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# Domestic Attribution of Income and Taxation of International Entertainers and Sportspersons

Theory and Practice of Art. 17 OECD Model Convention

5
European and International
Tax Law and Policy Series

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# Domestic Attribution of Income and Taxation of International Entertainers and Sportspersons

**Why this book?**
The attribution of income to a certain taxpayer is an issue that virtually every tax jurisdiction has to deal with. However, there is no uniform international consensus on how taxable profits are to be allocated to taxpayers, and the details on how to allocate profits are regulated individually by each state. However, consistent principles for the attribution of income are particularly of interest with regard to the application of article 17 of the OECD Tax Model Convention (MC), the relevant allocation rule for the income of entertainers and sportspersons. This provision not only applies to income that is directly attributable to a given entertainer or sportsperson but also to income from an entertaining or sporting activity that accrues to another person.

Therefore, this book will provide detailed insight into the treatment of entertainers and sportspersons in international tax law and, in this context, the relevance of the domestic attribution of income for the application of tax treaties with regard to entertainers and sportspersons will be the focus of attention. Given this focus, it will also be established how allocation conflicts – i.e. situations where the countries involved attribute the income at stake to different taxpayers according to their domestic attribution principles – can be resolved in a methodically consistent and comprehensive manner with regard to international entertainers and sportspersons.


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# Preface

This book aims at providing an in-depth analysis of the interplay between domestic income attribution and the proper application of article 17(1) and 17(2) of the OECD Model Convention (MC). In this context, it deals with how allocation conflicts involving international entertainers and sportspersons can be resolved in a systematically consistent and comprehensive manner, rather than merely addressing certain specific cases on an exemplary basis.

The doctoral study that led to this book was written during my time as a research and teaching associate at the Institute for Austrian and International Tax Law at WU Vienna. It was really a pleasure for me to have had this great opportunity to conduct research in such an inspiring and welcoming academic atmosphere. I would therefore like to thank all of the professors and colleagues at the Institute for enabling me to participate in the numerous projects, conferences and other events that enriched my doctoral project and helped me to deepen my knowledge of various aspects of international, European, and domestic tax law.

I would especially like to thank the supervisor of my thesis, Univ.-Prof. Dr DDr h.c. Michael Lang, who always supported me in the best manner during the whole project. His dedication to the subject of international tax law was truly a great inspiration for me to further intensify my research. His critical feedback was also invaluable for the process of defining the scope of the thesis and effectively bringing my thoughts to paper. My sincere gratitude also goes to Univ.-Prof. Dr Alexander Rust for accepting the role as my second supervisor and for sharing his knowledge with me. Special thanks also to Univ.-Prof. MMag Dr Josef Schuch and Univ.-Prof. Dr Claus Staringer for kindly agreeing to be members of my doctoral committee. Moreover, I would like to thank Jane Kerr and the editors at IBFD for enabling the publication of my thesis in the WU Vienna Series, Renée Pestuka for her great support during the publication process and Jenny Hill for her language editing.

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Last, but not least, special thanks, of course, go to all of the people outside the immediate working environment who supported me during the whole doctoral project. I would like to thank my parents, who have always been there for me and who were great role models to motivate me to start (and finish) writing a doctoral thesis at all, and all of my friends, who always fully assisted me, even at those times when the progress of the thesis did not seem to be as quick as I hoped for and when I might not have been the easiest companion to be with. Thank you very much for supporting me – this book is for you.

Erich Schaffer

Vienna, August 2016

Sample Chapter

# Chapter 1

# Introduction

## 1.1. Relevance of the topic

The attribution of income is one of the most fundamental issues in tax law. Indeed, the first step in any given instance of taxation is to determine who the taxable person is and what income possessed by that person can be taxed. In order to tax this income, there is a precondition that it is subjectively attributable to that specific person. Consequently, the topic of income attribution is an issue that virtually every tax jurisdiction must thoroughly address. However, there is still no uniform international standard regarding how income is to be attributed to taxpayers. Instead, the details of income attribution are regulated individually by each state. Quite often, the principles of income attribution are not explicitly stipulated in the laws of a given state but rather are developed in the literature or determined by case law. This leads to legal ambiguity for those who are subject to the laws of that state, as they cannot refer to concrete legal provisions but instead must rely on general principles of income attribution, which often tend to be rather vague.

In an international context – when two or more states are involved – this issue becomes even more challenging, since the details in respect of how to attribute income to taxpayers vary between jurisdictions. For example, it may be the case that the states involved attribute certain portions of income to different taxpayers, or it may even happen that certain "persons" are considered to be taxable individuals by only one or some, but not all, of the states involved. One of the most prominent examples of such a situation would be the case of a hybrid partnership that is treated as opaque by one contracting state and as fiscally transparent by another. In such a case, the first-mentioned state will qualify the partnership as a taxable person and attribute the income to the partnership, while the other state will not recognize the partnership as a taxable person and will allocate the income in question to its partners. This differing treatment in the domestic laws of the states involved inevitably leads to so-called allocation conflicts or attribution mismatches, which must be resolved at an international level in order to correctly apply the relevant tax treaties.

For all of these reasons, in order to ensure the proper application of tax treaties, it is a crucial preliminary necessity to determine the person to

whom the income at stake is attributable for tax purposes, because tax treaties themselves do not regulate this. Rather, it is the nature of tax treaties that they presuppose that an attribution of income has already occurred at the domestic level, and they thus merely provide for the legal consequences of that domestic attribution. In order for a tax treaty to apply, according to article 1 in combination with article 4 of the OECD Model Tax Convention on Income and on Capital (OECD MC), the taxable income must be attributable to a person who is a resident of one or both of the contracting states. If income is attributable to a person who is not a resident of either contracting state, the relevant tax treaty will not be applicable with regard to the income in question. This basic principle, according to which the applicability of a tax treaty is dependent on the domestic attribution of income, is the first important connection between domestic income attribution and tax treaty law. Yet it is not the only connection between these two different levels of legal rules. In addition to the issues concerning residency and treaty entitlement, connecting elements between domestic income attribution and tax treaty law can also be found at a later stage of treaty application, namely, at the stage of application of the various allocative rules[1] in the OECD MC. These connecting elements become particularly evident when the OECD MC uses personal attribution terms such as "derived by", "paid to" or "accrue to" in its allocative rules. Consequently, in these cases, the correct application and interpretation of the various allocative rules of the OECD MC is also closely connected to the attribution of income pursuant to the domestic laws of the contracting states.

The connection between the domestic attribution of income and the correct implementation of the various allocative rules is of particular interest with regard to the application of article 17 of the OECD MC, the relevant allocative rule for the income of entertainers and sportspersons. This provision of the OECD MC – consisting of two different paragraphs – is, by its nature, a very special treaty provision as far as its relation to the domestic attribution of income is concerned. In this regard, article 17(1) of the OECD MC stipulates that, if income is "derived by" an entertainer or a sportsperson and derived from an entertaining or sportive performance, then the source state – i.e. the state in which the performance takes place – is entitled to levy a tax on that income. In addition, article 17(2) of the OECD MC stipulates that the performance state is likewise entitled to levy a tax on such entertaining

1. In this context, the term "allocative" might be a bit misleading. The "allocation" or "attribution" of income to a taxpayer, which is an issue of domestic law, has to be distinguished from the allocation of taxing rights to the contracting states of a tax treaty, which is regulated by the allocative rules (arts. 6-8 and arts. 10-21 OECD MC) of that treaty.

or sportive income if the income is not derived directly by the entertainer or sportsperson but rather "accrues […] to another person". This raises the question of how the attribution of income according to domestic law is related to the proper application of article 17(1) and (2) of the OECD MC. Thus, for the proper application of this allocative rule, it is indispensable to analyse in detail whether and to what extent the terms "derived by", as used in article 17(1), and "accrue to", as used in article 17(2), are aligned with the principles of income attribution pursuant to the domestic laws of the states involved.

Until now, academic research on article 17 of the OECD MC has mostly focused on analysing the personal and substantive scope of this provision in order to delimit said scope from that of other allocative rules in the Model, especially article 7 and article 15. Additionally, extensive research has been conducted on policy aspects such as whether the scope of this provision should be broadened or narrowed down, or even whether it should be completely abolished. In contrast, a comprehensive analysis of the interplay between domestic income attribution and the proper application of article 17(1) and (2) of the OECD MC has not yet been carried out. Conducting such research will be the object of this book. However, no suggestions regarding how to standardize or harmonize the principles of income attribution in domestic laws will be made, since certain differences in these laws are simply an unavoidable consequence of the legislative autonomy of each state. Rather, the book will focus exclusively on an international tax law perspective, that is to say, on the proper interpretation of article 17(1) and (2) of the OECD MC after the attribution of income has already been predetermined in its various possible forms by the domestic laws of the states involved. By doing so, general principles for the correct application of this allocative rule for entertainers and sportspersons will be established in the most comprehensive manner. This approach will, on the one hand, provide consistent results in the interpretation of article 17 of the OECD MC if the two contracting states attribute the income at stake to exactly the same taxpayer according to their domestic laws. On the other hand, this approach will also allow for the development of consistent solutions in cases where the states involved attribute the income at stake to two or more different taxpayers. Consequently, based on the findings on the relation between domestic income attribution and article 17 of the OECD MC, this book will demonstrate how attribution mismatches involving entertainers or sportspersons can be solved on the basis of the current wording of the Model. In this regard, this book will thoroughly analyse not only the wording of the OECD MC but also the suggestions that the OECD has made in the course of the BEPS initiative in regard to how to change the Model to explicitly address certain forms of attribution mismatches.

## 1.2. Structure of the book

In order to set up the basic framework for the analysis of article 17 of the OECD MC, chapter 2 will briefly outline those principles concerning the interpretation of tax treaties which are most important for the analysis of the research topics. First, the principles of interpretation of international treaties according to the Vienna Convention on the Law of Treaties (VCLT) will be recalled. Second, the legal relevance of OECD documents such as the Commentary on the OECD MC and the discussion drafts published in connection with the ongoing OECD BEPS initiative will be discussed. Third, the interplay between tax treaty interpretation and domestic tax law, especially in light of article 3(2) of the OECD MC, will be examined. Finally, the general purpose of tax treaties will be discussed in order to further determine the possible implications of such a general purpose for the interpretation of a specific treaty provision.

Having laid these foundations for the analysis, chapter 3 will focus on a detailed interpretation of article 17 of the OECD MC. The scope of both paragraphs will be analysed in detail in order to determine whether certain items of income are covered by article 17(1), by article 17(2) or by other allocative rules of the OECD MC. In this regard, two examples involving entertainers and sportspersons – one bilateral scenario and one trilateral scenario – will serve as points of reference throughout the entire chapter in order to better illustrate the issues at stake. This should serve the primary purpose of the chapter, namely, to examine the extent to which the domestic attribution of income is aligned with the application of article 17 of the OECD MC.

In order to establish general principles on that issue, first, the historical background as well as the personal and substantive scope of article 17 of the OECD MC will be briefly discussed. Subsequently, the focus will turn to the exact meaning of the terms “derived by”, as used in article 17(1), and “accrues to”, as used in article 17(2). In this context, particular focus will be placed on the possibilities for applying a so-called proper look-through approach, according to which income qualifies as being directly “derived by” an entertainer or sportsperson even though another person is interposed between the payer of the income and that entertainer or sportsperson. In addition, the so-called improper look-through approach inherent in article 17(2) of the OECD MC will be subjected to analysis. Such an improper look-through approach is inherent in this provision because, by definition, the paragraph only applies if income in respect of personal activities exercised by an entertainer or sportsperson “accrues to” a person other than the

entertainer or sportsperson in question. Thus, in order to identify the items of income that can be covered by article 17(1) or article 17(2) of the OECD MC, those payments that are formally made from the payer of income to an interposed person and those payments that are formally made from the interposed person to an entertainer or sportsperson will be analysed separately, after which the focus will turn to the "parallel application" of article 17(1) and article 17(2). In this regard, it will be examined whether article 17(1) and article 17(2) of the OECD MC are mutually exclusive and must be strictly applied as alternatives or whether it is also possible that, with regard to certain items of income, both of these paragraphs can be applied in a cumulative manner. In the course of the analysis of this issue, it will be demonstrated why the additions made to the Commentary on the OECD MC in 2014 require closer examination and should not be applied too hastily in practice. Finally, at the end of the chapter, it will be shown how all of the principles established in respect of the interpretation of both article 17(1) and article 17(2) of the OECD MC can be applied to the two examples presented at the beginning of the chapter.

After having developed the most relevant interpretative standards for article 17(1) and article 17(2) of the OECD MC in light of the connection of this allocative rule to the domestic attribution of income in chapter 3, chapter 4 will analyse how these standards apply in those cases where the domestic laws of the states involved attribute the income at stake to different taxpayers. In short, the focus will be placed on the solution of the so-called attribution mismatches or allocation conflicts involving international entertainers and sportspersons. From a practical perspective, such attribution mismatches are undesirable, because they inevitably give rise to unresolved double taxation or double non-taxation. From a conceptual perspective, however, there is no common understanding of how to deal with such mismatches. Nonetheless, with regard to the tax treatment of international entertainers and sportspersons, there is plenty of opportunity for income attribution conflicts. Such conflicts may arise, inter alia, if a person – such as a team, troupe or orchestra, a nominee or agent, or a rent-a-star company – is interposed between the payer of income and the entertainer or sportsperson when the states involved have a different understanding of the tax status of the interposed person. Still, in spite of the importance of the domestic attribution of income for the proper application of article 17(1) and article 17(2) of the OECD MC, comparatively little research has been conducted on the implementation of this allocative rule in the case of attribution mismatches. Thus, chapter 4 will proceed to examine that issue in more detail.

For these purposes, the Partnership Report published by the OECD in 1999 will be given particular consideration. In this report, the OECD addressed the most typical scenarios involving attribution mismatches in a more comprehensive way and also attempted, for the first time, to develop practical solutions to these issues. However, the results of the Partnership Report, as well as its underlying conceptual premises, have been repeatedly criticized in the literature. These concerns about the findings of the report are also reflected in state practice, since many states do not follow its principles when dealing with allocation conflicts. For that reason, the most important alternative approaches to the solution of these conflicts, as well as the underlying methodical premises of these alternative approaches, will be discussed in more detail, not only in a theoretical manner but also as applied to several case studies involving entertainers and sportspersons. As a result, it will finally be established how allocation conflicts involving the application of article 17 of the OECD MC can be solved in a comprehensive and consistent manner.

Finally, in chapter 5, the scope of the new article 1(2) of the OECD MC, as proposed by the OECD in the course of the ongoing BEPS initiative, will be analysed in more detail. In this regard, reference will first be made to article 1(6) of the US Model Income Tax Convention (US MC). This is because said prospective provision of the OECD MC is clearly modelled after the provision on hybrid entities in the US MC, and the two provisions share very similar wording. For that reason, when interpreting the scope of article 1(2) of the OECD MC, the Technical Explanations to the US MC, as well as the literature and case law regarding the corresponding tax treaty provisions that are patterned after article 1(6) of the US MC, must be taken into account. Conversely, this also means that the few deviations in article 1(2) of the OECD MC from article 1(6) of the US MC – and in particular the possible explanations for these deviations – require closer examination. This will also be relevant for the assessment of the individual preconditions for the application of article 1(2) of the OECD MC. In this regard, the essential terms used in article 1(2) of the OECD MC, such as “entity or arrangement”, “wholly or partly fiscally transparent” and “income derived by or through”, will be analysed against the background of the similar provision in the US MC, as well as the corresponding provisions that have already been included in certain tax treaties. The analysis of these essential terms will also play an important role in the determination of the relevance and scope of the application of article 1(2) of the OECD MC in the case of allocation conflicts.

At the end of chapter 5, it will be shown how all of the findings on the individual preconditions for the application of the proposed article 1(2)

of the OECD MC, as well as on its legal relevance in the case of allocation conflicts, can be applied to cases of attribution mismatches involving international entertainers and sportspersons. In this regard, an analysis will be conducted of how the case studies discussed in detail in chapter 4 would have to be resolved if a provision equivalent to the prospective article 1(2) of the OECD MC were already included in the tax treaties between the states involved. Furthermore, special attention will be paid to those issues related to entertainers and sportspersons that states must bear in mind if they decide to implement the new article 1(2) of the OECD MC in their treaty networks. This analysis serves the purpose of developing and maintaining consistent and universally accepted standards for the interpretation of the provisions concerning entertainers and sportspersons in international tax law.

# Chapter 2

# Interpretation of Tax Treaties

## 2.1. Vienna Convention on the Law of Treaties

The interpretation of tax treaties follows the principles of interpretation enshrined in international law. The principles for this interpretation are codified in the Vienna Convention on the Law of Treaties[2] (VCLT) and can be seen as customary international law.[3] Article 31(1) of the VCLT stipulates as a basic rule that a treaty has to be interpreted in good faith and pursuant to the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose.[4] However, according to the literature, the interpretation in good faith cannot be seen as a special interpretation method; it only clarifies that the common interpretation methods for domestic law – namely, the grammatical, systematic, teleological and historical interpretation methods – should be applied in good faith in a tax treaty context.[5] An interpretation in good faith requires, for example, that all necessary means of interpretation are taken into account and all the legitimate interests of the contracting parties are considered.[6] According to article 31(2) of the VCLT, the context of a treaty comprises – in addition to the text, including its preamble and annexes – any agreement relating to the treaty that was made between all of the parties in connection with the conclusion of the treaty[7] and any instrument that was made by one or more

2. This multilateral convention was concluded in Vienna on 23 May 1969 and registered ex officio on 27 Jan. 1980. Its authentic texts are English, French, Chinese, Russian and Spanish; *see also*, for example, K. Dziurdz, *Kurzfristige Arbeitnehmerüberlassung im Steuerrecht* (Linde 2013) p. 21.

3. *See* K. Gardiner, *Treaty Interpretation* (Oxford 2008) pp. 12 ff.; O. Dörr/K. Schmalenbach, *Vienna Convention on the Law of Treaties* (Springer 2012) art. 31 paras. 6 f.; and C. Gloria, *Das steuerliche Verständigungsverfahren und das Recht auf diplomatischen Schutz: Zugleich ein Beitrag zur Lehre von der Auslegung der Doppelbesteuerungsabkommen* (Duncker & Humblot 1988) pp. 67 ff.

4. Art. 31(1) VCLT.

5. *See* M. Lang, *Introduction to the Law of Double Taxation Conventions* (2nd ed., IBFD/Linde 2013) para. 64; Dziurdz, *supra* n. 2, at p. 23; and H.F. Köck, *Vertragsinterpretation und Vertragsrechtskonvention: Zur Bedeutung der Artikel 31 und 32 der Wiener Vertragsrechtskonvention* (Duncker & Humblot 1976) p. 80.

6. *See* Gardiner, *supra* n. 3, at p. 148; Dziurdz, *supra* n. 2, at p. 23; and M.E. Villiger, *Commentary on the 1969 Vienna Convention on the Law of Treaties* (Brill 2009) art. 31 paras. 7 f.

7. Art. 31(2)(a) VCLT.

parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.[8]

The scope of article 31(2) of the VCLT has to be distinguished from the references in article 31(3) to any subsequent agreement between the parties,[9] any subsequent practice,[10] or any relevant rules of international law applicable in the relations between the parties.[11] In principle, both types of agreements – agreements pursuant to article 31(2) and those pursuant to article 31(3) – are considered to have the same legal value for interpretation. An agreement does not automatically have minor importance if it is not made at the time of the conclusion of a treaty but only at a later stage.[12] However, this does not mean that the two contracting parties have the authority to subsequently change the content of an already concluded treaty. If the tax authorities want to change the content of a treaty, such as a tax treaty, the treaty as such has to be renegotiated. In contrast, procedures such as a mutual agreement procedure between the two relevant tax authorities cannot completely modify the provisions of a treaty if their outcome is contrary to the treaty that was formerly concluded. Even though the mutual agreement can be seen as "subsequent agreement" in the sense of article 31(3)(a) and may serve as one means of interpretation,[13] if all the other means of interpretation lead to a different result, it is very likely that the subsequent mutual agreement procedure needs to be disregarded for the proper interpretation of the treaty.[14] The same standards have to be applied concerning "subsequent practice" of the tax authorities in the sense of article 31(3)(b), which cannot change the meaning of an already existing treaty[15] but can

8. Art. 31(2)(b) VCLT.
9. Art. 31(3)(a) VCLT.
10. Art. 31(3)(b) VCLT.
11. Art. 31(3)(c) VCLT.
12. *See* Dziurdz, *supra* n. 2, at p. 24 f.; Gardiner, *supra* n. 3, at p. 204; and, to the contrary, A. Rest, *Interpretation von Rechtsbegriffen in internationalen Verträgen* (Köln 1971) p. 148.
13. *See* Gloria, *supra* n. 3, at p. 77; and Dziurdz, *supra* n. 2, at pp. 26 f.
14. *See* in this respect, for example, DE: BFH, 10 Dec. 2001, I B 94/01; in this case, the BFH came to the conclusion that a mutual agreement between the competent authorities of Germany and France could not change the provisions of domestic law after the incorporation of the Germany-France DTC into domestic law. Thus, the taxpayer could not rely on the mutual agreement procedure between Germany and France.
15. *See*, for example, DE: BFH, 25 Oct. 2006, I R 81/04; in this case, the authorities of Germany considered the activity of an authorized signatory as being exercised where the company employing the signatory is resident. Here, the BFH found that – although the wording of the Germany-France DTC could also be interpreted in a different way – the fact that the view of Germany had not been changed in subsequent conventions or protocols and had even been confirmed by existing case law constituted subsequent

only give some guidance on its interpretation.[16] As a result, article 31(3) of the VCLT does not provide for a special interpretation rule in a treaty context, but any later agreements or practices have to be used for interpretation in the same way for treaty purposes and for purposes of domestic law.[17]

In addition to the aforementioned rules, article 31(4) stipulates that a special meaning is to be given to a term "if it is established that the parties so intended".[18] Again, this provision does not constitute a special means of interpretation in a treaty context. Rather, it has to be derived from all of the other means of interpretation according to article 31 whether there is any leeway for a term to have a "special meaning" according to the intention of the parties. For example, a "special meaning" of a term could be deduced from another provision of the treaty in which the term is used, which, in the end, would be nothing else but a systematic interpretation in light of the context of the treaty.[19] The main reason why article 31(4) was nevertheless included in the VCLT was to emphasize that the burden of proof lies on the party invoking the special meaning of the term and the strictness of the proof required.[20]

Finally, article 32 of the VCLT stipulates that supplementary means of interpretation may also be taken into account when the interpretation according to article 31 either leaves the meaning ambiguous or obscure[21] or leads to a result that is manifestly absurd or unreasonable.[22] As examples of such supplementary means, article 32 mentions the preparatory work (*travaux préparatoires*) of the treaty and the circumstances of its conclusion. Preparatory work in the sense of article 32 means all documents relevant to a forthcoming treaty and generated by the parties during the treaty preparation and up to its conclusion.[23] That comprises, for example, memoranda,

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practice in the sense of art. 31(3)(b) VCLT, which has a strong relevance for the interpretation of the relevant treaty provision.

16. *See*, in this context, for example, I. Sinclair, *The Vienna Convention on the Law of Treaties*[2] (Oxford 1984) p. 138, who states as follows: "It will be apparent that subsequent practice of the parties may operate as a tacit or implicit modification of the terms of the treaty. It is inevitably difficult, if not impossible, to fix the dividing line between interpretation properly so called and modification effected under the pretext of interpretation".
17. *See* Lang, *supra* n. 5, at para. 65.
18. Art. 31(4) VCLT.
19. *See* Dziurdz, *supra* n. 2, at pp. 28 f.
20. *See* Gardiner, *supra* n. 3, at p. 292, with reference to UN, *Yearbook of the International Law Commission 1964* (UN 1964) p. 205.
21. Art. 32(a) VCLT.
22. Art. 32(b) VCLT.
23. *See* Villiger, *supra* n. 6, at para. 3.

protocols, drafts of the treaty and other documents that have been drafted in the context of the negotiation and those of which the contracting parties have been made aware.[24] Regarding the circumstances of the conclusion of a treaty, it may be necessary to take into account the historical background against which the treaty was concluded. The individual attitudes of the parties such as, for example, their economic, political and social circumstances, their adherence to certain groups, or the status of the countries involved – e.g. whether they are import or export countries – may be of relevance for that purpose.[25] However, it has to be noted that article 32 of the VCLT is not a separate interpretation rule that may be applied completely independently of the general rule of interpretation as stipulated in article 31.[26] For the purposes of interpreting a treaty, all means of interpretation – the general rules according to article 31 as well as the supplementary means according to article 32 – are to be taken into account and to be weighed against each other in order to find an equitable interpretation for each underlying case. In short, the VCLT provides for some general guidelines on how to interpret treaties. These guidelines are very flexible and might keep the interpretation process open until a comprehensive result is reached for the present case.[27]

## 2.2. Legal relevance of the OECD Model Convention and the OECD Commentary

In cases where the interpretation of a tax treaty is unclear, the Commentary of the OECD Committee on Fiscal Affairs[28] is of particular importance. This stems from the fact that, very often, tax treaties are based on the OECD MC or on other treaty models that are, to a great extent, equivalent to the OECD MC. In this context, there is a common understanding in the

24. *See* Dörr, *supra* n. 3, at paras. 11 ff.; and Dziurdz, *supra* n. 2, at p. 30.
25. *See* Sinclair, *supra* n. 16, at p. 141, with reference to Crawford, *The Concept of Statehood in International Law* (1979) p. 82.
26. In fact, it is also very difficult to find a clear dividing line between the general provisions of art. 31 and the supplementary means of art. 32 VCLT. For example, "subsequent practice", which might not be covered by the relatively narrow scope of art. 31(2)(b) VCLT, can still be covered by art. 32 VCLT as "supplementary means"; *see*, with further references, Sinclair, *supra* n. 16, at p. 138.
27. *See* Dziurdz, *supra* n. 2, at p. 33; Gardiner, *supra* n. 3, at p. 292; and T. Bernardez, *Interpretation of Treaties by the International Court of Justice following the Adoption of the 1969 Vienna Convention on the Law of Treaties*, in *Liber Amicorum Professor Seidl-Hohenveldern in honour of his 80th birthday* (G. Hafner et al. eds., Kluwer 1998) p. 721 (726).
28. Hereinafter referred to as OECD Commentary.

literature that states that include provisions without any deviations from the OECD MC in their tax treaties also follow the understanding that is shared in the OECD Commentary, unless otherwise specified.[29] Consequently, the OECD MC and the Commentary are important means of interpretation in the sense of the VCLT. In this regard, the OECD MC and the OECD Commentary may either shed light on the "ordinary meaning" of a term in the sense of article 31(1) of the VCLT,[30] on the "special meaning" in the sense of article 31(4),[31] or they can also be seen as "supplementary means" in the sense of article 32.[32] However, as explained before, this distinction between the means of interpretation in articles 31 and article 32 of the VCLT is only of minor importance,[33] as the VCLT does not stipulate a specific order of priority for these means of interpretation and all systematic, teleological and historical aspects have to be taken into account and weighted according to the specific facts of the case.[34] Still, in any case, it is evident that the OECD MC and the OECD Commentary do not have as much weight as the text of the relevant treaty itself, because they are not part of the agreement. Similarly to other means of interpretation, they can only give some guidance on how to interpret a treaty provision.[35] If, however, the wording of the tax treaty deviates significantly from the OECD MC, the OECD Commentary can only play a very limited role for the interpretation of the treaty, because, obviously, the two contracting parties intended not to follow the understanding of the OECD.[36]

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29. *See*, with further references, F. Wassermeyer in F. Wassermeyer, *Doppelbesteuerungsabkommen* (129th ed., Beck 2015) vor Art. I para. 51; H. Schaumburg, *Internationales Steuerrecht* (3rd ed., Beck 2011) para. 16.77; M. Lehner in K. Vogel/M. Lehner, *DBA* (6th ed., Beck 2015), Grundlagen, para. 130; M. Lang/F. Brugger, *The Role of the OECD Commentary in Tax Treaty Interpretation*, ATF (2008) p. 102; and M.A. Lampert, *Germany*, in *The Impact of the OECD and UN Model Conventions on Bilateral Tax Treaties* (M. Lang et al. eds., Linde 2012) p. 469.

30. *See*, with further references, Dziurdz, *supra* n. 2, at p. 34.

31. *See*, for example, Lang, *supra* n. 5, at para. 83; and Dziurdz, *supra* n. 2, at pp. 35 f.

32. *See* in more detail Lehner, *supra* n. 29, at paras. 125 ff.; Wassermeyer, *supra* n. 29, at vor Art. I paras. 37 f.; M. Lang, *Die Bedeutung des Musterabkommens und des Kommentars des OECD-Steuerausschusses für die Auslegung von Doppelbesteuerungsabkommen*, in *Aktuelle Entwicklungen im Internationalen Steuerrecht* (W. Gassner et al. eds., Linde 1994) p. 16; Lang/Brugger, *supra* n. 29, at p. 102; Gloria, *supra* n. 3, at p. 91; and Dziurdz, *supra* n. 2, at p. 37.

33. *See*, in more detail, D.A. Ward, *The Interpretation of Income Tax Treaties with Particular Reference to the Commentaries on the OECD Model* (IBFD 2005) pp. 4f., Online Books IBFD; and Dziurdz, *supra* n. 2, at pp. 34 ff.

34. *See* in more detail Lehner, *supra* n. 29, at paras. 126 ff.; *see also* sec. 2.1.

35. *See* Lang, *supra* n. 5, at para. 84.

36. *See* Lehner, *supra* n. 29, at para. 133; and Lang, *supra* n. 5, at para. 86, with reference to DE: BFH, 13 Aug. 1997, I R 65/95.

Another issue that has been subject to ongoing debate in the literature is the question of which version of the OECD Commentary has to be applied to interpret a tax treaty. On the one hand, according to the static approach, only that version of the OECD Commentary can be applied which was already in place at the time of the conclusion of the treaty.[37] On the other hand, according to the dynamic approach, later versions of the OECD Commentary should also be taken into account for treaty interpretation.[38] The OECD itself is in favour of a dynamic approach and claims that existing conventions should, as much as possible, be interpreted in the spirit of the revised Commentaries.[39] If there are no changes in substance, later changes to the Commentary should be applicable to the prior treaties, because they reflect the consensus of the OECD member countries.[40] Many amendments to the Commentary are intended to simply clarify but not change the meaning of the OECD MC or the OECD Commentary. Thus, these clarifications should also be taken into account for treaty interpretation.[41] Another line of argumentation in favour of the dynamic approach is that the Commentary should not have a fixed meaning but rather should be flexible and adapt to changes in the legal environment, such as changing technologies or business models. If some states did not adapt to these changes and decided not to follow the common understanding as shared in the new version of the OECD Commentary, this would go against the principle of uniform interpretation of tax treaties.[42]

In contrast, according to the prevailing opinion in the literature, later versions of the OECD Commentary cannot be applied to treaty interpretation as they have not been taken into account by the parliaments that approved the tax treaties.[43] They cannot be considered "context" in the sense of ar-

37. *See*, with further references to the literature and case law applying a static approach, as well as on the possible implications of such an approach, Lehner, *supra* n. 29, at para. 127; *see also infra* n. 43.
38. *See*, with further reference to the literature and case law applying a dynamic approach, as well as on the possible implications of such an approach, Lehner, *supra* n. 29, at para. 127a; and Wassermeyer, *supra* n. 29, at paras. 60 ff.; *see also infra* nn. 39-42.
39. Introduction to the OECD Model Tax Convention 2014, para. 33.
40. Id., at para. 35.
41. Id., at para. 36.
42. *See* J.F. Avery Jones, *The Effect of Changes on the OECD Commentaries after a Treaty is Concluded*, 56 Bulletin for International Taxation 3 (2002) pp. 103 f., Journals IBFD; and P. Baker in P. Baker, *Double Taxation Conventions* (3rd ed., Sweet and Maxwell 2014), Introduction, E.15.
43. *See*, for example, H.J. Ault, *The role of the OECD Commentaries in the interpretation of tax treaties*, in *Essays on International Taxation* (H. Aupert/K. van Raad eds., IBFD 1995) p. 63, Online Books IBFD; K. Vogel, *The Influence of the OECD Commentaries on Treaty Interpretation*, 54 Bulletin for International Taxation

ticle 31(1) of the VCLT, because they are not implemented in connection with the conclusion of the treaty.[44] Furthermore, they cannot be perceived as "subsequent agreement" in the sense of article 31(1)(a), as such an agreement would require parliamentary approval.[45] Nor can they be seen as "subsequent practice" pursuant to article 31(1)(b), because this would require them to reflect actual common practice by both contracting states.[46] Finally, subsequent changes to the OECD Commentary cannot be regarded as reflecting a "special meaning" in the sense of article 31(4), because the two contracting states would have needed to already have such a special meaning in mind at the time of the conclusion of the treaty.[47] Summing up, as later versions of the Commentary cannot be used for the interpretation of a tax treaty according to the rules of the VCLT, adopting later versions would interfere with the competence of domestic legislative bodies.[48] Consequently, a static approach has to be applied, meaning that only the OECD

12, p. 612 (2000), Journals IBFD; K. Vogel, *Probleme der Auslegung von Doppelbesteuerungsabkommen*, SWI (2000) p. 109; P. Wattel/O. Marres, *The Legal Status of the OECD Commentary and Static or Ambulatory Interpretation of Tax Treaties*, 43 European Taxation 7 (2003) p. 222, Journals IBFD; M. Lang, *Haben die Änderungen der OECD-Kommentare für die Auslegung älterer DBA Bedeutung?,* SWI (1995) pp. 413 ff.; M. Lang, *Keine Bedeutung der jüngeren Fassung des Kommentars des OECD-Steuerausschusses für die Interpretation älterer Doppelbesteuerungsabkommen*, IWB (1996) pp. 923 ff.; Lang/Brugger, *supra* n. 29, at p. 107; Lang, *supra* n. 5, at para. 95; M. Lang, *The Application of the OECD Model Tax Convention to Partnerships* (Lexisnexis 2000) pp. 15 ff.; M. Lang, *Later Commentaries of the OECD Committee on Fiscal Affairs, Not to Affect the Interpretation of Previously Concluded Tax Treaties*, Intertax (1997) pp. 7 ff.; Dziurdz, *supra* n. 2, at pp. 37 f.; R. Prokisch, *Fragen der Auslegung von Doppelbesteuerungsabkommen*, SWI (1994) p. 53; C. Seitz, *DBA-Aspekte – ein Überblick anhand von Fallbeispielen*, in *Personengesellschaften im internationalen Steuerrecht* (F. Wassermeyer et al., eds., Otto Schmidt 2010) p. 178; D.A. Ward, *Is There an Obligation in International Law of OECD Member Countries to Follow the Commentaries on the Model?*, in *The Legal Status of the OECD Commentaries* (S. Douma/F. Engelen eds., IBFD 2008) p. 86, Online Books IBFD; Wassermeyer, *supra* n. 29, at vor Art. I paras. 60 ff.; and Lehner, *supra* n. 29, at paras. 127 ff.

44. *See*, with further references, Lehner, *supra* n. 29, at para. 127c; Wassermeyer, *supra* n. 29, at vor Art. I para. 60; H. J. Ault, *The role of the OECD commentaries in the interpretation of tax treaties*, Intertax (1994) pp. 147 f.; A. Hemmelrath/T. Keppert, *Die Bedeutung des "Authorized OECD Approach" (AOA) für die deutsche Abkommenspraxis*, IStR (2013) pp. 39 f.; and X. Oberson, *Précis de droit fiscal international* (4th ed., Berne 2014) p. 23.

45. *See*, for example, Wassermeyer, *supra* n. 29, at vor Art. I para. 63; Oberson, *supra* n. 44, at pp. 23 ff.; and Lang, *supra* n. 5, at para. 95.

46. *See*, for example, Schaumburg, *supra* n. 29, at paras. 16.76 f.; Wassermeyer, *supra* n. 29, at vor Art. I para. 63; and Lang, *supra* n. 5, at para. 95.

47. *See*, for example, Lang, *supra* n. 5, at para. 95.

48. *See* Wattel/Marres, *supra* n. 43, at p. 222; Lang, *supra* n. 5, at para. 97; and G. Michelsen, *Tax Treaty Interpretation in Denmark*, in *Tax Treaty Interpretation* (M. Lang ed., Linde 2001) p. 72; *see*, in more detail on the constitutional issue of such an interference with the domestic legislative bodies, Lehner, *supra* n. 29, at para. 128.

Commentary existing at the time of the conclusion of the treaty should be taken into account for interpretation.[49,50]

For the further analysis of the underlying topic of this book, whenever reference is made to certain changes to the OECD Commentary, one has to bear in mind that these changes do not influence already existing tax treaties but only those treaties that have been concluded after the changes to the Commentary have been made. In addition, even for tax treaties concluded subsequently to the changes, the Commentary serves only as guidance for interpretation. A systematic and teleological interpretation of the actual provision of the tax treaty may still lead to the conclusion that the changes in the Commentary should not be applied. This is especially relevant for all of the changes that were introduced into the OECD Commentary in 2001 when implementing the findings of the OECD Partnership Report,[51] which will be discussed later on in more detail in chapter 4.[52]

## 2.3. Legal relevance of OECD reports

As mentioned before, when a treaty is negotiated on the basis of the OECD MC, it is commonly accepted that the contracting states implicitly follow the understanding shared in the OECD Commentary.[53] This principle does not apply in the same manner concerning the views which are shared in OECD reports. It is not as obvious as with the OECD Commentary – where, at the time of the conclusion of the treaty, one comprehensive version exists – that the treaty's negotiating parties were also aware of the findings of every OECD report that may have been concluded in the past.[54] However, many paragraphs of the OECD Commentary are based on the findings of

49. *See supra* n. 43.
50. However, this does not mean that later versions of the OECD Commentary are completely irrelevant for interpretation. According to Lang, "the members of the working parties and the OECD Committee on Fiscal Affairs are [undoubtedly] highly qualified experts. More recent versions of the Commentary are therefore of importance as expert opinions. They have the same relevance as papers and other scientific publications; they can influence the understanding of provisions in practice, if the arguments are convincing. Frequently, however, the Commentary only presents the result of a certain interpretation without reference to the main arguments that led to this result. Consequently, they often lack the persuasiveness necessary for influencing practice". *See* Lang, *supra* n. 5, at para. 102.
51. OECD, *The Application of the OECD Model Tax Convention to Partnerships* (1999) (hereinafter referred to as the Partnership Report).
52. *See* ch. 4.
53. *See supra* n. 29.
54. *See* similarly Lang, *supra* n. 5, at para. 108.

**Notes**

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