueling the discussion regarding the Swiss special tax regimes.

4. EU Efforts in 2005

As discussed, the international tax community had on a recurring basis voiced concerns that some of the Swiss tax regimes could be ring-fencing. Other countries were of the view that those features have together with other factors contributed to make Switzerland an attractive location for MNC's. In 2005, "discussions" between the EU and Switzerland were initiated. The EU voiced the concern that some of the tax regimes could be viewed as infringing the free trade agreement with the EU[6] of 1972. The negotiations ended in a deadlock situation. The way out was complete overhaul of the Swiss tax system in the form of TRAF[7] and, amongst others, the abolishment of the criticized regimes.

5. Base Erosion and Profit Shifting ("BEPS")[8]

Shortly after the turn of the millennium different stakeholders voiced concerns that large MNCs "may not pay their fair share of tax". The G20 group mandated the OECD in June 2012 to develop an action plan to counter BEPS. The OECD defines BEPS as tax avoidance strategies that aim at exploiting gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations. The BEPS project aims to create a level playing field.

The OECD addressed 15 Action Points to tackle BEPS with the emphasis on the following elements:

- Coherence of the different tax systems to avoid "unfair tax competition"
- Substance as the criterion for taxation
- Transparency of the taxation of legal entities

The most relevant Action Points are:

a. Action 1

Action 1 addresses the challenges for international taxation created by the spread of the digital economy. The OECD established a two Pillar approach. Pillar 1 is focusing on the largest MNCs with global turnover above EUR 20 billion and profitability above 10%. The Secretariat adapted taxing rights by considering new business models and thereby expanded the taxing rights of market jurisdictions, which, for some business models, is the jurisdiction where the user is located.

Pillar 2 aims at safeguarding that a minimum level of taxation is achieved. If the minimal tax burden is not achieved, other countries may tax, through different mechanism, the difference. On November 21, 2021, 137 countries agreed to this approach comprising a minimum tax level of 15%. Switzerland was also amongst those 137 countries, being conscious that in most of the cantons the effective tax rate ("ETR") is below 15%. No tax practitioner would have thought that such a global harmonization could ever happen. Whilst the principles are easy to understand, the devil is as always in the details. Considering that all the tax laws around the globe are different, how should one arrive at a harmonized basis to compare the ETRs without comparing apples to pears? The OECD has developed a set of rules to calculate a harmonized tax basis on a country-by-country approach and thereby determine the ETR. However, the toolbox is extremely complicated and deviates from all the accounting standards that are available. In other words, there is a tremendous compliance effort needed to figure out what the harmonized ETR is.

b. Action 12

Under Action 12 "promoters", which may also include the group-internal tax department, have the obligation to report "aggressive tax planning". It must be noted that the term "aggressive tax planning" needs to be interpreted in the broadest sense of the word. The OECD has defined some "hallmarks" (categories) that deem a transaction to be "aggressive tax planning". As an example, cross border planning based on a "confidential paper" or reference to standardized transfer pricing, such as the use of safe haven rates may deem a transaction to be "aggressive tax planning". The OECD is of the view that mandatory disclosure regimes should enable countries to quickly respond to tax risks by providing early access to such information. The good news is that action 12 is not a minimum standard, so it is up to the respective country to determine whether to transcribe those rules into national law.

c. DAC 6

The bad news is that the EU as an early adopter came up with rules designed after Action 12 under the buzzword DAC 6 and approving those as minimal standards. DAC 6 is effective in all the member states in the EU. If there is a reportable transaction the taxpayer has a 30-days window to report it.

d. Action 13

Under BEPS Action 13, all large MNCs are required to prepare a country-by-country (CbC) report with aggregate data on the global allocation of income, profit, taxes paid and economic activity among tax jurisdictions in which it operates. It is a minimum standard that all OECD and G20 countries have committed to implementing. MNCs in Switzerland are obliged to do the country-by-country report on an annual basis since 2018.

6. Conclusion

At the beginning of the journey, the OECD mandated itself to stimulate economic relationship among the countries and to avoid double taxation. Over the past 60 years there has been a turn towards reporting obligations and harmonization of the tax laws of the different countries. In addition, the pace of the sequence of events has tremendously gained momentum. There are new reporting obligations all over the place. The scope of activities of the tax function has turned from a creative activity into an activity that manages reporting tools, to make sure that all the obligations are met. To sum up, there are few spaces left for the creative piece of the work in an environment that has become hostile to tax planning.

1) Johann Wolfgang von Goethe in "Der Zauberlehrling"
2) In more details, Markus F. Huber/Matthew S. Blum in Mélanges Walter Ryser, Stämpfli Verlag Bern, 2005 S. 28 et seq.
3) Federal Decree of 14 December 1962 on improper use of tax treaties (BRB 62; SR 672.202)
4) https://www.oecd.org/ctp/harmful/1904176.pdf, Page 25 seq. visited on April 10, 2022
5) https://www.oecd.org/ctp/harmful/1904176.pdf, Page 76 seq. visited on April 10, 2022
6) https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/switzerland_en visited on April 29, 2022
7) "Tax Reform and AHV Financing" approved by the Swiss voters in 2019, for additional information: https://www.efd.admin.ch/efd/en/home/the-fdf/legislation/votes/tax-reform-ahv-financing/fb-steuervorlage17.htmlinformation
8) https://www.oecd.org/tax/beps/ visited on April 30, 2022

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This article reflects the personal view of the author.