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Tax Treaties: Time for a New Approach?

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Abstract

The author revisits the question of whether tax treaties are necessary, and the possible alternatives to the current bilateral regime. The scholarship of distinguished academics and prominent practitioners, on whether the present treaty architecture adequately meets the demands of the modern-day business and investment landscape, is parsed.

The significance of tax treaties has been called into question.

Writing in 1991, Vann's belief was that the "adoption of the OECD Model as *the* solution to international tax problems is a concept whose time has come – and gone".¹ He foretold the waning influence of the [OECD Model \(1997\)](#), and argued that it is increasingly inefficient, irrelevant, and inflexible.² Indeed, Avi-Yonah proclaimed in 1996 that "[t]he current international tax regime is a flawed miracle".³ In 2000, Easson posited that when the source state is a developing country, it should *unilaterally* reduce its statutory withholding tax rates to "treaty" rates, "in order to attract investment, not to secure reciprocal treaty benefits",⁴ although he stopped short of advocating the abolition of treaties.⁵

None of the above has come to pass.⁶

True, [Wheeler's 2012 doctoral thesis](#) argued "that there is a fundamental flaw in the way that the route to treaty protection is currently defined".⁷ In this sense, she focused on the grounds upon which a treaty is *applied*, a matter which is far removed from the core question of whether a treaty is even *necessary* to begin with. Nonetheless, viewed from all angles, the stark reality is that 2016 finds the [OECD Model Convention](#) in robust health, and spawning an

¹ R.J. Vann, *A Model Tax Treaty for the Asian-Pacific Region? (Part I)*, 45 Bulletin for International Fiscal Documentation 3 (1991), p. 99, at p. 102, Journals IBFD.

² *Id.*, at pp. 102-111.

³ R.S. Avi-Yonah, *The Structure of International Taxation: A Proposal for Simplification*, 74 Texas Law Review (1996), p. 1301, at p. 1303.

⁴ A. Easson, *Do We Still Need Tax Treaties?*, 54 Bulletin for International Taxation 12 (2010), p. 619, at p. 624, Journals IBFD. The source state "is likely to derive more benefit from increased investment than it loses in terms of tax revenues foregone". *Id.*

⁵ *Id.*, at p. 625.

⁶ The author resists the temptation to draw any conclusions from his unsubstantiated suspicion that none of these positions are subsequently pursued by any of the commentators.

⁷ J. Wheeler, *The Missing Keystone of Income Tax Treaties* (IBFD Doctoral Series 2012), at p. 1.

While on this subject, Wheeler was a panel member of the seminar on the occasion of the [IFA 69th Congress in 2015](#), which investigated and catalogued a variety of timing issues in the application of tax treaties, and explored how such issues could be tackled in order to ensure that taxation by both contracting states is in accordance with the fundamental "treaty bargain". For the comprehensive IBFD report, click [here](#).

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extensive and ever-expanding treaty network⁸ – all of which, albeit unwittingly, confirms Avery Jones' contention⁹ during his landmark Tillinghast lecture in 1997, that “the tax treaty route [...] is self-perpetuating” and resulting only in more treaties.¹⁰ Hence, it comes as no surprise that Wilkie et al. – after a thorough review in 2012 of the literature in the context of article 7 (business profits)¹¹ – did not profess an answer to the provocative question of whether tax treaties are necessary, as “it would be presumptuous” of them “to purport to have the answer”.¹²

Easson was likewise reluctant to take an unequivocal stand on the matter, but he did not shy away from concluding with an equally gripping query whether it is “time for a new approach”.¹³ He thereby dropped a not-too-subtle hint on where his sympathy lies.

What, then, does the future hold for tax treaties?

As mentioned, Easson leaned toward a “unilateral ‘treaty regime’”: he framed his ideas within the developing-versus-developed country's perspective.¹⁴ Avi-Yonah advocated simplification: following a comprehensive analysis of the source-versus-residence state, and the active-versus-passive income, distinctions, he proposed that “[a]ll individual taxpayers should be taxed by their country of residence on their active and passive income, from whatever source derived”.¹⁵ However, he added that “[a]ll publicly held corporations (MNEs) should be taxed exclusively on a source basis, with the source of income determined on a unitary basis by applying a consensus formula”.¹⁶ Moreover, Avery Jones¹⁷ raised the issue of “how to limit the impact on international transactions of the diversity of income tax laws”.¹⁸

⁸ Conventional wisdom – and, it has to be said, the [IBFD Treaties Collection](#) – bear witness to this fact.

⁹ Or, as it turns out, self-fulfilling prophecy?

¹⁰ J.F. Avery Jones, *The David R. Tillinghast Lecture: Are Tax Treaties Necessary?*, 53 *Tax Law Review* 1 (1999), p. 1, at p. 3.

¹¹ S. Wilkie et al., *Are (These) Tax Treaties Necessary?*, in *Essays on Tax Treaties: A Tribute to David A. Ward* (G. Maisto et al. (eds.)), IBFD and CTF 2012), p. 393, at pp. 395-407.

¹² Id., at p. 409. They tentatively ventured, however, the proposition that because tax treaties are “premised on how personal and commercial relations actually take place and [...] on a seemingly outmoded international trade paradigm”, and that “there is a prominent dimension of legal fiction supporting tax systems”, “tax treaties may facilitate or even promote behaviour that [...] in fact helps to separate taxable income from its real economic sources and, correspondingly, from the tax bases to which the income rightfully belongs”. Id., at pp. 407-408.

¹³ Easson, *supra* n. 4, at p. 625.

¹⁴ Id., at pp. 621-625.

¹⁵ Avi-Yonah, *supra* n. 3, at p. 1352.

¹⁶ Id., at p. 1353.

¹⁷ Avery Jones, *supra* n. 10, at pp. 3-7.

¹⁸ L. Burns, *Commentary*, 53 *Tax Law Review* 1 (1999), p. 39.

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In his riposte, Burns refloated the concept of “a model income tax law that recognizes that there will be different policy choices in the design of the income tax”.¹⁹

Vann discerned that “[o]ne panacea that is often advanced for the ills of the bilateral treaty is the multilateral tax treaty”.²⁰ He suggested that the Asia-Pacific region should pursue “a multilateral, institutional rather than a bilateral, textual mode for international tax change”.²¹ Avery Jones seemed to embrace this notion – or, at least, a variation thereof – and expanded its reach from the regional to the international level. He informed that his perusal of the [Nordic Convention](#) failed to “detect any difference between it and a series of bilateral treaties”.²² Nevertheless, this discovery did not dissuade him from wondering thus:

If the Nordic treaty can be regarded as a series of bilateral ones sewn together, can one not equally regard the OECD Model Treaty as a template for a multilateral web of treaties?²³

In reality, states “sign up to variations on the Model Treaty”.²⁴

This much is fair to say: tantalizing prospects for future research are raised. What are the solutions to these intriguing and seemingly intractable problems? Perceived against the basic tenets of tax treaties, the very existence of which is being challenged, can there ever be any viable alternatives?

The IBFD welcomes your feedback, which can be forwarded to Victor T. Chew at V.Chew@ibfd.org.

¹⁹ Id., at pp. 46-48. Burns agreed with Avery Jones that “given the diversity of tax laws, purely textual multilateralism is likely to achieve little more than what is currently achieved through the bilateral tax treaty network”. Id., at pp. 44-45.

²⁰ R.J. Vann, *A Model Tax Treaty for the Asian-Pacific Region? (Part II)*, 45 Bulletin for International Fiscal Documentation 4 (1991), p. 151, Journals IBFD.

²¹ Id., at p. 163.

²² Avery Jones, *supra* n. 10, at p. 6.

²³ Id.

²⁴ Id.