

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI): Interpretation and Implementation Questions

Opinion of the Conference of the Parties of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting

Approved by the Parties to the MLI under written procedure on 3 May 2021

1. This note sets out a series of principles for addressing questions about the interpretation and implementation of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (hereafter “MLI”). Those principles, discussed and approved by the Conference of the Parties to the MLI, were drawn from public international law, the design of the MLI itself, and its drafting history.

1. The interpretation and implementation of the MLI is a matter for the Parties to the MLI to determine

The text of the MLI was negotiated and adopted by the jurisdictions that were members of the ad hoc Group. Questions of interpretation and implementation are therefore ultimately for the Parties themselves to determine. Indeed, the MLI explicitly provides for a mechanism by which the Parties can determine questions of the interpretation and implementation of i) the provisions of a Covered Tax Agreement as modified by the MLI; and ii) the provisions of the MLI itself.

For the first category, Article 32(1) of the MLI provides that questions of interpretation or implementation of the provisions of a Covered Tax Agreement as modified by the MLI should be settled in accordance with the provisions of the Agreement that govern the resolution of such questions.

In other words, Contracting Jurisdictions should use the Agreement’s mutual agreement procedure to endeavour to settle questions of interpretation and implementation of the provisions of the Agreement that have been modified by the MLI. This would include agreeing on how the MLI has modified a specific Agreement – as long as the agreement reached is consistent with the provisions of the MLI.

For the second category, Article 32(2) of the MLI provides that questions on the interpretation or implementation of the MLI itself may be addressed by a Conference of the Parties convened in accordance with the procedure set out in Article 31(3) of the MLI. Such questions could include recurrent questions about how the provisions of the MLI modify Covered Tax Agreements.

2. Article 31 of the Vienna Convention on the Law of Treaties and the basic principle for interpretation of the MLI: object and purpose, context and subsequent agreements

As with any international agreement, the basic principle for the interpretation of the provisions of the MLI is the following, as reflected in the rule set out in Article 31(1) of the Vienna Convention on the Law of Treaties (hereafter “VCLT”): the MLI 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.¹

¹ [Explanatory Statement](#), para. 12.

Article 31(2) of the VCLT provides that 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 connection with the conclusion of the treaty; (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

Article 31(3)(a) of the VCLT further provides that any subsequent agreement between the parties regarding the interpretation or application of a treaty shall be taken into account together with the context.

The rules set out in Article 31 of the VCLT and described above reflect the ordinary principles of treaty interpretation.

2.1. Object and purpose of the MLI and its provisions: the implementation of the treaty-related BEPS measures

Guiding Principle 1

The MLI should be interpreted in light of its object and purpose, which is to implement the tax treaty-related BEPS measures.

As one of the outcomes of the OECD/G20 Project to address Base Erosion and Profit Shifting (the “BEPS Project”), the MLI was developed by an ad hoc Group of jurisdictions “to enable jurisdictions that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties”.² As with any international agreement, the MLI should be interpreted in light of its object and purpose.

The object and purpose of the MLI is “to implement the tax treaty-related BEPS measures”.³

Guiding Principle 2

Each of the provisions of the MLI should be interpreted and implemented in light of the policy objectives of the relevant tax treaty-related BEPS measure implemented via the MLI.

Articles 3 through 17 of the MLI contain the substantive treaty-related BEPS measures and begin with one or more paragraphs that set out those measures. These treaty-related BEPS measures – which address hybrid mismatches, treaty abuse, and avoidance of permanent establishment status, as well as improving dispute resolution – share certain common objectives; helping jurisdictions to tackle treaty abuse in the broadest sense and ensuring the sustainability of the international framework for the elimination of double taxation.⁴ Each of them seeks to address specific concerns identified in the course of the BEPS Project. Some are stand-alone measures that are intended to be added to a Covered Tax Agreement⁵ while

² [Explanatory Statement](#), para. 1 and 2.

³ Preamble of the MLI, para. 7; [Explanatory Statement](#), para. 12 and, Objective of [mandate of the ad hoc Group](#): “The Group shall develop a multilateral instrument to modify existing bilateral tax treaties solely in order to swiftly implement the tax treaty measures developed in the course of the OECD-G20 BEPS Project.”

⁴ [OECD \(2015\), Explanatory Statement, OECD/G20 Base Erosion and Profit Shifting Project](#), para. 8.

⁵ For instance, Article 10 of the MLI that addresses BEPS concerns related to PE situated in third jurisdictions.

others are intended to modify an Agreement's specific existing provisions.⁶

All questions of interpretation and implementation of the BEPS tax-treaty related measures themselves (Articles 3 through 17 of the MLI) should be addressed in the light of the policy objectives of the relevant BEPS measure. With the exception of the arbitration provisions in Part VI of the MLI, all the substantive provisions in the MLI are intended to be identical in their effect to the provisions that were produced in the BEPS Project. The Commentary developed during the course of the BEPS Project, which was reflected in the Final BEPS Package and is now in the 2017 version of the OECD Model Tax Convention, therefore has particular relevance.⁷

Part VI of the MLI (Articles 18 through 26 of the MLI) reflects the result of the work of the Sub-Group on Arbitration to develop provisions for the resolution by mandatory binding arbitration of mutual agreement procedure cases in which the competent authorities are unable to reach agreement within a fixed period of time.⁸ Unlike the other BEPS measures, this work included the development of the substantive content of a mandatory binding arbitration provision. As a result, unlike Articles 3 through 17 of the MLI, the text of the Explanatory Statement related to Part VI of the MLI addresses both the substance of those provisions and their technical application to Covered Tax Agreements.⁹

2.2. The Explanatory Statement forms part of the “context” of the terms of the MLI

The interpretation of the provisions of the MLI should take into account the text of the Explanatory Statement to the MLI, which was adopted by the ad hoc Group at the same time it adopted the text of the MLI itself, on 24 November 2016. It reflects the agreed understanding of the negotiators with respect to the MLI¹⁰ and provides clarification of the approach taken in the MLI and how each provision is intended to affect tax agreements covered by the MLI. Accordingly, the Explanatory Statement forms part of the “context” for the purpose of the interpretation of the MLI pursuant to the ordinary rules of treaty interpretation as reflected in Article 31(2) of the VCLT.

⁶ For instance, Articles 12 and 13 of the MLI that implement changes to the PE definition or Article 4(1) of the MLI that could replace the “tie-breaker” provisions on the residence of persons other than individuals.

⁷ [Explanatory Statement](#), para. 12.

⁸ The BEPS Action 14 Report, “Making Dispute Resolution Mechanisms More Effective”, provided that a mandatory binding mutual agreement procedure arbitration provision would be developed as part of the negotiation of the MLI. See [Explanatory Statement](#), para. 9.

⁹ [Explanatory Statement](#), para. 19.

¹⁰ [Explanatory Statement](#), para. 11.

3. The later in time rule: modifications of existing tax treaties by the MLI

Guiding Principle 3

The MLI applies alongside existing tax treaties, modifying their application in order to implement the tax treaty-related BEPS measures. This follows the general legal principle that when two rules apply to the same subject matter, the later in time rule prevails (*lex posterior derogat legi priori*).

To the extent that they are incompatible, the provisions of the MLI prevail over the provisions of the Covered Tax Agreements.

An existing provision of a Covered Tax Agreement is considered “incompatible” with a provision of the MLI if there is a conflict between the two provisions.

As set out in the MLI and Explanatory Statement, the MLI operates to modify tax treaties between two or more Parties to the MLI.¹¹ It does not function in the same way as an amending protocol to a single existing treaty, which directly amends the text of that treaty; instead, it applies alongside existing tax treaties, modifying their application in order to implement the BEPS measures.¹² Some jurisdictions consider that due to their domestic law they may need to come to a mutual understanding with the competent authorities of their treaty partners of the precise effects of the modifications made by the MLI on their Covered Tax Agreements. Such agreements do not impact the applicability of the MLI.

The approach taken in the MLI follows the general legal principle that when two rules apply to the same subject matter, the rule that is later in time prevails (*lex posterior derogat legi priori*).¹³ Accordingly, to the extent that they are incompatible, a subsequent treaty (i.e. the MLI) prevails over a previously concluded treaty between the same Parties on the same subject matter (i.e. a Covered Tax Agreement).¹⁴ This rule is explicitly set out in Article 30(3) of the VCLT.¹⁵

The approach is explicitly reflected in the provisions of the MLI that provide that a paragraph of the MLI shall “supersede the provisions of the Covered Tax Agreement only to the extent that those provisions are incompatible”. However, all modifications made by the MLI on Covered Tax Agreements follow this “later in time” rule. An existing provision of a Covered Tax Agreement is considered “incompatible” with a provision of the MLI if there is a conflict between the two provisions.¹⁶

¹¹ Articles 1 and 2 of the MLI; [Explanatory Statement](#), para. 13.

¹² [Explanatory Statement](#), para. 13.

¹³ MLI: Functioning under public international law, Note by the OECD Directorate for Legal Affairs (“[Legal note on the MLI](#)”), para. 16.

¹⁴ [Explanatory Statement](#), para. 16.

¹⁵ [Vienna Convention](#), para. 3 of Article 30.

¹⁶ [Explanatory Statement](#), para. 17, which also provides an example of a possible conflict.

4. Respecting the boundaries of a Party's consent to modify its treaty network

Guiding Principle 4

The MLI should be interpreted in light of the consent given by each Contracting Jurisdiction to modify their Covered Tax Agreement, as expressed in their MLI Positions and with the consequences set out in the relevant provisions of the MLI.

The MLI was developed to implement all tax treaty-related BEPS measures in bilateral tax agreements while respecting the sovereign autonomy of the Contracting Jurisdictions and the bilateral nature of those agreements.¹⁷ As a result, the MLI can accommodate different positions and policy preferences by allowing jurisdictions to decide which treaty-related BEPS measures and alternatives they want to implement in their treaty network.¹⁸

The MLI allows for these different forms of flexibility through a system of reservations¹⁹, and notifications of choices of alternative provisions and optional provisions.²⁰ The lists of Covered Tax Agreements, reservations and notifications are submitted in the form of so-called “MLI Positions” which represent the boundaries of each Party's consent to modify its Agreements.²¹

These modifications can never go beyond the boundaries set out in a jurisdiction's MLI Position or the consequences set out in the relevant provisions of the MLI.²² The MLI does not modify a Covered Tax Agreement beyond the boundaries set by either of its two Contracting Jurisdictions, as set out in their MLI Positions. This ensures that the MLI can operate to implement the treaty-related BEPS measures while respecting the sovereign autonomy of the Contracting Jurisdictions and the bilateral nature of tax treaties.

¹⁷ [Final report on Action 15](#), para. 8.

¹⁸ [Explanatory Statement](#), para. 14.

¹⁹ An exhaustive list of authorised reservations to the MLI is set out in its Article 28(1). The only exception, as set out in Article 28(2) of the MLI, are reservations with regard to the scope of cases eligible for arbitration under Part VI of the MLI which can be formulated by a Party choosing to apply Part VI of the MLI. See also [Explanatory Statement](#), para. 264-270.

²⁰ [Legal note on the MLI](#), para. 21.

²¹ [Legal note on the MLI](#), para. 21.

²² [Legal note on the MLI](#), para. 25.

5. Compatibility clauses: defining the interaction between the provisions of the MLI and Covered Tax Agreements

Guiding Principle 5

Compatibility clauses set out whether, and to what extent, provisions in the MLI interact with existing provisions of Covered Tax Agreements.

In particular, when a substantive MLI provision conflicts with specific existing provisions in Covered Tax Agreements covering the same subject matter, this conflict is addressed through a description in the compatibility clause of the existing provisions which the MLI is intended to modify, as well as the effect the MLI has on those existing provisions.

Articles 3 through 17 of the MLI, which contain the substantive treaty-related BEPS measures, each contain a compatibility clause. As the cornerstone for the implementation of the MLI, the compatibility clauses objectively define the relationship of the provisions of the MLI with the provisions of Covered Tax Agreements. In particular, when an MLI provision conflicts with existing provisions in Agreements covering the same subject matter, this conflict is addressed through a compatibility clause, which describes the existing provisions that the MLI is intended to modify, as well as the effect the MLI has on those existing provisions.

The structure of Part VI (Arbitration) of the MLI differs from the structure of the other Articles of the MLI. These differences reflect the fact that Part VI of the MLI is intended to operate as a single cohesive arbitration provision. Thus, rather than including a compatibility clause in each Article of Part VI of the MLI, rules for compatibility with existing provisions are consolidated in Article 26 of the MLI.

The MLI contains different types of compatibility clause that determine the modifications to Covered Tax Agreements:

- *Compatibility clauses that provide that the MLI applies “in place of” an existing provision of a Covered Tax Agreement.* Where provisions of the MLI apply only “in place of” existing provisions, the MLI provisions are intended to replace the existing provisions described in the compatibility clauses. The MLI is not intended to replace provisions that are not described in the compatibility clauses.
- *Compatibility clauses that provide that the MLI “applies to” or “modifies” an existing provision of a Covered Tax Agreement.* Where a provision of the MLI “applies to” or “modifies” existing provisions, the MLI provisions are intended to change the application of existing provisions without replacing them. Accordingly, these MLI provisions can only apply if there is an existing provision as described in the compatibility clause.
- *Compatibility clauses that provide that the MLI applies “in the absence of” an existing provision of a Covered Tax Agreement.* Where provisions of the MLI apply only “in the absence of” existing provisions, the MLI provisions are intended to apply only when the Covered Tax Agreements do not contain the provisions described in the compatibility clauses.
- *Compatibility clauses that provide that the MLI applies “in place of or in the absence of” an existing provision of a Covered Tax Agreement.* Where provisions of the MLI apply “in place of or in the absence of” existing provisions, the MLI provisions apply in all cases and follow the “later in time” rule, by replacing existing provisions to the extent described in the compatibility clauses or by superseding the provisions of the Covered Tax Agreement to the extent that they are incompatible with the relevant MLI provision.

6. Notification clauses: method to ensure clarity and transparency

Guiding Principle 6

The notification clauses ensure clarity and transparency about the existing provisions of Covered Tax Agreements that are modified by the MLI.

While the notifications sometimes trigger the application of the MLI, the extent to which the MLI modifies existing provisions of Covered Tax Agreements is always as provided in the compatibility clauses.

Notification clauses were introduced in the MLI to ensure clarity and transparency about existing provisions of Covered Tax Agreements that are within the scope of the compatibility clauses. When an MLI provision modifies specific types of existing provisions described in compatibility clauses, Parties are generally required to make a notification to identify which existing provisions of Covered Tax Agreements are within the scope of compatibility clauses²³. Parties are expected to use their best efforts to identify those existing provisions within the objective scope of the compatibility clause.²⁴

Notifications made under the MLI can have the effect of triggering the application of the MLI. Notifications will trigger the application of the MLI where the MLI provisions have compatibility clauses that provide that the MLI applies “*in place of*” an existing provision, that it “*applies to*” or “*modifies*” an existing provision, or that it applies “*in the absence of*” an existing provision. However, in all of these cases, the extent to which the MLI modifies existing provisions of Covered Tax Agreements is provided in the relevant compatibility clauses.

Where Contracting Jurisdictions disagree about whether a provision in a Covered Tax Agreement is within the scope of a compatibility clause, they can endeavour to settle the matter through the Agreement’s mutual agreement procedure or, if it is a recurrent issue, through a Conference of the Parties convened in accordance with Article 31(3) of the MLI. An inadvertent omission of existing provisions can be addressed by making an additional notification pursuant to Article 29(6) of the MLI.²⁵

An MLI provision will always apply, irrespective of the notifications of the Contracting Jurisdictions, if the compatibility clause states that the MLI provision applies “*in place of or in the absence of*” an existing provision. In these cases, the notifications only ensure clarity and transparency about existing provisions that are within the scope of the compatibility clauses and do not trigger the application of the MLI.²⁶ If all Contracting Jurisdictions notify the existence of an existing provision, that provision is replaced by the provision of the MLI – to the extent described in the relevant compatibility clause. If there is a relevant existing provision which has not been notified by all Contracting Jurisdictions, the provision of the MLI will prevail

²³ In a few cases, Parties are required to notify a list of Covered Tax Agreements that do not contain a provision described in a compatibility clause. This is the case for Articles 6(3), 16(2) and 16(3) of the MLI.

²⁴ As provided in paragraph 18 of the [Explanatory Statement](#), it is therefore not intended that Parties would choose to omit some relevant provisions while listing others.

²⁵ [Explanatory Statement](#), para. 18.

²⁶ Article 8 of the MLI (Dividend transfer transactions), which contains a compatibility clause in its Article 8(2) referring to “*in place of or in the absence of*” does not operate in the same manner. Rather, Article 8(2) of the MLI describes the interaction between its Article 8(1) and existing provisions of Covered Tax Agreements only with respect to minimum holding periods. In this case, notifications made under Article 8(4) of the MLI have the effect of triggering the application of Article 8(1) of the MLI. This is also true for Article 9(2) of the MLI, which cannot apply without an existing provision described in Article 9(1) of the MLI.

over that existing provision, superseding it to the extent that it is incompatible with the relevant provision of the MLI. In both of these cases, the effect of the MLI on the provision of the Covered Tax Agreement is, in effect, identical. If there is no existing provision (or if no notifications have been made by the Contracting Jurisdictions), the provision of the MLI is, in effect, added to the Covered Tax Agreement.²⁷

²⁷ For example, Article 26 of the MLI provides that the provisions of Part VI (Arbitration) of the MLI will apply “*in place of or in the absence of*” of existing arbitration provisions that apply to issues arising from mutual agreement procedure cases (whether they provide for mandatory binding arbitration or not).