The Anti-Abuse Rule for Permanent Establishments Situated in Third States

A Legal Analysis of Article 29(8) OECD Model

Jean-Philippe Van West



Volume 16 WU Institute for Austrian and International Tax Law European and International Tax Law and Policy Series

Table of Contents

Acknowledgements Abstract Abbreviations		xvii xix xxi
Chapter 1:	Introduction to PE Triangular Cases and Article 29(8) of the OECD Model	1
1.1.	Aim and relevance of the research	1
1.2.	PE triangular structures in international tax planning	3
1.2.1.	Basic PE triangular structure	3
1.2.2.	Tax planning schemes	6
1.2.2.1.	Transfer of assets	6
1.2.2.2.	Transfer of residence	7
1.2.2.3.	Classic planning structure	8
1.2.3.	The facilitation of PE triangular structures by	
	some states	11
1.2.3.1.	Relevance	11
1.2.3.2.	Netherlands	13
1.2.3.3.	Switzerland	16
1.2.3.4.	Luxembourg	18
1.2.4.	Article 29(8) of the OECD Model: Closing the loophole?	19
1.3.	Scope, structure and methodology	20
Chapter 2:	The Interpretation of Tax Treaties	25
2.1.	Purpose of this chapter	25
2.2.	Interpretation according to the Vienna Convention (1969)	25
2.3.	The relevance of domestic law: Article 3(2) of the OECD Model	28
2.4.	Legal relevance of the OECD Commentary	21
2.4. 2.4.1.	Legal relevance of the OECD Commentary The OECD Commentary and the Vienna Convention (1969)	31
2.4.2.	Static or dynamic interpretation	31 33
<i>LL</i> .	State of a flame interpretation	55

2.5.	Legal relevance of the BEPS reports	34
2.6.	Legal relevance of US tax treaty practice	35
Chapter 3:	The Origins of Article 29(8) of the OECD Model	37
3.1.	Purpose of the historical analysis	37
3.2.	The Draft OECD Model (1963) and the OECD Model (1977)	39
3.3.	The 1992 OECD Report on Triangular Cases	43
3.3.1.	Putting PE triangular cases on the agenda of WP 1	43
3.3.2.	The draft report and its revisions	46
3.3.3.	The 1992 OECD Triangular Report	51
3.4.	The Netherlands-United States Income Tax Treaty	
	(1992)	53
3.4.1.	Background to the treaty	53
3.4.2.	Why did the United States insist on dealing with the	
	triangular issue in the tax treaty?	57
3.4.3.	Article 24(4) of the Netherlands-United States	
	Income Tax Treaty (1992)	58
3.4.4.	The Rostenkowski Bill	62
3.4.5.	Netherlands draft legislation	64
3.4.6.	The 1993 Protocol	66
3.4.6.1.	Inclusion of a triangular provision in the interest	
2462	and the royalties article	66
3.4.6.2.	Which PE triangular cases are regarded as abusive?	67
3.4.6.3.	Which PE triangular structures are not regarded as	-
2161	abusive?	70
3.4.6.4.	Which benefits are denied?	71
3.4.6.5.	Other relevant measures of the protocol	72
3.4.6.6.	Issues regarding the application of the PE triangular	70
3.4.7.	provision Relevance of the triangular provision of the	73
3.4.7.	Relevance of the triangular provision of the Netherlands-United States Income Tax Treaty (1992)	75
3.5.	From the Netherlands-United States Income Tax	
	Treaty (1992) to the BEPS Project	76
3.5.1.	The United States	76
3.5.1.1.	Tax treaty policy regarding triangular provisions	76

	3.5.1.2.	Overview of the triangular provisions included in	
		US tax treaties	82
	3.5.1.2.1.	In general	82
	3.5.1.2.2.	Article 30(5) of the France-United States Income	
		Tax Treaty (1994)	84
	3.5.1.2.3.	Article 16(4) of the Austria-United States Income	
		Tax Treaty (1996)	86
	3.5.1.2.4.	Article 23(7) of the Ireland-United States Income	
		Tax Treaty (1997)	88
	3.5.1.2.5.	Article 17(5) of the amended Sweden-United States	
		Income Tax Treaty (1994)	89
	3.5.1.2.6.	Article 22(6) of the Hungary-United States Income	
		Tax Treaty (2010)	90
	3.5.2.	The practice of other countries	91
	3.5.3.	The OECD	93
	3.5.3.1.	Not only an issue for the source state	93
	3.5.3.2.	The 2002 OECD Report on issues arising under	
		article 5 of the OECD Model	94
	3.5.3.3.	The 2010 OECD Report on the Attribution of Profits	
		to Permanent Establishments	95
	3.6.	The BEPS Project	97
	3.6.1.	In general	97
	3.6.2.	BEPS Action 6	98
	3.6.2.1.	BEPS Action 6: Public Discussion Draft	98
	3.6.2.2.	BEPS Action 6: 2014 Deliverable Report	99
	3.6.2.3.	BEPS Action 6: Revised Discussion Draft	100
	3.6.2.4.	BEPS Action 6: 2015 Final Report	101
	3.6.3.	The influence of developments in the United States	101
	3.6.4.	Article 10 of the MLI and article 29(8) of the	
		OECD Model	105
	3.6.5.	Impact on the tax treaty policy of countries	107
	3.7.	Interim conclusions on the origin of article 29(8)	
	5.7.	of the OECD Model	109
		of the OECD Model	109
Ch	apter 4:	Legal Analysis of Article 29(8) of the OECD Model	115
	4.1.	Structure of the legal analysis	115
	4.2.	Object and purpose of article 29(8) of the	
		OECD Model	116

4.3.	Scope: The positive criteria	122
4.3.1.	The constituent elements for article 29(8) of	
	the OECD Model to apply	122
4.3.2.	First requirement: A PE triangular structure	125
4.3.2.1.	An enterprise of a contracting state	125
4.3.2.1.1.	In general	125
4.3.2.1.2.	Article 3(1)(d) of the OECD Model: An enterprise	
	carried on by a resident of a contracting state	126
4.3.2.1.3.	The use of the term "enterprise" during the drafting	
	process	127
4.3.2.1.4.	The term "enterprise" in the context of the OECD	
	Model	128
4.3.2.1.5.	Meaning of the term "enterprise" in light of the	
	object and purpose of article 7 of the OECD Model	130
4.3.2.1.6.	Meaning of the term "enterprise" in light of the	
	object and purpose of article 29(8) of the OECD	
	Model	133
4.3.2.2.	Derives	135
4.3.2.3.	Income	137
4.3.2.4.	From the other contracting state	139
4.3.2.5.	A permanent establishment situated in a third	
	jurisdiction	140
4.3.2.5.1.	In general	140
4.3.2.5.2.	A permanent establishment: Which criteria?	140
4.3.2.5.3.	Situated in a third jurisdiction	146
4.3.2.6.	The first-mentioned state treats such income as	
	attributable	148
4.3.2.6.1.	The attribution of income to the PE: Which criteria?	148
4.3.2.6.2.	The first-mentioned state treats such income as	
	attributable	151
4.3.3.	Second requirement: Exemption in the residence state	154
4.3.3.1.	Profits	154
4.3.3.2.	Exempt from tax	156
4.3.4.	Third requirement: Low taxation in the PE state	160
4.3.4.1.	Any item of income	160
4.3.4.2.	The tax in the third jurisdiction	161
4.3.4.2.1.	Meaning of the expression "the tax in the third	
	jurisdiction"	161
4.3.4.2.2.	Calculation of the tax in the third jurisdiction	166
4.3.4.3.	Fixed-rate threshold	170
4.3.4.4.	The 60% threshold	172

4.4.	Scope: The negative criteria	175
4.4.1.	Two exceptions to the application of article $29(8)(a)$	
	of the OECD Model	175
4.4.2.	Article 29(8)(b) of the OECD Model: The active	
	conduct of a business test	176
4.4.2.1.	In general	176
4.4.2.2.	Origin	177
4.4.2.3.	Object and purpose	179
4.4.2.4.	First requirement: Active conduct of a business	
	carried on through the permanent establishment	180
4.4.2.4.1.	The active conduct of a business	180
4.4.2.4.2.	Through the permanent establishment	184
4.4.2.4.3.	The business of making, managing or simply	
	holding investments	184
4.4.2.4.4.	Banking, insurance or securities activities carried	
	on by a bank, insurance enterprise or registered	
	securities dealer	188
4.4.2.5.	Second requirement: Link between the income	
	generated and the business carried on through the	
	permanent establishment	191
4.4.2.5.1.	Emanates from	191
4.4.2.5.2.	Incidental to	192
4.4.3.	Article 29(8)(c) of the OECD Model: Discretionary	
	relief	193
4.4.3.1.	In general	193
4.4.3.2.	Origin	194
4.4.3.3.	Object and purpose	198
4.4.3.4.	First requirement: Denial of treaty benefits pursuant	
	to the previous provisions of article 29(8) of the	
	OECD Model	199
4.4.3.5.	Second requirement: Request by the taxpayer	201
4.4.3.6.	Third requirement: Consultation of the other	
	contracting state	202
4.4.3.7.	Consequence: Discretionary power of the competent	
	authority of the source state	204
4.4.3.7.1.	The competent authority of the source state	204
4.4.3.7.2.	Discretionary relief	204
4.5.	Legal consequences	209
4.5.1.	The benefits of this convention shall not apply	209
4.5.2.	Possible unrelieved double taxation	213

4.5.3.	Influence of the tax treaty between the source state and the PE state	213
4.6.	Interim conclusions on the legal analysis of article 29(8) of the OECD Model	215
Chapter 5:	The Relationship between Article 29(8) and Other Provisions of the OECD Model	221
5.1.	Purpose of this chapter	221
5.2.	Article 1(2) of the OECD Model	222
5.2.1.	The application of article 1(2) of the OECD Model	222
5.2.2.	Transparent entities and PE triangular cases	224
5.3.	Article 4(3) of the OECD Model	228
5.3.1.	The application of article 4(3) of the OECD Model	228
5.3.2.	Dual-resident triangular cases and article 29(8) of the OECD Model	229
5.4.	The beneficial ownership concept of articles $10(2)$, $11(2)$ and $12(1)$ of the OECD Model	232
5.5.	Article 29(1)-(7) of the OECD Model	233
5.6.	Article 29(9) of the OECD Model	234
5.7.	Interim conclusions on the relationship with other provisions of the OECD Model	241
Chapter 6:	Conclusions	245
Annex:	Overview Triangular Provisions	253
1.	OECD	253
1.1.	Provision BEPS Action 6: Public Discussion Draft	253
1.2.	Provision BEPS Action 6: 2014 Deliverable Report	253
1.3.	Alternative provision BEPS Action 6: 2014	
1.4	Deliverable Report	254
1.4.	Provision BEPS Action 6: Revised Discussion Draft	255

1.5.	Article 10 MLI (Anti-abuse Rule for Permanent	
	Establishments Situated in Third Jurisdictions)	256
1.6.	Article 29(8) OECD Model	257
1.7.	Alternative provision paragraph 168 Commentary	
	on Article 29 of the OECD Model	258
2.	United States	258
2.1.	Article 12(8) Netherlands-United States Income	
	Tax Treaty (1992) (Interest)	258
2.2.	Article 13(6) Netherlands-United States Income	
	Tax Treaty (1992) (Royalties)	259
2.3.	Article 30(5) France-United States Income Tax	
	Treaty (1994)	259
2.4.	Article 24(5) Luxembourg-United States Income	
	and Capital Tax Treaty (1996)	260
2.5.	Article 16(4) Austria-United States Income Tax	
	Treaty (1996)	261
2.6.	Article 22(4) Switzerland-United States Income	
	Tax Treaty (1996)	262
2.7.	Article 22(6) South Africa-United States Income	
	Tax Treaty (1997)	262
2.8.	Article 23(7) Ireland-United States Income Tax	
	Treaty (1997)	263
2.9.	Article 17(5) Sweden-United States Income Tax	
	Treaty (1994) (as amended through 2005)	264
2.10.	Article 16(5) Finland-United States Income and	
	Capital Tax Treaty (1989) (as amended through	
	2006)	265
2.11.	Article 28(5) Germany-United States Income and	
	Capital Tax Treaty (1989) (as amended through	
	2006)	265
2.12.	Article 22(6) Denmark-United States Income Tax	
	Treaty (1999) (as amended through 2006)	266
2.13.	Article 21(6) Belgium-United States Income Tax	
	Treaty (2006)	267
2.14.	Article 21(5) Iceland-United States Income Tax	
	Treaty (2007)	268
2.15.	Article 21(5) Bulgaria-United States Income Tax	
_	Treaty (2007)	268
2.16.	Article 22(5) Malta-United States Income Tax	_
	Treaty (2008)	269

2.17.	Article 16(5) New Zealand-United States Income	
	Tax Treaty (1982) (as amended through 2008)	270
2.18.	Article 30(5) France-United States Income Tax	
	Treaty (1994) (as amended through 2009)	270
2.19.	Article 22(6) Draft Hungary-United States Income	
	Tax Treaty (2010)	271
2.20.	Article 24(5) Draft Chile-United States Income	
	and Capital Tax Treaty (2010)	272
2.21.	Article IX Draft Protocol (2013) to the Spain-	
	United States Income Tax Treaty (1990)	273
2.22.	Article 22(6) Draft Poland-United States Income	
	Tax Treaty (2013)	273
2.23.	Article 1(7) Draft US Model (2015)	274
2.24.	Article 1(8) US Model (2016)	275
3.	Triangular provisions included in the tax treaties	
	concluded by Canada	276
3.1.	Article 29(8) Canada-France Income and Capital	
	Tax Treaty (1975) (as amended through 1995)	276
3.2.	Article 27(4) Draft Canada-Lebanon Income Tax	
	Treaty (1998)	277
3.3.	Article 27(5) Belgium-Canada Income and Capital	
	Tax Treaty (2002)	277
4.	Triangular provisions included in the tax treaties	
	concluded by the United Kingdom	278
4.1.	Article V Protocol (2008) to the Netherlands-United	
	Kingdom Income Tax Treaty (2008)	278
4.2.	Article 3 Protocol (2010) to the Germany-United	
	Kingdom Income and Capital Tax Treaty (2010)	278
4.3.	Article 23(2) Hungary-United Kingdom Income	
	Tax Treaty (2011)	279
5.	Triangular provisions included in the tax treaties	
	concluded by Chile	280
5.1.	Article 12 Protocol (2012) to the Austria-Chile	
	Income and Capital Tax Treaty (2012)	280
5.2.	Article 24(8) Argentina-Chile Income and Capital	
	Tax Treaty (2015)	281
5.3.	Article 26(6) Chile-China (People's Rep.) Income	
	Tax Treaty (2015)	281
5.4.	Article 27(2) Chile-Italy Income Tax Treaty (2015)	281

5.5.	Article 28(5) Chile-Czech Republic Income and	202
F (Capital Tax Treaty (2015)	282
5.6.	Article 22(2) Chile-Japan Income Tax Treaty (2016)	283
5.7.	Article 28(7) Chile-Uruguay Income and Capital Tax Treaty (2016)	283
6.	Triangular provisions included in tax treaties since the publication of the 2017 OECD Model	284
6.1.	Article XXVII(4) Argentina-Brazil Income and	
	Capital Tax Treaty (1980) (as amended through	
<i>(</i>)	2017)	284
6.2.	Article 27(7) Paraguay-Uruguay Income and	205
6.2	Capital Tax Treaty (2017)	285
6.3.	Article 21(7) Japan-Russia Income Tax Treaty (2017)	285
6.4.	Article 21(8) Denmark-Japan Income Tax Treaty	205
0.4.	(2017)	286
6.5.	Article 22(8) Iceland-Japan Income Tax Treaty	200
0.2.	(2018)	287
6.6.	Article 27(4) Brazil-Switzerland Income Tax Treaty	
	(2018)	288
6.7.	Article 28(7) Brazil-Singapore Income Tax Treaty	
	(2018)	289
6.8.	Article 28(3) Angola-Portugal Income Tax Treaty	
	(2018)	290
6.9.	Article 28(8) Japan-Spain Income Tax Treaty	
	(2018)	291
6.10.	Article 28(1) Croatia-Japan Income Tax Treaty	• • •
	(2018)	292
6.11.	Article 28(7) Colombia-Japan Income Tax Treaty	202
(10)	(2018)	293
6.12.	Article 3(5) Protocol (2019) to the Ecuador-Japan	204
6 12	Income Tax Treaty (2019) Article 26 A (7) Brezil Sweden Income Tax Treaty	294
6.13.	Article 26A(7) Brazil-Sweden Income Tax Treaty (1975) (as amended through 2019)	295
6.14.	Article 29(1) Argentina-Japan Income Tax Treaty	295
0.14.	(2019)	296
6.15.	Article 29(8) Brazil-Uruguay Income and Capital	270
0.10.	Tax Treaty (2019)	297
6.16.	Article 28(1) Japan-Uruguay Income Tax Treaty	
*	(2019)	298

6.17.	Article 29(1) Japan-Peru Income Tax Treaty	
	(2019)	299
6.18.	Article 28(1) Jamaica-Japan Income Tax Treaty	
	(2019)	300
Bibliography		301