

# *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*

The relationship between EU law and double taxation conventions is usually approached assuming the existence of a conflict; rarely is the issue raised and accurately investigated whether or not EU law could assist in the interpretation of those conventions. In this paper, it is submitted that this can be the case where the interpretation of terms not defined in double taxation conventions is at stake. The conclusion drawn after investigation is that EU law can indeed play such a role according to article 31(3)(c) of the 1969 Vienna Convention on the Law of Treaties and/or to article 3(2) of the OECD Model Tax Convention on Income and on Capital. Some examples of possible applications of this approach are also proposed in this paper, particularly that of beneficial ownership, and one may expect that the continuing evolution of EU law will likely increase the number of relevant cases.

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“To believe is very dull. To doubt is intensely engrossing.”

Oscar Wilde

## 1. Introduction

The relationship between double taxation conventions (“DTCs”) and EU law is usually approached assuming the existence of a conflict, i.e. assuming that one legal provision should necessarily prevail over the other (“relationship of conflict”). Rarely is the issue raised and accurately investigated, whether or not one such provision could assist in the interpretation of the other (“relationship of interpretation”).<sup>1</sup> In this paper, it is submitted that EU law can sometimes assist in the interpretation of terms not defined in DTCs.

The argument made herein in no way is meant to negate the possibility that conflicts exist between DTCs and EU law. In several cases conflicts do exist and it is necessary to establish the appropriate normative hierarchy (i.e. to apply the appropriate conflict resolution mechanisms). This paper, however, is not intended to cover this aspect. Rather, the aim is to investigate whether or not, and to what extent, there could be in some cases a relationship of interpretation between DTCs and EU law.

The conclusion drawn after investigation is, in a nutshell, that a relationship of interpretation can indeed exist between DTCs and EU law, so that EU law can play a role in establishing the legal meaning of terms which are not defined in DTCs, according to article 31(3)(c) of the 1969 Vienna Convention on the Law of Treaties and/or to article 3(2) of the OECD Model Tax Convention on Income and on Capital.

## 2. Using EU Law To Interpret Undefined Tax Treaty Terms: Article 31(3)(c) of the VCLT

The interpretation of treaties between States, such as DTCs, is regulated by articles 31-33 of the 1969 Vienna Convention on the Law of Treaties (“VCLT”).<sup>2</sup> Those articles provide for

1. See UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law: Difficulties arising from the Diversification and Expansion of International Law*, found at [http://untreaty.un.org/ilc/texts/l\\_9.htm](http://untreaty.un.org/ilc/texts/l_9.htm), para. 2: “In applying international law, it is often necessary to determine the precise relationship between two or more rules and principles that are both valid and applicable in respect of a situation. For that purpose the relevant relationships fall into two general types:
  - Relationships of interpretation. This is the case where one norm assists in the interpretation of another. A norm may assist in the interpretation of another norm for example as an application, clarification, updating, or modification of the latter. In such situation, both norms are applied in conjunction; and
  - Relationships of conflict. This is the case where two norms that are both valid and applicable point to incompatible decisions so that a choice must be made between them. The basic rules concerning the resolution of normative conflicts are to be found in the VCLT.”
2. See, *ex multis*, G. Wetzel and D. Rauschnig, *The Vienna Convention on the Law of Treaties. Travaux Préparatoires*, Frankfurt, 1978, p. 534 et seq.; Vv.Aa., *Interpretation of tax treaties*. Transcript of the panel discussion of Seminar B at the IFA Congress in London held on 11 September 1985, in Bull. Intl. Fiscal Docn., p. 75 et seq. (1986), Journals IBFD ; K. Vogel and R.G. Prokisch, *General Report*, in Interpretation of double taxation convention, Cahiers de Droit Fiscal International, 1993, LXXVIIIa, p. 66 et seq.; M. Edwardes-Ker, *Tax Treaty Interpretation*, Dublin, 1995; K. Vogel, *On Double Taxation Conventions*, 3<sup>rd</sup> edition, London-The Hague-Boston, 1997, Introduction m.nos. 58 et seq. (p. 32 et seq.); P Baker, *Double Taxation Conventions*, London, (loose-leaf), Introductory Topics nn.m. E.01 et seq.; F.A. Engelen, *Interpretation of Tax Treaties under International law*, Amsterdam, 2004; N. Shelton, *Interpretation and application of tax treaties*, London, 2004, p. 195 et seq.; U. Linderfalk, *On The Interpretation of Treaties*, Dordrecht, 2007; R. Gardiner *Treaty Interpretation*, Oxford-New York, 2008; A. Orakhelashvili, *The Interpretation of Acts and Rules in Public International Law*, Oxford-New York, 2008, p. 308 et seq.; and M.E. Villiger, *Commentary on the 1969 Vienna Convention on the Law of Treaties*, Leiden-Boston, 2009, p. 415 et seq. See, among Italian scholars, S. Bariatti, *L’interpretazione dei convenzioni internazionali di diritto uniforme*, Padua, 1986, p. 201; and G. Melis, *L’interpretazione nel diritto tributario*, Padua, 2004, p. 601 et

rules of interpretation that by vast majority are regarded as international custom, i.e. general practice accepted as law.<sup>3</sup>

According to those rules, a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose. Article 31(2) lists a number of items which are *part of the context* and article 31(3) lists a number of items which are to be *taken into account, together with the context*. A special meaning shall be given to a term, if the parties so intended [article 31(4)].

Matters that are to be taken into account together with the context are, among others, “relevant rules of international law applicable in the relations between the parties” [article 31(3) (c) of the VCLT]. The attention devoted to this canon by courts and scholars has however been very limited over the years. The impression is that article 31(3)(c) is generally underestimated. This is true not only in international tax law, but in all fields of international law.<sup>4</sup>

Nonetheless, in the author’s view the significance of article 31(3)(c) of the VCLT to the interpretation of DTCs should be reexamined, especially considering that article 31(3)(c) of the VCLT could assign a significant role to EU law in the interpretation process of DTCs.

## 2.1. The scope of article 31(3)(c) of the VCLT

Article 31(3)(c) is found in the “general rule of interpretation” of treaties set forth by article 31 of the VCLT. The general rule reads as follows [emphasis added]:

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
  - (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
  - (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
3. *There shall be taken into account, together with the context:*
  - (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
  - (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
  - (c) *any relevant rules of international law applicable in the relations between the parties.*
4. A special meaning shall be given to a term if it is established that the parties so intended.

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seq.; Id., *L'interpretazione delle convenzioni internazionali in materia di imposte sul reddito e sul patrimonio*, in *Rassegna Tributaria* (1996), p. 98 et seq.

3. See UN International Law Commission, *Draft articles on the law of treaties between States and International organizations or between international organizations with commentaries*, 1982, in particular *General commentary to section 3*: “Draft articles 31, 32 and 33 below reproduce unchanged articles 31, 32 and 33 of the Vienna Convention. This is rendered possible by the fact that, in substance, these articles of the Convention are based on the fundamental characteristics of a consensus of wills (...).” See also ICJ and ECJ cases and scholars mentioned in D. Verwey, *The European Community, the European Union and the International Law of Treaties*, The Hague, 2004, p. 88; in S. Bariatti, *op. cit.*, p. 181 et seq.; and in T. Treves, *Diritto internazionale: problemi fondamentali*, Milan, 2005, p. 380. Accord, more recently, ECJ, Case C-344/04, *IATA e ELFAA*, para. 40.
4. See P. Sands, *Treaty, Custom and the Cross-fertilization of International Law*, in *Yale Human Rights & Development Law Journal* (1998), p. 95 and the international law cases mentioned therein. That scholar very clearly observes: “On its face, Article 31(3)(c) appears straightforward. Its actual meaning in practice, however, is difficult to know since it appears to have been expressly relied upon only very occasionally in judicial practice. It also seems to have attracted little academic comment. There appears to be a general reluctance to refer to Article 31(3)(c).”

The provision of article 31(3)(c) – the customary nature of which is uncontested<sup>5</sup> – establishes a mandatory part of the interpretation process: any relevant rules of international law applicable in the relations between the parties *must* be taken into account.<sup>6</sup> They are not, as contrasted with the provisions of article 32 on supplementary means of interpretation, only to be referred to where confirmation is required or the meaning is ambiguous, obscure or manifestly absurd or unreasonable.

Nevertheless, article 31(3)(c) is only a part of a larger interpretation process where all significant means are to be considered. Means covered under article 31(3)(c) could even, in the end, prove not to be appropriate in the light of the object and purpose of the treaty being interpreted.<sup>7</sup>

A breakdown of article 31(3)(c) reveals the following:

- *Rules of international law.* Reference should be made to rules of public international law,<sup>8</sup> including other treaties;<sup>9</sup>

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5. See, e.g., *Arbitral Award of 31 July 1989 (Guinea-Bissau v. Sen.)*, 53 I.C.J. (1991), p. 69. Recently, the ICJ reconfirmed the customary nature of Article 31(3)(c) in *Certain Questions of Mutual Assistance in Criminal Matters (Djib. v. Fr.)*, 37 I.C.J. (2008), available at <http://www.icj-cij.org/docket/files/136/14550.pdf>. Accord C. McLachlan, *The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention*, in *International and Comparative Law Quarterly* (2005), p. 279 et seq. (p. 293).
6. See the recent judgment by the ECtHR, *Demir and Baykara v. Turkey* [GC], no. 34503/97, 12 November 2008, where the Court clearly stated that Article 31(3)(c) VCLT imposes a legally binding obligation on the states parties: “The Court ... can and must take into account elements of international law other than the Convention ...” (para. 85). Accord P. Sands, *op. cit.*, p. 103; C. McLachlan, *op. cit.*, p. 290; R. Gardiner, *op. cit.*, p. 259.
7. This point is very well described by A. Orakhelashvili, *The Interpretation of Acts and Rules*, *op. cit.*, p. 366: “The mere presence of the ‘relevant rules’ of international law does not mean that they have to be applied as if they formed part of treaty relations. These rules are inherently capable of being excluded from bilateral relations by the parties to a treaty and any construction of the treaty by reference to those rules must duly respect this factor. If extraneous rules under Article 31(3)(c) were to warrant interpretation of the treaty in defiance of the outcome required under its text and object and purpose, the Vienna Convention would end up requiring mutually exclusive interpretative outcomes ...”.
8. R. Gardiner, *op. cit.*, p. 261: “it seems clear enough that the reference to ‘any relevant rules of international law’ in its context, and in the light of the object and purpose of a treaty on the law of treaties, takes one to public international law”.
9. C. McLachlan, *op. cit.*, p. 290; R. Gardiner, *op. cit.*, p. 261 et seq.; F.A. Engelen, *op. cit.*, p. 251; U. Linderfalck, *Who Are ‘The Parties’? Article 31, Paragraph 3(c) of the 1969 Vienna Convention and the ‘Principle of Systemic Integration’ Revisited*, in *Netherlands International Law Review* (2008), p. 343 et seq.; A. Orakhelashvili, *The Interpretation of Acts and Rules*, *op. cit.*, p. 366; and further references found therein. According to the UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, *op. cit.*, paras. 18 and 21: “Article 31 (3) (c) deals with the case where material sources external to the treaty are relevant in its interpretation. These may include other treaties, customary rules or general principles of law. (...) Article 31 (3) (c) also requires the interpreter to consider other treaty-based rules so as to arrive at a consistent meaning. Such other rules are of particular relevance where parties to the treaty under interpretation are also parties to the other treaty, where the treaty rule has passed into or expresses customary international law or where they provide evidence of the common understanding of the parties as to the object and purpose of the treaty under interpretation or as to the meaning of a particular term.” An authoritative confirmation of the statement that rules of international law should be meant to include also other treaties comes from the recent judgment by the ICJ on the *Case concerning Certain Questions of Mutual Assistance in Criminal Matters (Djibouti v. France)*, 4 June 2008, where the ICJ applied Article 31(3)(c) VCLT and interpreted a Convention on Mutual Assistance in Criminal Matters of 1986 – the alleged violation of which by France constituted the essence of Djibouti’s claim – in the light of a Treaty of Friendship and Co-operation concluded between the two parties in 1977. The ICJ used Article 31(3)(c) VCLT also in the *Oil Platforms* case to place a specific bilateral treaty within the broader context of general international law [Case concerning Oil Platforms (*Islamic Republic of Iran v. United States of America*), 6 November 2003, para. 41].

- *Relevance*. Reference should be made to subject matter, in the sense that rules of international law qualify as “relevant” when they touch on the same subject matter as the treaty provision(s) being interpreted or have indirectly an impact on that subject matter, such as in the case of general principles.<sup>10</sup> Conversely, relevance should not be intended in the sense that rules of international law qualify as “relevant” when they were originally conceived to be significant to the interpretation of the treaty in question;<sup>11</sup> if they had such a particular relationship, they would be covered under article 31(3)(a) of the VCLT as subsequent agreements between the parties regarding the interpretation of the treaty or the application of its provisions<sup>12</sup> and article 31(3)(c) would be rendered meaningless;
- *Applicability in the relations between the parties*. Reference should be made to legal character, that is, to instruments of international law legally binding upon the parties.<sup>13</sup> According to a recent judgment by the ECtHR, however, nothing prevents a court from also taking into account intrinsically non-binding instruments (such as recommendations and resolutions)<sup>14</sup> and treaties that have not been ratified by the respondent State<sup>15</sup> insofar as they “denote a continuous evolution in the norms and principles applied in international law or in the domestic law of the majority of [the parties] and show, in a precise area, that there is common ground in modern societies”;<sup>16</sup>
- *The parties*. It is not specified whether or not “relevant rules of international law” have to be binding on all parties to the treaty under interpretation in order to contribute to the process of its interpretation. The issue is much debated among international law scholars<sup>17</sup> and there is no clear-cut answer. A restrictive approach – i.e. rules of international law should be binding on all parties to the treaty – prevails in the few international decisions which dealt with the issue,<sup>18</sup> but several scholars have been submitting that a

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10. See P. Sands, *op. cit.*, p. 102; R. Gardiner, *op. cit.*, p. 260; F.A. Engelen, *op. cit.*, p. 254.
  11. UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, *op. cit.*, para. 18: “Article 31 (3) (c) deals with the case where material sources external to the treaty are relevant in its interpretation” (emphasis added). See also M.E. Villiger, *op. cit.*, p. 432: “any relevant rules of international law applicable in the relations between the parties (...) need have no particular relationship with the treaty”.
  12. Or eventually under Article 31(3)(b) VCLT as subsequent practices in the application of the treaty which establish the agreement of the parties regarding its interpretation.
  13. See UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, *op. cit.*, fn. 1: “That two norms are applicable in a situation means that they have binding force in respect to the legal subjects finding themselves in the relevant situation”. See also, e.g., P. Sands, *op. cit.*, p. 102.
  14. ECtHR, *Demir and Baykara v. Turkey*, *cit.*, para. 74. *Contra* C. McLachlan, *op. cit.*, p. 290, according to which “reference for interpretation purposes must be to rules of law, and not to broader principles or considerations which may not be firmly established as rules”; and A. Orakhelashvili, *The Interpretation of Acts and Rules*, *op. cit.*, p. 366, who argues that “Article 31(3)(c) covers only established rules of international law, to the exclusion of principles of uncertain or doubtful legal status, so-called evolving legal standards, policy factors or more generally related notions”.
  15. ECtHR, *Demir and Baykara v. Turkey*, *cit.*, para. 86.
  16. ECtHR, *Demir and Baykara v. Turkey*, *cit.*, para. 86. The ECtHR further pointed out (para. 78) that “in searching for common ground among the norms of international law it has never distinguished between sources of law according to whether or not they have been signed or ratified by the respondent State”.
  17. See U. Linderfalk, *Who Are ‘The Parties’?*, *op. cit.*, for a deep examination of the issue and for further references (the scholar finally defends the idea of the strictest possible interpretation of the term “parties” in Article 31(3)(c), as all parties to the interpreted treaty). See also R. Gardiner, *op. cit.*, p. 263 et seq.; F.A. Engelen, *op. cit.*, p. 253; A. Orakhelashvili, *The Interpretation of Acts and Rules*, *op. cit.*, p. 368 et seq.; D. French, *Treaty Interpretation and the Incorporation of Extraneous Legal Rules*, in *International and Comparative Law Quarterly* (2006), p. 281 et seq. (p. 307).
  18. See the GATT panel in *United States-Restrictions on Imports of Tuna*, DS29/R, 16 June 1994, para 5.19; and the WTO panel in *Measures Affecting the Approval and Marketing of Biotech Products* WT/DS291/R, WT/DS292/R, WT/DS293/R (known as “EC Biotech”), 29 September 2006.

less restrictive approach is appropriate, so that “the parties” should be intended as “the two or more parties to a specific dispute concerning the interpretation or application of a treaty”<sup>19</sup> – i.e. rules of international law should be binding only on the parties to the dispute –; the recent findings by the ECtHR, as mentioned above, could to some extent support this less restrictive approach;

- *Inter-temporal issues.* An overview of the drafting history of article 31(3)(c)<sup>20</sup> gives credence to the view that article 31(3)(c) of the VCLT was originally intended to serve as a means to foster the inter-temporal rejuvenation of treaty provisions.<sup>21</sup> This view is supported by the case law of the ICJ and the ECtHR and by most legal scholars.<sup>22</sup> Therefore, “relevant rules of international law” should also be meant to embrace norms that were not applicable at the time of the conclusion of the treaty. In particular, rules of international law enacted subsequent to the treaty may be taken into account “especially where the concepts used in the treaty are open or evolving. This is the case, in particular, where: (a) the concept is one which implies taking into account subsequent technical, economic or legal developments; (b) the concept sets up an obligation for further progressive development for the parties; or (c) the concept has a very general nature or is expressed in such general terms that it must take into account changing circumstances”.<sup>23</sup>

The examination undertaken above reveals that article 31(3)(c) of the VCLT can operate “like a ‘master-key’ to the house of international law”<sup>24</sup> and favour systemic integration, i.e.

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19. A most qualified opinion supporting this view is that of the UN International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, Report of the Study Group of the International Law Commission finalized by M. Koskenniemi, found at [http://untreaty.un.org/ilc/texts/1\\_9.htm](http://untreaty.un.org/ilc/texts/1_9.htm), para. 472: “a better solution is to permit reference to another treaty provided that the parties in dispute are also parties to that other treaty”.
  20. See, in this respect, P. Merkouris, *Debating the Ouroboros of International Law: The Drafting History of Article 31(3)(c)*, in *International Community Law Review* (2007), p. 1 et seq. See also R. Gardiner, *op. cit.*, p. 256 et seq.; F.A. Engelen, *op. cit.*, p. 242 and p. 254 et seq.; C. McLachlan, *op. cit.*, p. 291 et seq.; U. Linderfalck, *Who Are ‘The Parties?’*, *op. cit.*, p. 358 et seq.; J. Klabbers, *Reluctant Grundnormen: Articles 31(3)(c) and 42 of the Vienna Convention on the Law of Treaties and the Fragmentation of International Law*, in Craven et al. (eds), *Time, History and International Law*, Leiden, 2007, p. 141 et seq. (p. 143-48).
  21. V.P. Tzevelekos, *The Use of Article 31(3)(C) of the VCLT in the Case Law of the ECtHR: An Effective Anti-Fragmentation Tool or a Selective Loophole for the Reinforcement of Human Rights Teleology? Between Evolution and Systemic Integration*, in *Michigan Journal of International Law* (2010), p. 633.
  22. Please refer to the scholars quoted in previous footnotes and to references found therein both to other scholars and to several international cases supporting this view. A significant statement is, in particular, that of the UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, *op. cit.*, para. 22, according to which “International law is a dynamic legal system. A treaty may convey whether in applying article 31 (3) (c) the interpreter should refer only to rules of international law in force at the time of the conclusion of the treaty or may also take into account subsequent changes in the law. Moreover, the meaning of a treaty provision may also be affected by subsequent developments, especially where there are subsequent developments in customary law and general principles of law. The traditional rule was stated by Judge Huber in the *Island of Palmas* case (the *Netherlands v. United States of America*) Award of 4 April 1928, UNRIIAA, vol. II, p. 829, at p. 845, in the context of territorial claims: ‘... a juridical fact must be appreciated in the light of the law contemporary with it, and not the law in force at the time when a dispute in regard to it arises or fails to be settled ... The same principle which subjects the act creative of a right to the law in force at the time the right arises, demands that the existence of the right, in other words, its continued manifestations, shall follow the conditions required by the evolution of law’.”
  23. UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, *op. cit.*, para. 23.
  24. UN International Law Commission, *Fragmentation of International Law*, *op. cit.*, para. 420. The metaphor is well explained by C. McLachlan, *op. cit.*, p. 281: “Mostly the use of individual keys will suffice to open the door to a particular room. But, in exceptional circumstances, it is necessary to utilize a master-key which permits access to all of the rooms. In the same way, a treaty will normally be capable of interpretation and

a process of interpretation which acknowledges that all international law exists in systemic relationship with other law, so that although a tribunal may only have jurisdiction in regard to a particular instrument, it should always interpret and apply that instrument in its relationship to its normative environment – that is, “other” international law.<sup>25</sup>

Whether or not article 31(3)(c) of the VCLT can legitimize EU law to actually contribute to establishing the legal meaning of terms which are not defined in DTCs, however, has not been answered yet and will be investigated in the forthcoming sub-sections.

## 2.2. EU law as part of international law

EU law could contribute to the interpretation of DTCs according to article 31(3)(c) of the VCLT if, first of all, its rules could be regarded as rules of international law.

In this respect, there is no unanimous opinion among scholars, who basically hold two different positions. On the one hand, certain scholars maintain that the European Community (and European Union) has been giving rise to a *sui generis* legal order that does not fit in the traditional dichotomy between (federal) states and international organizations; accordingly, rules of EU law would be something other than rules of international law.<sup>26</sup> On the other hand, certain scholars hold that no matter how *sui generis* the European Community (and European Union) might be, it is still an international organization; hence, rules of EU law would be rules (also) of international law.

The latter position definitely is, to date, the prevailing one.<sup>27</sup>

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application according to its own terms and context. But in hard cases, it may be necessary to invoke an express justification for looking outside the four corners of a particular treaty to its place in the broader framework of international law (...).”

25. UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, op. cit., para. 17; Id., *Fragmentation of International Law*, op. cit., para. 423. See also B. Simma, *Universality of International Law from the Perspective of a Practitioner*, in European Journal of International Law (2009), p. 289; and P. Sands, op. cit., p. 95, who affirms that “Article 31(3)(c) VCLT ‘reflects a ‘principle of integration’. It emphasizes both the ‘unity of international law’ and the sense in which rules should not be considered in isolation of general international law.’” According to V.P. Tzevelekos, op. cit., Article 31(3)(c) VCLT can operate like an “anti-fragmentation tool”.
26. See, for instance, S. Douglas Scott, *Constitutional Law of the European Union*, London, 2002, p. 260; J.H.H. Weiler U.R. Haltern, *Constitutional or International? The Foundations of the Community Legal Order and the Question of Judicial Kompetenz-Kompetenz*, in: Slaughter-Stone Sweet-Weiler (eds), *The European Courts and National Courts – Doctrine and Jurisprudence*, Oxford-Evanston, 1998, p. 342; P. Pescatore, *Le droit de l’intégration. Emergence d’un phénomène nouveau dans les relations internationales selon l’expérience des Communautés européennes*, Dordrecht, 1972. This theory basically moves from the Guggenheim’s aspiration that supranational European institutions open the door for the development of jus publicum europeum which exists alongside national and international legal systems – an autonomous system of new European law (P. Guggenheim, *Das jus publicum europeum und Europa*, in *Jahrbuch des Öffentlichen Rechts der Gegenwart* (1954), p. 10 et seq.).
27. See B. De Witte, *European Union Law: How Autonomous is its Legal Order?*, in *Zeitschrift für Öffentliches Recht* (2010), p. 141 et seq.; A. Orakhelashvili, *The Idea of European International Law*, in *European Journal of International Law* (2006), p. 315 et seq. (at p. 345); R. Barents, *The Autonomy of Community Law*, The Hague, 2004, p. 192; P.M. Dupuy, *L’unité de l’ordre juridique international*, Académie de Droit International, Recueil des cours, Volume 297, 2002, p. 438; E. Denza, *The Intergovernmental Pillars of the European Union*, Oxford, 2002; J. Klabbers, *The Changing Image of International Organizations*, in: Coicaud-Heiskanen (eds), *The Legitimacy of International Organizations*, Tokyo, 2001, p. 224; Id., *Presumptive Personality: The European Union in International Law*, in Koskenniemi (ed.), *International Law Aspects of the European Union*, The Hague, 1997, p. 231 et seq.; A. Pellet, *Les fondements juridiques internationaux du droit communautaire*, in *Collected Courses of the Academy of European Law*, Vol. V, Book 2, 1994, p. 193, and seemingly UN International Law Commission, *Fragmentation of International Law*, op. cit., para. 219. Accord, among Italian scholars, B. Conforti, *Diritto internazionale*, Naples, 2006, p. 148;

A thorough analysis of the topic was recently carried out by De Witte. He observed<sup>28</sup> that “It is true that the ECJ has repeatedly stated that ‘the EEC Treaty has created its own legal system’, or similar language, but it did not add that this legal system was situated outside the scope of international law. In its famous early judgments *Van Gend en Loos* and *Costa v. ENEL*,<sup>29</sup> the European Court sought to differentiate the EEC Treaty from ‘other’ or ‘ordinary’ international treaties, but that otherness was not expressly held to mean that the EEC Treaty had created something else than an international organization.<sup>30</sup> (...) In *Kadi*,<sup>31</sup> which is rightly hailed as a strong confirmation of the autonomy of EC law, the ECJ discussed what it called ‘the relationship between the international legal order under the United Nations and the Community legal order’, and although this formula might suggest that the Community legal order is not one of international law, it does not actually say this, and the outcome of the case did not depend on the legal qualification of the EC. (...) it is hard to conclude, as some authors have done, that the *Kadi* judgment conveys a ‘strong and consistent dualist approach’ in the relation between EU law and (the rest of) international law”. De Witte also noted<sup>32</sup> that “the prevalent view, from the perspective of national constitutional law, seems to be that the EC and EU are indeed creatures of international law and therefore international organizations, and that State sovereignty has not been abandoned or entirely transferred but rather is being ‘exercised in common’ within the framework of the EU”. De Witte thus concluded that EU law is still part of international law and laconically affirmed: “the autonomy of the special legal order which the EU member states have decided to carve out by using the instrument of ... an international treaty”.

Several other scholars examined the issue and concluded in favour of the thesis that EU law is part of international law. Among many, Dupuy very effectively maintained<sup>33</sup> that “Il ne faut pas se cacher qu’il y a eu à la querelle sur la nature juridique du droit communautaire un arrière-plan idéologique et une confrontation de cultures juridiques. Pour s’en tenir à l’idéologie, la volonté de souligner le caractère radicalement novateur de la construction européenne a incité certains commentateurs à trahir notamment le sens de la jurisprudence communautaire (*Van Gend en Loos* et *Costa v. ENEL*). Or, la technique juridique est une chose, l’idéologie devrait en être une autre. On peut en tout cas être un Européen convaincu et reconnaître la réalité juridique de l’articulation du droit communautaire au droit international. (...) on doit donc reconsidérer sans dogmatisme la situation juridique exacte du droit communautaire et des institutions qu’il anime par rapport au droit international public; et l’on constatera qu’il demeure très certainement soumis à ce dernier, notamment si on compare sa situation avec celle que l’ordre juridique interne de chaque Etat souverain entretient

U. Draetta, *Elementi di diritto dell’Unione Europea, Parte istituzionale*, Milan, 2009, p. 45 et seq.; F. Pocar, *Diritto dell’Unione Europea*, Milan, 2010, p. 1 et seq.; G. Gaja, *Introduzione al diritto comunitario*, Rome-Bari, 2005, p. 7 et seq.; P. Fois, *Il diritto dei trattati. Raccolta di scritti*, Naples, 2009, p.383 et seq.; scholars quoted in A. Gianelli, *Unione Europea e diritto internazionale consuetudinario*, Turin, 2004, p. 155, fn. 85; and seemingly R. Adam and A. Tizzano, *Lineamenti di diritto dell’Unione Europea*, Turin, 2010, p. 24.

28. B. De Witte, *op. cit.*, pp. 147 and 154.  
 29. ECJ, Case 26/62, *Van Gend en Loos*; and Case 6/64, *Costa v. ENEL*.  
 30. De Witte also acknowledged that, however, AG Póiares Maduro affirmed that the ECJ, in *Van Gend en Loos*, had considered the EEC Treaty to form a new legal order which was “beholden to, but distinct from the existing legal order of public international law” (see Opinion of 23 January 2008, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat v. Council*, para. 21).  
 31. ECJ, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat v. Council*. The *Kadi* judgment triggered an extensive debate among international law scholars, part of which is reflected in the articles and contributions quoted in the present paper.  
 32. B. De Witte, *op. cit.*, p. 148.  
 33. P.M. Dupuy, *op. cit.*, p. 438 and fn. 870.



avec ce même droit international. La base conventionnelle des Communautés comme de l'Union, la personnalité juridique internationale de la Communauté européenne, celle de l'Union européenne, l'organisation des rapports du droit communautaire avec le droit international et les conditions d'application de ce dernier par les instances juridictionnelles de la Communauté permettent de parvenir, sans équivoque, à un tel constat; cela, sans négliger ni la grande originalité ni le degré particulièrement élevé de développement et d'autonomie de l'ordre juridique communautaire, que nul ne saurait nier.”<sup>34</sup>

Furthermore, Orakhelashvili held<sup>35</sup> that “the system of European Union law is there because it is based on treaties which are sources of international law, and further specified and developed by institutions which are organs of an international organization whose every feature is due to international law factors. (...) EU law is part of international law and its operation is subject to compliance with international law. The European Union can exercise the extensive powers delegated to it by Member States but every such exercise is subject to compliance with the relevant international legal norms. In relation to international law, EU law forms a complex system of *lex specialis* – a quite explainable phenomenon in terms of traditional principles and categories of international law. (...) As it is not exclusive in relation to the rest of international law, the law of the European Union does not give rise to any system of European international law.”

In the light of the above, there seems to be no reason why rules of EU law should not be regarded as rules of international law for the purposes of article 31(3)(c) of the VCLT. Thus, the author's view is that rules of EU law can be significant to the interpretation of DTCs pursuant to article 31(3)(c) of the VCLT.<sup>36</sup>

This conclusion holds true even if one adheres to pluralist approaches to the relationship between legal orders that are progressively emerging among international law scholars. Pluralist approaches, together with their opposites (i.e. constitutionalist approaches), are increasingly establishing themselves, so that the monism/dualism discussion is being

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34. Unofficial translation by the author: “One can not hide that there has been an ideological confrontation of legal cultures in the dispute on the legal nature of European law. The desire to emphasize the innovative character of the European system has led some authors to follow the ideology and fail the sense of the European jurisprudence (*van Gend en Loos* and *Costa v. ENEL*). Now, the legal technique is one thing, the ideology should be another. One can certainly be a convinced European and recognize the legal truth of European law as an articulation of international law. [...] One must therefore reconsider, without dogmatism, the exact legal status of European law and its institutions in relation to public international law; and she will see that the former is certainly subject to the latter, especially if one compares its status with that of the domestic law of each State with international law. The conventional basis of the Communities and of the Union, the international legal personality of the European Community, that of the European Union, the organization of relationships of European law with international law and the conditions for the application of the latter by the courts of the Community, lead unequivocally to such a conclusion; this, without denying the great originality and the very high degree of development and autonomy of the Community legal order, that nobody can negate.”

35. A. Orakhelashvili, *The Idea of European International Law*, *op. cit.*, p. 345 et seq.

36. This conclusion is apparently shared, at least in principle, by F.A. Engelen, *op. cit.*, p. 436, who affirms that: “The rule laid down in Article 31(3)(c) VCLT reflects the basic principle that a tax treaty, as well as any other treaty, cannot be seen in isolation from the other rules of international law applicable in the relations between the contracting States. (...) In the relations between EU Member States, for example, the rules of primary and secondary EC law may assume particular importance in this respect. Indeed, when a tax treaty is open to two constructions one of which does and the other does not conflict with the obligations of the contracting States under EC law, good faith demands that the latter construction be adopted”.

replaced by a constitutionalism/pluralism debate.<sup>37</sup> The doctrines of monism and dualism<sup>38</sup> are increasingly regarded as outdated and inadequate for a proper reflection on the relationships between legal systems, while constitutionalism and pluralism are more and more often considered to better explain that relationship. The two new approaches are explained by De Búrca as follows: “*constitutionalist approaches to the international order advocate some form of systemic unity, with an agreed set of basic rules and principles to govern the global realm [a sort of international constitution]*”;<sup>39</sup> “[*p*]luralist approaches ... emphasize the existence of a multiplicity of distinct and diverse normative systems, and the likelihood of clashes of authority-claims and competition for primacy amongst these”.<sup>40</sup>

Since constitutionalism assumes that only one legal order exists, formed by all rules of law (either from EU, international or national sources of law) and headed by a sort of international constitution,<sup>41</sup> there seems to be no reason why under this approach rules of EU law should not be regarded as rules of international law for the purposes of article 31(3)(c) of the VCLT. Therefore, the conclusion drawn above would be confirmed even adhering to constitutionalism.

Pluralism instead assumes that more legal orders exist (i.e. EU law, international law, national law, etc.), each legal order forming a normative system which is not “*a normative universe, but is, rather, an element in a normative pluriversum*”.<sup>42</sup> If this approach is followed,

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37. For an overview see R.A. Wessel, *Reconsidering the Relationship between International and EU Law: Towards a Content-Based Approach?*, in E. Cannizzaro, P. Palchetti and R.A. Wessel (eds), *International Law as Law of the European Union*, Leiden-Boston, 2011, p. 7 et seq.; P. Eeckhout, *The Growing Influence of European Union Law*, in *Fordham International Law Journal* (2011), p. 1490 et seq.; G. De Búrca, *The European Court of Justice and the International Legal Order After Kadi*, in *Harvard International Law Journal* (2010), p. 1 et seq.; W. Twining, *Normative And Legal Pluralism: A Global Perspective* (The Seventh Annual Herbert L. Bernstein Memorial Lecture in International and Comparative Law as held at Duke University School of Law April 7, 2009), in *Duke Journal of Comparative & International Law* (2010), p. 473 et seq.; A. Von Bogdandy, *Pluralism, Direct Effect, and the Ultimate Say: On the Relationship Between International and Domestic Constitutional Law*, in *International Journal of Constitutional Law* (2008), p. 397 et seq.; B. Kingsbury, *The International Legal Order*, New York University School of Law Public Law & Legal Theory Research Paper Series Working Paper No. 01-04 and Institute for International Law and Justice Working Paper No. 2003/1, available at <http://ssrn.com/abstract=692626>.
  38. “Monism/dualism relates to the ‘validity’ (or existence) of international norms in [domestic legal] orders. In monist systems, international norms enjoy automatic validity, whereas in dualist systems, they need to be transferred into domestic law in order to become valid” (R.A. Wessel, *op. cit.*, p. 13).
  39. G. De Búrca, *op. cit.*, p. 12. De Búrca further explains that: “The strongest versions of constitutionalism propose an agreed hierarchy among such rules to resolve conflicts of authority between levels and sites. Soft constitutionalist approaches assume the existence of an international community, posit the need for common norms and principles for addressing conflict, and emphasize the possibility of universalization.”
  40. G. De Búrca, *op. cit.*, p. 12. De Búrca further explains (p. 33-34) that: “what joins pluralist approaches to the international legal order is the significance they ascribe to the existence of a multiplicity of distinct and diverse normative systems and the likelihood of clashes of authority-claims and competition for primacy in specific contexts. ... Rather than advocating coordination between legal systems, they promote agonistic, ad hoc, pragmatic, and political processes of interaction. Pluralist approaches applaud this diversity, competition, and lack of coordination as being more likely to lead to a healthy degree of global accountability.”
  41. In an EU perspective, constitutionalism has been construed in the sense that primary EU law forms the international constitution, so that “it is no longer exclusively the EU Member States’ national legal systems that determine how the decisions of international organizations are implemented and which legal rank they have in their domestic legal order, but rather [...] the European legal order which supersedes and thus replaces this function of the national legal orders.” (N. Lavranos, quoted in R.A. Wessel, *op. cit.*, p. 24, fn. 64). This is perhaps derived from the statement by the ECJ in *Kadi* (Joined Cases C-402/05 P and C-415/05 P, quoted above) that “the obligations imposed by an international agreement cannot have the effect of prejudicing the constitutional principles of the EC Treaty, which include the principle that all Community acts must respect fundamental rights.” (para. 285).
  42. A. Von Bogdandy, *op. cit.*, p. 401.

the conclusion that EU law can be significant to the interpretation of DTCs under article 31(3)(c) of the VCLT could appear to be invalid; one could argue that EU law is a normative system other than international law. Such an objection, however, is very formalistic and forgets that the VCLT was concluded in 1969, when pluralism was not even considered and EU law still was very embryonic. Article 31(3)(c) of the VCLT should be interpreted in good faith and in the light of its object and purpose and, if this is made, one would acknowledge that the key aspect of that provision does not lie in the term “international” but rather lies in the term “applicable in the relations between the parties”, which is valid for rules of EU law when “the parties” are EU Member States. Hence, even if pluralism is preferred to construe the relationship between legal orders, rules of EU law would still be significant to the interpretation of DTCs pursuant to article 31(3)(c) of the VCLT.

### **2.3. What DTCs? DTCs concluded between Member States**

After having established that rules of EU law can be regarded as rules of international law under article 31(3)(c) of the VCLT and, therefore, can contribute to the interpretation of DTCs, one should investigate what DTCs must be interpreted taking into account EU law.

In this respect, note that article 31(3)(c) of the VCLT refers to rules which are “applicable in the relations between the parties”, thus it appears that EU law must be taken into account only when the interpretation of DTCs concluded between Member States is at stake. There seems to be no room, conversely, to maintain that EU law must be considered to interpret DTCs concluded between a Member State and a third country or DTCs concluded between third countries.

In conclusion, it is submitted that, under article 31(3)(c) of the VCLT, EU law must be taken into account in the interpretation only of DTCs concluded between Member States.

### **2.4. What rules of EU law? Primary versus secondary sources of EU law**

The analysis of the possible significance of EU law to the interpretation of DTCs deserves further considerations. There are many sources of EU law, and it could well be that not all of them qualify as “rules applicable in the relations between the parties”.

Sources of EU law are generally classified as primary sources and secondary sources. The former are meant to be acts adopted by Member States in their capacity as “constituent authority” (the founding Treaties) and general principles of EU law. The latter are intended as all acts however adopted by institutions and bodies of the European Union (such as regulations, directives, agreements between the Union and third countries or international organizations) and can be further distinguished between binding acts (for instance, regulations) and non-binding acts (for instance, recommendations and opinions).

The fact that Member States are liable for breaches of EU law not only vis-à-vis the Union (i.e. the other Member States), but also vis-à-vis individuals,<sup>43</sup> does not seem to prevent

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43. The ECJ has repeatedly held that the principle of liability on the part of a Member State for damage caused to individuals as a result of breaches of EU law for which the State is responsible is inherent in the system of the Treaty (*see, ex multis*, Joined Cases C-6/90 and C-9/90, *Francovich and Others*, para. 35; Joined Cases C-46/93 and C-48/93, *Brasserie du Pêcheur and Factortame*, para. 31; Case C-392/93, *British Telecommunications*, para. 38; Case C-5/94, *Hedley Lomas*, para. 24; Joined Cases C-178/94, C-179/94, C-188/94, C-189/94 and C-190/94, *Dillenkofer and Others*, para. 20, Case C-127/95 *Norbrook Laboratories*, para. 106).

sources of EU law from qualifying as “rules applicable in the relations between the parties”: there is no requirement that rules be applicable *only* in the relations between the parties.

Furthermore, the fact that the implementation of EU law can be enforced by institutions and bodies that have a certain degree of independence from the parties, does not seem to prevent sources of EU law from qualifying as “rules applicable in the relations between the parties”: there is no requirement that rules be necessarily *enforceable* by (one or more of) the parties.

Having said that, it appears that all binding sources of EU law can qualify as “rules applicable in the relations between the parties”. Member States are in fact liable for breaches of binding sources of EU law vis-à-vis the Union, i.e. vis-à-vis the other Member States. Considering that applicability in the relations between the parties should be meant to legal character, in the sense that sources of law should be binding upon the parties (*see* section 2.1 above), one should conclude that all binding sources of EU law are “applicable in the relations between the parties” and thus relevant under article 31(3)(c) of the VCLT.<sup>44</sup>

Still, nothing theoretically prevents a court from taking into account also non-binding sources (following the ECtHR approach mentioned above<sup>45</sup>). With particular regard to EU recommendations, one can even try to extend the *Grimaldi* doctrine to the interpretation of DTCs and argue that courts must take those recommendations into account.<sup>46</sup>

Directives, which are most commonly used in the tax field, should be regarded as binding instruments under the above classification, since there are no doubts that directives by their nature impose obligations on Member States<sup>47</sup> and that the Member States’ obligation to achieve the results envisaged by directives and to take all appropriate measures, whether general or particular, to ensure the fulfilment of that obligation, is binding on all authorities of Member States.<sup>48</sup> The binding force of directives is enduring even after their transposition into national law by Member States: national courts are required to interpret the provisions of national law specifically introduced to implement a directive, in the light of the wording

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44. This conclusion is apparently shared by F.A. Engelen, *op. cit.*, p. 436, who affirms that “Article 31(3)(c) VCLT reflects the basic principle that a tax treaty (...) cannot be seen in isolation from the other rules of international law applicable in the relations between the contracting State. (...) In the relations between EU Member states, for example, the rules of primary and secondary EC law may assume particular importance in this respect.” (emphasis added)

45. ECtHR, *Demir and Baykara v. Turkey*, cit., para. 74.

46. In Case C-322/88, *Grimaldi*, paras. 16, 18 and 19, the ECJ stated that “there is no reason to doubt that the measures in question are true recommendations, that is to say measures which, even as regards the persons to whom they are addressed, are not intended to produce binding effects. Consequently, they cannot create rights upon which individuals may rely before a national court. (...) However, ... it must be stressed that the measures in question cannot therefore be regarded as having no legal effect. (...) [N]ational courts are bound to take those recommendations into consideration in order to decide disputes submitted to them, in particular where they are capable of casting light on the interpretation of other provisions of national or Community law”.

47. *See, ex multis*, ECJ, Case 148/78, *Pubblico Ministero v. Ratti*, para. 46.

48. ECJ, Case 14/83, *von Colson and Kamann v. Land Nordrhein-Westfalen*, para. 26; Case C-106/89, *Marleasing*, para. 8; Case C-334/92, *Wagner Miret v. Fondo de Garantia Salarial*, para. 20; Case C-91/92, *Faccini Dori*, para. 26.

and the purpose of the directive<sup>49</sup> and consistently with possible interpretations already given by the ECJ in previous case law.<sup>50</sup>

Given the above, any objection that EU directives should not be regarded as binding instruments for the purposes of article 31(3)(c) of the VCLT – by arguing, for instance, that directives are binding on Member States only as to the results to be achieved<sup>51</sup> and are not directly applicable<sup>52</sup> (unless their provisions are capable of having direct effects<sup>53</sup>) – should be rejected. Any such objection should also be rejected because the non-direct applicability of EU directives does not concern the relations between Member States, but insists only on the direct applicability for individuals against Member States.

In conclusion, it is submitted that all sources of EU law can be significant to the interpretation of DTCs pursuant to article 31(3)(c) of the VCLT and that EU directives, in particular, should be taken into account as binding instruments applicable in the relations between the parties. The fact that rules of EU law were not originally conceived to be significant to the interpretation of DTCs does not prevent this conclusion, since “article 31(3)(c) deals with the case where material sources external to the treaty are relevant in its interpretation”<sup>54</sup> and “any relevant rules of international law applicable in the relations between the parties (...) need have no particular relationship with the treaty”<sup>55</sup> (see also section 2.1 above).

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49. ECJ, Case 14/83, *von Colson and Kamann*, cit., para. 26; Case C-106/89, *Marleasing*, cit., para. 8; Case C-334/92, *Wagner Miret*, cit., para. 20; Case C-91/92, *Faccini Dori*, cit., para. 26. For instance, the ECJ has often stated that the nature of a tax, duty or charge must be determined, under Community law, irrespective of its classification under national law (Case 295/84, *Rousseau Wilmot v. Organic*; Case C-200/90, *Dansk Denkavit and Poulsen Trading v. Skatteministeriet*; Joined Cases C-197/94 and C-252/94, *Bautiaa and Société française maritime*, para. 39; C-294/99, *Athinaiki Zithoptia*, para. 27) and it is settled case-law that the exemptions provided for in the VAT Directive have their own independent meaning in EU law and must be given a Community definition (Case 348/87, *Stichting Uitvoering Financiële Acties v. Staatssecretaris van Financiën*, para. 11; Case C-453/93, *Bulthuis-Griffioen v. Inspecteur der Omzetbelasting*, para. 18, and Case C-2/95, *SDC v. Skatteministeriet*, para. 21).
  50. The ECJ is in fact competent to interpret EU law (see, *ex multis*, Case 155/73, *Sacchi*; Case 111/75, *Mazzalai*; Case C-231/89, *Gmurzynska-Bscher*; and Joined Cases C-428/06 to C-434/06, *UGT-Rioja and Others*) and the interpretation given by the ECJ of a provision of EU law clarifies and defines its meaning and scope (*ex multis*, Case C-35/97, *Commission v. France*, para. 46; and C-481/99, *Georg Heininger and Helga Heininger*, para. 51).
  51. It is established case law, that the obligation imposed upon Member States to transpose directives into national legislation makes these States responsible for the consequences of their failure to do so (see, *ex multis*, ECJ, Joined Cases C-6/90 and C-9/90, *Francoovich and Others*, para. 35).
  52. Directives must in fact be first transposed into national law. This obligation follows from Art. 4(3) EU and Art. 288(3) TFEU, which impose upon Member States, according to the ECJ (Case C-129/96, *Inter-Environment Wallonie v. Région Wallonne*), an obligation not to take any measure liable seriously to compromise the result prescribed in the directive. However, “the liability of a Member State by reason of incorrect transposition ... is conditional on a finding of manifest and serious disregard by that State for the limits set on its discretion” (ECJ, Case C-278/05, *Robins*, para. 75).
  53. The ECJ has consistently held that it is necessary to examine whether the nature, general scheme and wording of the provision in question are capable of having direct effects (Case 41/74, *Van Duyn*, para. 12) and that wherever the provisions of a directive appear, so far as their subject-matter is concerned, to be unconditional and sufficiently precise, they may be relied upon by an individual against the Member State concerned, i.e. they have direct effects (see, *ex multis*, Case 8/81, *Becker*; Joined Cases 231/87 and 129/88, *Carpaneto Piacentino*; Case 194/94, *CIA Security Int.*; Case 188/95, *Fantask*; Case 56/98, *Modelo*).
  54. UN International Law Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law*, op. cit., para. 18.
  55. M.E. Villiger, op. cit., p. 432.

### **2.5. What rules of EU Law qualify as “relevant”? Rules concerning the taxes to which the convention applies or any rules of EU law?**

Since article 31(3)(c) of the VCLT requires that relevant rules of international law be taken into account, it is essential to establish what rules of EU law qualify as “relevant” in respect of DTCs.

Considering that relevance should be construed in terms of subject matter (*see* section 2.1. above), the interpreter should be led by the objective scope of DTCs. So, for instance, when DTC provisions affecting taxes on income are at issue, rules of EU law dealing with income tax should be considered to be “relevant”. This approach is consistent with the idea that only rules touching on the very same field of tax law as the DTC provision(s), or indirectly having an impact on that field of tax law, must be referred to under article 31(3)(c) of the VCLT.<sup>56</sup>

Nevertheless, nothing theoretically prevents a court from also considering provisions in other fields of EU law, insofar as they are consistent with the object and purpose of the DTC under interpretation. In particular, a court may find it useful to consider other provisions of EU tax law, such as provisions found in the VAT directive; still, those provisions should rarely be relied on, since they do not qualify as “relevant” under article 31(3)(c) of the VCLT.

In conclusion, it is submitted that rules of EU law dealing with the taxes covered by the DTC provisions at issue, *must* be taken into account under article 31(3)(c) of the VCLT and evaluated in the light of the DTC’s object and purpose. Conversely, other rules of EU law should rarely be relied on, although they could theoretically be used if appropriate in the light of the DTC’s object and purpose.

### **2.6. What rules of EU law? Inter-temporal issues**

It has been observed already under section 2.1., that article 31(3)(c) of the VCLT should be intended to serve as a means to foster the inter-temporal rejuvenation of treaty provisions, so that it should be meant to embrace norms that were not applicable at the time of conclusion of the treaty. This being said, it is submitted that EU legislation in force at the time the DTC is applied should be taken into account for the interpretation of that DTC.<sup>57</sup>

Nevertheless, if making reference to EU legislation in force at the time the DTC is applied can lead to violation of the principle of good faith – which is the basis for the law of treaties

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56. This approach mirrors, to some extent, the statement of the ECJ in *FCE Bank* that “the OECD Convention is irrelevant since it concerns direct taxation whereas VAT is an indirect tax” (Case C-210/04, *FCE Bank plc*, para. 39). The AG Philippe Léger, in his opinion delivered on 29 September 2005 on the very same case, similarly concluded that the OECD MC is based on principles that are not compatible with the European system of VAT (para. 64). Note that the ECJ went further in Joined Cases C-338/08 and C-339/08, *Ferrero & General Beverage*, and basically affirmed that DTCs are not decisive in the interpretation of EU law (para. 27: “the fact that the bilateral convention specifically categorises the refund of the adjustment surtax as ‘dividends’ in Article 10(5) is not decisive for how it is to be classified under European Union law”). This, however, does not contradict the conclusion drawn above, which does not regard the relevance of DTCs in the interpretation of EU law but rather regards the opposite case, i.e. the relevance of EU law in the interpretation of DTCs.

57. This conclusion, that regards a very technical field of law (i.e. tax law), seems to be consistent with the statement of the UN International Tax Commission, *Conclusions of the work of the Study Group on the Fragmentation of International Law, op. cit.*, para. 23, according to which rules of international law subsequent to the treaty may be taken into account especially where “the concept is one which implies taking into account subsequent technical, economic or legal developments (...)”.

and their interpretation<sup>58</sup> and prevents the States from profiting from a term the meaning of which is ambiguous<sup>59</sup> – one should ignore that legislation and refer to a different meaning as required by the object and purpose of the DTC.

Generally, one should never forget that article 31(3)(c) is only a part of a larger interpretation process where all significant instruments are to be considered: instruments covered under article 31(3)(c) – such as EU law – could even prove not to be appropriate in the light of the object and purpose of the DTC. Therefore, the possible relevance of EU law for the interpretation of DTCs under article 31(3)(c) is always to be examined together with the other means of interpretation listed in the VCLT and, in the end, it may be, or conversely, it may not be, that reference to EU law is appropriate in the concrete case.

### 3. Using EU Law To Interpret Undefined Tax Treaty Terms: Article 3(2) of the OECD MC

The issue of the possible relevance of EU law to the interpretation of undefined DTC terms can be tackled not only in terms of article 31(3)(c) of the VCLT, but also in terms of DTC provisions patterned along the lines of article 3(2) of the OECD Model Tax Convention on Income and on Capital (“OECD MC”), which are found in most DTCs.

According to article 3(2), any term not defined in the DTC shall, unless the context otherwise requires, have the meaning which it has under the law of the State which applies the DTC.<sup>60</sup> In certain DTCs, that provision is patterned along the lines of article 3(2) as found in the OECD MC existing until 1995 and usually sets forth the following:

- .....
58. The primary importance of the principle of good faith has been recognised also by the ICJ in its judgment of 11 June 1998, *Affaire de la frontière terrestre et maritime entre le Cameroun et le Nigéria*, where it has affirmed that “the principle of good faith is a well-established principle of international law. It is set forth in Article 2, paragraph 2, of the Charter of the United Nations; it is also embodied in Article 26 of the Vienna Convention on the Law of Treaties of 23 May 1969. It was mentioned as early as the beginning of this century in the *Arbitral Award of 7 September 1910 in the North Atlantic Fisheries case* (United Nations, *Reports of International Arbitral Awards*, Vol. XI, p. 188). It was moreover upheld in several judgments of the Permanent Court of International Justice (...). The principle of good faith is one of the basic principles governing the creation and performance of legal obligations”. This interpretation is confirmed by the preparatory works of the VCLT and by the fact that the principle of good faith is mentioned not only in Article 31 VCLT (“General rule of interpretation”), but also in the Preamble (where it is affirmed that the principles of good faith and the *pacta sunt servanda* rule are universally recognized) and in Articles 26 (“*Pacta sunt servanda*”), 46 (“Provisions of internal law regarding competence to conclude treaties”) and 69 (“Consequences of the invalidity of a treaty”).
  59. Accord, *ex multis*, E. van der Bruggen, *Unless the Vienna Convention Otherwise Requires: Notes on the Relationship between Article 3(2) of the OECD Model Tax Convention and Articles 31 and 32 of the Vienna Convention on the Law of Treaties*, in 43 *Eur. Taxn.* 5, p. 145 et seq. (2003), *Journals IBFD*; M. Edwardes-Ker, *op. cit.*, chapter 10; S. Bariatti, *op.cit.*; T. Treves, *Diritto internazionale: problemi fondamentali*, *op. cit.*; G. Melis, *L'interpretazione nel diritto tributario*, *op. cit.*, p. 604; F. Rubinstein, *Interpretazione ed applicazione degli accordi contro la doppia imposizione; il ruolo della buona fede oggettiva*, in *Diritto e Pratica Tributaria Internazionale* (2006), p. 53 et seq. See also the case commented by P.M. Smit, *Classification of Income under a Treaty – Application of the Vienna Convention on Treaty Law?*, in *Eur. Taxn.*, p. 57 et seq. (1992), *Journals IBFD*.
  60. With regard to Article 3(2) OECD MC see: K. Vogel, *La clause de renvoi de l'article 3, par. 2, Modèle de Convention de l'OCDE*, in *Réflexion offertes à Paul Sibille. Etudes de fiscalité*, Bruxelles, 1981, p. 957 et seq.; J.F. Avery Jones et al., *The Interpretation of Tax Treaties with Particular Reference to Article 3(2) of the OECD Model (part I)*, in *British Tax Review* (1984), p. 18 et seq.; Id., *The Interpretation of Tax Treaties with Particular Reference to Article 3(2) of the OECD Model (part II)*, in *British Tax Review* (1984), p. 90 et seq.; Vv. Aa., *Interpretation of tax treaties*. Transcript of the panel discussion of Seminar B at the IFA Congress in London held on 11 September 1985, *op. cit.*, p. 75 et seq.; J.F. Avery Jones, *Article 3(2) of the OECD Model Convention and the Commentary to It: Treaty Interpretation*, in *Eur. Taxn.*, p. 252 et seq. (1993), *Journals IBFD*; K. Vogel and R. G. Prokisch, *General Report*, *op. cit.*, p. 76 et seq.; K. Vogel, *On Double Taxation*

As regards the application of the Convention by a Contracting State any term not defined therein shall, unless the context otherwise requires, have the meaning which it has under the law of that State concerning the taxes to which the Convention applies.

In other DTCs, that provision is instead patterned along the lines of article 3(2) as found in the current OECD MC and commonly sets forth the following:

As regards the application of the Convention at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State.

### 3.1. The scope of article 3(2) of the OECD MC

An analysis of article 3(2) OECD MC reveals the following:

- Differences between the two versions. Article 3(2) “was amended in 1995 to conform its text more closely to the general and consistent understanding of member states” (2010 Commentary on Article 3 of the OECD MC, paragraph 13.1). From this statement – which should be part of the context relevant to article 3(2) even when patterned along the lines of the OECD MC existing until 1995 – it derives that any conclusions drawn in respect of article 3(2) of the current OECD MC should in principle also be valid for article 3(2) of the OECD MC existing until 1995;
- The meaning it has under the law of the State which applies the DTC. Article 3(2) permits reference to the law of the State which applies the DTC only when the undefined DTC term has an established legal meaning under that law.<sup>61</sup> In other words, it is not sufficient that a DTC term is used in the law of the State which applies the DTC and has been already interpreted for purposes other than a DTC; it is necessary that the law of the State applying the DTC also provides for a legal definition of the term. The term “law” should be intended as statute law, and should include judgments when they are regarded as case law (typically in common law jurisdictions);<sup>62</sup>
- The same or similar term. Article 3(2) may be invoked even where the law of the State establishes the meaning of a similar but not identical term (think for instance to very similar terms such as “alienation”, “disposal”, “sale”); in other words, article 3(2) may be

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*Conventions, op. cit.*, Art. 3 m.nos. 57 et seq.; K. van Raad, *1992 additions to Articles 3(2) (interpretation) and 24 (Non-discrimination) of the 1992 OECD Model and Commentary*, in Intertax (1992), p. 672 et seq.; Id., *Interpretation and Application of Tax Treaties by Tax Courts*, in Eur. Taxn., p. 3 et seq. (1996), Journals IBFD; J. Sasseville, *Interpretation of Double Taxation Conventions in Canada: An Update*, in Bull. Intl. Fiscal Docn. (1994), Journals IBFD p. 374 et seq.; N.Shelton, *Interpretation and application of tax treaties, op. cit.*, p. 195 et seq.; H. Shannon, *US Income Tax Treaties: Reference to Domestic Law for the Meaning of Undefined Terms*, in Intertax (1989), p. 453 et seq.; J.A. Becerra, *Interpretation and Application of Tax Treaties in North America*, Amsterdam, 2007, p. 69 et seq.; M. Edwardes-Ker, *Tax Treaty Interpretation, op. cit.*, chapter 10; P. Baker, *Double Taxation Conventions, op. cit.*, Introductory Topics m.nos. E.19 et seq.; F.A Engelen, *op. cit.*, p. 473 et seq.; E. van der Bruggen, *Unless the Vienna Convention Otherwise Requires, op. cit.*, p. 142 et seq.; G. Melis, *L'interpretazione nel diritto tributario, op. cit.*, p. 659 et seq.; Id., *L'interpretazione delle convenzioni internazionali, op. cit.*, p. 98 et seq.

61. The Australian Supreme Court, for instance, in its judgment on the case *Thiel v. FCT*, 21 ATR 531, 532 (1990), did not accept an interpretation of the terms “enterprise” and “profits” ground on domestic legislation, since “these words have no particular or established meaning under the laws relating to Australian income tax”.

62. See K. Vogel, *On Double Taxation Conventions*, cit., Art. 3 m.no. 62b; J. Sasseville, *op. cit.*, p. 375; P. Arginelli, *Interpretation of Multilingual Tax Treaties*, to be published.



invoked even where the law of the State establishes the meaning of any term achieving a similar purpose;<sup>63</sup>

- The law for the purposes of the taxes to which the Convention applies, any meaning under such law prevailing over a meaning given to the term under other laws of that State. Primary relevance should be given to the law for the purposes of the taxes to which the Convention applies (more frequently income taxes), while other laws should be given secondary relevance (other tax laws, such as VAT law, or non-tax laws, such as private law). In fact, when income tax law does not give a meaning to the term at issue, article 3(2) requires that other fields of law be investigated. According to some scholars, however, it is inappropriate to search for a meaning beyond tax law<sup>64</sup> or even beyond the law for the purposes of the taxes to which the Convention applies.<sup>65</sup> Nevertheless, non-tax law can be significant where the non-tax meaning is relevant for the purposes of the applicable tax law;<sup>66</sup>
- Inter-temporal issues. Reference should be made to the legislation in force at the time the DTC is applied. This is consistent with the fact that DTCs affect the application of that legislation and not of the legislation in force when they were concluded. Such a “dynamic” reference, however, should operate only insofar as it does not violate the principle of good faith that grounds the law of treaties and their interpretation and binds the States not to profit from a term which meaning is ambiguous.<sup>67</sup> Thus, if making reference to the legislation in force at the time the DTC is applied can lead to violation of the principle of good faith, one should ignore that legislation and refer to a different meaning as required by the context;<sup>68</sup>
- Unless the context otherwise requires. By its very nature, the term “context” cannot be circumscribed to a series of examples that represent it exhaustively. However, according to the majority of scholars,<sup>69</sup> its meaning is wide and apt to include, e.g., all instruments

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63. Accord F.A. Engelen, *op. cit.*, p. 488 et seq., who affirms that if Article 3(2) is interpreted in good faith, “it is only reasonable to assume that it also applies to the terms of tax treaty that have the same content and meaning as similar but not identical terms of domestic law”. The Author adds that “it is a generally accepted principle of interpretation that in cases where the text of a treaty is open to two interpretations, one of which does and the other does not enable its provisions to have appropriate effects, good faith and, in particular, the principles of effectiveness require that the former interpretation be adopted”. Accord the US tax court judgment on the case *Estate of Burghardt v. Commissioner of Internal Revenue* 80 TC 705 (1983), confirmed by the US Court of Appeals for the Third Circuit by an order (without written opinion) dated 18 April 1984.

64. N. Shelton, *op. cit.*, p. 203 et seq.; K. Vogel and R. G. Prokisch, *General Report, op. cit.*, p. 80.

65. F.A. Engelen, *op. cit.*, p. 487, maintains that Article 3(2) should not be interpreted literally but in good faith and this requires that, in the provisions of the domestic law of the contracting state applying the treaty, the term in question must be used in a context similar to that of the DTC.

66. J. Sasseville, *op. cit.*, p. 375; G. Melis, *L'interpretazione delle convenzioni, op. cit.*, p. 104.

67. See J.F. Avery Jones et al., *The Interpretation of Tax Treaties with Particular Reference to Article 3(2) of the OECD Model (part I)*, *op. cit.*, pp. 47-48; K. Vogel, *On Double Taxation Conventions*, cit., Introduction m.no. 124d.; M. Edwardes-Ker, *op. cit.*, chapter 10; P. Baker, *op. cit.*, Introductory Topics, m.no. E.25.

68. See I. Sinclair in Vv.Aa., *Interpretation of tax treaties, op. cit.*, p. 85; N. Shelton, *op. cit.*, p. 204 et seq.; J.A. Becerra, *op. cit.*, p. 71. See also the cases mentioned in D. Ward in Vv.Aa., *Interpretation of tax treaties, op. cit.*, p. 82 et seq., and in A.H. Ogutu, *The relevance of domestic law of the source state in the interpretation of distributive rules under special consideration of Art. 6 para. 2 and Art. 10 para. 3 of the OECD-MC*, in M. Schilcher and P. Weninger (eds), *Fundamental Issues and Practical Problems in Tax Treaty Interpretation*, Vienna, 2008, p. 284.

69. See K. Vogel, *On Double Taxation Conventions, op. cit.*, Art. 3 m.no. 72; K. Vogel and R.G. Prokisch, *General Report, op. cit.*, p. 82 (“the function of the term in the two provisions is completely different”); J.F. Avery Jones et al., *The Interpretation of Tax Treaties with particular reference to art. 3(2) of the OECD Model (part II)*,

mentioned in articles 31-33 of the VCLT as well as the OECD Commentary.<sup>70</sup> An open issue regards the possibility of including, within the context, unilateral instruments that do not necessarily show the agreement between the parties:<sup>71</sup> the prevailing view among scholars is that they should at least be taken into account.<sup>72</sup> Not all instruments will have the same weight for DTC interpretation: so, for instance, instruments showing the agreement between the parties should be attributed a greater weight compared to other instruments, since they can assure “common interpretation” by contracting states.<sup>73</sup>

After examination of article 3(2) of the OECD MC, it is possible to investigate whether or not EU law can legitimately be used to establish the legal meaning of terms which are not defined in DTCs that include a provision patterned along the lines of article 3(2). Accordingly, it will first be investigated whether or not EU law can be regarded as law of the State which applies the DTC. It is in fact crystal-clear that under article 3(2) “[i]f the context is to require the non-application of the domestic law meaning, then it is logical that a domestic law meaning should first have been determined and this meaning must be regarded as inappropriate in the context of the treaty”.<sup>74</sup> Hence, irrespective of how strong the preference of any interpreter is for the meaning given under the law of the State which applies the DTC, or for any different

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*op. cit.*, p. 104. For an excellent overview of the various positions on the meaning of “context” in Article 3(2) see E. van der Bruggen, *Unless the Vienna Convention Otherwise Requires*, *op. cit.*, p. 143 et seq.

70. Following this approach, even Reports published by the OECD on specific issues of interpretation could be considered to be part of the context of Article 3(2). The role to be attributed to Reports for interpretation purposes is, however, a quite unexplored issue. See K. Provdová, *The relevance of the OECD reports for the interpretation of tax treaties*, in M. Schilcher and P. Weninger (eds., *Fundamental Issues and Practical Problems in Tax Treaty Interpretation*, *op. cit.*, p. 139 et seq., although the Author does not deal with the issue of whether Reports have relevance as part of the Article 3(2) context.

71. Such as the legislation of the other contracting state, the judgments issued by courts of the other contracting state and the unilateral materials prepared by one of the contracting states (e.g. the US Technical Memoranda prepared by the US Treasury).

72. With regard to the legislation of the other contracting state, it is commonly accepted that it is included among instruments covered under Article 3 OECD MC. This position is found in paragraph 12 of the Commentary on Article 3 OECD MC, where it is affirmed that the context includes “the meaning given to the term in question in the legislation of the other Contracting State”; furthermore, it is shared by the prevailing doctrine [see K. Vogel, *On Double Taxation Conventions*, *op. cit.*, Art. 3 m.no. 72, although the very same scholar has noticed, in another paper (see Vv.Aa., *Interpretation of tax treaties*, *op. cit.*, p. 78 et seq.), that tax courts tend to make reference to their own legislation without considering the legislation of the other contracting state; see also D. Ward in Vv.Aa., *Interpretation of tax treaties*, *op. cit.*, p. 77 et seq.; for a different opinion see N. Shelton, *op. cit.*, p. 197 et seq.]

With regard to judgments issued by courts of the other contracting state and unilateral materials prepared by one of the contracting states (e.g. the US Technical Memoranda prepared by the US Treasury), the tendency by tax courts and scholars is to consider that they should at least be taken into account. On the relevance of judgments issued by courts of the other contracting state, K. Vogel and R.G. Prokisch, *General Report*, *op. cit.*, p. 63, affirm that those judgments “if they are plausible and if their application may lead to the avoidance of double taxation, they should at least be considered and any deviation from them should be explained explicitly and convincingly.” See also D. Ward, *Use of Foreign Court Decisions in Interpreting Tax Treaties*, in G. Maisto (ed.), *Courts and Tax Treaty Law*, Amsterdam, 2007, Vol. 3 EC and International Tax Law Series, chapter 7, p. 161 et seq. (at p. 175), and P. Baker, *op. cit.*, Introductory Topics m.nos. E.26 et seq.

As to the debate over the possibility to give relevance to unilateral materials prepared by one of the contracting states, see P. Baker, *op. cit.*, Introductory Topics m.no. E.30 et seq.; K. Vogel and R.G. Prokisch, *General Report*, *op. cit.*, p. 69 and J. Sasseville, *op. cit.*, p. 376.

73. On the requirement for a common interpretation of DTCs see, *ex multis*, K. Vogel and R.G. Prokisch, *General Report*, *op. cit.*, p. 62 et seq. See also K. van Raad, *International Coordination of Tax Treaty Interpretation and Application*, in Intertax (2001), p. 212 et seq. In more general terms, see S. Bariatti, *op. cit.*, p. 92 and further references found therein.

74. P. Baker, *op. cit.*, Introductory Topics m.no. E.20. Accord K. Vogel, *On Double Taxation Conventions*, *op. cit.*, Art. 3 m.no. 70.

meaning required by the context,<sup>75</sup> the first question to be answered is whether or not EU law is covered under article 3(2).

### 3.2. EU law as part of the law of the state which applies the DTC

The natural tendency over the years has been to implicitly assume that “national” law be at stake under article 3(2) of the OECD MC, notwithstanding the fact that article 3(2) does not qualify the law to be referred to. This interpretation, for instance, is implicit in the Commentary on Article 3 of the OECD MC, at paragraph 13.1.<sup>76</sup>

A strict limitation to national law, however, is not definitely supported by the wording of article 3(2). Moreover, it is contradicted by the fact that scholars, when considering the possible relevance of “parallel treaties” in order to interpret a DTC, generally reckon that other tax treaties concluded by the same contracting state are part of the law of that State for the purposes of article 3(2) (although they argue that in most cases those other treaties should, in the end, be disregarded because of the context);<sup>77</sup> this means that article 3(2) is not necessarily understood as limited to national law.

The reference in article 3(2) to the law of the State which applies the DTC seems to be broad enough to include law which is not “national”. Accordingly, it seems to be broad enough to include EU law. Such an interpretation of article 3(2) – by the way – has been already proposed by Vogel.<sup>78</sup>

However, since the law at issue must be law “of the State which applies the DTC”, EU law can be relevant under article 3(2) only when the State which applies the DTC is an EU Member State. There is no requirement that the other contracting state be an EU Member State as well, thus reference to EU law can be made both for DTCs concluded between Member States and for DTCs concluded between Member States and third countries.

In conclusion, it is submitted that when interpreting a DTC concluded by a Member State either with other Member States or with third countries, EU law should be regarded as part of the law of that State for the purposes of article 3(2).

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75. Some scholars submit that the law of the State which applies the DTC should almost always be referred to, since the context can rarely otherwise require (see J.F. AveryJones et al., *The Interpretation of Tax Treaties with particular reference to art. 3(2) of the OECD Model (part II)*, op. cit., p. 107). Some others, conversely, maintain that the law of the State which applies the DTC should almost never be referred to, since the context would almost always give a solution which renders useless referring to domestic law (see M. Lang, *Die Bedeutung des originär innerstaatlichen Rechts für die Auslegung von Doppelbesteuerungsabkommen (Art. 3 Abs. 2 OECD-MA)*, in Burmester-Endres (eds), *Aussensteuerrecht Doppelbesteuerungsabkommen und EU-Recht im Spannungsverhältnis: Festschrift für Helmut Debatin zum 70. Geburtstag*, 1997, p. 283 et seq., in particular p. 302). Finally, there are those who prefer an intermediary solution, according to which ignoring the law of the State which applies the DTC is something that the context requires in exceptional situations, where there are relatively strong and convincing arguments (see K. Vogel, *On Double Taxation Conventions*, op. cit., Art. 3 m.nos. 70-71; K. Vogel and R.G. Prokisch, *General Report*, op. cit., p. 81 et seq.).

76. “(...) For purposes of paragraph 2, the meaning of any term not defined in the Convention may be ascertained by reference to the meaning it has for the purpose of any relevant provision of the domestic law of a Contracting State, whether or not a tax law. (...)” (emphasis added)

77. See J.F. Avery Jones et al., *The Interpretation of Tax Treaties with Particular Reference to Article 3(2) of the OECD Model (part I)*, op. cit., p. 25; K. Vogel, *Interpretation of Double Taxation Treaties. In particular the Problem of Qualification*, in *Rassegna Tributaria* (1988), p. 178 et seq.; Id., *On Double Taxation Conventions*, op. cit., Introduction m.nos. 83 et seq.; P. Baker, op. cit., Introductory Topics m.no. E.32. Among Italian scholars, see G. Bizzioli, *Brevi riflessioni sull’uso dei cd. ‘parallel treaties’ nell’interpretazione dei trattati contro le doppie imposizioni*, in *Rivista di Diritto Tributario* (2005), IV, p. 156 et seq.

78. See K. Vogel, *On Double Taxation Conventions*, op. cit., Art. 3 m.no. 62b.

### 3.3. What rules of EU law? Primary versus secondary sources of EU law

The author's view is that, for the same reasons already brought forward under section 2.3 above, both primary and secondary sources of EU law should be regarded as part of the law of an EU Member State for the purposes of article 3(2). The fact that certain rules of EU law were not originally conceived to be significant to the interpretation of DTCs does not prevent this conclusion, since no such requirement is found in article 3(2).

### 3.4. What rules of EU law? Rules concerning the taxes to which the convention applies or any rules of EU law?

Under article 3(2), reference should be made to (EU) law "for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State" (see also section 3.1. above).

Accordingly, when interpreting DTC provisions affecting income taxes, EU directives regarding income tax law should be given primary relevance (think of the parent-subsidiary directive, the merger directive, the interest-royalties directive, the savings directive and the forthcoming, if ever, CCCTB directive). Secondary relevance should be given to other EU law provisions if appropriate in the light of the DTC's context (e.g. provisions found in the VAT directive and related regulations and provisions found in company law directives).

Interesting cases would be those where a treaty term has more than one meaning under EU law. A given term could in fact have a certain meaning under an income tax directive and another meaning under the VAT directive: in such cases, the former would prevail according to the clear wording of article 3(2). It is also possible that a given term has two different meanings under two income tax directives,<sup>79</sup> in such cases, the wording of article 3(2) is unhelpful and the author's view is that the choice should be driven by the context.<sup>80</sup>

### 3.5. What rules of EU law? Inter-temporal issues

It has already been observed under section 3.1., that article 3(2) generally requires one to refer to the legislation in force at the time the DTC is applied. This being said, it is submitted that EU legislation in force at the time the DTC is applied should be taken into account for the interpretation of that DTC.

Nevertheless, if making reference to EU legislation in force at the time the DTC is applied can lead to violation of the principle of good faith which grounds the law of treaties and their interpretation, or if the context mentioned in article 3(2) otherwise requires for any other

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79. Actually, this case is not entirely hypothetical, since the very same term "beneficial owner" is defined differently in the interest-royalties directive and in the savings directive.

80. See however G. Melis, *L'interpretazione delle convenzioni internazionali*, *op. cit.*, p. 105, who maintains that when a treaty term has more than one meaning under the same field of tax law, the principle *lex specialis derogat generali* should be applied. The point of treaty interpretation where a treaty term has more than one meaning under the law of the State which applies the DTC is raised, though without drawing any conclusion, by J.F. Avery Jones et al., *The Interpretation of Tax Treaties with Particular Reference to Article 3(2) of the OECD Model (part I)*, *op. cit.*, p. 25; and P. Baker, *op. cit.*, Introductory Topics, m.no. E.22. See also the point raised by F.A. Engelen, *op. cit.*, p. 487 et seq., in respect of the case where a contracting state levies a withholding tax and an income tax at the same time, both of which are covered by the DTC, and a term used in the DTC is defined differently for the purposes of the different laws imposing those taxes.

reasons, one should ignore that legislation and refer to a different meaning as required by the context.

Generally, one should never forget that reference to the law of the State which applies the DTC is only a part of a larger interpretation process required by article 3(2), where the context of the DTC is also to be considered: the meaning of a given term as found under EU law could even prove not to be appropriate in the light of the context. Therefore, the possible relevance of EU law for the interpretation of DTCs under article 3(2) is always to be tested in the light of the context of the DTC and, in the end, it may be, or conversely, it may not be, that reference to EU law is appropriate in the concrete case.

#### **4. Preliminary Thought on Some Issues Deriving from the Use of EU Law To Interpret Undefined Tax Treaty Terms**

The analysis carried out so far leads to the conclusion that EU law can play a role in establishing the legal meaning of terms which are not defined in DTCs, pursuant either to article 31(3)(c) of the VCLT and to DTC provisions patterned along the lines of article 3(2) of the OECD MC. Depending on whether article 31(3)(c) of the VCLT or article 3(2) is concretely invoked, EU law can be relevant to slightly different extents.

Where article 31(3)(c) of the VCLT is invoked:

- EU law can play a role in the interpretation of DTCs concluded between Member States, since article 31(3)(c) of the VCLT requires that rules be “applicable in the relations between the parties”;
- both primary and secondary EU law can be relevant in DTC interpretation;
- only EU law dealing with the tax covered by the DTC provisions at issue must be taken into account; courts, however, are not prevented from taking into account provisions in other fields of EU law, but are not required to (that is to say, provisions in other fields of EU law do not enjoy secondary relevance);
- EU law can play a role in the interpretation of DTC undefined terms only; in the opposite case where the interpretation of DTC defined terms is at issue, article 31(4) of the VCLT requires that the definition found in the DTC be used;
- EU law in force at the time the DTC is applied should be referred to, unless this entails a violation of the principle of good faith (in which case a different meaning, as required by the object and purpose of the DTC, should be used).

Conversely, where article 3(2) is invoked:

- EU law can play a role in interpreting both DTCs concluded between Member States and DTCs concluded between Member States and third countries;
- both primary and secondary EU law can be relevant in DTC interpretation;
- EU law dealing with the tax covered by the DTC provisions at issue has primary relevance, while provisions in other fields of EU law enjoy secondary relevance;
- EU law can play a role in the interpretation of DTC undefined terms only;
- EU law in force at the time the DTC is applied should be referred to, unless the context of the DTC otherwise requires (in which case a different meaning, as required by the context, should be used).

In any case, EU law can play a *very important* role, since it can assure “common interpretation” of the same DTC by contracting states,<sup>81</sup> especially where a DTC concluded between Member States is at issue. The possibility to use EU law to interpret DTCs can however raise a number of issues.

#### 4.1. EU law as interpreted by the ECJ?

A first issue is whether or not, when referring to EU law provisions in order to interpret DTCs, one should necessarily refer to the interpretation of those provisions given by the ECJ (if any). This issue deserves some thought.

Legally speaking, the provision under interpretation is a DTC provision and not an EU law provision. Hence, the tax court called to interpret an undefined DTC term may decide to take the definition of that term found in EU law and to give its own interpretation of that definition. The ECJ is in fact competent to interpret EU law only<sup>82</sup> and not to interpret DTCs.

Nevertheless, it appears that referring to an EU law provision does imply the need to refer also to the interpretation of that provision given by the ECJ, if any. This conclusion seems to be preferable both in case article 31(3)(c) of the VCLT is invoked and in case DTC provisions patterned along the lines of article 3(2) of the OECD MC are invoked. With regard to article 31(3)(c) of the VCLT, the need to consider the interpretation given by the ECJ is supported by the following statement of the ECtHR found in the recent judgment on the case *Demir and Baykara v. Turkey* (emphasis added): “The Court, in defining the meaning of terms and notions in the text of the Convention, can and must take into account elements of international law other than the Convention, the interpretation of such elements by competent organs, and the practice of European States reflecting their common values”.<sup>83</sup> With regard to article 3(2), the need to consider the interpretation given by the ECJ is further supported by the position of those scholars who have argued that article 3(2) can give relevance also to case law.<sup>84</sup>

#### 4.2. Article 31(3)(c) of the VCLT and EU law in multilateral DTCs

A further issue is whether or not, under article 31(3)(c) of the VCLT, EU law must be taken into account in the interpretation of multilateral DTCs concluded among Member States and third countries. To date, there is only one such DTC, known as the Nordic Convention (concluded among Denmark, Faroe Islands, Finland, Iceland, Norway and Sweden).

Dealing with this issue entails the need to answer the question whether or not “relevant rules of international law” have to be binding on all parties to the treaty under interpretation in order to contribute to the process of its interpretation. As mentioned in section 2.1. above, there is no clear-cut answer to this question, since, on the one hand, the few international decisions on the topic took the restrictive approach that rules of international law should be

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81. Accord K. Vogel, *On Double Taxation Conventions*, cit., Art. 3 m.no. 62b.  
82. See, *ex multis*, Case 155/73, *Sacchi*; Case 111/75, *Mazzalai*; Case C-231/89, *Gmurzynska-Bscher*; and Joined Cases C-428/06 to C-434/06, *UGT-Rioja and Others*. The interpretation given by the ECJ of a provision of EU law clarifies and defines its meaning and scope (*ex multis*, Case C-35/97, *Commission v. France*, para. 46; and Case C-481/99, *Georg Heiningner and Helga Heiningner*, para. 51).  
83. ECtHR, *Demir and Baykara v. Turkey*, cit., para. 85.  
84. K. Vogel, *On Double Taxation Conventions*, cit., Art. 3 m.no. 62b; J. Sasseville, *op. cit.*, p. 375; P. Arginelli, *Interpretation of Multilingual Tax Treaties*, to be published.

binding on all parties to the treaty,<sup>85</sup> while, on the other hand, several scholars have been submitting that rules of international law should be binding only on the parties to the dispute.<sup>86</sup>

So, if one follows the former approach, there is no obligation under article 31(3)(c) of the VCLT to take into account EU law in the interpretation of the Nordic Convention, since some contracting states to that Convention are not EU Member States. If, conversely, one takes the latter approach, article 31(3)(c) of the VCLT requires that EU law is taken into account when the Nordic Convention is applied to a situation involving two or more Member States.

Note, in any event, that the Nordic Convention includes a provision patterned along the lines of article 3(2) of the OECD MC and, therefore, EU law can possibly be relevant in the interpretation of the Nordic Convention according to that provision, irrespective of article 31(3)(c) of the VCLT.

#### **4.3. Article 3(2) of the OECD MC and EU law in respect of conflicts of qualification in DTCs concluded between Member States and third countries**

Another issue is the possibility that EU law also becomes indirectly relevant for a third country which has concluded a DTC with an EU Member State, when a conflict of qualification is at stake. In particular, when the Member State is the State of source and its classification of a given item of income is driven by EU law pursuant to article 3(2), one may wonder whether or not the third country – being the State of residence – is required to give relief under article 23 on the basis of the State of source income classification, irrespective of its own classification (*see* paragraphs 32.1 et seq. of the Commentary on Articles 23A and 23B of the OECD MC).<sup>87</sup>

This issue should be given a positive answer, i.e. the third country (State of residence) should give relief under article 23 on the basis of the income classification by the EU Member State (State of source), thus it should indirectly give relevance to EU law. There seems to be no reason why the State of residence should refuse to solve the conflict of qualification simply because the State of source income classification is driven by EU law provisions. Nonetheless, the State of residence could dispute the application of article 3(2) by the State of

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85. See the GATT panel in *United States-Restrictions on Imports of Tuna*, DS29/R, 16 June 1994, para 5.19; and the WTO panel in *Measures Affecting the Approval and Marketing of Biotech Products* WT/DS291/R, WT/DS292/R, WT/DS293/R (known as “*EC Biotech*”), 29 September 2006.

86. A most qualified opinion supporting this view is that of the UN International Law Commission, *Fragmentation of International Law*, *op. cit.*, para. 472.

87. With regard to conflicts of qualification in DTCs, one can refer to the papers in E. Burgstaller and K. Haslinger (eds), *Conflicts of Qualification in Tax Treaty Law*, Vienna, 2007, where many further references can be found. Note that it is doubtful whether or not the State of residence is bound to grant relief when “complete” distributive rules are applicable (“shall be taxable only”); on this issue, *see* K. Vogel, *Conflicts of Qualification: The Discussion is not Finished*, in 57 Bull. Intl. Taxn. 2, p. 43 et seq (2003), Journals IBFD. and A. Rust, *The New Approach to Qualification Conflicts has its Limits*, in 57 Bull. Intl. Taxn. 2, p. 49 (2003), Journals IBFD.

source and regard as illegitimate any reference to EU law; such an approach, however, could be challenged by the taxpayer with the arguments made in this paper.

## 5. Some Concrete Examples where EU Law Could Be Used To Interpret Undefined Tax Treaty Terms

Once it is established that EU law can play a role in interpreting undefined DTC terms, it is useful to try and find some examples where EU law could actually be relevant.

### 5.1. Beneficial owner

A first and significant example is the term “beneficial owner”.<sup>88</sup> This term is found in the vast majority of DTCs and, in most of them, it is not given a definition. Relevance could thus be attributed to EU law both under article 31(3)(c) of the VCLT and article 3(2).

88. This term has been the subject of attention by several tax scholars. See, *ex multis*, K. Vogel, *On Double Taxation Conventions*, *op. cit.*, Preface to Arts. 10-12 m.nos. 7 et seq.; A. Rowland, *Beneficial Ownership in a Corporate Context: What is it? When is it lost? Where does it go?*, in *British Tax Review* (1997), p. 178 et seq.; Vv.Aa., *The OECD Model Convention 1998 and Beyond. The Concept of Beneficial Ownership in Tax Treaties*, Deventer, 1998; S. Van Weeghel, *The Improper Use of Tax Treaties. With particular reference to the Netherlands and the United States*, London-The Hague-Boston, 1998, p. 54 et seq.; C. Du Toit, *Beneficial Ownership of Royalties in Bilateral Tax Treaties*, Amsterdam, 1999, p. 172 et seq.; J. David Oliver, J.B. Libin, S. Van Weeghel and C. Du Toit, *Beneficial Ownership*, in 54 *Bull. Intl. Taxn.* 7, p. 310 et seq. (2000), *Journals IBFD*; C. Vargas, *Beneficial Ownership Lacks Proper Meaning*, in *International Tax Review*, 2004, p. 18 et seq.; J. Avery Jones et al., *The Origins of Concepts and Expressions Used in the OECD Model and their Adoption by States*, in 60 *Bull. Intl. Taxn.* 6, p. 246 et seq. (2006), *Journals IBFD*; J. Bernstein, *Beneficial Ownership: An International Perspective*, in *Tax Notes International* (2007), p. 1211; R. Fraser and D. Oliver, *Beneficial Ownership: HRMC’s draft guidance on interpretation of the Indofood decision*, in *British Tax Review* (2007), p. 51; L. De Broe, *International Tax Planning and Prevention of Abuse. A Study under Domestic Tax Law, Tax Treaties and EC Law in relation to Conduit and Base Companies*, Amsterdam, 2008, p. 654 et seq.; P. Arginelli et al., *The Royal Bank of Scotland Case: More Controversy on the Interpretation of the term “beneficial owner”*, in P. Russo and R. Fontana (eds), *A decade of Case Law: Essays in honour of the 10th Anniversary of the Leiden Adv. LLM in International Tax Law*, Leiden, 2008, p. 217 et seq.; B. Gibert, *Beneficial Ownership – A French Perspective*, in 48 *Eur. Taxn.* 1, p. 2 et seq. (2008), *Journals IBFD*; K.R. Sekar, *No Consensus on Beneficial Ownership*, in *International Tax Review* (2008), p. 159; P. Baker, paper on beneficial owner presented on 17 October 2008 to the attention of the UN Committee of Experts on International Cooperation in Tax Matters, found at <http://www.un.org/esa/ffd/tax/fourthsession/index.htm>; B. Arnold, *Tax Treaty News*, in 63 *Bull. Intl. Taxn.* 5, p. 175 et seq. (2009), *Journals IBFD*; D. Shapiro, *OECD Tax Treaties: Who Beneficially Owns Dividends in a Total Return Swap*, in *Journal Taxation of Investments* (2009), p. 63 et seq.; C. Elliffe, *The Interpretation and Meaning of “Beneficial Owner” in New Zealand*, in *British Tax Review* (2009), p. 276 et seq.; F. De Moraes e Castro, *The Influence of Beneficial Owner Clauses in the Prevention of International Tax Treaty Abuse*, in *Diritto e Pratica Tributaria Internazionale* (2010), p. 121 et seq.; A.M. Jimenez, *Beneficial Ownership: Current Trends*, in 2 *World Tax J.* 1, p. 35 et seq. (2010), *Journals IBFD*; A. Chawla and S. Singhi, *Ramifications on Notional Theories of Ownership – Evolution of Beneficial Ownership*, in *International Taxation* (2010), p. 121 et seq.; A. Aggarwal, *Beneficial Ownership – Concept and International Practices*, in *International Taxation* (2010), p. 134 et seq.; C. Du Toit, *The Evolution of the Term ‘Beneficial Ownership’ in Relation to International Taxation over the Past 45 Years*, in 64 *Bull. Intl. Taxn.* 10, p. 500 et seq. (2010), *Journals IBFD*; J. Li, *Beneficial Ownership in Tax Treaties: Judicial Interpretation and the Case for Clarity*, in P. Baker and C. Bobbett (eds), *Tax Polymath. A life in international taxation. Essays in honour of John F. Avery Jones*, Amsterdam, 2010, p. 187 et seq.; G. Watson and S. Baum, *Beneficial Owner as a Treaty Anti-Avoidance Tool?*, in *Canadian Tax Journal* (2012), p. 149 et seq.

The term “beneficial owner” has also been the subject of attention by several tax courts worldwide. See the Hoge Raad judgment on the case *Royal Dutch Shell* (known as the *Market maker case*) of 6 April 1994, n. 28638, BNB 1994/217 (commented by H. Born, *Beneficial Ownership – Decision of the Netherlands Supreme Court of 6 April 1994, n. 28638*, in *Eur. Taxn.* p. 469 et seq. (1994), *Journals IBFD*; and H. Pijl, *The Definition of ‘Beneficial Owner’ under Dutch Law*, in 54 *Bull. Intl. Taxn.* 6, p. 257 et seq.) (2000), *Journals IBFD*; judgment of the Swiss Federal Tax Commission of Appeal n. JAAC 65.86 of 28 February 2001 (commented by F. Aramini and N. Savini, *La nozione di beneficial owner nel diritto tributario internazionale e*



In particular, relevance could be attributed to one of the definitions found in the interest-royalties directive (Council Directive 2003/49/EC of 3 June 2003) and in the savings directive (Council Directive 2003/48/EC of 3 June 2003).

According to article 1(4) of the interest-royalties directive:

A company of a Member State shall be treated as the beneficial owner of interest or royalties only if it receives those payments for its own benefit and not as an intermediary, such as an agent, trustee or authorised signatory, for some other person.

No relevance should be given to article 1(5) of the interest-royalties directive regarding the notion of “beneficial owner” for a permanent establishment, since in DTCs beneficial ownership is an issue only for persons, which do not include permanent establishments.

According to article 2(1) of the savings directive:

For the purposes of this Directive, ‘beneficial owner’ means any individual who receives an interest payment or any individual for whom an interest payment is secured, unless he provides evidence that it was not received or secured for his own benefit, that is to say that:

- (a) he acts as a paying agent within the meaning of article 4(1); or
- (b) he acts on behalf of a legal person, an entity which is taxed on its profits under the general arrangements for business taxation, an UCITS authorised in accordance with Directive 85/611/EEC or an entity referred to in article 4(2) of this

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*nel diritto tributario comunitario*, in *Diritto e Pratica Tributaria Internazionale* (2002), p. 994 et seq.; non-tax judgment by the UK Court of Appeal on the case *Indofood* of 2 March 2006 (see, *ex multis*, P. Baker, *Beneficial Ownership: After Indofood*, in *GITC Review* (2007), found at [http://www.taxbar.com/documents/Beneficial\\_Ownership\\_PB.pdf](http://www.taxbar.com/documents/Beneficial_Ownership_PB.pdf)); judgment by the French Conseil d’Etat on the case *Royal Bank of Scotland* of 29 December 2006, in *ITLR* (2009), p. 683 (commented by, *ex multis*, B. Gibert and Y. Ouamrane, *op. cit.*; P. Arginelli et al., *op. cit.*); judgment by the Spanish Audiencia Nacional on the case *Real Madrid F.C. v. Oficina Nacional de Inspeccion* of 18 July 2006, in *Westlaw Aranzadi JUR/2006/204307*; judgment by the Indonesian Supreme Court on the case *PT Indah Kiat Pulp & Papper v. US Bank National Association* of 21 June 2006, in *ITLR* (2008), p. 1 et seq.; judgment by the Indonesian Tax Court sul caso *PT Transportasi Gas Indonesia v. Direktur Jenderal Pajak* of 14 March 2008; non-tax judgment by the Court of New York (U.S. South District Court, NY) on the case *CSX Corporation* of 11 June 2008; judgment by the Tax Court of Canada on the case *Prévost* of 22 April 2008, in *ITLR* (2008), p. 736, and the subsequent judgment by the Federal Court of Appeal of 26 February 2009, in *ITLR* (2009), p. 757; judgment by the Swiss Federal Administrative Tribunal of 30 October 2008 on the case *A GmbH*, A-2163/2007; judgment by the Indonesian Tax Court on the case *PT Indosat Tbk & Indosat Finance BV* of 27 April 2010 (commented by F. Karyadi, *Tax Court Ruling on Beneficial Ownership of Interest on Bonds Issued by Dutch Special Purpose Vehicle*, in 12 *Derivs. & Fin. Instrum.* 6, p. 184 et seq. (2010), *Journals IBFD*); decisions by the Danish *Landskatteretten* on cases SKM 2010.268 LSR of 16 April 2010; SKM 2010.729 LSR of 17 November 2010; SKM 2011.57.LSR of 27 January 2011 and SKM 2011.485.LSR of 13 July 2011 (commented by B.Tolstrup and N. Bjørnholm, *Beneficial Ownership – Withholding Tax on Dividends and Interests from the Danish Perspective*, in 65 *Bull. Intl Taxn.* 9, p. 503 (2011), *Journals IBFD*); judgment by the Czech Supreme Administrative Court No. 2 Afs 86/2010-141 of 10 June 2011 (commented by P. Fekar, *Czech Supreme Administrative Court on Beneficial Ownership*, in 51 *Eur. Taxn.* 9/10, p. 418 et seq. (2011), *Journals IBFD*); judgment by the Indian High Court of Mumbai on the case *Aditya Birla Nuvo Limited, New Cingular Wireless Services Inc. and Tata Industries Limited v. Deputy Director of International Tax* of 14 July 2011; decision by the Danish *Landskatteretten* on the case SKM2012.26.LSR of 16 December 2011; judgment by the Danish High Court of 20 December 2011; judgment by the Tax Court of Canada on the case *Velcro Canada Inc. v. The Queen* of 24 February 2012; judgment by the Swiss Federal Administrative Court on the case A-6537/2010 of 7 March 2012. It should also be recalled the less recent US case *Aiken Industries v. Commissioner of Internal Revenue*, 56 T.C. 925 (1971), commented by S. Van Weeghel, *The Improper Use Of Tax Treaties*, cit., p. 59 et seq., concerning a DTC (United States–Honduras, concluded on 25 June 1956) that did not include any beneficial owner clause.

See also the instructions on the term “beneficial onwer” issued by the HM Revenue & Customs after *Indofood* (found at <http://www.hmrc.gov.uk/manuals/intmanual/INTM332060.htm>); the *United States Model Technical Explanation* accompanying the *United States Model Income Tax Convention* of November 15, 2006; the Circular 601 of 27 October 2009 issued by the Chinese tax administration.

- Directive and, in the last mentioned case, discloses the name and address of that entity to the economic operator making the interest payment and the latter communicates such information to the competent authority of its Member State of establishment, or
- (c) he acts on behalf of another individual who is the beneficial owner and discloses to the paying agent the identity of that beneficial owner in accordance with article 3(2).

Both definitions are “relevant” in the sense required by article 31(3)(c) of the VCLT and are part of the law for the purposes of the taxes to which DTCs apply according to article 3(2). So, in all cases where a given DTC can be interpreted in the light of EU law with regard to the parties to the DTC and does not include a treaty definition of the term “beneficial owner”, one of the above definitions can play a role in establishing the meaning of “beneficial owner” for the purposes of that DTC.

This approach, which is not contradicted by the Commentaries on the articles of the OECD MC, is corroborated by the recent works undertaken at the OECD. In the 2010 OECD report *The Granting of Treaty Benefits with respect to the Income of Collective Investment Vehicles*,<sup>89</sup> paragraph 31, it is affirmed that: “Because the term ‘beneficial owner’ is not defined in the Model, it ordinarily would be given the meaning that it has under the law of the State applying the Convention, unless the context otherwise requires.” Furthermore, in the 2011 OECD Discussion Draft *Clarification of the Meaning of “Beneficial Owner” in the OECD Model Tax Convention*, it is proposed that the Commentaries on the articles 10, 11 and 12 are amended to include the following statement “(...) This does not mean, however, that the domestic law meaning of “beneficial owner” is automatically irrelevant for the interpretation of that term in the context of the article: that domestic law meaning is applicable to the extent that it is consistent with the general guidance included in this Commentary”.<sup>90</sup>

An EU law definition should thus be rejected only when its use is inappropriate in the concrete case in the light of the means of interpretation listed in the VCLT or because the context otherwise requires.

The author’s view is, however, that in most cases neither the means of interpretation listed in the VCLT nor the context of the DTC will otherwise require. Those means of interpretation and the context, conversely, will be of help in establishing which EU definition should be preferred. In this respect, it is submitted that the context and the means of interpretation listed in the VCLT should concretely lead one to prefer the definition found in article 1(4) of the interest-royalties directive and to use it for DTC purposes. The definition found in the savings directive, in fact, seems inappropriate for DTCs, because of its many peculiarities strictly linked to the mechanisms of the savings directive, the scope and purpose of which are much different from those of DTCs. Conversely, the definition found in the interest-royalties directive with respect to companies appears to be appropriate for DTCs, since its scope and purpose are similar to those of DTCs.<sup>91</sup>

89. OECD, *The Granting of Treaty Benefits with respect to the Income of Collective Investment Vehicles*, Paris, 2010.

90. OECD, Discussion Draft *Clarification of the Meaning of “Beneficial Owner” in the OECD Model Tax Convention*, Paris, 2011.

91. The conclusion that the definition found in Article 1(4) of the interest-royalties directive should be used for DTC purposes is also supported by a number of arguments already made in F. Avella, *Il beneficiario effettivo nelle convenzioni contro le doppie imposizioni: prime pronunce nella giurisprudenza di merito e nuovi spunti di discussione*, in *Rivista di Diritto Tributario* (2011), V, p. 3 et seq., that can be summarized as follows: (i) the disagreement existing among scholars and courts worldwide on the meaning to be given to “beneficial owner” shows that, at the moment, there is no agreed autonomous treaty meaning of “beneficial owner” to be referred to; (ii) the EU law meaning of “beneficial owner” can guarantee common interpretation of

It is also submitted that the definition found in article 1(4) of the interest-royalties directive should be considered to be equally applicable to dividends, interest and royalties as far as DTCs are concerned, notwithstanding that it is taken from a set of rules meant to cover only interest and royalties.<sup>92</sup>

### 5.2. Centre of vital interests (tie-breaker rule)

A second example where EU law could actually be relevant in the interpretation of undefined DTC terms, can be inferred from the tax jurisprudence of the Italian Supreme Court.<sup>93</sup> In cases regarding the residence of individuals for income tax purposes where the domicile had to be identified (please note that the Italian notion of “domicile” is very similar to the treaty notion of “centre of vital interest”), the Court was faced with a situation where personal interests were located in a State different from the State where the individual had his economic interests. The Court decided to refer to EU law and, in particular, to a directive for the exemption of temporary imports from another Member State of motor-driven road vehicles from turnover tax, excise duties and any other consumer tax (Council Directive 83/182/EEC of 28 March 1983), i.e. a directive on indirect taxation.

In order to make its choice of personal interests or economic interests, the Court referred to article 7 of that directive, which provided for a definition of the term “normal residence” and established that personal interests were to be preferred over economic ones. The Court also referred to the interpretation of that provision given by the ECJ in the judgment on the case *Louloudakis*.<sup>94</sup> Hence, the Court finally supported its choice of personal interests over economic ones by reference to that EU law provision and its interpretation as given by the ECJ.

The above case gives an idea of how EU law could affect the interpretation of tax law. Actually, however, the Italian Supreme Court was facing the interpretation of the domestic law term “domicile” and not of a DTC, hence it could not sustain its reasoning with arguments of treaty interpretation. Nonetheless, a similar reasoning could apply to the interpre-

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DTCs, especially DTCs concluded between Member States; (iii) the meaning of “beneficial owner” provided for in the interest-royalties directive is in line with the worldwide tendency of tax courts to give relevance to the powers of the person whose interposition is contested, and not to the attribution of income according to the legislation of the State of residence; (iv) the meaning of “beneficial owner” provided for in the interest-royalties directive is appropriate to deal only with some forms of tax avoidance (i.e. those involving the interposition of a recipient who is obliged to pass the income to someone else) and not with all cases of treaty shopping; this is confirmed by the approach found in the Commentaries on the Article of the OECD MC and by the OECD Discussion Draft *Clarification of the Meaning of “Beneficial Owner” in the OECD Model Tax Convention, op. cit.*, where it is proposed that the Commentaries include the following statement: “Whilst the concept of ‘beneficial owner’ deals with some forms of tax avoidance (i.e. those involving the interposition of a recipient who is obliged to pass the dividend to someone else), it does not deal with other cases of treaty shopping and must not, therefore, be considered as restricting in any way the application of other approaches to addressing such cases”.

92. In fact, nothing seems to prevent the possibility to refer to the interest-royalties directive definition even when DTC provisions on dividends are at issue. The term “beneficial owner” is, as far as DTCs are at issue, generally construed in identical terms either when dividends, interest and royalties are concerned. An authoritative confirmation comes from the fact that the 2010 Commentaries on Article 10, Article 11 and Article 12 of the OECD MC read almost identically with respect to the interpretation of the term “beneficial owner”, apparently showing that dividends should not be substantially distinguished from interest and royalties where beneficial ownership is at stake. These elements suggest that no significant distinction should be made between dividends, interest and royalties in respect of beneficial ownership.

93. Corte di Cassazione, judgment No. 13803 of 7 November 2001; judgment No. 9856 of 14 April 2008; and judgment No. 14434 of 15 June 2010.

94. ECJ, Case C-262/99, *Paraskevas Louloudakis v. Elliniko Dimosio*.

tation of the DTC term “centre of vital interests” and could be substantiated through the approach proposed in this paper.

In particular, article 3(2) could be invoked, so that reference to the provisions of the above directive would be mandatory unless the context otherwise requires.<sup>95</sup> Those EU provisions, in fact, though they are not part of the law for the purposes of the taxes to which DTCs apply, enjoy secondary relevance according to article 3(2). When there is no other income tax provision that can be considered in order to find a definition of “centre of vital interests”, the above directive should be referred to.<sup>96</sup> Note that that directive included a definition of a similar term and not of an identical one (“normal residence” vs. “centre of vital interests”); nevertheless, as already said above, article 3(2) may be invoked even where the law of the State establishes the meaning of any term achieving a similar purpose (*see* section 3.1.).

However, as already remarked many times in the course of this paper, finding an EU definition does not necessarily mean that that definition is appropriate for the purposes of a DTC: the EU definition of “normal residence” must be tested in the light of the context of the DTC. So, the appropriateness of using the definition of “normal residence” for the purposes of a DTC should be deeply investigated. It is however out of the scope of this paper to draw a conclusion in this respect.<sup>97</sup>

**5.3. Transfer pricing and the Arbitration Convention**

There are perhaps further examples that can be found, of EU provisions which could be relevant in the interpretation of DTCs.<sup>98</sup> This paper, however, is not intended to exhaustively list all the cases where this could happen, but to draw attention to the possibility that EU law may be used to construe DTCs.

The approach found in this paper, though proposed with regard to EU law, can prove to be effective also with respect to other multilateral instruments that have some points of contact with EU law. Reference is made, in particular, to the Arbitration Convention of 23 July 1990 on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, which however is not an EU law instrument, but a multilateral international public law convention.<sup>99</sup> It appears, in fact, that the Arbitration Convention could also be

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95. Conversely, Article 31(3)(c) VCLT would not bind the Court to refer to the provisions of the above directive, since they are not “relevant” in the sense required by Article 31(3)(c) VCLT as they do not touch on the same subject matter as the DTC provisions. Thus, Article 31(3)(c) VCLT does not require the Court to consider the above mentioned directive.

96. Conversely, when other income tax provisions found in the law of the contracting state can be considered in order to find a definition of “centre of vital interests”, those provisions should be preferred under Article 3(2) to those found in a directive on indirect taxation.

97. Reference can be made to S. Pittman, *The Centre of Vital Interests Rule: Do Personal Interests Prevail over Economic Interests?*, in M. Hofstätter and P. Plansky (eds), *Dual Residence in Tax Treaty Law and EC Law*, Vienna, 2009, p. 35 et seq., and to further references found therein. Note that, according to that scholar, referring to the Directive 83/182/EEC for the purposes of a DTC is not appropriate (p. 48).

98. Think, for instance, to those DTCs which include provisions on frontier workers or workers that move from a frontier area in a contracting state to a frontier area in the other contracting state: it cannot be excluded that EU law can play a role in interpreting those DTC provisions; this issue, however, will not be covered in the present paper.

99. B.J.M. Terra and P.J. Wattel, *European Tax Law*, Alphen aan den Rijn, 2008, p. 568. Those scholars recall that the Arbitration Convention is based on Article 293 of the EC Treaty (repealed in the new TFEU) but still is not an EU law instrument, and notice that the use of Article 293 of the EC Treaty as a legal basis has several consequences. For instance, the Convention does not confer any jurisdiction on the ECJ; the Convention does not have of itself direct effect; the Convention does not contain an implementation dead-

relevant in the interpretation of DTCs pursuant to article 31(3)(c) of the VCLT and, possibly, to treaty provisions patterned along the lines of article 3(2) of the OECD MC, to a very similar extent to that examined in respect of EU law.

Furthermore, it is submitted that nothing prevents a court from taking into account also intrinsically non-binding instruments made in connection with the Arbitration Convention, insofar as they “denote a continuous evolution in the norms and principles applied in international law or in the domestic law of the majority of [the parties] and show, in a precise area, that there is common ground in modern societies”.<sup>100</sup> Accordingly, nothing prevents a court from taking into account the Revised Code of Conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (2009/C 322/01). This view is apparently shared by the Member States which adopted the Revised Code of Conduct, considering that at point 4 it is affirmed that “[a]s far as transfer pricing cases are concerned, Member States are recommended to apply this definition also to the determination of the 3-year period as provided for in article 25.1 of the OECD Model Tax Convention on Income and on Capital and implemented in the double taxation treaties between Member States”<sup>101</sup> and that at point 6.5 it is stated that “[a]s far as transfer pricing cases are concerned, Member States are recommended to apply the provisions of points 1, 2 and 3 also to mutual agreement procedures initiated in accordance with article 25(1) of the OECD Model Convention on Income and on Capital, implemented in the double taxation treaties between Member States”.<sup>102</sup>

In addition, a court could also take into account intrinsically non-binding instruments made at EU level with regard to transfer pricing, such as the Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council, of 27 June 2006 on a Code of Conduct on Transfer Pricing Documentation for Associated Enterprises in the European Union (2006/C 176/01).

## 6. Conclusion

The examples made above reflect only some of the possible applications of the approach proposed in this paper, i.e. to give relevance to EU law for the interpretation of DTCs under article 31(3)(c) of the VCLT and/or under treaty provisions patterned along the lines of article 3(2) of the OECD MC. Further examples can perhaps be found and the author’s view is that the continuing evolution of EU law will likely increase the number of cases where it can be relevant in the interpretation of DTCs.<sup>103</sup>

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line; and a State may unilaterally terminate the Convention but it cannot unilaterally terminate being bound by an EU regulation or directive.

100. ECtHR, *Demir and Baykara v. Turkey*, cit., para. 86.

101. The definition at stake regards the starting point of the three-year period which represents the deadline for submitting the request to start a mutual agreement procedure under Article 6(1) of the Arbitration Convention.

102. Provisions of points 1, 2 and 3 regard the scope of the Arbitration Convention, the admissibility of a case and the commitment not to apply serious penalties except from exceptional cases like fraud, respectively.

103. This conclusion is corroborated by the following statement of the European Commission found in the *Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee – Double Taxation in the Single Market*, COM(2011) 712 final of 11 November 2011: “Double taxation often results from interpretation conflicts. There is a need to assess the scope for developing in the European Union, where possible, a common understanding of some concepts contained in DTC applicable between MS (...). Depending on the case, it may be appropriate to have regard to identical or similar notions contained in EU law, as a specific EU dimension to the problem. Because of their importance for the internal market, it is appropriate to discuss these issues at EU level. However, such coordination may

Lord Denning once famously said that “the flowing tide of Community law is coming in fast. It has not stopped at the high water mark. It has broken the dykes and the banks. It has submerged the surrounding land. So much so that we have to learn to become amphibious if we wish to keep our heads above water” [*Shields v. E Coomes (Holdings) Ltd*, (1978) 1 WLR, p. 1408 et seq. (at p. 1416)]. He was commenting on the pervasive importance of Community Law to Member States. Who knows whether he was also thinking of the possibility that the flowing tide could be submerging the land of other treaties such as Double Taxation Conventions.

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also contribute to the discussions held by international bodies such as the OECD and the UN, including when it comes to developing wider international standards. (...)”. (emphasis added)

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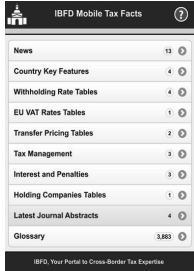

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