

IFA 2025 Lisbon CONGRESS

Subject 2

Improper Use of Tax Treaties and Source Taxation: Policy, Practice and Beyond

Outline

General reporters: Eivind Furuseth (Norway) and Jinyan Li (Canada)

INTRODUCTION

The reasons for choosing the topic

This topic is focused on the improper use of tax treaties from the Source State perspective. Taking stock of all recent changes (at both OECD, UN and EU level), the focus will be on:

- i. what countries/jurisdictions have done since the OECD/G20 BEPS 1.0, especially the publication of the final reports in 2015 and the signing of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI) in 2017 in revising their tax treaties or treaty practices;
- ii. whether countries/jurisdictions have determined if their existing treaties are effective in preventing treaty-based BEPS in terms of source taxation;
- iii. whether countries/jurisdictions have mapped the outstanding issues and developed policies to address them.

The general report will be the first assessment, at the global level, of the real impact of BEPS in increasing the protection of source states' tax bases through tax treaties.

The scope of branch reports

Branch reports are to focus on the three areas identified above. Treaty-based anti-avoidance rules are grouped into specific anti-avoidance rules (SAARs) and general anti-avoidance rules (GAAR). In addition to treaty developments and practices, branch reports are expected to provide some general information on the domestic SAARs and GAARs and situate these domestic rules in the context of the domestic international tax system, especially the source-based tax regime. The main reasons for including the domestic rules are that some of them may be viewed as effective in protecting source taxation, thereby reducing the need for treaty-based SAARs or GAARs, and some of them may constitute treaty overrides which may also reduce the need for having treaty-based SAARs or GAARs.

Prior Work in IFA on related topics

Abuse and improper use of tax treaties have already been addressed at many IFA congresses¹:

- at the 1983 Congress in Venice ("*Tax avoidance/tax evasion*", with general reporter Victor Uckmar);
- at the 1996 Congress in Seoul ("*International aspects of thin capitalisation*", with general reporter Detlev Piltz);

¹ This list takes into account the Cahiers published as of 1980 and available at the website of IFA.

- at the 2018 Congress in Seoul ("*Seeking anti-avoidance measures of general nature and scope*", general reporters Paulo Rosenblatt and Manuel Tron), the focus was on the design of the rules countering tax avoidance;
- at the 2010 Congress in Rome ("*Tax treaties and tax avoidance*", general reporter Stef Van Weeghel);
- at the 2020 Virtual Congress ("*Reconstructing the treaty network*", general reporters Daniel Gutmann/David Duff), it was partly covered when considering the impact of the BEPS initiative on tax treaty policy; however, it was too early to assess the practical impact of the BEPS on tax treaty practice;

Despite that, no Congress has ever designed the topic as it is currently proposed, i.e. assessing the improper use of tax treaties from the source state perspective.

Moreover, BEPS had a major impact on tax systems leading to a significant reform of the measures against improper use of tax treaties. The specific discussion regarding the interpretation and application of the BEPS standards and tax treaty practice has just begun. A prominent recent example is the *Alta Energy* case decided by the Supreme Court of Canada,² which will likely impact the interpretation of the Principal Purpose Test (PPT) – a treaty-based GAAR. By 2025, other similar examples will undoubtedly emerge (as national reports are scheduled to be delivered by December 2024).

GENERAL INFORMATION

General Reporter's contact information

The general reporters are Associate Professor Eivind Furuseth (Norway) and Professor Jinyan Li (Canada). Branch reporters who wish to contact the general reporters are invited to do so using the following email address: eivind.furuseth@bi.no and jli@osgoode.yorku.ca

What is expected from the branch reporters

Two specific tasks should be completed by each branch reporter:

- First, and most importantly, branch reporters need to draft a branch report for the jurisdiction that they represent. The report should be prepared on the basis of the present directives and, as explained below, should focus on the relevant legislation, tax treaty provisions and guidance produced, in that jurisdiction, by courts, administrative organs and tax administrations as regards the application of anti-avoidance provisions in the context of tax treaties. The report should be preceded by a **1,000** words "Summary and conclusions" section that will constitute a short "executive summary" of the report.
- Second, as indicated in Annex 2, branch reporters are invited to provide to the general reporter a copy of the relevant legislation, court decisions and administrative pronouncements that are referred to in their branch report. Preferably, such guidance should be available in English and in electronic form. Where, however, the information is not available in English, it should be provided in its original language.

² *Canada v. Alta Energy Luxembourg S.A.R.L* [2021] SCC 49

Language and format of the branch reports

While IFA rules allow the branch reports to be submitted in English, French or German, it is clear that branch reports that are in English will reach a much larger audience as branch reports in French and German will not be translated. Also, if a report is submitted in either French or German, summaries/conclusions in English will need to be provided by the branch reporters.

Each branch report should be readable on its own without reference to these directives, which will not be reproduced in the Cahiers. The branch reports should not attempt to address all the issues included in these directives since these issues are merely illustrative of issues that may be covered under each subsection. In order to facilitate comparison and to make sure that the same topics are covered, branch reports should, however, follow the general structure of these directives as per the format of the Table of Contents attached hereto as Annex 1.

The maximum length for a branch report is **10,000** words (including footnotes, appendices and bibliography). This, however, does not include the Summary and conclusions section and the text of court decisions and administrative pronouncements that branch reporters are also invited to provide (as indicated above). Branch reporters should allocate that overall limit based on the guidance that is available, in their jurisdiction, on the various topics covered in these directives since it is unlikely that, in any jurisdiction, there will be guidance on all the issues raised in these directives. In order to facilitate the comparison between the different jurisdictions, the general reporter would appreciate it very much if branch reporters could follow the various headings and the section numbering found in the Table of Contents attached to these directives as Annex 1. Headings under which a branch reporter has little to contribute should still appear in the branch report, if only to report that there is no guidance on the topic in that jurisdiction.

The branch report should not contain references to page numbers of the report itself.

Relationship between Description of the Subject and Annex 1: The Description of the Subject that follows the general information part of these directives provides branch reporters with an overview of the Subject. Annex 1 contains the table of contents and the text in italics that follows each heading in Annex 1 purports to give specific guidelines with respect to the information that the Branch reporters are requested to give under that heading, all within the context of the subject as described in the description of the subject.

Timetable

The final deadline for submission of the branch reports to the general reporter and the IFA General Secretariat is 31 December. The deadline date must be strictly adhered to, in view of publication schedules. The Cahiers must be made available electronically well in time before the start of the congress. Furthermore, the deadline is important to the general reporters to allow them sufficient time to write their general report for submission by the 15th of April. It would also really be appreciated if first drafts, or at least outlines, could be sent to the general reporters **by the end of August 2024** so as to allow the general reporters to offer comments before a final draft is submitted and to allow discussion of possible common issues during the Cape Town (*upcoming*) congress.

Addendum

If a branch reporter expects radical changes in his domestic legislation relating to the subject between the date of submission of the report and the publication date thereof, he may, following prior consultation with the General Secretariat, supply an additional one-page Addendum to the report, for publication in the Cahiers, explaining such changes in legislation, but not subsequent to the **1st of March**.

Reporters' biographies

The branch reporters are requested to include an abstract with a maximum of 400 words together with a half page biography with a maximum of 300 words and a color photo in portrait style and high resolution which shall be included in the digital publication of the Cahiers. Full personal biographies will not be printed, but shortened at IFA's discretion.

DESCRIPTION OF THE SUBJECT

Purpose and Scope

As described in the Introduction, this subject is designed to a sense about the impact of BEPS/MLI on tax treaty development and practices. Given the short amount of time elapsed since the BEPS/MLI and large amount of time required to revisit tax treaty policies and implement the BEPS minimum standards, this subject was designed to not only look at the policy and practice of the past and present, but also the future.

Structure

This subject was divided into five parts.

Part One: Introduction. Branch reports are requested to provide an overview of the general information about their jurisdiction in terms of the type of legal system, membership of the OECD/EU/Inclusive Framework, signatory to the MLI and the number of tax treaties concluded. In addition, branch reports are asked to provide an overview of the domestic tax system in regard to source-based taxation and domestic SAARs and GAAR.

Part Two: Overview of treaty-based anti-abuse rules aimed to protect source taxation. This part covers the following specific issues:

- a) broadly-construed treaty-based SAARs, such as the beneficial ownership rule in Articles 10, 11 and 12, artificial PE rules in Article 5, the look-through rules in Article 13, and Article 12A and Article 12B of the UN Model.
- b) Treaty GAARs
- c) The relationship between domestic GAARs and treaty GAARs
- d) Typical treaty abuse situations in your jurisdiction
- e) Potential conflicts of rules (ordering rules).

Part Three: Dispute resolution mechanism. This part ask branch reporters to the dispute resolution mechanism, practice, and cases that involve treaty SAARs or GAARs.

Part Four: Policy. Branch reports will explain if there are any significant policy concerns about improper use of tax treaties in their country, and if their country has not signed the MLI, whether they have intentions to do so and if not, why not.

Part Five: Beyond – how to counteract improper use of tax treaties in the future. Branch reports are to explain whether their country have taken initiatives to strengthen anti-abuse measures, to implement the subject-to-tax-rule in Pillar Two and/or Pillar One multilateral convention (when it is ready for signature), and the GloBE rules in Pillar Two.

Branch Reports and documents

Branch reporters are requested to:

- a) present the pertinent materials as clearly as possible. Knowing that English is not the first language for many, it is the content, as opposed to the style or grammatical correctness that is more important.
- b) follow the outline in Annex 1 as closely as possible. If additional information is necessary, such information should be clearly identified.
- c) provide citations for the sources of information.
- d) Provide a searchable link for the source or attach a digital copy of the supporting materials.
- e) Provide the year in which a treaty that is mentioned was concluded.

ANNEX 1

CONTENTS OF THE BRANCH REPORTS

Table of contents

Summary and conclusions

The report should be preceded by a "Summary and conclusions" section that will constitute a short "executive summary" of the report. This summary should not exceed 1.000 words and should logically be prepared after the report has been completed. The Summary and conclusions section shall be printed in the Cahiers.

Part One: Introduction – domestic law

This part should contain a brief high-level overview of the types of information listed in the questions.

1.1 General information about your country [maximum 400 words]

a) Is your country a civil law or common law country?

Do you think it matters whether your country is a civil law or common law country when it comes to application of both domestic and tax treaty anti-avoidance rules. Please provide one or two examples that shows the interaction (or lack of interaction) between domestic anti-avoidance rules and tax treaty anti-avoidance rules

b) Is your country a member of OECD?

If so, has your country agreed to include provisions of the UN Model in your tax treaties? Name a few treaties as examples. Further, if your country is a member of the OECD, does the tax treaty strictly follow the OECD Model and the commentary? If not, does your country anyhow rely on the OECD Model and its commentary when concluding tax treaties?

c) Is your country member of EU or EEA?

If so, does that impact on how your anti-abuse measures are drafted and how tax treaties are drafted and interpreted? Please provide one or two examples, if available.

d) Is your country a member of OECD/G20 BEPS Inclusive Framework?

e) Has your country taken part of the BEPS work and how is the work implemented in your domestic legislation and in your tax treaties?

- 1) Has your country signed the MLI? (<https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf>)?*
- 2) How many of your treaties are "covered tax agreements"?*

f) How many tax treaties have been concluded by your country? Please provide a list of these treaties.

1.2 Domestic tax system

- a) *Is source-based taxation important in your international tax policy?*
- b) *What are the main specific anti-avoidance rules (SAARs) in your domestic law that are designed to protect source taxation?*

For example, do you have: thin capitalization rules, anti-base erosion rules, such as limitation on excessive interest and financial expenses, fat capitalization rules, hybrid mismatch arrangement rules, back-to-back loans or other arrangements, withholding taxes and accompanying anti-avoidance rules, anti-surplus stripping rules, domestic SAARs included in domestic permanent establishment rules etc.?

- c) *Are these SAARs perceived to be effective? Have these SAARs been litigated in court? Please provide examples of case law that deals with such specific domestic anti-avoidance rules. And which types of domestic SAARs are most often dealt with by the tax authorities and/or the court?*
- d) *Is there a General Anti-avoidance Rule (GAAR) in your domestic law (“Domestic GAAR”)? If so, what are the essential elements of the Domestic GAAR? If the GAAR were found to apply, is there a penalty? And if so, is it mandatory for the tax authorities to levy the penalty, or is it based on the tax authorities' discretion?*
- e) *Application of SAARs and Domestic GAAR to treaty abuse:*
 - 1) *Have there been any cases in which a SAAR and/or the domestic GAAR was involved? Please provide examples.*
 - 2) *Has any domestic SAAR or GAAR been found by the courts to be inconsistent with a tax treaty?*
- f) *Were any of the SAARs or the domestic GAAR modified in response to BEPS 1.0 (e.g., since the publication of the Final Reports in 2015)? For example, was any of the SAARs modeled on the BEPS recommendations on interest expense or hybrid mismatch arrangements?*
- g) *Are there any proposals to reform any of the SAARs or domestic GAAR in order to strengthen source-based taxation?*

Part Two: Overview of treaty-based anti-abuse rules aimed to protect source taxation

2.1 Treaty-based SAARs

- a) *Is the beneficial ownership rule in Arts.10, 11 and 12 of the OECD Model included in some or all of your country's tax treaties?*
- b) *Is Article 5(4.1), Article 5(5), and/or Article 5(6) of the OECD Model (2017) included in any of your country's tax treaties? If so, when was it added? Provide one or two samples.*
- c) *Is Article 5(6) of the UN Model (2021) included in any of your country's tax treaties? If so, provide one or two samples.*

- d) *Is Article 13(4) of the OECD Model (2017) and/or Article 13(5) of the UN Model (2021) included in any of your country's tax treaties? Provide one or two samples.*
- e) *Is Article 13(6) of the UN Model (2021) included in any of your country's tax treaties? Provide one or two samples.*
- f) *Is Article 13(7) of the UN Model (2021) included in any of your country's tax treaties? Provide one or two samples.*
- g) *Is Article 12A of the UN Model (2021) included in any of your country's tax treaties? Provide one or two samples.*
- h) *Is Article 12B of the UN Model (2021) included in any of your country's tax treaties? Provide one or two samples.*
- i) *How are transparent entities, viewed from the source state, dealt with in your tax treaties? (see Article 3 of MLI).*
- j) *The fact that there is a hybrid entity (i.e. mismatch in classification of the entity in the source state and the resident state) may create tax planning opportunities. How is this dealt with under the application of anti-avoidance measure in tax treaties?*
- k) *Are there any other SAARs in your country's tax treaties? If so, what are they? Provide one or two sample treaties.*

2.2 Treaty GAARs

- a) *Does any of your country's tax treaty contain a principal purpose test (PPT) within the meaning of Article 7 of the MLI or Article 29(9) of the OECD Model (2017) or UN Model (2021)? How many treaties have the PPT?*
- b) *Does any of your country's tax treaty contain a limitation on benefits (LOB) provision within the meaning of Article 7 of the MLI or Article 29(1)-(8) of the OECD Model (2017) or UN Model (2021)? How many treaties have the LOB?*

2.3 The relationship between domestic GAARs and treaty GAARs

- a) *Is the content of your domestic GAAR the same as or similar to the PPT in OECD Model (2017) Art. 29(9)?*
- b) *If not, what are the significant differences between the domestic GAAR and the PPT?*
- c) *Has the relationship between a domestic GAAR and treaty GAAR been litigated in your country? If so, please briefly discuss the case(s).*
- d) *If your country is an EU or EEA country, does the relationship between domestic GAAR and treaty GAARs become different because of the membership of EU/EEA? Domestic rules may as a starting point not restrict the fundamental freedoms of the EU-/EEA-treaty. Hence, may it be that your domestic anti-avoidance rules must be interpreted more restrictively in an EU/EEA situation than in a non-EU/EEA situation? Please provide some examples.*

2.4 Typical treaty abuse situations in your country

- a) *Are there cases involving treaty shopping? If so, please briefly describe the case(s) and a searchable link to the full text of the case(s).*
- b) *Are there cases involving artificial avoidance of PE status? If so, please briefly describe the case(s) and a searchable link to the full text of the case(s).*
- c) *Are there cases involving indirect transfers? If so, please briefly describe the case(s) and a searchable link to the full text of the case(s).*
- d) *Are there cases involving surplus stripping (e.g., converting dividends into capital gains)? If so, please briefly describe the case(s) and a searchable link to the full text of the case(s).*
- e) *Are there cases involving other forms of treaty abuse to avoid source-based taxation? If so, please briefly describe the case(s) and a searchable link to the full text of the case(s).*

2.5 Potential conflicts of rules (ordering of rules)

- a) *If your country has a domestic GAAR and a treaty GAAR, does the treaty prevail?*
- b) *Is it possible to have potential conflict between a treaty GAAR and treaty SAAR as described in the following example? If so, how do you see such conflict be resolved?*

Example:

Are the recipients of a dividend payment entitled to the reduced tax treaty withholding tax rate? To answer this question, there is a two-step process.

First, it must be determined whether the reduced withholding tax rate under OECD MC Art. 10 (2) applies, i.e., the recipients are beneficial owners resident in the other contracting state.

Secondly, provided that the reduced rate under OECD MC Art. 10 (2) applies, it must be considered whether the transaction is subject to OECD MC Art. 29 (and especially OECD MC Art. 29(9)). Under the interpretation of OECD MC art. 10, the principles of VCLT Art. 31 (1) are applied, including taken into consideration the wording of the treaty and the object and purpose of OECD MC Art. 10. Hence, provided that OECD MC Art. 10 (2) applies, the object and purpose of the treaty entails that the recipient of the payment is entitled to the reduced treaty rate. Second, the PPT rule in Article 29(9) may apply to deny the treaty benefit (i.e., reduced withholding tax rate) if two requirements are met: (1) obtaining that treaty benefit obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit; (2) although the principal purpose of the transaction was to achieve a treaty benefit, taxpayer is entitled to the treaty benefit provided that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.

But if we first conclude that OECD MC Art. 10(2) applies (having taken into the object and

purpose, cf. VCLT Art. 31 (1)), haven't we already confirmed that the object and purpose is in favour of accepting the reduced treaty rate under OECD MC Art. 10(2)?

- c) *Can you identify and briefly describe the most important decisions (by tax authorities or courts) regarding the application of these clauses?*
- d) *In your country's treaty practice, how relevant are the OECD Commentaries on the Model Convention and other OECD materials?*

Part Three: Dispute resolution mechanism

[Please note, there are some sub-questions in a), b) and c)]

- a) *In cases where your country's source-based taxation, including those charged by virtue of a treaty-based SAAR or GAAR, but the residence country interprets the treaty provision(s) differently, does your country actively use the mutual agreement procedure (MAP)? If so, are there any data or examples of the MAP cases?*
- b) *Has any taxpayer challenged your country's tax administration's interpretation of treaty SAAR or GAAR in court? If there are domestic litigation, please describe the case(s) and provide a link to a searchable source for such case(s).*
- c) *Does any of your country's treaties allow the use of arbitration under a provision like Article 25 Alternative B of the UN Model (2021) or Article 25(5) of the OECD Model (2017)? If so, is there any published information on arbitration cases? What kind of arbitration (final offer or independent opinion)? With which countries? Are disputes involving the application of a SAAR or GAAR eligible for arbitration?*
- d) *Are there other dispute resolution mechanism (e.g., mediation) available?*

Part Four: Policy

- a) *Is there any significant policy concern about improper use of tax treaties in your country? If so, has the government published any policy papers or evidence on treaty abuse?*
- b) *If your country has not signed the MLI, are there any indications that it might in the near future? What are the indications?*
- c) *If your country has not signed the MLI, is it because the treaty-abuse rules in the MLI have already been included in bilateral treaties?*

Part Five: Beyond – how to counteract improper use of tax treaties in the future

- a) *Has your country taken any initiatives to strengthen anti-abuse measures, both under domestic law and/or in tax treaties since 2015?*
- b) *Does your country plan to incorporate the subject-to-tax-rule (STTAR) in Pillar Two into tax treaties?*

- c) *Does your country think that the implementation of Pillar One will likely reduce treaty-based tax planning? Does your country plan to sign a Pillar One convention and implement Pillar One?*
- d) *Does your country think that implementing the GloBE rules in your country will help reduce treaty abuse? Does your country think that Pillar Two can help protect source-based taxation by providing a floor for tax competition?*
- e) *Has your country introduced measures to implement the GloBE rules?*

Annex 2

Documents to be provided

Branch reporters are invited to provide to the general reporters a copy of any of the following documents which are referred to in their branch report if they are not available on publicly accessible website.

- interpretative provisions found in a treaty itself, in a protocol to a treaty, in a memorandum or letter of understanding between the Contracting States or in any other instrument prepared in connection with a treaty, including an instrument prepared by one Contracting State and endorsed by another Contracting State;
- court decisions;
- publicly available mutual agreements;
- publicly available decisions by any administrative review board that may be part of or independent from a tax administration (e.g. assessment board or appeal board that would not constitute a court);
- legislative texts, such as an interpretative provision found in a statute, regulation or decree;
- circulars, rulings or other official administrative pronouncements by the tax authorities;
- any other similar document that can be considered to be an official statement with respect to the subject of this report originating from that jurisdiction.

Preferably, these documents should be provided in English and in electronic form as the objective is to make such information available on the IFA website. Where, however, the information is not available in English, it should be provided in its original language.

The documents provided should not exceed 200 pages (in print form). Branch reporters of jurisdictions where documents referred to in the branch report would greatly exceed that limit are invited to exercise discretion in choosing which documents to provide and to send what they consider as likely to be the most useful and influential documents for other countries (e.g. for judicial decisions, those that are most recent or rendered by the highest courts).