
TABLE OF CONTENTS

Acknowledgements	v
1 Introduction	1
1.1. Content and purpose	1
1.2. Structure	2
1.3. Authors	3
2 Sources of international tax law	5
2.1. General	5
2.2. Domestic legislations	5
2.2.1. In general	5
2.2.2. Worldwide versus territorial systems	6
2.2.3. Residents versus non-residents	6
2.2.4. The source of income	7
2.2.5. The concept of international double taxation	8
2.2.6. Double tax relief methods	9
2.3. Tax treaties	11
2.3.1. Introduction	11
2.3.2. Double tax treaties and domestic law	12
2.3.3. The purposes of double tax treaties	14
2.3.4. Structure and functioning of double tax treaties	15
2.3.5. Interpretation of double tax treaties	17
2.3.5.1. The Vienna Convention on the Law of Treaties	17
2.3.5.2. The legal status of the OECD Commentary	18
2.3.5.3. Art. 3(2) of the OECD Model: a rule of interpretation	19
2.4. EC law	21
2.4.1. EC law and taxation	21
2.4.2. EC Treaty	22
2.4.3. EC Directives	23

Table of contents

2.4.3.1.	EC Parent-Subsidiary Directive	23
2.4.3.2.	EC Merger Directive	25
2.4.3.3.	EC Interest and Royalties Directive	27
2.4.3.4.	Other EC instruments relevant for tax purposes	30
2.4.4.	The European Court of Justice	30
3	Guiding concepts for international tax planning	33
3.1.	General	33
3.2.	The arm's length principle	34
3.2.1.	General	34
3.2.2.	Transfer pricing methods consistent with the arm's length principle	35
3.2.2.1.	Comparable uncontrolled price method (CUP)	35
3.2.2.2.	Resale price method ("resale minus")	36
3.2.2.3.	Cost-plus method	36
3.2.2.4.	Difficulties in applying traditional methods	37
3.2.2.5.	Transactional net margin method (TNMM)	37
3.2.2.6.	Profit split method	37
3.2.2.7.	Global formulary apportionment method	38
3.3.	The permanent establishment concept	38
3.3.1.	Domestic law	38
3.3.2.	Double tax treaties	39
3.3.2.1.	Physical permanent establishment	39
3.3.2.2.	List of examples	41
3.3.2.3.	Construction permanent establishments	41
3.3.2.4.	List of exceptions	42
3.3.2.5.	Agency permanent establishment	43
3.3.2.6.	Group companies	46
3.3.3.	Concluding remarks on the concept of permanent establishment	48
4	Defining international tax planning, avoidance and evasion	49
4.1.	General	49
4.2.	Tax evasion	49

4.3.	Tax avoidance and tax planning	51
4.3.1.	General principles of domestic law	51
4.3.2.	OECD documents	52
4.3.3.	EC law	55
4.4.	Tax saving diagrams	57
4.5.	Concluding remarks	60
5	Categorizing international tax planning	63
5.1.	General	63
5.2.	Three species	63
5.3.	Temporary versus permanent tax savings	65
5.4.	Substantive versus formal tax planning	66
5.5.	Double tax treaty versus non-tax treaty planning	69
5.6.	Concluding remarks	70
6	Structure and goals of a multinational enterprise	71
6.1.	Globalization and its impact on tax planning	71
6.2.	Impact of tax strategy and planning on shareholder value	73
6.3.	Benchmarking and tax rate drivers	74
6.4.	Tax planning strategies	75
6.4.1.	Profit migration strategies	76
6.4.2.	Jurisdictional strategies	78
6.5.	Developing a tax planning strategy	79
6.6.	Concluding remarks	82

Table of contents

7	Holding activities	85
7.1.	Use of holding companies	85
7.1.1.	General	85
7.1.2.	Key requirements for a holding company jurisdiction	86
7.1.3.	Selection of the holding company location	88
7.2.	Holding company foundational structures	89
7.3.	Overview of European holding company locations	92
7.3.1.	General	92
7.3.2.	Holding company taxation	92
7.3.3.	Taxation of trading income	94
7.3.4.	Taxation of dividends	94
7.3.5.	Capital gains	96
7.3.6.	Taxation of financing and royalty income	97
7.3.7.	Deduction of interest costs and thin capitalization	98
7.3.8.	Capital losses and write-offs	99
7.3.9.	Withholding taxes	99
7.3.10.	Capital duty	100
7.3.11.	Other taxes	101
7.3.12.	Liquidation regime	101
7.3.13.	Tax consolidation	101
7.3.14.	Comparison of holding company jurisdictions	102
7.4.	Special considerations for Asia-Pacific	102
7.5.	Special considerations for Latin America	104
8	Financing activities	107
8.1.	General	107
8.1.1.	The choice between debt and equity	107
8.1.2.	Generation of cash in the leveraged subsidiary	111
8.1.3.	How an MNE can subsequently modify the mix of debt and equity	112
8.1.4.	Currency aspects	114
8.1.5.	The arm's length interest rate	116
8.2.	Use of intragroup financing companies	117
8.2.1.	Outline of low-tax finance company models	117
8.2.2.	Key requirements for a finance company jurisdiction	118

8.2.3.	Use of traditional tax havens	118
8.2.4.	Non-tax haven low-tax regimes	119
8.2.5.	Low-tax branch models	120
8.2.6.	Synthetic low-tax finance companies using hybrid instruments	121
8.2.7.	Synthetic low-tax finance companies using hybrid entities	122
8.2.8.	Policy aspects	122
8.3.	Use of hybrid financing instruments	124
8.3.1.	Simple qualification conflicts	124
8.3.2.	Complex qualification conflicts	126
8.4.	Use of hybrid entities	133
8.4.1.	Why hybrid entities exist	133
8.4.2.	Types of hybrid entities	134
8.4.3.	Classic hybrid entities	135
8.4.3.1.	Main models	135
8.4.3.2.	Other uses of classic hybrids	139
8.4.3.3.	Outbound classic hybrid models for US MNEs	141
8.4.4.	Reverse hybrid entities	142
8.4.4.1.	Main models	142
8.4.4.2.	Outbound reverse hybrid models for US MNEs	146
8.5.	Other techniques	148
8.5.1.	General	148
8.5.2.	Use of dual resident companies	148
8.5.3.	Inclusion in a tax consolidation of a branch of a foreign company	149
8.5.4.	Separating principal and interest of a debt	151
8.5.5.	Allocation of partnership profits/losses	153
8.6.	Asset financing	154
8.6.1.	In general	154
8.6.2.	Tax breaks from leasing	155
8.6.3.	”Sale and leaseback” transactions	157
8.7.	Financing mergers and acquisitions	157
8.8.	Concluding remarks	158

Table of contents

9	Derivative instruments	161
9.1.	Definition of derivatives	161
9.2.	Main types of derivatives	161
9.2.1.	Futures/Forwards	161
9.2.2.	Options	162
9.2.3.	Swaps	163
9.3.	Tax treatment of derivatives	164
9.3.1.	Domestic tax issues	164
9.3.2.	Double tax treaty issues	166
9.4.	Derivatives and tax planning	168
9.4.1.	General	168
9.4.2.	Timing issues	168
9.4.3.	Characterization issues	169
9.4.4.	Withholding taxes	169
10	Intellectual property management	171
10.1.	General	171
10.2.	The creation of intellectual property	172
10.2.1.	Main models	172
10.2.2.	Main tax issues	174
10.2.3.	Domestic incentives for the creation of IP	176
10.3.	The management of intellectual property	177
10.3.1.	Main tax issues	177
10.3.2.	Some commonly used locations for IP companies	179
10.4.	The migration of intellectual property	180
10.4.1.	Main tax issues and common practices	180
10.4.2.	Possible options	181
11	Supply chain management	183
11.1.	General	183
11.2.	Tax planning for manufacturing activities	183
11.2.1.	Different forms of manufacturing	183

11.2.2. Arm’s length return and different forms of manufacturing	185
11.2.3. Locations for the principal	187
11.2.4. Where is the principal subject to tax?	187
11.2.5. Economic substance at the level of the principal	189
11.2.6. Model conversion and transitional issues	190
11.2.7. Related aspects	193
11.3. Tax planning for wholesale distribution	194
11.3.1. General	194
11.3.2. Conventional distribution models	194
11.3.3. Limited risk distributorships	195
11.3.3.1. Commissionaires	197
11.3.3.2. Arm’s length return and different forms of distribution	199
11.3.3.3. Practical applications of limited risk distributor and commissionaire models	199
11.3.3.4. Model conversion and transitional issues	200
11.4. Tax planning for retail business	201
11.4.1. General	201
11.4.2. Procurement companies	201
11.4.3. Inventory management companies	203
11.4.4. Franchising companies	204
12 Anti-avoidance rules	207
12.1. General	207
12.2. Domestic anti-avoidance rules	207
12.2.1. General anti-avoidance rules	207
12.2.1.1. Preliminary remarks	207
12.2.1.2. Domestic laws	208
12.2.1.3. Relationship with double tax treaties	211
12.2.2. CFC legislation	212
12.2.2.1. Preliminary remarks	212
12.2.2.2. Domestic laws	214
12.2.2.3. Relationship with double tax treaties	218
12.2.3. Thin capitalization rules	221
12.2.3.1. In general	221
12.2.3.2. Domestic laws	222

Table of contents

12.2.3.3. Relationship with double tax treaties	226
12.2.4. Anti-debt creation rules	227
12.2.5. Anti-dual resident and anti-hybrid rules	228
12.2.6. Anti-tax haven rules	228
12.3. Treaty anti-avoidance rules	228
12.3.1. Beneficial owner	228
12.3.1.1. In general	228
12.3.1.2. Different views as regards the interpretation of the term “beneficial owner”	230
12.3.1.3. Case law on beneficial ownership	231
12.3.2. Limitation on benefits clauses	234
12.3.3. A treaty anti-avoidance interpretation principle	236
12.4. Other measures to prevent erosion of the taxable base	237
12.4.1. Preliminary remarks	237
12.4.2. Residence	237
12.4.3. Permanent establishment	239
12.4.4. Concluding remarks on anti-avoidance rules	240
Reading list	241