

Treaty Abuse

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Paragraphs 22 and 22# of the Commentary on Article # provide a general discussion of the interaction between tax treaties and domestic anti-abuse rules

These paragraphs conclude that a conflict would not occur in the case of the application of certain domestic anti-abuse rules to a transaction that constitutes an abuse of the tax

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Action 6

Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the erosion of treaty benefits in inappropriate circumstances" - or . will also be done to clarify that tax treaties are not intended to be used to generate double non-taxation and to identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country" ' he wor . will be co-ordinated with the wor . on hybrids"

- # Limitation-on-benefits (LOB) rule to address a large number of treaty shopping situations based on the legal nature, ownership in, and general activities of, residents of a contracting state
- # Minimum shareholding period to prevent dividend transfer transactions
- # References to Article #4(5) to prevent transactions that circumvent the application of that rule dealing with capital gains on shares of immovable property companies
- # References to the tie-breaker rule for determining the treaty residence of dual-resident entities
- # Anti-abuse rule for permanent establishments situated in third states

Treaty abuse, like abuse of domestic law, is best addressed through a combination of

- # Specific anti-abuse rules, which provide greater certainty but can only deal with known abusive strategies that can be addressed through general objective criteria
- # More general anti-abuse rules or judicial doctrines, which are less certain but offer protection against abusive transactions that have not previously been identified or addressed or that require a more case-by-case analysis



- A" Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the erosion of treaty benefits in inappropriate circumstances
- 1" Clarify that tax treaties are not intended to be used to generate double non-taxation
- \$" Identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country

Paragraphs to be added to the introduction of the Model Tax Convention

- will make it easier for countries to justify their decision not to enter into tax treaties with certain low- or no- tax jurisdictions

Also relevant with respect to the question of whether a treaty previously concluded should be maintained, changed or terminated, especially after substantial changes to domestic law of a treaty partner

One deals with tax policy; other factors may be relevant to the decision of concluding, maintaining or terminating a tax treaty

Article 9

Convention between (State A+ and (State 1+ for the elimination of double taxation with respect to taxes on income and on capital and the prevention of tax evasion and avoidance

Convention between (State A+ and (State 1+ with respect to taxes on income and on capital#

Preamble

Desire to further develop their economic relationship and to enhance their cooperation in tax matters,

Intend to conclude a Convention for the elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States)



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#1 - when a person tries to circumvent the limitations provided by the treaty itself

#2 - when a person tries to abuse the provisions of domestic tax law using treaty benefits

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' these are cases where a person seeks to obtain treaty benefits that would otherwise be unavailable by trying to circumvent treaty provisions

- # Treaty shopping arrangements
- # Dividend/share transfer transactions to get to reduced rate of * ? in Art 17(2+a)
- # Airin-out of labour cases, to obtain benefit of Art 17(2+a)
- # Others

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Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of an arrangement or

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3 an% countries have domestic anti-abuse rules or
,udicial doctrines that address such examples

The report notes that the Commentar% already addresses a number of these issues, for example

\$E\$ rules in para" 24 of the Commentar% on Article
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'hin capitalisation rules in para" 4 of the
Commentar% on Article)

The inclusion of the '!' rule (which is based in the
&uidin& principle+ will confirm that treat% provisions do



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"" the tax benefits that would otherwise appl% under the other provisions of the \$onvention will not appl% to an% item of income on which the tax in the third ,urisdiction is less than 6@ per cent of the tax that would be imposed in the first-mentioned 2tate if the income were earned or received in that 2tate b% the enterprise and were not attributable to the permanent establishment in the third ,urisdiction" ...

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' his \$onvention shall not affect the taxation, b% a \$ontractin& 2tate, of its residents except with respect to the benefits & ranted under para& raph 4 of Article B, para& raph 2 of Article) and Articles #), 2@, 24, 25 and 2* and 2I

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' he =eport clarifies that treaties do not prevent "departure taxes" ("exit taxes"+, which are tri&&ered when a resident ceases to be a resident of a 2tate)

" ' o the extent that the liabilit% to such a tax arises when a person is still a resident of the 2tate that applies the tax and does not extend to income accru& after the cessation of residence, nothin& in the \$onvention, and in particular in Articles #4sñ

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