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**Committee of Experts on International
Cooperation in Tax Matters
Fourteenth session**

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Agenda item 3(a)

**Proposed changes in Article 13 (4) and (5) of the United Nations Model
Double Taxation Convention between Developed and Developing
Countries to prevent the granting of treaty benefits in inappropriate
circumstances**

**Need for preventing transactions that circumvent the application of paragraph 5 of
Article 13 in UN Model Convention**

1. The purpose of Action 6 Report was to prevent the granting of treaty benefits in inappropriate circumstances, and for this purpose, certain changes have been recommended in the OECD Model Convention and Commentary in the Final Report on Action 6. Since that exercise was undertaken keeping only the OECD Model Convention in view, it will be appropriate for Committee of Experts to consider treaty abuse concerns that arise only in the UN Model Convention while implementing the agreed changes in Action 6 Report.

2. Paragraphs 41 to 43 of the Report on Action 6 address the issue of transactions that circumvent the application of Article 13 (4) of the OECD Model Convention. It does not refer to the UN Model as the practice followed during BEPS was to focus exclusively on the OECD Model Convention, though it is expected that concerns specific to the UN Model can be subsequently dealt by the Committee of Experts.

3. Unlike OECD Model Convention, paragraph 5 of Article 13 grants certain taxing rights to the country of source for taxation of capital gains from shares. While Article 13 (4) addresses abusive transactions with a purpose of avoiding tax in respect of paragraph 1 of Article 13, it does not prevent similar abusive transactions in respect of taxation of capital gains under paragraph 5. Since the nature of transactions that circumvent taxation of capital gains under paragraph 1 and paragraph 5 are exactly the same, there appears to every reason and justification for preventing abusive transactions that circumvent the application of paragraph 5 of Article 13.

4. Given the emphasis on preventing granting of treaty benefits in inappropriate circumstances and all possible measures being recommended by the global community for addressing abusive

transactions for avoiding tax, we must consider measures that will prevent transactions that circumvent the application of Article 13 (5) of the UN Model Convention. The need for such measures is only further highlighted by the urgency shown in further strengthening of the anti-abuse provision in Article 13(4) in the OECD Model Convention.

5. In view of the above, I strongly urge that the Committee may take up the issue of adopting measures for preventing transactions that circumvent the application of paragraph 5 of Article 13 in the UN Model Convention. Accordingly, I would like to suggest possible measures for preventing transactions that circumvent the application of paragraph 5 of Article 13.

Extend the scope of anti-abuse rule in paragraph 4 of Article 13 to cover capital gains in paragraph 5.

6. The basic principle of preventing treaty benefit in inappropriate circumstances as applicable to capital gains covered in paragraph 1 of Article 13 may also be extended to gains covered under paragraph 5 of the Article 13 of the UN Convention, so as to ensure a fair and principled stand in respect of safeguarding the interests of developing countries following UN Model Convention. This should not be difficult, and can be achieved without making major changes in the text of paragraph 4. As an illustration, I would like to propose the following amendment to the text of this paragraph, as proposed in this document:

4. *Gains derived by a resident of a Contracting State from the alienation of shares or comparable interests, such as interests in a partnership or trust, may be taxed in the other Contracting State if, at any time during the 365 days preceding the alienation, these shares or comparable interests derived more than 50 per cent of their value directly or indirectly from immovable property, as defined in Article 6, situated in that other State **or from shares referred in paragraph 5 of this Article.***

7. Such an amendment would extend the safeguards provided by paragraph 4 (which are currently restricted to gains covered in paragraph 1 only following the OECD Convention and completely overlook the possibility of treaty abuse in respect of gains covered in paragraph 5) against treaty shopping and treaty abuse to gains covered under paragraph 5, harmonize the principle stand of preventing treaty benefit in inappropriate circumstances and take care of treaty shopping and treaty abuse concerns that are faced by the developing countries in respect of capital gains taxable in the country of source under paragraph 5 of Article 13.

8. In case, it is felt that some countries may not wish to provide for source based taxation of capital gains under paragraph 5, it can be clarified in the Commentary on paragraph 4 that such countries may not include the words “..or from shares referred in paragraph 5 of this Article” in their treaties.

9. In case it is felt that this issue is not equally pressing for all countries, instead of recommending this as the default rule in the Convention itself, it can be recognized as a possible option in the Commentary on paragraph 4 of Article 13, for instance by a paragraph that reads as under:

8.3 Countries that consider it necessary to extend the protection provided in this paragraph to capital gains in paragraph 5 of this Article, may extend its application to paragraph 5 by adopting this paragraph with the following modification:

*4. Gains derived by a resident of a Contracting State from the alienation of shares or comparable interests, such as interests in a partnership or trust, may be taxed in the other Contracting State if, at any time during the 365 days preceding the alienation, these shares or comparable interests derived more than 50 per cent of their value directly or indirectly from immovable property, as defined in Article 6, situated in that other State **or from shares referred in paragraph 5 of this Article.***