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The Interaction between Directives and Tax Treaties: Three Case Studies

This article applies the findings of the author's doctoral thesis, *The Effect of Directives in the Area of Direct Taxation on the Interpretation and Application of Tax Treaties*, which was awarded the International Fiscal Association's 2024 Mitchell B. Carroll Prize, to three case studies of conflicts between directives and tax treaties.

1. Introduction

The relationship between tax treaties and directives can be described as a difficult marriage[1] or complex.[2] The complexity of this relationship may be due to the fact it relates to three different sources of law and their interaction: (i) tax treaties; (ii) directives; and (iii) national law. Considering there are three sources of law involved, the relationship can be studied from three different perspectives. First, it may be studied from the perspective of public international law under which tax treaties are governed. Second, it may be studied from the perspective of the laws of the European Union because directives are legal acts of the European Union and, hence, governed by EU law. Third, the relationship may be studied from the perspective of the laws of the Member States given that such Member States are required, as a matter of EU law, to implement directives by means of national law.

The purpose of this article is to assess, on the basis of the framework set out in the author's thesis, *The Effect of Directives in the Area of Direct Taxation on the Interpretation and Application of Tax Treaties* (Kluwer), which was awarded the 2024 Mitchell B. Carroll prize by the International Fiscal Association at its Annual Congress in Cape Town,[3] how directives may affect the interpretation and application of tax treaties and interact with them from the three perspectives in isolation, while also addressing their interaction. The outcome of such an assessment would then contribute to a more in-depth understanding of the complex relationship between tax treaties and directives.

The structure of the article is as follows. First, examples of conflicts between directives and tax treaties are presented (*see* section 2.). Such examples serve as a basis for illustrating the interaction between directives and treaties. Second, the effect of directives on the interpretation of treaties is considered, taking into account the EU law duty of consistent interpretation and the legal framework governing the interpretation of tax treaties (*see* section 3.). This is followed by an assessment of the effect of directives on the application, in terms of applicability, of treaties, from the same three perspectives and their interaction (*see* section 4.). After this assessment, a conclusion is drawn as to the extent to which directives may affect treaties (*see* section 5.). The article concludes with recommendations aimed to decrease the complexity of the relationship between directives and treaties (*see* section 6.).

2. Conflicts between Directives and Tax Treaties

2.1. Introductory remarks

The question as to whether directives may conflict with treaties has become more relevant following the introduction of the obligation to tax income in directives in 2014.[4] This is because tax treaties restrict the extent to which income may be taxed. Hence, if a directive requires taxation of income that may not be taxed under a tax treaty, there would be a conflict. With respect to such a conflict, which is generally not addressed in the directive or tax treaty itself,[5] the question arises as to which obliga-

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1. C. Docclo, *EU-richtlijnen inzake BEPS en belastingverdragen: een moeilijk huwelijk*, Fiscoloog Internationaal 404 (2017).
2. *See* V. Bendlinger, *The OECD's Global Minimum Tax and Its Implementation in the EU: A Legal Analysis of Pillar Two in the Light of Tax Treaty and EU Law*, p. 344 (Kluwer Law International 2023). *See also* L. Hinnekens, *Compatibility of Bilateral Tax Treaties with European Community Law. The Rules*, 3 EC Tax Review 4, p. 147 (1994).
3. This article has been prepared in connection with the submission of the present author's thesis for the Mitchell B. Carroll prize 2024. The author would like to thank Professor Johann Hattingh for his comments in respect of an earlier version of this article that was submitted for the Mitchell B. Carroll prize 2024. The content of this article is the sole responsibility of the present author.
4. For a recent overview of the relevant literature on this topic, *see* footnote 4 in T.M. Vergouwen, *Conflicts between Directives and Tax Treaties: which obligation takes precedence? Three perspectives*, 33 EC Tax Review 4 (2024).
5. In this respect, it is noted that article 9(5) of the ATAD 2 would be the only provision in a directive containing an obligation to tax income that addresses a conflict between the directive and a tax treaty. Pursuant to this provision, Member States are not obliged to tax profits attributable to a disregarded permanent establishment situated in a third state that must be exempt under a tax treaty with such a third state. The other directives, as well as provisions of the ATAD 2, that impose an obligation to tax income do not address the interaction or relationship with tax treaties. Similarly, tax treaties concluded by the Member States also do not, as a rule, contain provisions regarding their interaction with the obligations of the Member States under the laws of the European Union. Notable exceptions in that regard are recent Hungarian tax treaties, as well as article 1(4) of the Protocol to the tax treaty between the Netherlands and Belgium (2023) regarding the Pillar Two Directive (*see*, in that respect, T.M. Vergouwen, *The subordination clause in the new tax treaty between the Netherlands and Belgium that grants primacy to the Pillar 2 Directive*, Kluwer International Tax Blog, available at

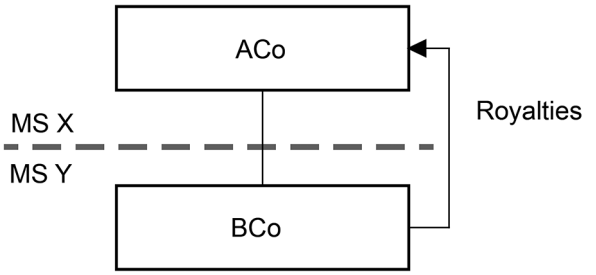
tion takes precedence: the directive-based obligation to tax income or the tax treaty-based obligation not to tax income.

The purpose of this section is to illustrate to what extent conflicts may arise between a directive and a tax treaty. In illustrating this, a distinction is drawn between conflicts between *beneficial* directives, i.e. directives that seek to grant rights to taxpayers (such as the right to an exemption of income), and *detrimental* directives, i.e. directives adopted as of 2014 that require taxation of income. The rationale for drawing this distinction is based on case law of the Court of Justice of the European Union (CJEU) pursuant to which the primacy of beneficial directives is enforceable, whereas the primacy of detrimental directives is not (due to the prohibition of reverse vertical direct effect; *see* section 4.).

2.2. Conflict I: Beneficial directives and treaties

With respect to beneficial directives, i.e. the Parent-Subsidiary Directive (PSD) (before its amendment in 2014),[6] the Merger Directive,[7] and the Interest and Royalties Directive (IRD),[8] and tax treaties between Member States (intra-EU treaties), there does not seem to be any room for conflict.[9] This is because these directives and intra-EU treaties provide for similar obligations, i.e. they limit the extent to which Member States are allowed to tax cross-border income. Consequently, both obligations can be complied with simultaneously. This can be illustrated as follows.

Figure 1. Conflict I



ACo, resident in Member State X, holds all the shares of BCo, resident in Member State Y. BCo makes a royalty payment to ACo, of which ACo is the beneficial owner for the purposes of the IRD and the applicable treaty, which is based on the OECD Model (2017).[10]

In this example, the royalty payment is covered by article 1(1) of the IRD and article 12(1) of the intra-EU treaty. Under both provisions, Member State Y (MS Y) is required to exempt the royalty payment from withholding tax: article 1(1) of the IRD requires MS Y to exempt the payment "from any taxes imposed" while article 12(1) of the intra-EU treaty grants an exclusive taxing right to Member State X (MS X), which means that MS Y must refrain from taxing the royalty payment. Given that the IRD and the intra-EU treaty impose identical obligations, there would seem to be no room for conflict as compliance with one obligation implies compliance with the other.

It is recognized that, in practice, contracting states may agree to allow the source state, i.e. MS Y, to tax royalty payments up to a certain percentage of the gross amount. If such source taxation were agreed to, there would still seem to be no room for conflict. This is because treaties can only restrict the extent to which MS Y can tax income; they cannot impose an obligation to tax the royalty payments.[11] Consequently, if source taxation were allowed, there would be no conflict because compliance with the IRD, i.e. exemption at source, implies compliance with the treaty because the taxes levied, i.e. none, do not exceed the limit imposed by the treaty.[12]

While there appears to be no room for conflict between beneficial directives and intra-EU treaties, it should be borne in mind that the general anti-abuse principle of EU law, i.e. the principle that EU law cannot be relied on for abusive or fraudulent ends (the "anti-abuse principle"),[13] obliges Member States to refuse the benefit of a beneficial directive, such as the exemption of article 1(1) of the IRD, where there is a fraudulent or abusive practice.[14] If there would be an abusive practice in the foregoing example, MS Y would be obliged, based on the anti-abuse principle, to deny the exemption of the royalty payment. Refusal of the exemption would then conflict with MS Y's obligations under article 12 of the intra-EU treaty.[15] It follows that, although there does not appear to be a direct conflict between beneficial directives and intra-EU treaties, there may be an indirect conflict if, in the case of an abusive practice, the benefit of such directives must be denied on the basis of the anti-abuse principle. This would then be a conflict not between the directive and the intra-EU treaty,

https://kluwertaxblog.com/2023/07/13/the-subordination-clause-in-the-new-tax-treaty-between-the-netherlands-and-belgium-that-grants-primacy-to-the-pillar-2-directive/ (accessed 22 Aug. 2024).

6. Council Directive 2011/96/EU of 30 November 2011.
7. Council Directive 2009/133/EC of 19 October 2009.
8. Council Directive 2003/49/EC of 3 June 2003.
9. With respect to tax treaties with third states, there would also be no room for conflict because the territorial scope of the beneficial directives is limited to cross-border transaction within the European Union by companies that are resident in the European Union, including permanent establishments situated in the European Union.
10. *OECD Model Tax Convention on Income and on Capital* (21 Nov. 2017), Treaties & Models IBFD.
11. K. van Raad, *Five fundamental rules in applying tax treaties*, in *Liber Amoricum Luc Hinnekens*, pp. 587-590 (Bruylant 2002).
12. *See* T.M. Vergouwen, *The Effect of Directives in the Area of Direct Taxation on the Interpretation and Application of Tax Treaties*, Series on International Taxation No. 84, pp. 104-105 (Kluwer Law International 2023).
13. DK: ECJ, 26 Feb. 2019, Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16, *N Luxembourg 1 v. Skatteministeriet*, para. 122, Case Law IBFD.
14. Id.
15. It is acknowledged that a conflict would only arise if BCo were to qualify as the beneficial owner of the royalty payments under the intra-EU treaty and would be entitled to the benefits of such treaty under the principal purpose test. It is furthermore acknowledged that is has not been assessed whether directives may result in an interpretation that would avoid such a conflict from arising (which effect is discussed in section 3. of this article).

but between the anti-abuse principle, which constitutes primary EU law,[16] and the intra-EU treaty.

2.3. Detrimental directives and treaties

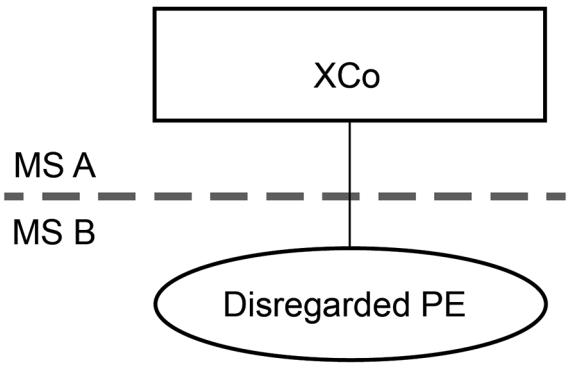
Initially, the directives in the area of direct taxation were focused on being beneficial to taxpayers by imposing an obligation not to tax income. Since the amendment of the PSD in 2014, directives can, however, be aimed at being detrimental to taxpayers by imposing an obligation to tax their income, which is also covered by intra-EU treaties. Such an obligation to tax income can, following the adoption of the controlled foreign company rules in the ATAD 1 in 2016, also extend to income covered by treaties between a Member State and a third state (an "extra-EU treaty").[17,18] If a directive imposes an obligation to tax income that may not be taxed under a treaty, a conflict arises between the directive obligation and the treaty obligation. In the following sections, an example is provided of a conflict between a detrimental directive and an intra-EU treaty (*see* section 2.3.1.) and an extra-EU treaty (*see* section 2.3.2.). The examples provided are illustrations of the overarching basic conflict that may arise: a directive imposes an obligation on a Member State to tax income that may not be taxed under a treaty by that Member State.

2.3.1. Conflict II: Detrimental directives and intra-EU treaties

Since the introduction of the linking rule in the PSD, directives can be detrimental to taxpayers and impose an obligation to tax cross-border income within the European Union. Obligations to tax such cross-border income within the European Union can also be found in the ATAD 1, the ATAD 2[19] and, more recently, in the Pillar Two Directive.[20] Such an obligation to tax would conflict with an intra-EU treaty if such a treaty requires non-taxation of that income. For the purposes of the subsequent sections of this article, reference will be made to the following example of a conflict that may arise between a detrimental directive and an intra-EU treaty.

XCo, resident in Member State A, carries out activities in Member State B. According to Member State A's interpretation of the intra-EU treaty with Member State B, these activities give rise to a permanent establishment in Member State B for the purposes of the treaty. Member State B, however, does not treat the activities of XCo as giving rise to a permanent establishment. Pursuant to the elimination of double taxation provision in the intra-EU treaty, which is based on article 23(A) of the OECD Model,

Figure 2. Conflict II



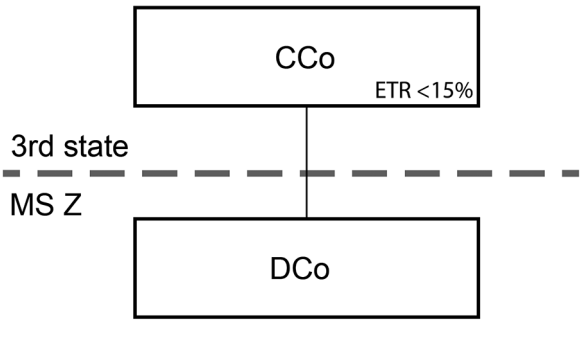
Member State A exempts the income attributable to the permanent establishment.

In this example, article 9(5) of the ATAD 2 requires Member State A (MS A) to include the income attributable to the permanent establishment (PE) in the tax base of XCo. This obligation to include the income in the tax base conflicts with MS A's obligation under the intra-EU treaty to exempt the income attributable to the (disregarded) PE in Member State B (MS B).[21]

2.3.2. Conflict III: Detrimental directives and extra-EU treaties

Since the adoption of the ATAD 1, directives may impose an obligation to tax income falling within the scope of extra-EU treaties. For example, article 7(2) of the ATAD 1 requires taxation of income attributed to a PE in a third state if such a PE qualifies as controlled foreign company, which income should generally be exempt under an OECD Model- patterned extra-EU treaty.[22] For the purposes of this article, reference is made to another, more recent, example of a directive imposing an obligation to tax income that may not be taxed under an OECD Model-patterned extra-EU treaty.

Figure 3. Conflict III



16. *See* R. Ismer, *Abuse of Law as a General Principle of European Union (Tax) Law*, in *A Guide to the Anti-Tax Avoidance Directive* p. 66 (W. Haslehner, K. Pantazatou, G. Kofler & A. Rust eds. Edward Elgar Publishing 2020).
17. Council Directive (EU) 2016/1164.
18. *See* W. Haslehner, *The General Scope of the ATAD and its Position in the EU Legal Order*, in *A Guide to the Anti-Tax Avoidance Directive* p. 60 (W. Haslehner, K. Pantazatou, G. Kofler & A. Rust eds., Edward Elgar Publishing 2020).
19. Council Directive (EU) 2017/952.
20. Council Directive (EU) 2022/2523.
21. *See*, inter alia, S. Pancham, *Permanent Establishment Mismatches under ATAD II*, in *The Implementation of Anti-BEPS Rules in the EU: A Comprehensive Study* para. 19.4.6 (P. Pistone & D. Weber eds. IBFD 2018), Books IBFD; P. Arginelli, *The ATAD and Third Countries*, in *The External Tax Strategy of the EU in a Post-BEPS Environment* para. 8.3.3 (A. Martin Jiménez ed. IBFD 2019), Books IBFD.
22. *See*, to this effect, Haslehner, *supra* n. 18.

CCo, resident in a third state, is the ultimate parent entity of a multinational group that falls within the scope of the Pillar Two Directive. The profits of CCo are subject to an effective tax rate of less than 15% while the third state has not implemented a qualified domestic top-up tax. DCo, resident in Member State Z, is part of the multinational group of CCo. The extra-EU treaty is based on the OECD Model (2017).

In this example, article 13 of the Pillar Two Directive requires Member State Z (MS Z) to apply the undertaxed profits rule (UTPR) and to impose a top-up tax on DCo in respect of the (undertaxed) profits of CCo. Based on article 7(1) of the extra-EU treaty, MS Z is precluded from taxing the profits of CCo in the absence of a permanent establishment of CCo in MS Z. Consequently, there appears to be a conflict between the obligation under the Pillar Two Directive to apply the UTPR and to impose a top-up tax in respect of (undertaxed) profits of CCo and the obligation of MS Z under the OECD Model-patterned extra-EU treaty not to tax such profits of CCo.[23]

3. The Effect of Directives on the Interpretation of Treaties: Avoiding Conflicts

3.1. Introductory remarks

The preceding section provided examples of conflicts between directives and treaties. In those examples, it was assumed that the directive would not affect the interpretation of the (conflicting) treaties.[24] The purpose of this section is to illustrate the extent to which the directives can affect the interpretation of these treaties to avoid a conflict, with reference to the three conflicts set out in section 2. The interaction between the duty of consistent interpretation and the rules of governing the interpretation of treaties is discussed first (*see* section 3.2.), followed by a discussion of the framework of international law governing the interpretation of treaties, i.e. the Vienna Convention on the Law of Treaties 1969 (Vienna Convention)[25] (*see* section 3.3.) and article 3(2) of the OECD Model (*see* section 3.4.). This section concludes with an answer to the question to what extent a directive may affect the interpretation of a treaty within the context of the conflicts set out in section 2. (*see* section 3.5.).

3.2. The interaction between the duty of consistent interpretation and the framework of international law governing the interpretation of treaties

The starting point for assessing the effect of directives on the interpretation of treaties is that Member State courts are, as a matter of EU law, subject to the duty of consistent interpretation. Pursuant to this duty, Member State courts are required to interpret domestic law in a way that is consistent with both primary and secondary EU law.[26] This duty applies not only to domestic law, but also to (tax) treaties.[27] Member State courts are thus under a duty to interpret treaties in a way that is consistent with the directives.

With respect to the duty of consistent interpretation, it follows from settled case law of the CJEU that there are limits to this duty.[28] Member State courts are required to arrive at a consistent interpretation "so far as possible".[29] The limits of the duty of consistent interpretation relate to general principles such as legal certainty and non-retroactivity.[30] Based on such principles, Member State courts are not required, on the basis of the duty of consistent interpretation, to interpret a treaty in a way that would be *contra legem*,[31] or would require them to go beyond what is possible under the interpretative methods recognized by the domestic laws of the Member States.[32] For the purposes of this article, the limit relating to the methods of interpretation recognized by the domestic laws indicates that the scope of the duty of consistent interpretation depends on the national law perspective. If a Member State court would conclude that it is not possible, based on methods of interpretation recognized by domestic law, to interpret a treaty in a way that is consistent with a directive, the duty of consistent interpretation would not require that court to nevertheless arrive at a directive-consistent interpretation. Consequently, the interpretative methods within a Member State are highly relevant in answering the question whether a Member State court is required to interpret a treaty in a way that is consistent with a directive based on the duty of consistent interpretation.

Generally, the interpretative methods recognized by domestic law may vary among Member States. Consequently, differences may arise as to the effect that directives may have on the interpretation of treaties under the duty of consistent interpretation.[33] In order to nevertheless have a notion of the extent to which the interpretative methods recognized by domestic law may limit the extent to which the duty of consistent interpretation requires treaties to be interpreted in a directive-consistent way, reference may be made to the framework of international law that governs the interpretation of tax treaties,

23. In support of the position that there is a conflict, *see*, inter alia, V. Bendlinger, *supra* n. 2, at pp. 504-506; S. Douma et al., *The UTPR and International Law: Analysis From Three Angles*, 110 Tax Notes International (2023) and F. Debelva & L. De Broe, *Pillar 2: An Analysis of the IIR and UTPR from an International Customary Law, Tax Treaty Law and European Union Law Perspective*, 52 Intertax 12 (2022), para. 2. There are, however, also legal scholars who argue that there is no conflict. *See*, to that effect, S. Pancham, *De Pillar 2-heffing en belastingverdragen. Toch geen strijdigheid?*, NLF Opinie 4 (2023) and A. Christians & S.E. Shay, *The Consistency of Pillar 2 UTPR With U.S. Bilateral Tax Treaties*, Tax Notes (23 Jan. 2023).
24. *See supra* n. 14.
25. *UN Vienna Convention on the Law of Treaties* (23 May 1969), Treaties & Models IBFD.
26. *See* K. Lenaerts & P. van Nuffel, *European Union Law* p. 757 (Sweet & Maxwell 2011) and the case law referred to therein.
27. *See* Vergouwen, *supra* n. 12, pp. 98-100.
28. *See*, to this effect, the opinion of Advocate General Bobek, 26 June 2018, Case C-384/17 (*Dooel Uvoz*), para. 57.
29. GR: ECJ, 4 July 2006, C-212/04, *Konstantinos Adeneler and Others v. Ellinikos Organismos Galaktos (ELOG)*, para. 108.
30. Id., at para. 110.
31. Id., at para. 110.
32. Id., at para. 111.
33. *See*, to this effect, S. Prechal, *Joined Cases C:397/01 to C-403/01, Bernhard Pfeiffer et al.*, 42 Common Market Law Review 5, p. 1459 (2005).

i.e. articles 31 through 33 of the Vienna Convention and article 3(2) of the OECD Model.

3.3. The effect of directives on the interpretation of treaties under the Vienna Convention

The Vienna Convention applies to treaties. Consequently, the interpretation of treaties is governed by articles 31 to 33.[34] This section examines the effect of directives under the general rule of interpretation of article 31 of the Vienna Convention.[35] Pursuant to this general rule, a Member State court, when interpreting a treaty, must take into account the following means of interpretation: good faith, the ordinary (or special) meaning of a treaty term, the object and purpose of the treaty and the (internal and external) context.[36] It follows that a directive would have to be one of these means of interpretation to be able to affect the interpretation of a treaty under the general rule of interpretation. If it were not one of them, there would be no basis for taking a directive into account and it could therefore not affect the interpretation of the treaty.

Regarding the question as to whether directives would be among the means of interpretation referred to in article 31 of the Vienna Convention, the starting point is that this provision aims to give effect to the common intention of the parties to a treaty in respect of that treaty.[37] This starting point implies that, in any event, directives cannot affect the interpretation of extra-EU treaties because the directives do not provide evidence of a common intention between a third state and a Member State because the third state has not agreed to the adoption of the directives. With respect to intra-EU treaties, this would appear to be different because a directive can be regarded as reflecting a common intention of the Member States to achieve the result of that directive, given the requirement of unanimity in the Council under article 115 of the Treaty on the Functioning of the European Union (TFEU).[38] With respect to intra-EU treaties, the question remains whether it can be regarded as one of the means of interpretation referred to in article 31 of the Vienna Convention.

Based on the reference in article 31(3)(c) of the Vienna Convention to the rules of international law applicable in the relations between the parties, this question should be answered in the affirmative. Directives, as decisions of an international organization (a source of international law),[39] are applicable in the relations between the Member States and should therefore be taken into account if they would be relevant.[40] If a directive is to be taken into account when interpreting an intra-EU treaty, the question arises as to how much weight a Member State court should attach to it (the weight question).

In relation to this weight question, it is relevant to take the overarching purpose of article 31 of the Vienna Convention into account, which is to give effect to the common intention of the parties to a treaty with respect to that treaty. Based on this purpose, the effect of directives would seem to depend on the extent to which they may reflect such a common intention, as well as on the text of the treaty interpreted because an interpretation under article 31 of the Vienna Convention should, above all, be based on the text of the treaty.[41] With respect to the extent to which directives can provide direct evidence of a common intention, two categories can be distinguished. First, a directive may provide for explicit evidence of a common intention by referring to treaties in its provisions or in its preamble. Second, directives may provide for implicit evidence by covering situations which are also covered by treaties or by using terminology that is similar to that of treaties.[42] Additionally, the presumption against conflict and the duty of EU loyalty, although not part of the directives themselves, may also be relevant in determining the effect of directives under the general rule of interpretation of the Vienna Convention. Under the presumption against conflict, which is part of the principle of good faith, Member States would be presumed to have intended not to derogate from their obligations under directives when concluding later intra-EU treaties.[43] The duty of EU loyalty, which is applicable in to the relations between two Member States, may give rise to a presumption that Member States share a common intention so as to apply their intra-EU treaties in a way that is consistent with a directive.[44]

Whereas directives may provide direct evidence of a common intention of the Member States with respect to their intra-EU treaties, as well as indirect evidence through the presumption against conflict and the duty of EU loyalty, such evidence must be weighed against the other means of interpretation referred to in article 31 of the Vienna Convention, which may also provide evidence of such a common intention. Regarding this question of weight, the starting point would be that there is no a priori hierarchy among the means of interpretation, other than that the interpretation must be based on the text of the treaty. This starting point means that the effect of directives on the interpretation of a treaty under article 31 of the

34. Regarding the interaction between articles 31 to 33 of the Vienna Convention and article 3(2) of the OECD Model, it has been submitted that article 3(2) of the OECD Model functions as the *lex specialis* vis-à-vis articles 31 to 33 of the Vienna Convention as the *lex generalis*. *See*, to this effect, Vergouwen, *supra* n. 12, at p. 40, n. 153.
35. For the effect of directives under articles 32 and 33, *see* Vergouwen, *supra* n. 12, at pp. 59-60.
36. *See* Vergouwen, *supra* n. 12, at p. 60.
37. *See*, to this effect, M. Samson, *High Hopes, Scant Resources: A Word of Scepticism about the Anti- Fragmentation Function of Article 31(3)(c) of the Vienna Convention on the Law of Treaties*, 24 Leiden Journal of International Law 3, p. 705 (2011).
38. Consolidated Version of the Treaty on the Functioning of the European Union (TFEU), art. 115, OJ C115/01 (2008), Primary Sources IBFD; *see also* Vergouwen, *supra* n. 12, p. 146.
39. *See*, to this effect, Vergouwen, *supra* n. 12, at chap 2. If directives would not qualify as a source of international law, *see* Vergouwen, *supra* n. 12, at pp. 246-247.
40. Regarding the question when a directive would be relevant, *see* Vergouwen, *supra* n. 12, at pp. 61-63. In support of the conclusion that directives are to be considered under article 31(3)(c) of the Vienna Convention, *see*, for example, F. Avella, *Using EU Law to Interpret Undefined Tax Treaty Terms: Article 31(3)(c) of the Vienna Convention on the Law of Treaties and Article 3(2) of the OECD Model Convention*, 4 World Tax J. 2 (2012), Journal Articles & Opinion Pieces IBFD.
41. *See*, to this effect, inter alia, Judgment of the ICJ, 3 February 1994, *Territorial Dispute (Libyan Arab Jamahiriya/Chad)*, I.C.J. Reports 1994, p. 6, para. 41.
42. *See* Vergouwen, *supra* n. 12, at pp. 80-82.
43. *See*, in this respect, International Law Commission ("ILC"), *Report on the Fragmentation of International Law*, A/CN/L.682, p. 26.
44. *See* Vergouwen, *supra* n. 12, at pp. 86-87.

Vienna Convention, if relevant and taken into account, may vary from one treaty to another. Nevertheless, if a Member State court were to conclude that an intra-EU treaty can be interpreted in two ways, only one of which is consistent with a directive, the principle of good faith would oblige that court to adopt the meaning that is consistent with the directive.[45]

3.4. The effect of directives on the interpretation of treaties under article 3(2) of the OECD Model

In accordance with article 3(2) of the OECD Model, undefined treaty terms shall have the meaning they have under the laws of the state applying the treaty unless, in the absence of a mutual agreement, the context requires otherwise. With respect to the effect of directives on the interpretation of treaties under this interpretative provision, the effect of directives as "laws of that State" (*see* section 3.4.1.) and as context (*see* section 3.4.2.) is discussed in the following sections.

3.4.1. The effect of directives as part of the "laws of that State"

The starting point for determining the effect of directives as part of the "laws of that State" is that, according to settled case law of the CJEU, directives are part of the laws of the Member States.[46] Consequently, the meaning of an undefined treaty term in both intra-EU and extra-EU treaties can be determined by reference to directives under article 3(2) of the OECD Model.[47] By way of example, this means that the meaning of the term "beneficial owner" in the IRD, as interpreted by the CJEU in *N Luxembourg 1*,[48] may be used when interpreting the undefined "beneficial owner" term in article 12 of the OECD Model. If a Member State court interprets an undefined treaty term by reference to the meaning of that term in a directive, this does not, however, mean that such meaning is decisive. After all, the meaning based on the laws of the state applying the treaty is subject to the context requiring otherwise. Therefore, if the context requires otherwise, the directive-based meaning would have to be rejected.

3.4.2. The effect of directives as "context"

It follows from the wording of article 3(2) of the OECD Model that the meaning of an undefined treaty term based on the laws of the state applying the treaty is subject to the context requiring otherwise. Whether the context requires otherwise depends on the elements that make up the context and whether those elements, taken together, require a meaning that is different from the meaning based on the laws of the state that applies the treaty. With respect to the elements that make up the context, no consensus seems to exist between legal scholars.[49]

Assuming the context would in any case consist of the elements mentioned in the OECD Commentaries (2017), directives can be part of the context of intra-EU treaties. This can be illustrated as follows. First, according to the OECD Commentaries, the context is determined in particular by the common intentions of the contracting states at the time a treaty is signed.[50] Thus, if an intra-EU treaty is concluded between, at the time of signing, two Member States, it seems conceivable, based on the duty of EU loyalty as well as the presumption against conflict, that the contracting states had a (presumed) common intention that their treaty must be applied in a way that is consistent with their obligations under EU law.[51] If one or both contracting state(s) accede(s) to the European Union after conclusion of the treaty, such presumption does not seem part of the context given the reference to "at the time a treaty is signed". Second, reference is made in the OECD Commentaries to the legislation in the other contracting state. Considering that directives are part of the laws of the Member States, they may be considered part of the context of each intra-EU treaty based on this reference. Whereas directives can be regarded as part of the context of intra-EU treaties on the basis of the OECD Commentaries, this would not be the case for extra-EU treaties because directives do not provide evidence of an intention of the third state nor would they be part of the national legislation of the third state.

If a directive were part of the context of an intra-EU treaty, the question arises when it may require a directive-consistent meaning to be adopted under article 3(2) of the OECD Model. The starting point in this respect is that article 3(2) of the OECD Model refers to the "context" (in the singular). Hence, the mere fact that a directive would require a directive-consistent meaning would not be sufficient to confirm or reject a meaning based on the laws of the Member State applying the intra-EU treaty. Instead, all elements of the context would have to be considered and it would have to be decided in good faith whether the context requires such a meaning to be rejected (or not). As a rule, however, the more closely a directive reflects the common intention of the parties to the intra-EU treaty, the more weight may be attributable to it as part of the context.[52]

3.5. The effect of directives on the interpretation of treaties: The conflicts

3.5.1. Conflict I: Beneficial directive and intra-EU treaty

With respect to Conflict I, the question may arise whether the directive or the anti-abuse principle may be able to affect the interpretation of the intra-EU treaty in such a way so as to not require an exemption at source. In that respect, it seems conceivable that the directive or anti-abuse principle would be able to affect the interpretation of the undefined "beneficial owner" term or the principal purpose test (PPT). This can be illustrated as follows. Regarding the

45. *See*, to this effect, F.A. Engelen, *Interpretation of Tax Treaties under International Law*, p. 436 (IBFD 2004), Books IBFD.
46. *See*, to this effect, SK: ECJ, 6 Mar. 2018, Case C-284/16, *Slowakische Republik v. Achmea BV*, para. 41.
47. *See*, to this effect, Vergouwen, *supra* n. 12, at pp. 41-47.
48. *See* ECJ, *supra* n. 13.
49. For an overview of the various views, *see* Vergouwen, *supra* n. 12, at pp. 47-49.
50. *Commentaries on the Articles of the Model Tax Convention* (21 November 2017), Treaties & Models IBFD.
51. *See* Vergouwen, *supra* n. 12, at pp. 49-51.
52. *See* Vergouwen, *supra* n. 12, at p. 55.

interpretation of the term beneficial owner, it seems conceivable that MS Y resorts to the meaning of such undefined term in article 1(4) of the IRD as interpreted by the CJEU. If, based on such a directive-based interpretation, ACo would not qualify as the beneficial owner to the royalties, MS Y would not be obliged to exempt the royalty payment under article 12 of the intra-EU treaty. Consequently, the conflict with the anti-abuse principle would be avoided. If a directive-based interpretation would not be sufficient for avoiding the conflict with the anti-abuse principal, the question may arise whether the anti-abuse principle, as part of the context within the meaning of article 3(2) of the OECD Model, could require a different meaning of the undefined "beneficial owner" term that ensures that MS Y is not required to exempt the royalty payment. If it were concluded that the context, as a whole, does not require otherwise and the exemption must be granted under the intra-EU treaty, the question arises whether the duty to not exempt under the anti-abuse principle would be able to affect the interpretation of the PPT in such a way that ACo would not be entitled to the treaty benefit of an exemption by MS Y to the extent that the exemption must be denied under the anti-abuse principle.

3.5.2. Conflict II: Detrimental directive and intra-EU treaty

Regarding Conflict II, the conflict arises because the elimination of the double taxation provision in the intra-EU treaty requires MS A to exempt the income attributable to the permanent establishment. The question that would have to be answered is whether taking into account the ATAD 2 could result in this provision being interpreted in a way that is consistent with article 9(5) of the ATAD 2. In general terms, this would seem more difficult as compared to Conflict I. This is due to the fact that the obligation under the elimination of double taxation provision is rather clear and absolute: if the income may be taxed in MS B in accordance with (MS A's interpretation of) the intra-EU treaty, MS A must exempt the income.[53] There seems to be little room for interpreting this provision so as to not require an exemption in the event of a disregarded permanent establishment. This then raises the question whether taking into account article 9(5) of the ATAD 2 when interpreting the PPT could result in XCo being denied the benefit of the exemption in Conflict II because, for example, granting the exemption would not be in accordance with the purpose of the treaty, which could be to prevent non-taxation.

3.5.3. Conflict III: Detrimental directive and extra-EU treaty

Considering that Conflict III relates to a conflict between a directive and an extra-EU treaty, the starting point for determining the effect of the Pillar Two Directive on the interpretation of the extra-EU treaty is that this would only be possible as part of the laws of MS Z under article 3(2) of the OECD Model. The question that would arise in this respect would then be whether the undefined "profits" term in article 7(1) of the OECD Model may be interpreted by reference to the Pillar Two Directive so as to include profits of CCo. In the author's view, this would seem unlikely as the Pillar Two Directive does not contain a definition of the term "profits". As such, the Pillar Two Directive does not seem to have a meaning of the term "profits" and, consequently, would not seem able to affect the interpretation of the term "profits" in article 3(2) of the OECD Model as part of the laws of MS Z.

53. *See*, to this effect, OECD Commentaries (2017) on Article 23, para. 34.1.

4. The Effect of Directives on the Application of Treaties: Resolving Conflicts

4.1. Introductory remarks

The purpose of this section is to examine the extent to which directives can affect the application, in terms of applicability, of treaties in the event of a conflict. The central question in that respect will be whether the directive can take precedence over the treaty. The answer to this question will be addressed by assessing the effect of directives on the application of treaties, in turn, under international law (*see* section 4.2.), domestic law (*see* section 4.3.) and EU law (*see* section 4.4.),[54] with reference to the conflicts set out in section 2.

4.2. The public international law perspective

4.2.1. Introductory remarks

The starting point for the purposes of assessing the effect of directives on the application of treaties in this section is that directives, as decisions of the European Union as an international organization, qualify as a source of public international law.[55] As a source of public international law, Member States are obliged to perform their obligations under the directives in good faith (pacta sunt servanda). The same applies to treaties. Consequently, obligations under both directives and treaties must be performed in good faith. If an obligation under a directive conflicts with an obligation under a treaty, a Member State cannot comply with both obligations at the same time because compliance with one obligation implies non-compliance with the other. There are, however, general conflict rules in international law, i.e. the *lex posterior* and *lex specialis*, which may result in the treaty being inapplicable under international law to the extent that it conflicts with a directive. The purpose of this section is to assess the extent to which the *lex posterior* (*see* section 4.2.2.) and *lex specialis* (*see* section 4.2.3.) conflict rules may have such an effect. With respect to this assessment, it is acknowledged that it addresses this question from the perspective of public international law in isolation. In practice, it would be relevant whether a Member State court, as a matter of domestic law, applies the *lex posterior* and/or *lex specialis* conflict rules to conflicts between sources of international law.

54. For a (more) elaborate analysis of the effect of directives under these perspectives, as well as the interaction between them, *see* Vergouwen, *supra* n. 4, at pp. 158-159.

55. *See* Vergouwen, *supra* n. 12, at ch. 2, pp. 21-36. If directives would not qualify as a source of international law, *see* Vergouwen, *supra* n. 12, at p. 259.

For the purposes of the assessment in the following sections regarding the effect of directives on the application of intra-EU treaties, it is noted that, according to the principle of *pacta tertiis*, directives cannot affect the application of extra-EU treaties without the consent of the third states concerned. Hence, these conflict rules can only affect the application of intra-EU treaties. Furthermore, it is assumed that the *lex posterior* and *lex specialis* conflict rules, whose application to conflicts between directives and treaties seems only arguable or conceivable,[56] can indeed be applied to conflicts between a directive and a treaty. It is furthermore assumed that there are no conflict clauses in the treaties or in the directives that provide explicit evidence of a common intention that the directive should prevail in the event of a conflict. If there were such conflict clauses, they should be resorted to for the purpose of assessing the effect of directives under international law. This is due to the residual nature of the *lex posterior* and *lex specialis* conflict rules. These conflict rules seek to resolve conflicts based on presumed intentions, which means that they should not be decisive where there is evidence of the actual intentions between states as to how a conflict between a directive and a treaty should be resolved.[57]

4.2.2. The effect of directives on intra-EU treaties under the lex posterior conflict rule

Under the *lex posterior* conflict rule, a later directive takes precedence over an earlier intra-EU treaty if they relate to the same subject matter. To determine whether a directive and an intra-EU treaty relate to the same subject matter, a substance-based approach entails that such sameness must be assessed on an overall basis.[58] Hence, mere overlap in the event of a conflict would not be sufficient for concluding that they relate to the same subject matter.

Instead, the sameness must be assessed based on the overall nature of the directive and the intra-EU treaty. The application of the sameness of subject matter test under the *lex posterior* conflict rule can be illustrated as follows by reference to the conflicts between directives and intra-EU treaties as set out in section 2.

With respect to Conflict I, an assessment would have to be made between the subject matter of the EU treaties, i.e. the Treaty on European Union (TEU)[59] and TFEU, on which the anti-abuse principle must ultimately be based, and the intra-EU treaty. As regards the subject matter of the EU treaties, it follows from case law of investment tribunals that it can be described as the creation of a common market between the EU Member States.[60] Regarding intra-EU treaties, it seems that their subject matter can be described as the elimination of double taxation of cross-border income of residents of the contracting states without creating opportunities for non-taxation or reduced taxation through tax avoidance or tax evasion.[61] A comparison of these subject matters seems to indicate that intra-EU treaties may contribute to the achievement of a common market, but it is not their purpose or subject matter to create one. Consequently, the EU treaties and intra-EU treaties do not seem to relate to the same subject matter within the meaning of the *lex posterior* conflict rule.[62] This would then entail that the general anti-abuse rule cannot take precedence over the intra-EU treaty in Conflict I on the basis of the *lex posterior* conflict rule.

Regarding Conflict II, a comparison must be made between different sources because the conflict arises between the directives, i.e. the ATAD 2, and the intra-EU treaty. Hence, the subject matter of the ATAD 2 would have to be compared with the subject matter of an intra-EU treaty as set out in the previous paragraph. The starting point for such a comparison would seem to be that the ATAD 2 contains rules that are aimed at tackling hybrid mismatches with a view to combatting tax avoidance. Such rules overlap with tax treaties in the sense that the ATAD 2 provides rules for the taxation of profits of an enterprise that may also fall within the scope of article 7 of the OECD Model. Such mere (incidental) overlap would, however, not be sufficient for concluding that the subject matter of the ATAD 2 would be the same as that of the intra-EU treaty.[63] There must be sameness of subject matter on a more general, overall, level. In that respect, it appears that the substantive scope, in terms of cross-border income covered, as well as the personal scope, in terms of persons covered, of the ATAD 2 would be significantly narrower than that of the intra-EU treaty. Ultimately, the ATAD 2 is concerned with tackling hybrid mismatches that arise for companies only, whereas tax treaties provide a comprehensive set of rules aimed at eliminating double taxation with respect to, in principle, all categories of cross-border income, both for individuals and for companies.[64] Taking this into account, it would seem that the ATAD 2 relates to a more narrow, different subject matter than the intra-EU treaty in Conflict II. If not relating to the same subject matter, the ATAD 2 would not be able to set aside the intra-EU treaty under the *lex posterior* conflict rule. If, however, the ATAD 2 were to relate to the same subject matter, it would take precedence over nearly all intra-EU treaties (98.2%; measured 16 June 2022) in the event of a conflict such as Conflict II.[65]

56. Regarding the conclusion that their application is merely arguable or conceivable, *see* Vergouwen, *supra* n. 12, at p. 149 (*lex posterior*) and p. 182 (*lex specialis*).
57. *See*, to this effect, Vergouwen, *supra* n. 12, at pp. 191-193.
58. *See*, regarding the adoption of a substance-based approach, Vergouwen, *supra* n. 12, at pp. 131-141.
59. *Treaty on European Union* (TEU) (as amended through 2008), art. 3(2), OJ C115 (2008), Primary Sources IBFD.
60. *See*, for example, ICSID, 7 May 2019, No. ARB/15/50 (*Eskosol*), para. 146.
61. *See* Vergouwen, *supra* n. 12, at p. 139.
62. Id., at pp. 138-139. For a similar line of reasoning within the context of the application of the *lex posterior* conflict rule to a conflict between the EU treaties and investment treaties, *see* ICSID, ARB/15/50 (*Eskosol*), para. 144.
63. In support of the position that incidental overlap would be insufficient, *see* ICSID, ARB/15/50 (*Eskosol*), para. 144 as well as ILC, Summary of the plenary meetings and of the meetings of the Committee of the Whole, 9 April-022 May 1969, p. 253, para. 41.
64. *See* Vergouwen, *supra* n. 12, at p. 257.
65. Id., at p. 277.

4.2.3. The effect of directives on intra-EU treaties under the lex specialis conflict rule

Under the *lex posterior* conflict rule, a directive takes precedence over an intra-EU treaty in the event of a conflict if it would be adopted after the conclusion of a treaty. The *lex specialis* conflict rule applies a different criterion for resolving a conflict. Pursuant to the *lex specialis* conflict rule, a directive takes precedence over an intra-EU treaty if the directive provision that conflicts with the intra-EU treaty (i) relates to the same subject matter as the provision(s) of the treaty with which it is incompatible; and (ii) is sufficiently more specific as regards such subject matter as compared to the subject matter of the intra-EU treaty's provision(s).[66] Taking this into account, in order to determine the effect of a directive on an intra-EU treaty under the *lex specialis* conflict rule, it is necessary to carry out an assessment of the subject matter of the directive provision and the provision(s) of the intra-EU treaty with which it conflicts.

In Conflict I, for example, the subject matter of the anti-abuse principle and article 12 of the intra-EU treaty should be compared. Regarding the subject matter of the anti-abuse principle, the starting point would be that it aims to ensure that the benefits of EU law, including those of directives, cannot be claimed in fraudulent or abusive situations. Its scope is therefore very broad in the sense that it is not limited to the benefits of the IRD. The subject matter of article 12 of the intra-EU treaty is, by contrast, more specific. It relates only to royalty payments. As such, the subject matter of article 12 appears to be more specific than that of the anti-abuse principle. Consequently, the anti-abuse principle would not be able to take precedence over the intra-EU treaty under the *lex specialis* conflict rule. It is furthermore noted that the intra-EU treaty would also not be able to take precedence over the anti-abuse principle because the intra-EU treaty, concluded between two Member States, would not be able to reflect the common intention of the 27 Member States which are parties to the EU treaties.

Whereas the *lex specialis* conflict rule would not be able to render the intra-EU treaty inapplicable under international law in Conflict I, this seems to be different for Conflict II. In general terms, article 9(5) of the ATAD 2 and article 7 in conjunction with article 23 of the intra-EU treaty relate to the taxation of business profits. Article 7 of the intra-EU treaty provides the general rule that profits of XCo may not be taxed by MS B in the absence of a PE. If there were a PE, article 7 in conjunction with article 23 requires MS A to exempt the profits attributed to the PE. Article 9(5) of the ATAD 2 also relates to the taxation of business profits attributed to a PE. It does so in a more specific way as well. First, it applies only to the taxation of profits by companies. Second, it applies only to the extent that such profits would not be taxed in MS B because MS B does not recognize a PE. In the light of the above, it can be concluded that article 9(5) of the ATAD 2 relates to the same subject matter as the intra-EU treaty's provisions in Conflict II and in a way that is more specific than those provisions. Based on such a conclusion, article 9(5) of the ATAD 2 could take precedence over the intra-EU treaty under international law based on the *lex specialis* conflict rule. If it were to take precedence, MS A would no longer be obliged to exempt the profits under international law and would not face conflicting obligations of international law.

4.3. The domestic law perspective

Within the context of assessing the effect of directives on the application of treaties, the relevance of the domestic law perspective can be explained as follows. Article 288 of the TFEU requires Member States to achieve the result of directives. Generally, Member States seek to achieve this result by transposing a directive into their domestic laws. If the result of a directive conflicts with treaties, the question arises whether a Member State can, as a matter of domestic law, override its treaties when implementing such a directive.

If a Member State can override the treaties, it can achieve the result of a directive by means of its domestic law if that result conflicts with obligations under treaties. A recent example of such a (potential) treaty override when implementing a directive can be found in article 100 of the German Minimum Tax Act, which seeks to implement the Pillar Two Directive. Pursuant to this provision, taxpayers would not be entitled to apply a treaty in connection with taxation under the German Minimum Tax Act. Applied to Conflict III, if Germany were to tax the profits of CCo at the level of DCo, DCo would not seem able – as a matter of domestic law – to rely on the extra-EU treaty. The inability to rely on the treaty, would, however, entail that Germany risks state responsibility under international law because (i) the Pillar Two Directive would be incapable of taking precedence over the extra-EU treaty under international law (*pacta tertiis*) while (ii) provisions of domestic law, such as article 100 of the German Minimum Tax Act, cannot be invoked as a justification for failure to perform a treaty (article 27 of the Vienna Convention).

Whereas there may be Member States that can override their treaties, the majority of Member States seem unable to do so because treaties would be superior to the legislation implementing the directive from their domestic (constitutional) perspective.[67] For the majority of the Member States, the outcome of the domestic law perspective would thus be that domestic law aimed at implementing a directive would be set aside by their treaties. If a directive would thus require a result that conflicts with treaties, these Member States would be unable to achieve such a result (unless a directive affects the application of its treaties under international law or EU law).

66. Id., at pp. 182-188.

67. Id., at pp. 13-17.

4.4. The EU law perspective

Within the context of the effect of directives on the application of tax treaties, EU law provides for an absolute conflict rule: if it were concluded that application of a treaty, after having established that a consistent interpretation is not possible,[68] conflicts with EU law, a Member State court must disapply such tax treaty (the Primacy-Based Conflict Rule).[69] Considering that the Primacy-Based Conflict Rule requires the application of a treaty to conflict with EU law, such a conflict rule can only be resorted to after it has been established that the tax treaty's interpretation (*see* section 3.), as well as its application has not been affected by the rules (*see* section 4.2.) or by domestic law (*see* section 4.3.) because it may follow that the treaty would, ultimately, not conflict with EU law. This can be illustrated as follows by reference to the conflicts set out in section 2.

If a consistent interpretation were possible in Conflict I, the application of the treaty would (ultimately) not conflict with the anti-abuse principle of EU law. Similarly, if the ATAD 2 were to take precedence over the intra-EU treaty in Conflict II under the *lex specialis* conflict rule, MS B would seem able to achieve the result of article 9(5) of the ATAD 2 (irrespective of the superiority of the intra-EU treaty under its domestic (constitutional) law). Finally, regarding Conflict III, no conflict between the treaty and the directive arises if it were established that MS Z overrides the extra-EU treaty by means of its domestic laws.

If, however, a Member State court were to conclude that a treaty prevents achievement of the result of a directive and, hence, conflicts with EU law, the Primacy-Based Conflict Rule requires that court to set aside the treaty. This obligation applies to any treaty, unless the setting aside of the treaty would result in the rights of, and obligations towards,[70] third states being affected under an extra-EU treaty that has been concluded before the relevant Member States acceded to the European Union (because article 351 of the TFEU provides that such treaties shall not be affected by the EU treaties and directives).[71] Applied to Conflict III, if the setting aside of the extra-EU treaty were to affect such rights and obligations of the third state, the Primacy-Based Conflict Rule would not apply, and hence could not be relied upon to set aside the extra-EU treaty, if the extra-EU treaty would have been concluded before MS Z's accession to the European Union. Hence, article 351 of the TFEU affects the extent to which directives may be able to affect the application of (extra-EU) treaties under the EU law perspective.

If, however, article 351 of the TFEU were not applicable in the context of a conflict between a directive and a treaty, the Primacy-Based Conflict Rule applies and requires a Member State court to set aside the treaty. Whereas the Primacy-Based Conflict Rule seems to provide an effective tool for resolving conflicts between directives and treaties, it should be acknowledged that its enforceability may be limited in practice. This is due to settled case law of the CJEU that (the primacy of) directives may not be relied upon, even if such directives were to be sufficiently clear, precise and unconditional to have direct effect, to impose an additional obligation on taxpayers, such as a higher tax burden (prohibition of reverse vertical direct effect).[72] The prohibition of reverse vertical direct effect thus entails that, to the extent that application of a treaty would be more beneficial for a taxpayer as compared to application of a directive with which it conflicts, the primacy of the directive would be unenforceable before a Member State court. Applied to the conflicts set out in section 2., the Primacy-Based Conflict Rule would not be enforceable in Conflicts II and III because the setting aside of the treaties based on such a conflict rule would entail that the (primacy of the) relevant directives impose(s) a higher tax burden on the taxpayers. This illustrates that, within the context of conflicts between detrimental directives and treaties, the Primacy-Based Conflict Rule can be regarded as an ineffective tool for resolving such conflicts.[73] Whereas this may be the case for conflicts between detrimental directives and treaties, this is different for conflicts between beneficial directives and treaties. With respect to those conflicts, the prohibition of reverse vertical direct effect does not apply.[74] As such, the Primacy-Based Conflict Rule would be enforceable and would require a Member State court to set aside the treaty that conflicts with the directive or the anti-abuse principle. Consequently, a Member State court would be required, in Conflict I, to set aside the intra-EU treaty based on the Primacy-Based Conflict Rule if its application conflicts with the obligation under the anti-abuse principle to deny an exemption.

5. Conclusions

The purpose of this article has been to assess how directives may affect (the interpretation and application of) tax treaties and interact with them, considering the three perspectives in isolation, as well as their interaction. To this end, three examples of conflicts have been set out in section 2. and the extent to which directives may affect the application of treaties within the context has been assessed in the subsequent sections.

In section 3., it has been demonstrated that the extent to which directives may affect the *interpretation* of treaties under international law is, considering the duty of consistent interpretation, essentially dependent on the rules of international law. Table 1 summarizes the ways in which directives may be taken into account under international law when interpreting treaties, based on the findings

68. *See*, to this effect, inter alia, CJEU, 24 June 2019, Case C-573/17 (*Poplawski II*), para. 58.
69. Id., at para. 58.
70. CJEU, 27 Feb. 1962, Case 10/61 (*Commission v. Italy*), p. 10.
71. An analogous application of this provision to extra-EU treaties concluded after accession to the European Union, but before the adoption of a directive, which was deemed conceivable by Advocate General Kokott in *Commune de Mesquer* (Case C-188/08), has been rejected by the CJEU in its judgment of 28 Oct. 2022, Case C-435/22 PPU (*Generalstaatsanwalt München v. HF*).
72. *See* CJEU, *supra* n. 68, at paras. 64-67.
73. *See* Vergouwen, *supra* n. 4, at p. 269.
74. *See* CJEU, *supra* n. 13, at para. 118.

of section 3.[75] If they are taken into account, it must be acknowledged that their effect on the interpretation of a treaty may vary from case to case and, essentially, depends on the extent to which a directive-based or directive-consistent meaning is consistent with the common intention between the parties to the treaty.

Table 1. Can a directive affect the interpretation of a treaty under international law?

Provision	Capacity	Intra-EU Treaties	Extra-EU Treaties
Article 31 VCLT 1969 (section 3.3.)	*"rules of international law"*	Yes	No
Article 3(2) OECD Model (section 3.4.)	*"laws of that State"*	Yes	Yes
	"context"	Yes	No

Regarding the effect of directives on the *application* of treaties, it follows from section 4. that the effect of directives may differ from one perspective to another and that the effect of a directive on a tax treaty under one perspective may be relevant for its effect under another. For example, the question as to whether a directive affects the application of treaties under the EU law perspective can only arise after the international law and domestic law perspectives on the effect of directives on treaties have been considered. Notwithstanding the interaction between the three legal perspectives, the effect of directives on the application of treaties under each individual perspective can be summarized as follows.[76]

Table 2. Can a directive affect the application of a treaty?

	Intra-EU Treaties	Extra-EU Treaties
International law (section 4.2.)	Potentially (*lex posterior* and *lex specialis*)	No (*pacta tertiis*)
Domestic law (section 4.3.)	If the EU Member State can override: yes	If the EU Member State can override: yes
	If the EU Member State cannot override: no	If the EU Member State cannot override: no
EU law (section 4.4.)	Beneficial directive: yes	Beneficial directive: yes
	Abuse of a beneficial directive: yes	Abuse of a beneficial directive: yes
	Detrimental directive: no (prohibition of reverse vertical direct effect)	Detrimental directive: no (prohibition of reverse vertical direct effect irrespective of application of article 351 of the TFEU)

75. This table is an edited version of the table in Vergouwen, *supra* n. 12, at p. 246.
76. This table is an edited version of the table in Vergouwen, *supra* n. 4, at p. 160.

6. Recommendations

It follows from the conclusion in the previous section that the effect of directives on the interpretation and application of treaties varies, especially when it concerns a detrimental directive. In general, international law seems to be the key perspective to avoiding such a variety of effects of directives on treaties. It is, therefore, recommended that conflict clauses, or more specifically subordination clauses, are included in treaties that grant priority to obligations under EU law in the event of a conflict.[77] If such clauses were included, it follows that, under international law, Member States would not have to perform their obligations under the treaty in the event of a conflict. This would then, in turn, entail that Member States that cannot override treaties would be able to achieve the result of a directive by means of their domestic laws because such laws would no longer conflict with (superior) treaties. At the same time, Member States that would be able to override, would avoid international responsibility if they would otherwise have overridden the treaty.

With respect to this recommendation, it is recognized that third states may not be willing to agree to such subordination clauses. Assuming that Member States would generally not intend to override extra-EU treaties, it is recommended that directives explicitly clarify whether extra-EU treaties should be affected by directives and, if so, within what time frame.[78] Such a clarification seems particularly warranted because the CJEU has clarified that article 351 of the TFEU does not apply to extra-EU treaties concluded after a Member State's accession to the European Union.[79]

77. *See* Vergouwen, *supra* n. 12, at pp. 264-265.
78. Id., at pp. 266-268.
79. *See* CJEU, *supra* n. 71.