# Beneficial Ownership – Global Tax Treaty Commentaries


## Author

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## Latest Information

This chapter is based on information available up to 1 August 2020. Please find below the main changes made to this chapter up to that date:

Completely new chapter.

## 0. Abbreviations and Terms

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| 2002 Reports | OECD Committee on Fiscal Affairs, *2002 Reports on the OECD Model Tax Convention* (OECD 2002) |
| AG | Advocate General |
| AN | *Audiencia Nacional* (National Court) (Spain) |
| BEPS | Base erosion and profit shifting |
| BO | Beneficial owner |
| BoS | Bank of Scotland |
| CE | *Conseil d'État* (Supreme Administrative Court) (France) |
| CIV | Collective investment vehicle |
| CIVs Report | OECD Committee on Fiscal Affairs, *The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles* (OECD 2010) |
| CRC | *Commission fédérale de recours en matière de contributions* (Federal Tax Appeal Commission) (Switzerland) |
| DGT | Directorate-General for Taxation (Indonesia) |
| DTC | Double taxation convention |
| ECJ | Court of Justice of the European Union |
| FATF Recommendations | Financial Action Task Force, *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations* (FATF 2019) |
| FCA | Federal Court of Appeal (Canada) |
| GAAR | General anti-avoidance rule |
| HMRC | Her Majesty's Revenue and Customs (UK) |
| ICG Report | OECD Ctr. for Tax Policy and Admin., *Report of the Informal Consultative Group on the Taxation of Collective Investment Vehicles and Procedures for Tax Relief for Cross-Border* |


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| | *Investors on Possible Improvements to Procedures for Tax Relief for Cross-Border Investors* (OECD 2009) |
| LOB | Limitation on benefits |
| MLI | *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (7 June 2017) |
| MNE | Multinational enterprise |
| OECD | Organisation for Economic Co-operation and Development |
| OECD 2011 Discussion Draft | OECD Ctr. for Tax Policy and Admin., *Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention – Discussion Draft: 29 April 2011 to 15 July 2011* (OECD 2011) |
| OECD 2012 Revised Draft | OECD Comm. on Fiscal Affairs, *OECD Model Tax Convention – Revised Proposals Concerning the Meaning of "Beneficial Owner" in Articles 10, 11 and 12: 19 October 2012 to 15 December 2012* (OECD 2012) |
| OEEC | Organisation for European Economic Co-operation |
| Partnerships Report | OECD Committee on Fiscal Affairs, *The Application of the OECD Model Tax Convention to Partnerships* (OECD 1999) |
| PPT | Principal purpose test |
| TCC | Tax Court of Canada |
| TEAC | *Tribunal Económico-Administrativo Central* [Central Economic-Administrative Court] (Spain) |
| TIN | Taxpayer identification number |
| WP27 | Working Party 27 of the Fiscal Committee |

# 1. Introduction

Some years ago, the discussion of a panel of experts commenced by pointing out that there is still much uncertainty about the meaning of "beneficial ownership" or 'beneficial owner' (hereinafter BO ), despite the importance of the concept for application of the dividends, interest and royalties articles of tax treaties (DTCs).[1]The same panel also noted that "there are remarkably

1. J.D.B. Oliver et al., *Beneficial Ownership and the OECD Model* , Brit. Tax Rev. 1, p. 27 et seq. (2001); also published as *Beneficial Ownership* , 54 Bull. Intl. Fisc. Docn. 7, p. 310 et seq. (2000), Journal Articles & Papers IBFD. *See also* , on this concept, K. Vogel, *On Double Taxation Conventions* preface to arts. 10-2, paras. 5-14 (Kluwer 1997); S. van Weeghel, *The Improper Use of Tax Treaties* p. 64 et seq. (Kluwer 1998); C. Du Toit, *Beneficial Ownership of Royalties in Bilateral Tax Treaties* (IBFD 1999), Books IBFD; J. Walser, *The Concept of Beneficial Ownership in Tax Treaties* , in *The OECD Model Convention – 1998 and Beyond: Proceedings of a Seminar held in London in 1998 during the 52nd Congress of the International Fiscal Association* (Kluwer Law International 2000); P. Baker, *Double Taxation Conventions* art. 10, para. 10B-09 et seq. (Sweet & Maxwell 2000); H. Pijl, *The Definition of "Beneficial Owner" under Dutch Law* , 54 Bull. Intl. Fisc. Docn. 6, pp. 256-60 (2000), Journal Articles & Papers IBFD; H. Pijl, *Beneficial Ownership and Second Tier Beneficial Owners in Tax Treaties of the Netherlands* , 31 Intertax 10, pp. 353-61 (2003); R. Danon, *Switzerland's Direct and International Taxation of Private Express Trusts* p. 296 et seq. (Schulthess 2004); R. Danon, *Le concept de bénéficiaire effective dans le cadre du MC OCDE* , IFF Forum für Steuerrecht 1, pp. 38-55 (2007); R. Danon, *Le concept de bénéficiaire effective et les structures de relais direct* , 77 Archives de Droit Fiscal Suisse 1-2, pp. 105-117 (2008); J. Wheeler, *The Attribution of Income to a Person for Tax Treaty Purposes* , 59 Bull. Intl. Fisc. Docn. 11, pp. 478-479 (2005), Journal Articles & Papers IBFD; J. Wheeler, *General Report* , in *Conflicts in the Attribution of Income to a Person* (IFA Cahiers vol. 92b, 2007), Books IBFD; J. Bernstein, *Beneficial Ownership: An International Perspective, 47 Tax Notes Intl.* 17, pp. 1211-1216 (2007); L. De Broe, *International Tax Planning and Prevention of Abuse* p. 654 et seq. (IBFD 2008); A.J. Martín Jiménez, *Beneficial Ownership: Current Trends* , 2 World Tax J. 1, p. 35 et seq. (2010), Journal Articles & Papers IBFD; or the various contributions in *Beneficial Ownership: Recent Trends* (M. Lang et al. eds., IBFD 2013), Books IBFD – in this book, of special interest for understanding the evolution of beneficial ownership (BO) are the contributions by R. Vann, *Beneficial Ownership: What Does History (and Maybe Policy) Tell Us* , p. 267 et seq., and J.F. Avery Jones, *The Beneficial Ownership Concept Was Never Necessary in the Model* , p. 333 et seq. More recent contributions include A. Meindl-Ringler, *Beneficial Ownership in International Tax Law* (Kluwer 2016); R. Danon, *Treaty Abuse in the Post-BEPS World: Analysis of the Policy Shift and Impact of the Principal Purpose Test for MNE Groups* , 72 Bull. Intl. Taxn. 1, pp. 31 et seq. (2018), Journal Articles & Paper IBFD; and R. Danon, *Tax treaty abuse from a Swiss perspective: Current state of affairs, uncertainties and future perspective* in *Au carrefour des contributions: Mélanges de droit fiscal en l'honneur de Monsieur le Juge Pascal Mollard* pp. 413-446 (Stämpfli 2020).

few court cases on the tax treaty meaning of term".[2] Things changed dramatically in the years that followed: many court decisions as well as administrative positions on the concept of BO were released not only before but also after the changes made in the Commentaries on articles 10-12 of the OECD Model (2014),[3] to the point that it can probably be said that the concept was (and still is) regarded as a powerful tool in the arsenal of tax authorities to attack certain kinds of presumably abusive behaviours.

The rise in case law and administrative positions in recent years is directly connected with the changes promoted by the OECD in the Commentaries on articles 10-12 of the OECD Model over time (mainly 1977, 2003, 2014), and with the (unfortunate) conversion of BO into a handy replacement for certain anti-abuse tools at a certain point in time (i.e. 2003). As will be shown in this chapter, the history of the expression is unfortunate and is riddled with mistakes, misunderstandings and biased or interested use. Precisely this unfortunate history makes it very difficult to apply the term as the OECD desires following the 2014 changes to the Commentaries on articles 10-12 of the OECD Model, especially now that the Court of Justice of the European Union (ECJ) has made clear that it will defend a concept of BO that has little to do with the one recognized at OECD level.

The main goal of this chapter is to give the reader a clearer idea of the concept of BO, its evolution over time, the problems it presents and the administrative position and case law in representative jurisdictions. For that purpose, first, the policy and history of BO is explained in section 2. The history and evolution of BO in the OECD context plays a crucial role in understanding this term and its inherent problems and difficulties. Three different sub-sections have been devoted to this. After a brief introduction on the function of BO (section 2.1.), section 2.2. concentrates on the evolution of the meaning of the BO concept up to 2014. The crucial changes in the Commentaries on the OECD Model (2014) deserve dedicated attention, as they represent the meaning of BO currently defended by the OECD (section 2.3.). However, the effects of the OECD's base erosion and profit shifting (BEPS) outputs and the approval of the Multilateral Instrument (2017) (MLI)[4] and the OECD Model (2017)[5] also entail a truly fundamental shift in direction that, although not dealing directly with BO, has affected its meaning and relevance to the point that BO has been bypassed by other tools (section 3.). The evolution of BO in the UN Model is also referred to, in order to establish that the problems of the BO concept do not have much to do with the tax debate between developing and developed countries (section 4.). No study of BO is complete without an attempt to look into the most relevant positions and cases in different jurisdictions. This is done in section 5., in order to show that there is a fundamental gap between the OECD's current understanding of the term and how it is applied in most jurisdictions. Lastly, the conceptual and interpretative problems of BO will be dealt with in section 6. The conclusions there are in line with the paradoxes of a term that today forms part of the "international tax landscape",[6] but which is an important candidate to disappear from the OECD Model if legal certainty is taken seriously. However, deleting BO from the OECD Model need not mean that the concept is totally irrelevant: in the end, its original meaning represents a principle or rule that is present in all legal and tax systems, as it will be shown, and this should also be recognized at tax treaty level.

The way that BO has developed and been used should lead us to think about the making of international tax law and its interaction with domestic systems, and about whether tax and legal certainty calls for improved practices. This issue will also be dealt with in the conclusions in section 7.

# 2. Policy and History

## 2.1. The function of BO in the OECD and UN Models

The concept of BO is used only in articles 10, 11 and 12 of the OECD Model. The benefits of those articles (reduced rates in articles 10 and 11, no taxation in article 12) are subject to fulfilment of the BO requirement. Therefore, access to articles 10 through 12 depends not only on the recipient being a resident of the other contracting state, but also on the recipient being recognized as the BO of the specific item of income paid and received. However, as will be explained in section 6.5., the BO requirement, although not present in other distributive rules of the OECD Model, can be assumed as an implicit condition of other articles.

2. C. Du Toit, in Oliver et al., *supra* n. 1, at p. 31.
3. *OECD Model Tax Convention on Income and on Capital: Commentary on Article 10* (26 July 2014), Treaties & Models IBFD; *OECD Model Tax Convention on Income and on Capital: Commentary on Article 11* (26 July 2014), Treaties & Models IBFD; *OECD Model Tax Convention on Income and on Capital: Commentary on Article 12* (26 July 2014), Treaties & Models IBFD.
4. *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (7 June 2017), Treaties & Models IBFD [hereinafter *Multilateral Instrument*].
5. *OECD Model Tax Convention on Income and on Capital* (21 Nov. 2017), Treaties & Models IBFD.
6. D. Gutmann, *The 2011 Discussion Draft on Beneficial Ownership: What Next for the OECD?*, in *Beneficial Ownership: Recent Trends* p. 342 (M. Lang et al. eds., IBFD 2013), Books IBFD.

The UN Model (2017)[7] also uses the BO concept in articles 10, 11, 12 and 12A (for a more detailed explanation of how BO is used in the UN context, *see* section 4. ). In all those articles, the reduced taxation in the source state is dependent on the recipient being the BO of the dividends, interest, royalties or fees for technical services.

## 2.2. History and evolution of BO up to 2014

### 2.2.1. The origins of the concept prior to the OECD Model (1977): an answer to UK needs

The introduction of the concept of BO was directly linked with the needs of the United Kingdom in the 1960s and some peculiarities of its legal order at that time.[8] In the United Kingdom, unlike in many countries, "nominees" and "trustees" were liable to tax when they received income, even if it belonged to their true owners and the trustees and nominees were not entitled to it ( this tax treatment was applicable even in the case of non-accumulation trusts).[9] However, the rule had an exception: nominees or trustees were not subject to tax in the United Kingdom with regard to non-UK income that would belong to non-residents of the United Kingdom.

In the absence of the second sentence of article 4(1) of the OECD Model (1977-2017),[10] which did not exist in the version of article 4 appearing in the OECD Draft Model (1963) ,[11] the effect of the domestic UK treatment of nominees, trusts and trustees was that a resident of a third country could use UK nominees or trustees to invoke UK tax treaties and obtain reductions from withholding taxes in source states.[12] Therefore, treaty shopping of UK tax treaties to the detriment of the other contracting state was easy if UK nominees and trusts were interposed. Initially, the United Kingdom used subject-to-tax provisions to prevent this type of abuse of its treaties. Eventually, the United Kingdom decided that a BO clause would better attain the intended purpose without excluding entities such as pension funds and charities from the benefits of tax treaties, as can happen with subject-to-tax clauses.[13] In 1967, in the context of efforts to revise the OECD Draft Model (1963) and in connection with articles 10-12 thereof, the UK delegates expressed the following doubts:

> If a "subject to tax" test is not included in these Articles [10, 11 and 12][14] we think that the drafting is defective. The items of income which qualify for relief in the country of source are those which are paid to a resident of the other contracting State. In our view the relief provided for under these Articles ought to apply only if the beneficial owner of the income in question is resident in the other contracting State, for otherwise the Articles are open to abuse by taxpayers who are resident in third countries and who could, for instance, put their income into the hands of bare nominees who are resident in the other contracting State. You will no doubt have noticed that in our recent protocols with the United States and with Switzerland we have introduced this test of beneficial ownership which clearly reflects what was intended by the Committee when the Model Convention was prepared.[15]

The issue was further studied by Working Party 27 of the Fiscal Committee (Luxembourg, France, the Netherlands). With regard to article 12, the WP27 largely regarded the BO concept as an administrative problem of determining who the "true recipient" of the income is, rather than an anti-abuse problem, as the United Kingdom first presented the issue.[16] The WP27

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7. *United Nations Model Double Taxation Convention between Developed and Developing Countries* (1 Jan. 2017) , Treaties & Models IBFD.
8. In UK practice and in treaty negotiations, however, the term BO had previously been used with a number of different meanings and policy goals: (i) to deal with the situation of agents and nominees (the meaning that later found its way into the *OECD Model Tax Convention on Income and on Capital* arts. 10-12 (11 Apr. 1977) , Treaties & Models IBFD); (ii) in connection with the protection of lower rates on intra-group dividends, so that they only applied in the case of true subsidiaries; (iii) to refer to trustees of "accumulation trusts" when they were taxed; and (iv) in connection with certain conflicts of attribution involving deceased estates and beneficiaries. *See* Vann, *supra* n. 1 , at p. 271, and R. Ng, *The Concept of Beneficial Ownership* , in *History of Tax Treaties* p. 509 et seq. (T. Ecker & G. Ressler eds., Linde 2011), for an excellent explanation of the pre- OEEC /OECD situation before 1977.
9. *See* Avery Jones, *supra* n. 1 , at p. 333 et seq. The discussion of UK domestic legislation in this chapter relies on this work by Avery Jones.
10. The second sentence of art. 4(1) *OECD Model* (2017) reads as follows: "This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein."
11. *OECD Draft Model Tax Convention on Income and on Capital* art. 4 (30 July 1963) , Treaties & Models IBFD [hereinafter *OECD Draft Model* (1963)]. An equivalent sentence – although referring to individuals and not persons – was, however, included in the *OECD Draft Model Tax Convention on Income and on Capital: Commentary on Article 4* para. 10 (30 July 1963) , Treaties & Models IBFD. As noted by Avery Jones, *supra* n. 1 , at pp. 336-337, the sentence was evidently important enough to be included in the text of article 4; it could otherwise be regarded as a case of the Commentary unduly changing the meaning of the article.
12. *See* , for a detailed explanation, Avery Jones, *supra* n. 1 , at p. 333 et seq.
13. On the early use of BO clauses in the UK tax treaties and their connection with subject-to-tax clauses, *see* Vann, *supra* n. 1 , at p. 271 et seq.; and J.F. Avery Jones et al., *The Origins of Concepts and Expressions Used in the OECD Model and Their Adoption by States* , 60 Bull. Intl. Taxn. 6, p. 249 (2006), Journal Articles & Papers IBFD.
14. Although the comment appears only in connection with articles 10 and 12, it seems that the UK delegation was also referring to article 11.
15. *Observations of Member Countries on Difficulties Raised by the OECD Draft Convention on Income and on Capital (Note by the Secretary of the Committee)* , TFD/FC/216 (9 May 1967), available at https://www.taxtreatieshistory.org (last accessed 4 Nov. 2019).
16. Vann, *supra* n. 1 , at p. 283; *Working Party no. 27 of the Fiscal Committee (Luxembourg – France – Netherlands), Preliminary report on suggested amendments to articles 11 and 12 of the Draft Convention, relating to interest and royalties respectively* , FC/WP27(68)1 (30 Dec. 1968), p. 14, made the following comment, chiefly in connection with royalties (although the same observations could be made with regard to interest or dividends):
If it is the desire of the United Kingdom Delegation to make relief in the country of source dependent on effective liability to tax in the recipient's country of residence, then the suggestion would be contrary to the spirit and the general arrangement of the Draft Convention.

seemed to reject the inclusion of a subject-to-tax clause as incompatible with the spirit of the Convention, and also to regard the attribution of income to the "true recipient" as somewhat implicit and applicable to all articles of a tax treaty. For the WP27, therefore, unlike for the United Kingdom, determining the "true owner" had more to do with correctly applying the treaty (the treaty should be applied when the income could be allocated to a resident of the other State) than with abuse of tax treaties *stricto sensu* .

Later, the Fiscal Committee discussed the inclusion of the BO concept in general for all articles of the OECD Model or only for articles 10-12 (this concept was added to article 10 at a later stage),[17]without formally adopting a decision,[18]but the scope of the discussion was already limited to "agents" and "nominees" (including within these terms also trustees), which were the cases that presented problems for the United Kingdom. No other cases were considered.

Eventually, the WP27 accepted the inclusion of BO in articles 11 and 12 instead of subject-to-tax clauses, which, they continued to believe, were contrary to the spirit of the Convention and difficult to administer. The WP27 also explicitly considered that payment of income to an agent or nominee did not present difficulties for most countries, because income was always attributable to its true owners and not to the agent or nominee. For those countries, unlike for the United Kingdom, it was not a problem to attribute income received by a trust to its beneficial true owners who were immediately entitled to the income. However, those countries were not harmed by the inclusion of BO if it solved a problem for the United Kingdom.[19]

This course of events confirms that the BO concept found its way into articles 10, 11 and 12 of the OECD Model (1977) to satisfy a UK need, and clarified that although nominees, agents and trustees in the United Kingdom could be taxed when they received passive income (except if derived from foreign sources and when it belonged to a non-UK resident), they, as such, could not benefit from the dividends, interest and royalties articles of income tax treaties. For other countries, the issue was fairly clear and did not present problems even if BO was not added to their tax treaties.[20]

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On the other hand, it is evident that relief in the country of source applies only if the recipient is actually resident in the other contracting State.
This is stated clearly in the text of paragraph 1. Moreover, determining who is the true recipient and his State of residence is a matter of administration and inspection.
Moreover, there is nothing in the Draft Convention to prevent Contracting States from agreeing upon a procedure whereby the State of source first levies tax according to its law and subsequently refunds the excess tax on production of a certificate by the competent administration that the recipient is resident in the other contracting State.
The Committee will be asked to give its opinion on the comment made by the United Kingdom Delegation.

17. *Working Party no. 1 of the Committee on Fiscal Affairs on Double Taxation – Working Group no. 23 (Germany – Belgium)* , *Revision of Article 10 of the 1963 Model Convention, and the Commentary Thereon* , CFA/WP1(73)2 (31 Jan. 1973), p. 2; *Summary of Discussions at the Seventh Meeting of Working Party no 1 on Double Taxation (13th-15th February, 1973)* , DAF/CFA/WP1/73.5 & Corrigendum (11 Apr. 1973), p. 5.

18. *Note on the Discussion of the First Report of Working Party no. 27 of the Fiscal Committee on Interest and Royalties during the 31st session of the Fiscal Committee held from 10th to 13th June, 1969* , DAF/FC/69.10 (4 July 1969), p. 6:
The Delegate for the United Kingdom considered that as they stood Articles 10, 11 and 12 were defective in that they would apply to dividends, interest and royalties paid to an agent or a nominee with a legal right to the income. He thought that there were two possible ways of remedying the situation: either a "subject to tax clause" could be introduced (as in the Luxembourg-United Kingdom Conventions) under which the source country would give up its taxing rights only if the resident country taxed the interest, or the Articles could be made to apply only to interest, etc., paid to the "beneficial owner" (as in the Netherlands-United Kingdom Convention). The Delegates for Switzerland and the United States both preferred the "beneficial owner" solution. The Delegate for the United Kingdom thought that it should be inserted in the Convention itself, not necessarily in Articles 10, 11 and 12, but possibly as a general provision in a separate Article. The Delegate for Germany found no trouble with the existing text and would prefer to make it clear in the commentaries that the recipient must be the beneficial owner. The Rapporteur agreed to take up this problem in his new report.

19. *See* Vann, *supra* n. 1 , at pp. 285-286. The relevant text in *Working Party No. 27 of the Fiscal committee (Luxembourg – France – Netherlands), Report on suggested amendments to Articles 11 and 12 of the Draft Convention, relating to interest and royalties respectively* , FC/WP27(70)1(16 Feb. 1970), pp. 13-14, is as follows:
The United Kingdom Delegation considers that as they stand Articles 10, 11 and 12 are defective in that they would apply to dividends, interests and royalties paid to an agent or a nominee with a legal right to the income. To remedy this situation, it proposes either that a "subject to tax clause" be introduced, under which the country of source would give up its right to tax only if the country of residence taxed the income, or else that these Articles be made to apply only to income paid to the "beneficial owner".
The Working Party recommends the second solution which seems more likely to meet with the general agreement of the Fiscal Committee. The first solution, which is aimed at making relief in the country of source dependent on effective taxation in the country of residence, would be contrary to the spirit and general economy of the Draft Convention and would moreover give rise to difficulties in the appreciation of the concept of "effective taxation".
The second solution consists in taking into consideration the State of residence of the beneficial owner, the dividends, interest or royalties and in disregarding the State of residence of the person having the receipt of such income, whether so doing in the name and on behalf of the beneficial owner, or in his own name but on behalf of the beneficial owner.
There is no reason to think that the case of the person acting manifestly as an agent in the name and on behalf of the beneficial owner gives rise to any difficulties.
It may be otherwise with the trustee acting legally in his own name out on behalf of the beneficial owner.
It is probable that certain States have no difficulty from the legal standpoint in attributing to the beneficial owner income received through a trustee.
Such States would, however, be in no way harmed by the insertion into the Model Convention of a text to ensure legal safety in other States for whom the interposition of a trustee could cause complications.
The Working Party therefore recommends that there be written into the Model Convention a provision whereby the "beneficial owner text" would be applied.
The tenor of such a provision might be modelled on that formulated for the same purpose in the convention between the Netherlands and the United Kingdom.

20. Vann, *supra* n. 1 , at p. 285-288; Avery Jones, *supra* n. 1 , at pp. 333-339.

In this initial stage, BO had nothing to do with "holding and conduit companies or conflicts of attribution";[21] it simply found its way into the OECD Model (1977) to solve a UK need that did not bother the other states. Paradoxically, when it was included in the OECD Model (1977), the United Kingdom no longer needed BO in tax treaties due to the addition of the second sentence in article 4(1) of that Model: from that sentence it was clear that UK trustees, agents or nominees that received foreign income on behalf of non-UK residents could not invoke the benefits of UK income tax treaties.[22]

The problems around the real meaning of BO, however, started to emerge in this period. First, the contours of the concept were not well delimited, as shown by the parallel work in the 1960s in the OEEC/OECD context on tax treaty abuse, in which the concept began to be used with the meaning of ultimate economic owner, rather than of real/legal owner.[23] Second, the translation of the expression into other languages and legal contexts compounded the problems, as the term was not known or had no equivalents in tax orders outside the Anglophone world.

## 2.2.2. The concept of BO in the OECD Model (1977)

Unlike their precursors in the OECD Draft Model (1963), articles 10(2), 11(2) and 12(1) of the OECD Model (1977) made the benefits of those articles (reduced withholding taxes or exemption at source) conditional on the recipient of the dividend, interest or royalty being the BO of the income. The Commentaries on articles 10-12 of the OECD Model (1977) noted that:

> the limitation of tax in the State of source is not available when an intermediary, such as an agent or nominee, is interposed between the beneficiary and the payer, unless the beneficial owner is a resident of the other Contracting State. States which wish to make this more explicit are free to do so during bilateral negotiations.[24]

In the 1977 Commentaries, a conduit or holding company was not explicitly mentioned, contrary to what was stated in some of the preparatory works on abuse in the 1960s. However, the reference to "intermediaries" in general and agents and nominees in particular left room for ambiguity, as "holding companies" were lumped together with those terms in the works of Working Party 27 before 1977.[25] However, the 1977 Commentaries drew attention to the following case:

> the beneficial owner of [dividends, interest or royalties] arising in a Contracting State is a company resident in the other Contracting State; all or part of its capital is held by shareholders resident outside that other State; its practice is not to distribute its profits in the form of dividends; and it enjoys preferential taxation treatment (private investment company, base company). The question may arise whether in the case of such a company it is justifiable to allow in the State of source of the [dividends, interest or royalties] the [limitation of tax or exemption] which is provided in paragraph 2 [dividends and interest or] 1 [royalties]. It may be appropriate, when bilateral negotiations are being conducted, to agree upon special exception to the taxing rule laid down in this Article, in order to define the treatment applicable to such companies.[26]

Contrary to the ambiguous reference to "intermediaries" (if read in the context of the WP27 report on treaty abuse) the paragraph quoted here suggests that the use of intermediate companies controlled by residents of third countries is not a problem to be solved by BO (even if the quoted example refers to a situation of non-distribution of the income received). If the contracting states had wished to attack that structure, a specific provision should have been added to the tax treaty, because the intermediate company would otherwise qualify as BO of the income received. Why would the outcome be different if the intermediate company receiving the income distributed it to the shareholders? Eventually, all intermediary companies will

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21. Vann, *supra* n. 1, at p. 288.
22. Avery Jones, *supra* n. 1, p. 339.
23. Vann, *supra* n. 1, at pp. 288-296. Although the outcome of the OEEC/OECD work on abuse in this period is far from impressive, they started to exclude holding companies from the scope of the term BO and, therefore, the discussion began to mix together problems of "fraud" (legal entitlement to income) and abuse (economic owner of the income). This is especially clear, as Vann, *supra* n. 1, at p. 291 explains, in *Working Party no. 21 (United States – Denmark), Third Report on Tax Avoidance through the Improper Use or Abuse of Tax Conventions*, FC/WP21(67)1 (21 Dec. 1967), p. 5:
Still another aspect of the problem of shifting incomes involves residents of third countries. A resident of such a country may have investments in state A, the income from which is subject to a given withholding tax. If there is a convention between A and B that provides for reduced withholding taxes on income flowing from either state to the other, the third country resident may use an intermediary in state B, *a holding company* or a nominee or other agent, through which to make his investments in state A [...] The factors required to bring into being the tax benefits described above are the following: (1) an individual or firm must be able to arrange its business or investment transactions so as to receive income in a foreign country in which little or no tax would be levied; (2) the country where the income is generated must exempt such income or tax it at a low rate; and (3) *the beneficial owner* of the income must either not be taxed at all on such income in his home country or he must be free of tax until the income is repatriated. (Emphasis added.)
From the text it seems clear that "holding companies" were, at least in certain cases, put on the same level as "agents and nominees". As Vann, *supra* n. 1, at p. 292, suggests, "[t]he apparent lumping together of holding companies, intermediaries, nominees and agents, however, suggests that they are all being tarred with the same brush and so susceptible to the same solution. This has proved to be an unfortunate coincidence, as it mixes up a legal style of test with an economic one."
24. Para. 12 *OECD Model: Commentary on Article 10* (1977); para. 8 *OECD Model: Commentary on Article 11* (1977). An identical text, but referred to the exemption in article 12, can be found in para. 4 *OECD Model: Commentary on Article 12* (1977).
25. *See supra* n. 23.
26. Para. 22 *OECD Model: Commentary on Article 10* (1977); para. 12 *OECD Model: Commentary on Article 11* (1977); para. 7 *OECD Model: Commentary on Article 12* (1977). The text as rendered here has been slightly modified to refer to the three articles at the same time.

distribute their income to the shareholders, so there is no reason to lift the veil of that company regardless of its distribution policy. This is not contradicted by the classification of BO as a clause designed to fight "improper use" of tax treaties in paragraph 10 of the Commentary on Article 1 of the OECD Model (1977), as tax avoidance and tax evasion are considered together under that label and, therefore, the reference did not mean anything different from the use of that term in articles 10-12 of the OECD Model (1977).

At that time, in the context of article 3 of the OECD Model (1977), New Zealand observed that "[f]or the purposes of Articles 10, 11 and 12 New Zealand would wish to treat dividends, interest and royalties in respect of which a trustee is subject to tax in the State of which he is a resident as being beneficially owned by that trustee". If the origins of the term are taken into account, the observation by New Zealand was not really necessary, as the problem of BO was connected with the specific treatment of trusts in the United Kingdom if the beneficiary was a non-UK resident and the income did not have its source in the United Kingdom. Because the issue was resolved with the second sentence of article 4 of the OECD Model (1977), the BO concept was no longer relevant and had no impact upon New Zealand trusts as long as they were subject to tax in that country. Nonetheless, New Zealand felt the need to clarify that "trustees" and "trusts", in general, were BOs if they were subject to tax in their State of residence. In such a case, however, there were no concerns about using a trust to treaty shop New Zealand's tax treaties, and this was not the case the BO concept was intended to address.

## 2.2.3. The Base and Conduit Companies Reports (1986)

The OECD returned to work on BO in the Base Companies Report and Conduit Companies Report.[27]Neither deals with BO in particular, but both have important references to it.

With a perspective oriented towards residence countries and abuse, the Base Companies Report mentions BO only in paragraph 38:

> While recognising that the base company as a legal entity has its place of effective management in the country where it has been set up and does not have a permanent establishment in the country of residence of the taxpayer, the latter country could at least, under its national tax law, attribute to the taxpayers the activities and/or the income of the base company. This approach would clearly not be contrary to the OECD Model if the base company acted as a mere intermediary, an agent, a fiduciary or nominee of the taxpayer (cf. for example the notion of beneficial owner in Articles 10 to 12 of the OECD Model). However, the question arises as to whether, quite generally, domestic rules as to who is regarded as the recipient of specific income for tax purposes are compatible with treaties. This question especially arises in the case of "anti-abuse" or "substance-over-form" rules according to which it is not the base company itself but its shareholder, who is regarded as the true recipient of the income shifted to the base company.

Vann has remarked that this paragraph suggests "an acceptance that beneficial ownership is not an appropriate remedy for base companies".[28]He interprets it as saying that BO is not a tool or solution to decide about the "true" or "ultimate owner" of income, an issue for which anti-avoidance rules would be required. In this author's opinion, the paragraph shares some of the ambiguity of the Commentaries on articles 10-12 of the OECD Model (1977) regarding the use of the term "intermediaries". In line with the work in the 1960s,[29]it seems to suggest that some base companies that are not mere agents or nominees could be regarded as "intermediaries" to which income could not be attributed as BOs.[30]In these cases, there would be no need to resort to any further anti-avoidance legislation or doctrine. Vann's position, however, is certainly right in suggesting that from the paragraph it cannot be derived that any interposed company could be attacked with the BO concept.

The interpretation suggested above of the reference to "intermediaries" in the Base Companies Report as connected with the same reference in the Commentaries to articles 10-12 of the OECD Model (1977) is in line with the Conduit Companies Report. The latter mentions BO only in paragraph 14:

> The OECD has incorporated in its revised 1977 Model provisions precluding in certain cases persons not entitled to a treaty from obtaining its benefits through a "conduit company". [...] Articles 10 to 12 of the OECD Model deny the limitation of tax in the State of source on dividends, interest and royalties if the conduit company is not the "beneficial owner". Thus the limitation is not available when, *economically*, it would benefit a person not entitled to it who interposed the conduit company as an intermediary between himself and the payer of the income (paragraphs 12, 8 and 4 of the Commentary to Articles 10, 11 and 12 respectively). The Commentaries mention the case of a nominee or agent. *The provisions would,*

27. OECD, *Double Taxation Conventions and the Use of Base Companies* (OECD 1986), Primary Sources IBFD [hereinafter *Base Companies Report*]; OECD, *Double Taxation Conventions and the Use of Conduit Companies* (OECD 1986), Primary Sources IBFD [hereinafter *Conduit Companies Report*].
28. Vann, *supra* n. 1, at p. 297.
29. *See supra* n. 23.
30. In the Commentaries on articles 10-12 of the OECD Model (1977), agents and nominees were cited as types of "intermediaries", whereas in the *Base Companies Report*, *supra* n. 27, at para. 38, the reference to "intermediaries" seems to be a different category placed alongside "an agent, a fiduciary or nominee of the taxpayer".

> *however, apply also to other cases where a person enters into contracts or takes over obligations under which he has a similar function to those of a nominee or an agent. Thus a conduit company can normally not be regarded as the beneficial owner if, though the formal owner of certain assets, it has very narrow powers which render it a mere fiduciary or an administrator acting on account of the interested parties (most likely the shareholders of the conduit company)*. In practice, however, it will usually be difficult for the country of source to show that the conduit company is not the beneficial owner. The fact that its main function is to hold assets or rights is not itself sufficient to categorise it as a mere intermediary, although this may indicate that further examination is necessary. [Emphasis added; in view of the difficulties of this further examination, the remainder of the paragraph further explained that paragraph 22 of the Commentary on Article 10 of the OECD Model (1977) suggested that such companies should be the object of special treatment in negotiations].

As in the Base Companies Report, this paragraph assimilates certain intermediate ("conduit") companies to nominees, but, unlike it, it describes what it means: companies with narrow powers that render them a mere fiduciary or administrator acting on account of other persons. The use in the text of "economically" is confusing, as a fiduciary or administrator is not the legal owner of the income, which belongs to the "legal owner", and the legal owner (the reference to administrator or fiduciaries is connected with legal ownership) is very different from the economic owner. An intermediate company, unlike the administrator or nominee, may be the legal owner of an item of income received, but, if the economic standard of traditional general anti-avoidance rules (GAARs) is applied, it may turn out not to be the economic owner of the income received.

The main innovation of the Base and Conduit Companies Reports is precisely the assimilation of some intermediate companies with agents or nominees in line with the work of the OECD in the 1960s and the ambiguity left open by the OECD Model (1977). They do so in a more limited manner than the work of the 1960s: the reports do not generally suggest an identification of "holding companies" with "nominees" or "agents" (the term "fiduciary" was also included in the Base Companies Report). Vann criticizes the Reports for extending the BO test from base companies to conduits,[31] but, in this author's opinion, the form in which they do so is an attempt to clarify cases in which an interposed company will perform the same function as an agent or nominee and, therefore, like agents or nominees, cannot be regarded as the legal owner of the income received. However, the reference to economic interpretation in the Conduit Companies Report is confusing, as it gives the impression that the conclusions on the BO concept apply to all forms of conduits or holdings and, therefore, that the meaning of BO is being expanded to make it coincide with a sort of general clause against conduit companies.

It is relevant also to stress that the Conduit Companies Report adopted a very formalistic (and, in this author's opinion, incorrect) attitude on the compatibility of domestic anti-abuse provisions and tax treaties. At that time the OECD defended the position that the international principle *pacta sunt servanda* would prevent the parties of an income tax treaty from applying their domestic anti-abuse norms and doctrines. In such a formalistic context, it was only a matter of time before tax administrations fixed their eyes upon the ambiguous BO concept and turned it into an anti-abuse tool, especially because the contours detailing when an interposed company would not be regarded as such were not well defined and were subject to interpretation (it is not clear when an interposed company has "narrow powers", or whether this expression refers to factual or legal powers; moreover, the reference to "economically" seems to evoke GAARs and not strict legal standards).

Although both reports had an impact on the 1992 revision of the Commentary on article 1 of the OECD Model, the Commentaries on articles 10-12 on BO, ambiguous as they were, remained largely unchanged in this respect until 2003.

## 2.2.4. The 1995 and 1997 changes to articles 10 and 11 of the OECD Model (and the further refinement of 2014): payments to recipients in account of BOs of the other state

The drafting of articles 10 and 11 of the OECD Model was slightly modified in 1995. The original words "if the recipient is the beneficial owner [of the dividends or interest]" were replaced with "if the beneficial owner [of the dividends or interest] is a resident of the other Contracting State".[32] The change sought to clarify that the article would apply even if the recipient was not the same person as the BO but both were resident in the same country. As the Commentary suggests, this clarification sought to eliminate uncertainty and could even be applied to the interpretation of tax treaties drafted in accordance with previous versions of the OECD Model (1963-1995).[33] A similar change with identical effects was introduced in article 12(1) of the OECD Model in 1997.

In 2014 it was further made clear that the reduced rates of articles 10-11 of the OECD Model were also applicable if the recipient was not a resident of the other country, but the BO was. This required changing the drafting of articles 10(2) and 11(2) of the OECD Model. The main reason for this new change was that this point was unclear, at least from a literal reading of

31. Vann, *supra* n. 1, at p. 298.
32. OECD Comm. on Fiscal Affairs, *The 1995 Update to the Model Tax Convention*, DAFFE/CFA(95)16 (10 Jan. 1995), pp. 6-7.
33. *See* *OECD Model Tax Convention on Income and on Capital: Commentary on Article 10* para. 12 (1 Sept. 1996), Treaties & Models IBFD; and *OECD Model Tax Convention on Income and on Capital: Commentary on Article 11* para. 8 (1 Sept. 1996), Treaties & Models IBFD.

articles 10 and 11, although from the Commentaries on these articles there was no doubt about the conclusion that the reduced rates would apply as long as the BO was a tax resident of the other contracting state.[34]

## 2.2.5. The 2003 changes to the Commentary on articles 10-12 of the OECD Model

In 1998, the OECD's report on Harmful Tax Competition heralded changes to the concept of BO that suggested a relevant broadening of its meaning.[35]Those changes were proposed in the 2002 Reports Related to the OECD Model Tax Convention by the OECD Committee on Fiscal Affairs (2002 Reports),[36]and were later included in the Commentaries to articles 10-12 of the OECD Model (2003) . Hence, paragraph 12 of the Commentary on Article 10 of the OECD Model (2003) was changed to the following (similar changes were made to paragraphs 8 and 4, respectively, of the Commentaries on articles 11 and 12 of the OECD Model (2003)):

> 12. The requirement of beneficial ownership . . . makes plain that the State of source is not obliged to give up taxing rights over dividend income merely because that income was immediately received by a resident of a State with which the State of source has concluded a convention. *The term beneficial owner is not used in a narrow technical sense, rather, it should be understood in its context and in the light of the object and purposes of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance* .
>
> 12.1. Where an item of income is received by a resident of a Contracting State acting in the capacity of agent or nominee it would be inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption merely on account of the status of the immediate recipient of the income as a resident of the other Contracting State. The immediate recipient of the income in this situation qualifies as a resident but no potential double taxation arises as a consequence of that status since the recipient is not treated as the owner of the income for tax purposes in the State of residence. *It would be equally inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption where a resident of a Contracting State, otherwise than through an agency or nominee relationship, simply acts as a conduit for another person who in fact receives the benefit of the income concerned*. For these reasons, the report from the Committee on Fiscal Affairs entitled "Double Taxation Conventions and the Use of Conduit Companies" concludes that a conduit company cannot normally be regarded as the beneficial owner if, though the formal owner, it has, as a practical matter, very narrow powers which render it, in relation to the income concerned, a mere fiduciary or administrator acting on account of the interested parties.[37][Emphasis added.]

Paragraph 21 of the 2002 Reports presented the changes as a "clarification" of the concept of BO. However, the policy goals of the changes were unclear and not explained. The 2002 Reports claimed to follow the work of the Conduit Companies Report, but the new paragraphs in the Commentaries on articles 10-12 of the OECD Model seem to exclude conduit companies from the concept of BO in a more general manner (as emphasized in the quotation). The new commentaries proposed by the 2002 Reports and accepted in 2003 presented the situations considered in the Conduit Companies Report as one of the cases, but not the only one, in which a conduit company would not be regarded as the BO. The message that the reader of the 2003 Commentaries received regarding the meaning of BO is, to say the least, ambiguous: conduit companies will not be BOs and the BO concept can be the tool to fight against conduits in general. This is not the meaning the BO concept had originally, or even in 1986 in the Conduit Companies Report , where its scope was much narrower.[38]

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34. *See* OECD, *OECD Model Tax Convention: Revised Proposals Concerning the Meaning of "Beneficial Owner" in Articles 10, 11 and 12* (OECD 2012), available at https://www.oecd.org/ctp/treaties/Beneficialownership.pdf (last accessed 15 May 2020), para. 30: "A literal interpretation of the words 'such dividends' in the preamble of paragraph 2 of Article 10 could lead to the conclusion that these dividends must be dividends that are paid direct to a resident of a Contracting State, which would be problematic where the direct recipient and the beneficial owner of the dividends are residents of two different States. Whilst existing paragraph 12.2 of the Commentary clearly indicates that such an interpretation should be rejected, it suggests that some States may wish to adopt a clearer wording in their bilateral treaties. The Working Party decided that, in order to remove any doubt, such clearer wording should be included in the Article itself. At the same time, it decided to clarify in the Commentary that this issue was dealt with through two different changes to the wording of the Article since the 1995 change that is already referred to in paragraph 12.2 only addressed the issue where the direct recipient and the beneficial owner of the dividends are both residents of the same State." The changes may have also been a reaction to the case law in some countries: for instance, the case of Italy, where access to the Italy-Japan tax treaty was refused in a case of payments from an Italian source to a US transparent partnership controlled by Japanese residents. *See* P. Pistone, *Italy: Beneficial Ownership and the Entitlement to Treaty Benefits in Presence of Transparent Entitities* , in *Beneficial Ownership: Recent Trends* p. 209 et seq. (M. Lang et al. eds, IBFD 2013).
35. *See* OECD, *Harmful Tax Competition: An Emerging Global Issue* (OECD 1998), para. 199, commenting on the strategies for fighting harmful tax regimes offered by some countries: "Another example involves denying companies with no real economic function treaty benefits because these companies are not considered as beneficial owner of certain income formally attributed to them. The Committee intends to continue to examine these and other approaches to the application of the existing provisions of the Model Tax Convention, with a view to recommending appropriate clarification to the Model Convention."
36. OECD Comm. on Fiscal Affairs, *Restricting the Entitlement to Treaty Benefits* , in *2002 Reports Related to the OECD Model Tax Convention* (OECD 2002), para. 21 et seq., Primary Sources IBFD.
37. *OECD Model Tax Convention on Income and on Capital: Commentary on Article 10* paras. 12 and 12.1 (28 Jan. 2003) , Treaties & Models IBFD.
38. Vann, *supra* n. 1 , at p. 300, holds a similar position. For him, the problem is that the concept of BO is linked with a much broader problem and policy: the fight against conduit companies. For Vann, the Conduit Companies Report had already embraced a completely different goal (fighting in general against conduit companies) than the one it had originally had (excluding agents and nominees from tax treaties). In this author's view, it was the 2003 changes that really broadened the BO concept and, therefore, created the confusion that Vann describes.

As Vann has pointed out, it cannot be discarded that the broad meaning attributed to BO in the 2002 Reports was linked with the absence of agreement regarding the interaction of domestic anti-avoidance rules with tax treaties. But when that issue was resolved in 2003 by adding to the Commentary on Article 1 of the OECD Model specific paragraphs on the guiding anti-abuse principle and compatibility of domestic GAARs or similar doctrines, "there was little need for the comments on beneficial ownership".[39]The outcome has been, as Vann also rightly remarked, a discretionary use of BO by tax administrations in different countries to fight against conduit companies in a broad sense, and not only against those conduit companies that have a function similar to an agent or nominee.[40]Such a use of BO is more in line with the policy goals of GAARs than with the narrow meaning that the concept of BO originally had, more connected with true legal ownership and unconcerned with establishing the economic or ultimate owner of the income. As will be seen in section 5., most countries currently use BO with this broad meaning, close to a GAAR, even after the 2014 changes to the OECD Model.

History repeats itself, and a similar mistake has been made as in 1977, when BO was added even though the term was no longer needed because of the inclusion of the second sentence in article 4(1) of the OECD Model. The more recent expansion of the concept was likewise unnecessary, because the policy need of fighting against conduit companies was already covered by the Commentary on Article 1 of the OECD Model (2003) and the new policy (for the OECD) of recognizing the compatibility of GAARs with tax treaties.

## 2.2.6. Other meanings of BO in the OECD materials

### 2.2.6.1. The Partnerships Report

The 1999 Partnerships Report of the OECD Committee on Fiscal Affairs (Partnerships Report)[41]also referred to BO, but with a slightly different meaning: it identified BO with attribution of income for tax purposes.[42]In its origins, the BO concept was intended to be an exception to the rules of attribution of income in the state of residence and, in particular, the UK rule that attributed income to agents, nominees and certain trusts in the United Kingdom. As a consequence, it may be supposed that the interpretation of BO as an attribution of income rule goes against its original intent, and is another twist that makes the BO concept accommodate still another tax policy purpose different from its original meaning. In this context, the BO principle is used to reinforce the idea that source states should take into account how an item of income arising in its jurisdiction is treated in the jurisdiction of the taxpayer claiming the benefits of the treaty.[43]

However, such a contradiction is less relevant than it may seem at first sight. From the beginning, the BO concept was also protecting the principle that attribution of income in the state of residence to the taxpayer should be the prevailing rule in tax treaties.[44]That was the general rule. The exception introduced by BO sought to reinforce this principle in a case where it was clear that the UK special rule (that income could be attributed to trustees and was taxable in their hands, but with exceptions in the case of non-UK residents) did not lead to a reasonable result because foreign income derived by the UK trustee for non-resident individuals was, in fact, allocated in the United Kingdom to the third-country resident, who was the true owner of the income. With the special rule, the United Kingdom did not tax that income belonging to residents of other states even if received by UK trustees. BO was, therefore, intended to allocate income to the person who really obtained it and to exclude from the scope of tax treaties treaties persons (trustees, nominees) that were not taxable in the United Kingdom in this specific case in connection with the income they received. In itself, this is an attribution rule that, in its original meaning, is not inconsistent at all with the general principle of the Partnerships Report. Rather it tries to apply it in a case where domestic rules on attribution of income produce unreasonable outcomes from the perspective of tax treaties.

The general approach of the Partnerships Report was incorporated into articles 10-12 of the OECD Model (2003).[45]The construction of BO as an attribution rule from the state of residence perspective, in line with paragraph 53 of the Partnerships

39. Vann, *supra* n. 1, at p. 300. A similar position was also expressed in A.J. Martín Jiménez, *The 2003 Revision of the OECD Commentaries on the Improper Use of Tax Treaties: A Case for the Declining Effect of the OECD Commentaries?*, 58 Bull. Intl. Fisc. Docn. 1, p. 20-21 (2004).
40. Vann, *supra* n. 1, at p. 301.
41. OECD Comm. on Fiscal Affairs, *The Application of the OECD Model Tax Convention to Partnerships* (OECD 1999) [hereinafter *Partnerships Report*].
42. Id., at para. 54: "Another approach would involve consideration of the terms of the distributive rules in the relevant Articles of the Convention. Under that analysis, in the case of dividends, interest and royalties, the inquiry would be whether or not the recipient of the ítem of income was the beneficial owner of the income under the laws of the State of residence of the taxpayer claiming the treaty benefits and thus the taxpayer in relation to the income. In the case of a partnership treated as transparent under the laws of the residence State, the entity itself and not the partners would be treated as beneficial owner. Because of the treatment of the income in the State of residence, the partners would not be the beneficial owners of the income for the purposes of the treaty. Thus the partners would not be entitled to treaty benefits in those circumstances and whether the entity was so entitled would depend on whether it independently qualified as a resident."
43. Id., at para. 53, claims that this principle is inherent in tax treaties; Vann, *supra* n. 1, at p. 302.
44. Vann, *supra* n. 1, at pp. 301-302, points out that there is a considerable contradiction in applying this approach only to articles 10-12, which are the only ones that use the concept of BO. In this author's view, the attribution approach could be applied with regard to all articles of a DTC, as, in the end, the BO concept does not add anything and merely stresses in the context of articles 10-12 a principle that is evident in most tax orders.
45. For instance, para. 12(1) *OECD Model: Commentary on Article 10* (2003) explains: "The immediate recipient of the income in this situation qualifies as a resident but no potential double taxation arises as a consequence of that status *since the recipient is not treated as the owner of the income for tax purposes in the State of residence*" [emphasis added].

Report, could, however, be regarded as implicit in previous versions of the OECD Model and DTCs. The elimination in 2003 of New Zealand's observation with respect to the consideration as BOs of trusts subject to tax in the state of residence confirms this impression, as does the fact that, when added in 1977, it had a clarifying nature. And this interpretation of BO is probably the best and most coherent ( *see* section 5.4. ).

However, the interpretation of BO as an attribution rule contradicts the broader interpretation that conduit companies are excluded from the BO concept, as also confirmed by the Commentaries on articles 10-12 of the OECD Model (2003) . From a legal perspective, a conduit company is usually attributed the dividends, interest and royalties it receives by the state of residence. Therefore, when conduits are excluded from the the BO concept and treaty benefits, this solution is at odds with the attribution principle derived from the Partnerships Report and, after 2003, also from the Commentaries on articles 10-12.

As a consequence, it appears that the concept of BO derived from the 2003 Commentaries undermines the solution that the Partnerships Report provided,[46]and was even in contradiction to the inclusion of the principles of the Partnerships Report in the Commentaries on article 10-12 of the OECD Model (2003) .

### 2.2.6.2. The CIVs Report and the TRACE project

The 2010 report by the OECD Committee on Fiscal Affairs on The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles ( CIVs Report )[47]observed that, in a few cases, collective investment vehicles (CIVs) have been denied treaty benefits by source countries because they are not regarded as BOs. The CIVs Report explained that investors in CIVs have no rights over the underlying assets managed by the CIV , and that the managers have discretion to manage the assets generating the income. As widely held CIVs meet these requirements, they should be regarded as BOs regardless of their treatment as transparent entities. The conclusions of the CIVs Report were later included in the Commentary on Article 1 of the OECD Model (2010) , especially paragraph 6(14) ( paragraph 28 of the Commentary on Article 1 of the OECD Model (2017) ), but the CIVs Report in itself is interesting because it recognized that some countries applied a BO concept from the perspective of their internal legislation as source countries, whereas others applied a different approach.

The CIVs Report (and, later, the Commentary on Article 1 of the OECD Model) produced yet another concept of BO that, ostensibly at least, is not directly connected with the interpretation of BO in the context of articles 10-12 of the OECD Models since 2003 or with the Partnerships Report . For the purposes of the CIVs Report, the concept of BO was linked with discretion in the management of assets and distribution policies of the CIVs (in comparison with publicly held corporations). This is a confusing test, which certainly contradicts the exclusion of conduit companies from the scope of BO, as most conduits have legal discretion, at least in theory, to dispose of the income they receive.[48]

Traditionally BO referred to the relationship of a stream of income with the recipient, not to the rights or powers of the recipient over the underlying asset. It appears that the OECD is using BO in the CIVs context with a different meaning from how it is used in connection with articles 10-12 of the OECD Model. It may also be the case that the OECD is using discretion as a proxy for allocation of the income to a taxpayer: if the managers have discretion over the assets and investments, then, in the end, they control the stream of income that will flow to the final investors and can be allocated the income (the CIV that is the BO must also be a person and a resident for the purposes of the applicable tax treaty). If that is the case, the meaning of BO in this context seems to be closer to its original formulation, but still some relevant contradictions remain. First, it is surprising that this principle applies only to widely held CIVs, and not to others in which there is a similar detachment between investors and assets and in which the managers also have broad discretion. Second, this formulation stands in contradiction to the "conduit position" after 2003: a conduit may be the legal owner and have discretion over income producing assets and the income received, but it will nevertheless not be considered the BO if there is an ultimate economic owner of the income that can be identified in view of the factual situation. The reasons for these inconsistencies (why are public CIVs regarded as BOs when a private CIV can have the same discretion and powers over the assets? Why is the approach to "conduits" stricter than the approach to CIVs, even if the conduit has the same legal powers as a public CIV?) are not easy to explain.

The CIVs Report is also linked with the OECD TRACE project,[49]which seeks to facilitate treaty access to portfolio investors who hold their investments (securities, including interest in CIVs) through one or more financial intermediaries. The 2009 OECD report on Possible Improvements to Procedures for Tax Relief for Cross-Border Investors (hereinafter ICG

46. Vann, *supra* n. 1 , at p. 302.
47. OECD Comm. on Fiscal Affairs, *The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles* (OECD 2010) , especially paras. 31-35 [hereinafter *CIVs Report* ].
48. As Vann, *supra* n. 1 , at p. 303, remarks, many stockbroker firms have discretion in management and they cannot be regarded as BOs. Likewise, the conduit may have at least theoretical discretion to manage the passive income generating assets, but may still be required de facto, even if not de jure, to pass on the income to other parties. The same can happen with CIVs.
49. On this project, *see* http://www.oecd.org/tax/treaties/aboutthetracegroup.htm (last accessed 6 Nov. 2019).

Report )[50]extensively used the concept of BO, but did not attempt to define it, although it recognized that countries applied different versions of the term. Later, in 2013, the OECD's TRACE Implementation Package[51]used an ambiguous concept of BO that is similar to the one in the Commentaries on articles 10 and 11of the OECD Model, but recognizes that countries' views on BO may vary; this was not of much help in clarifying its meaning.[52]The TRACE project, however, is interesting for understanding the problems that withholding agents have with the smooth application of tax treaties and with determining the BO of a specific payment ( *see* section 6.6. ).

### 2.2.6.3. Exchange of tax information, money laundering and registries of BOs

The generalization of exchange of information (on request and automatic) introduced yet another variation of the concept of BO in the international tax world.[53]In this area of tax law, BO has the same meaning as in money laundering legislation. In particular, the Financial Action Task Force's International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation ( FATF Recommendations )[54]defines BO in its General Glossary as follows:

> *Beneficial owner* refers to the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.

In fact, the Common Reporting Standard (for automatic exchange of information) tends to use the term "controlling person" as a synonym of BO as defined in the FATF Recommendations, but the expression BO also shows up often in exchange of information materials (e.g. in the Common Reporting Standard itself)[55]and is a fundamental pillar of the tax transparency standards promoted worldwide: thus, the Global Forum decided in 2014 that the Standard for exchange of information upon request should include a condition that BO information be available in respect of relevant legal persons and legal arrangements.[56]For exchange of information purposes, the concept of BO put forward is almost identical to that of the FATF Recommendations, taking into account that anti-money laundering legislation and tax laws pursue different goals: "Beneficial owners are always natural persons who ultimately own or control a legal entity or arrangement, such as a company, a trust, a foundation, etc."[57]In this context, the registries of BOs that have become popular in recent years are more closely connected with the meaning of the term in the context of money laundering or for exchange of tax information purposes than with the usual meaning in DTCs.[58]In all these cases, the main goal of the concept of BO is to identify and acquire information about the individuals who are the ultimate owners of a company, structure or arrangement.

## 2.2.7 The outcome of the historical evolution of BO up to 2014

Throughout history, the use of BO has been confusing. It was included in tax treaties and the OECD Model (1977) to correct a domestic effect of UK legislation, which attributed income to those that were not their true owners and could facilitate tax evasion by non-UK residents who could interpose agents, nominees or trustees to gain access to UK tax treaties without being taxed in the United Kingdom. The underlying idea of the BO concept from its origins was that income should be attributed to its true legal owners for tax treaty purposes. The concept, however, found its way to the OECD Model (1977) , even though it was no longer needed because of the inclusion of the second sentence of article 4(1) of that model. Unlike Vann, this author does not think that the Partnerships Report or CIVs Report follow a completely different policy, albeit there have been distortions in the way in which BO is used in the different documents and the meaning attributed to this expression through the years.

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50. *See* OECD Ctr. for Tax Policy and Admin., *Report of the Informal Consultative Group on the Taxation of Collective Investment Vehicles and Procedures for Tax Relief for Cross-Border Investors on Possible Improvements to Procedures for Tax Relief for Cross-Border Investors* (OECD 2009), Primary Sources IBFD [hereinafter *ICG Report* ].
51. OECD Comm. on Fiscal Affairs, *TRACE Implementation Package for the Adoption of the Authorised Intermediary System: A Standardised System for Effective Withholding Tax Relief Procedures for Cross-Border Portfolio Income* (OECD 2013), available at https://www.oecd.org/ctp/exchange-of-tax-information/TRACE_Implementation_Package_Website.pdf (last accessed 22 June 2020) [hereinafter *TRACE Implementation Package* ].
52. Id., at pp. 60, 63 and 72, notes in the instructions for self-declaration and intermediaries that "Beneficial Owner means the person that is entitled to the Securities Income for tax purposes and has the benefit thereof, taking into account the economic, legal, factual and other relevant circumstances under which the income is received; it does not mean a person who receives income as an agent, nominee or mere conduit for another person. Countries' views of the meaning of beneficial owners vary. Therefore you should consult available guidance to determine whether you are considered to be beneficial owner for purposes of claiming the applicable withholding relief."
53. On exchange of tax information in general and the Common Reporting Standards in particular, *see* D. Ring, *Article 26: Exchange of Information – Global Tax Treaty Commentaries* , Global Topics IBFD.
54. Financial Action Task Force, *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations* (FATF 2019), p. 113, available at http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf (last accessed 6 Nov. 2019).
55. *See* , for instance, OECD, *Standard for Automatic Exchange of Financial Information in Tax Matters: Implementation Handbook* (2nd ed., OECD 2018), pp. 21-22; or Global Tax Forum on Transparency and Exchange of Information & Inter-American Development Bank, *A Beneficial Ownership Implementation Toolkit* (OECD/IDB 2019), p. 38 et seq., available at https://www.oecd.org/tax/transparency/beneficial-ownership-toolkit.pdf (last accessed 7 Nov. 2019).
56. *See* id. on BO in the sphere of exchange of information in general.
57. Id., at p. 3; on the differences between BO in the context of money laundering and in exchange of tax information, *see* id., at p. 10 et seq.
58. On these registries, *see* id., at p. 18 et seq.

The most problematic interpretation of BO has its roots in the attempts to turn it into an anti-avoidance tool in 2002 and 2003, and, possibly, in the ambiguity (or lack of clarity) of its use in the previous Conduit Companies Report and Base Companies Report. As another irony of history, the meaning of BO was broadened in the Commentaries on the OECD Model (2003) just when it was no longer needed, because the 2003 changes in the Commentary on Article 1 of the OECD Model (2003) already permitted the application of domestic anti-avoidance doctrines in the context of income tax treaties. To a certain extent, the broad interpretation of BO and its widespread use as an alternative to GAARs by many states can be regarded as a natural reaction to the formalistic interpretation adopted by the OECD until 2003, under which GAARs and domestic anti-avoidance doctrines were not compatible with tax treaties. Many tax administrations (and judges) seem to have discovered in the BO concept a valve that permitted the flexibility that GAARs or similar doctrines provide in many domestic systems, without being significantly constrained by procedural obstacles to GAARs or the problem of whether domestic GAARs could be applied in a treaty context ( *see* section 5. on case law in this connection).

However, after 2003, the situation got out of control and began to pose a threat to the uniform application of tax treaties, with the result that the OECD stepped in again to clarify the concept ( *see* section 2.3. ). In this author's opinion, once the application of anti-abuse principles in a treaty context had been recognized, the best the OECD could have done was delete the concept from articles 10-12 of the OECD Model: most of the cases of interposition of persons to receive income that legally belongs to other persons can be dealt with by means of general principles or sham or simulation doctrines, whereas cases of conduits (true owners but not the ultimate economic beneficiaries) can better be approached by means of anti-avoidance rules and principles.[59]The principle that income should be allocated to its real and true legal owner could be simply stated in the Commentary on Article 1 of the OECD Model ( *see* section 6.5. ). Leaving the concept of BO in articles 10-12 of the OECD Model and at the same time permitting the application of anti-avoidance principles could only lead to uncertainty (i.e. the taxpayer may be exposed to the discretion of the tax authorities to use the tool that is more convenient for them). The OECD, however, opted for another round of "clarifications" of the concept.

## 2.3. The 2014 changes to articles 10-12 of the OECD Model

The process leading to the 2014 reform of the Commentaries to article 10 to 12 OECD MC on the concept of BO was not easy.[60]The decision to change the Commentaries was probably motivated by judgments in different jurisdictions ( *see* section 5. ) that clearly showed that the understanding of BO was far from universal, which posed a threat to the uniform application of tax treaties.

### The OECD 2011 Discussion Draft

In 2011, the OECD Centre for Tax Policy and Administration released for comments a first Discussion Draft on the Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention ( OECD 2011 Discussion Draft ),[61]which triggered reactions on various fronts and general criticism. The OECD 2011 Discussion Draft proposed to amend the Commentaries on articles 10-12 of the OECD Model[62]to the following effect:

- BO was not to be interpreted within the technical meaning it could have under the domestic law of a specific country, such as the meaning it could have in trust law. This meant that accumulation trusts could also be regarded as BOs;
- recipients of dividends, interests or royalties are the BOs where they have the full right to use and enjoy the dividends, interest and royalties. The recipient would not be considered the BO if the powers of that recipient over the dividend, interest or royalty are "constrained in that the recipient is obliged (because of a contractual, fiduciary or other duty) to pass the payment received to another person. The recipient ... is the 'beneficial owner' ... where he has the full right to use and enjoy the [dividend, interest or royalty] unconstrained by a contractual or legal obligation to pass the payment received to another person. Such a legal obligation will normally derive from relevant legal documents but may also be found to exist on the basis of facts and circumstances showing that, in substance, the recipient clearly does not have the full right to use and enjoy the [dividend, interest or royalty]";

59. *See* sec. 6. and especially sec. 6.6.3. ; Martín Jiménez, *supra* n. 1 ; and A.J. Martín Jiménez, *Beneficial Ownership as a Broad Anti-Avoidance Provision: Decision by Spanish Courts and the OECD's Discussion Draft* , in *Beneficial Ownership: Recent Trends* p. 139 et seq. (M. Lang et al. eds, IBFD 2013), Books IBFD. Other authors have also defended a similar position: *see* D.G. Duff, *Beneficial Ownership: Recent Trends* , in *Beneficial Ownership: Recent Trends* p. 25 (M. Lang et al. eds, OECD 2013), Books IBFD; and Vann, *supra* n. 1 , at p. 307.
60. The drafting of articles 10(2) and 11(2) was also changed in 2014; these changes have been explained in sec. 1.2.4.
61. OECD Ctr. for Tax Policy and Admin., *Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention – Discussion Draft: 29 April 2011 to 15 July 2011* (OECD 2011), Primary Sources IBFD, also available at https://www.oecd.org/ctp/treaties/47643872.pdf (last accessed 7 Nov. 2019) [hereinafter *OECD 2011 Discussion Draft* ].
62. Id., at pp. 3-5: proposed paras. 12-12.6 *OECD Model: Commentary on Article 10* . Similar paragraphs were proposed regarding articles 11 and 12.

- use and enjoyment of the dividend, interest and royalty must be distinguished from the legal ownership, as well as from the use, of the property (shares, debt claim or intangible);
- the conclusion that a person is the beneficial owner does not exclude the application of other anti-avoidance provisions (specific anti-avoidance clauses in treaties, GAARs, substance-over-form or economic substance approaches). BO deals only with some forms of avoidance (i.e. those involving the interposition of a recipient who is obliged to pass the dividend, interest or income to someone else); it does not deal with other cases of treaty shopping; and
- the BO concept does not refer in the context of articles 10-12 of the OECD Model to the meaning given to this term in the context of money laundering or exchange of information, where the expression refers to the persons (individuals) that exercise ultimate control over entities or assets.

The OECD 2011 Discussion Draft was widely criticized for its vagueness, mainly because there was no explanation of when the obligation to pass the income to a third party would exclude the status of BO.[63]The draft clearly identified the BO as the recipient having a "full right to use and enjoy the income", but, between that position and that of nominee, agent or conduit acting as a beneficiary, there are many situations that were not clarified. Moreover, the obligation to pass on income to a third party when income was received (which seemed to be the defining characteristic leading to exclusion from the BO) was too general and unclear and could capture many legitimate situations. Definition of the BO as per the OECD 2011 Discussion Draft would have caused even more uncertainty than before in a good number of very frequent business transactions in which income is received and later paid to a third party (e.g. banks receiving and paying interest; holding companies; use of dividends to settle loans or any other obligations; transactions in derivative and financial markets in general; issuance of securities, bonds and securitization agreements; payments for licences or sublicences; finance and cash pooling companies; and CIVs).[64]

Apart from the specific reference to accumulation trusts in a footnote, the OECD 2011 Discussion Draft also did not make fully clear whether taxation in the state of the recipient was sufficient for a person to be regarded as the BO, contrary to the position already adopted by the OECD in the Partnerships Report. This was an element of uncertainty, although the principles of the Partnerships Report had already been incorporated in the Commentaries to articles 10-12 of the OECD Model (2003) (access to the treaty should be granted if the recipient was subject to tax in the state of residence). A further refinement of the definition of BO was therefore needed.

## The OECD 2012 Revised Draft

On 19 October 2012, the OECD Committee on Fiscal Affairs released Revised Proposals Concerning the Meaning of "Beneficial Owner" in Articles 10, 11 and 12 ( OECD 2012 Revised Draft ), with relevant changes to the proposed commentaries to article 10 to 12 OECD on the concept of BO.[65]The main changes, in comparison with the OECD 2011 Discussion Draft, affected paragraph 12.4 of the Commentary on Article 10, paragraph 10.2 of the Commentary on Article 11 and paragraph 4.3 of the Commentary on Article 12. The OECD 2012 Revised Draft first emphasized the autonomy of the BO concept with respect to domestic law.[66]

Although the OECD 2012 Revised Draft continued to emphasize the connection between revenue received and paid as an essential feature that could disqualify a person as BO, it eliminated the references to the "full right to use and enjoy the payment" that had caused confusion in the OECD 2011 Discussion Draft. In addition, it better explained the relationship between the payment received and the payment made that causes the recipient not to be regarded as the BO: the obligation to pass on the payment received to another person "must be related to the payment received". This link will not exist when the "contractual or legal obligation" to pay income to a third party is "unrelated to the payment received even if those obligations could effectively result in the recipient using the payment received to satisfy those obligations". Some examples in which the link would not exist (and in which, therefore, the person making the payment would be regarded as BO) include "unrelated obligations that the recipient may have as a debtor or as a party to financial transactions or typical distribution obligations of pension schemes and collective investment vehicles". After those examples, the status of BO was identified with the right of the recipient of the dividends, interests or royalties to use and enjoy the revenue received "unconstrained by a contractual or legal obligation to pass on the payment received to another person".

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63. *See* , for instance, the response by J.F. Avery Jones, R. Vann and J. Wheeler, available at http://www.oecd.org/tax/treaties/48420432.pdf (last accessed 8 Nov. 2019); Duff, *supra* n. 59 , at pp. 2-3 and pp. 17-21; Vann, *supra* n. 1 , at 304-305; and Martín Jiménez, *supra* n. 59 , at pp. 138-139.
64. A full list of situations in which the proposed paragraph 12.4 could have negative effects on legitimate situations was included in OECD Comm. on Fiscal Affairs, *OECD Model Tax Convention – Revised Proposals Concerning the Meaning of "Beneficial Owner" in Articles 10, 11 and 12: 19 October 2012 to 15 December 2012* (OECD 2012), pp. 6-7, available at https://www.oecd.org/ctp/treaties/Beneficialownership.pdf (last accessed 5 June 2020) [hereinafter *OECD 2012 Revised Draft* ].
65. Id.
66. Para. 12.1 *OECD Model: Commentary on Article 10* (2014) would delete the sentence included in the *OECD 2011 Discussion Draft* referring to domestic law meanings of the term that could be applied in a treaty context if they were compatible with the Commentaries. Similar changes were proposed with regard to the interest and royalty articles.

As suggested by some commentators, the OECD 2012 Revised Draft was much less uncertain and more concrete than its 2011 predecessor. Therefore, although still vague in certain aspects, the proposed changes were better drafted.[67]However, the fact that the OECD 2012 Revised Draft did not define with more clarity when obligations (reception of the income and payment of it) are related or unrelated might be interpreted as still giving the tax administrations some leeway in interpreting the BO concept as a fairly broad anti-abuse tool. Although there was an attempt to clarify the situation of conduits (by specifying that "conduits acting as a fiduciary or administrator" were excluded from the concept of BO,[68]or by referring to other anti-avoidance clauses),[69]there was still margin for a broad interpretation of the conduit concept – as had been the case with the 2003 changes to the Commentaries and, to a lesser extent, with the 1986 Conduit Companies Report. On the other hand, it is also positive that (i) it was made clear that BO refers to the income (and not to the underlying asset);[70]and (ii) the proposed changes excluded BO from having, in the context of articles 10-12, the meaning given to the same expression in other contexts (e.g. in relation to the law of trusts,[71]money laundering or exchange of information).[72]

## The 2014 revision of the Commentaries on articles 10-12 of the OECD Model

The 2014 revision of the OECD Model and Commentaries included all the changes proposed in the OECD 2012 Revised Draft and only added some minor drafting modifications in paragraph 12.4 of the Commentary on Article 10, (the same changes were added in paragraph 10.2 of the Commentary on Article 11 and in paragraph 4.3. of the Commentary on Article 12). The definition of BO remained the same:

> In these various examples (agent, nominee, conduit company acting as a fiduciary or administrator), the direct recipient of the dividend [or interest or royalty] is not the "beneficial owner" because that recipient's right to use and enjoy the dividend is constrained by a contractual or legal obligation to pass on the payment received to another person. Such an obligation will normally derive from relevant legal documents but may also be found to exist on the basis of facts and circumstances showing that, in substance, the recipient clearly does not have the right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass on the payment received to another person.

But the second part of paragraph 12.4 of the Commentary on Article 10 of the OECD Model (2014) (as also paragraph 10.2 of the Commentary on Article 11 and paragraph 4.3. of the Commentary on Article 12) was indeed modified in a slight but relevant manner. The OECD 2012 Revised Draft stated that the obligation that disqualifies the recipient as BO "must be related to the payment received" and would not include obligations unrelated to the payment received "even if those obligations could effectively result in the recipient using the payment received to satisfy those obligations". However, the final text of paragraph 12.4 is more ambiguous, because it eliminates the expression "must be related to the payment received" in connection with the obligation to pay the funds received that disqualifies the recipient from BO. The 2014 Commentaries refer only to "obligations" that are not dependent on the payment received as cases of "repayment" of the funds received that would not exclude the recipient from the category of BO. This suggests that, in the final text accepted in the Commentaries, when revenue received is used to pay another obligation, there is a chance that the "dependency" relation between revenue received and paid could be appreciated with more subjectivity and, therefore, the classification of the recipient/payer as BO will be excluded. The final sentence of paragraph 12.4 in which changes were made is now as follows (the rest of paragraph 12.4 remained unchanged):

> This type of obligation would not include contractual or legal obligations that are not dependent on the receipt of the payment by the direct recipient such as an obligation that is not dependent on the receipt of the payment and which the direct recipient has as a debtor or as a party to financial transactions, or typical distribution obligations of pension schemes and of collective investment vehicles entitled to treaty benefits under the principles of paragraphs 6.8 to 6.34 of the Commentary on Article 1

The rest of the modifications proposed by the 2012 OECD Draft were included in the 2014 revision of the OECD Model and were not modified in 2017. Therefore, the comments made above with regard to the OECD 2012 Revised Draft could be reiterated here: the definition of the BO concept is now less broad and ambiguous than in 2003. As a consequence, it is also

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67. Vann, *supra* n. 1 , at p. 307.
68. *OECD 2012 Revised Draft* , *supra* n. 64 , at pp. 5-6: proposed drafting of paras. 12.3 and 12.4 *OECD Model: Commentary on Article 10* . Identical proposals were made with respect to the drafting of the Commentaries on articles 11 and 12. Similar references to conduits acting as fiduciaries or administrators were also present in the Commentaries after 2003, but they were vaguer on whether this was only an example of a conduit that would not be regarded as the BO, so that, therefore, other conduits could also be excluded from the concept of BOs.
69. Id., at p. 10: proposed drafting of para. 12.5 *OECD Model: Commentary on Article 10* . Identical proposals were made with respect to the drafting of the Commentaries on articles 11 and 12.
70. Id., at p. 6: the last sentence of the proposed para. 12.4 *OECD Model: Commentary on Article 10* remarked that "Article 10 refers to the beneficial owner of a dividend as opposed to the owner of the shares, which may be different in some cases" (the previous formulation in the OECD 2011 Discussion Draft was more obscure).
71. Id., at pp. 2-3: proposed drafting of para. 12.1 *OECD Model: Commentary on Article 10* and footnote to that paragraph. Identical proposals were made with respect to the drafting of the Commentaries on articles 11 and 12.
72. Id., at pp. 12-13: proposed drafting of para. 12.6 *OECD Model: Commentary on Article 10* . Identical proposals were made with respect to the drafting of the Commentaries on articles 11 and 12.

less related to a broad anti-abuse clause for excluding from treaty access any type of conduit used. But, at the same time, not all the doubts surrounding the meaning of BO have been dispelled: a (smaller) margin for administrative discretion still remains, and the BO concept could still be used against treaty shopping/conduit situations in more cases than was originally intended. That is to say, it is likely that the Commentaries on articles 10-12 of the OECD Model (2014) have managed to bring the term closer to its original meaning of excluding from tax treaties cases in which the recipient of income was not the real legal owner of it (unless the intermediate recipient was taxed for that income); however, there still remains a margin of subjectivity in the appreciation of this clause. Proof of this is that the impact of the changes on administrative positions or on the case law of different countries has been minimal ( *see* section 5. ).

# 3. BO, BEPS, the MLI and the OECD Model (2017): BO as a Redundant Clause?

## 3.1. Introduction: The 2014 narrower scope of BO further reinforced by BEPS Action 6, the MLI and the OECD Model (2017)

The Commentaries on articles 10-12 of the OECD Model (2014) pointed in the direction of the concept of BO having a much narrower scope than (domestic or treaty) anti-avoidance clauses.[73]As explained in section 2.3. , however, doubts over the interpretation and scope of the concept still remained. The BEPS Action 6 Final Report[74]suggested relevant changes in the approach to treaty shopping that were later included in the MLI and in the OECD Model (2017) . In particular, it was suggested that a new preamble be added (article 6 of the MLI) as well as a specific provision combating the abuse of treaties ( article 7 of the MLI and article 29 of the OECD Model (2017) ).[75]These changes are also relevant to interpreting the concept of BO. If specific provisions are needed to fight against conduits and treaty shopping in general, this may suggest that BO has another purpose. However, it is necessary to study the scope of the changes introduced by the BEPS Action 6 Final Report, the MLI and the OECD Model (2017) before reaching a more solid conclusion.

## 3.2. The “new” title and preamble of tax treaties and BO

The BEPS Action 6 Final Report aimed to make clear that tax treaties are not intended to generate double non-taxation and that one of their main goals is to prevent tax evasion or avoidance.[76]This idea, which was also present in the Commentaries on article 1 of the OECD Model after 2003, led to the following significant changes: (i) a reference to “prevention of tax evasion and avoidance” in the title of the convention; (ii) a new preamble indicating that tax treaties do not create opportunities for non-taxation or reduced taxation through tax evasion or avoidance (“including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of third States”); and (iii) new paragraphs in the introduction to the OECD Model explaining the scope of the new title and preamble. The proposals were implemented with differing nuances by the MLI (article 6) and the OECD Model (2017) (title and preamble, as well as introduction paras. 2, 16 and especially 16.1).

The changes emphasize that “treaty shopping” is an example of “treaty avoidance” that tax treaties should not allow. It was also stressed that the new title and preamble form part of the “context of the Convention”, define its object and purpose and should play an important role in interpreting it.[77]Although the relationship between the new article 29 of the OECD Model (2017) and the new preamble is emphasized at different points in the Commentary on Article 29(9) of the OECD Model (2017) , nothing is said about BO . Nevertheless, the Commentaries on articles 10-12 of the OECD Model (2017) explicitly refer to the object

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73. Para. 12.5 *OECD Model: Commentary on Article 10* (2014) : “The fact that the recipient of a dividend is considered to be the beneficial owner of that dividend does not mean, however, that the limitation of tax provided for by paragraph 2 must automatically be granted. This limitation of tax should not be granted in cases of abuse of this provision (see also paragraphs 17 and 22 below). As explained in the section on “Improper use of the Convention” in the Commentary on Article 1, there are many ways of addressing conduit company and, more generally, treaty shopping situations. These include specific anti-abuse provisions in treaties, general anti-abuse rules and substance-over-form or economic substance approaches. 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 on 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.” The same statements can be found in *OECD Model: Commentary on Article 11* (2014) and *OECD Model: Commentary on Article 12* (2014) , and in *OECD Model* (2017) , with some minor variations to acknowledge the introduction of art. 29 *OECD Model* (2017) .

74. OECD/G20, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances – Action 6: 2015 Final Report* (OECD 2015), Primary Sources IBFD [hereinafter *Action 6 Final Report* ].

75. On the specific details of art. 29 *OECD Model* (2017) , the approaches admitted to meet the requirements of the “minimum standard” of the BEPS Action 6 Final Report and the specific details of the configuration of the LOB clauses and the principal purposes test, *see* L. De Broe & S. Gommers, *Article 29: Entitlement to Benefits (European Union) – Global Tax Treaty Commentaries* , Global Topics IBFD.

76. OECD/G20, *Action 6 Final Report* , *supra* n. 74 , at pp. 91-93.

77. Introduction paras. 16.1 and 16.2 *OECD Model* (2017) ; OECD/G20, *Action 6 Final Report* , *supra* n. 74 , at pp. 91-93; and art. 6 *Multilateral Instrument* (2017). *See also* UN, *Vienna Convention on the Law of Treaties* art. 31(1) (23 May 1969) , Treaties & Models IBFD.

and purpose of the convention in interpreting the meaning of BO.[78]This has led some scholars to wonder whether the new title, preamble and introduction have the effect of expanding the meaning of BO and turning it into a broader instrument to fight treaty shopping.[79]

However, it is doubtful whether the new title, preamble and introduction to tax treaties play any role in the interpretation of the meaning of BO. First, the 2014 changes with regard to BO in the Commentaries on articles 10-12 of the OECD Model emphasized that, although this concept has a role to play in the fight against treaty shopping (in a broad sense), it has a different role from GAARs (and, after it was added, from article 29 of the OECD Model (2017)) or the principles set out in the Commentary on Article 1 of the OECD Model (which have very similar effects to article 29(9) of the OECD Model).[80]Second, the BEPS Action 6 Final Report, the MLI and the OECD Model (2017) did not introduce any relevant change in connection with BO specifically. If anything, the new title, preamble and introduction enhance the role of BO as a tool against some forms of treaty shopping (with shams or simulations), but nothing more. A contextual interpretation of the object and purpose of tax treaties should take into account that the meaning of BO was not affected by the BEPS changes and that the Commentaries on articles 10 and 12 of the OECD Model (2017) explicitly recognize that its function remains the same as was defined in 2014.

## 3.3. The principal purpose test (article 29(9) of the OECD Model) and BO

The principal purpose test (PPT) in article 29(9) of the OECD Model (2017) is a general provision that applies to a broader set of cases and articles than BO, which is limited to articles 10-12 of the OECD Model (2017). The PPT is the general anti-treaty-shopping provision of tax treaties, and can be applied in the case of conduit companies or treaty or rule shopping in general (if a state opts for limitation on benefits (LOB) provisions, they should be complemented with anti-conduit regulations that are not needed with a PPT).[81]The scope of BO is much narrower than that of the PPT and is limited to some specific cases of treaty shopping that are closer to shams or simulations (however, many administrations and courts do not follow this position: *see* section 5.). It also seems that there is a clear hierarchy between BO and article 29(9) of the OECD Model (2017). BO applies first, and article 29(9) can take effect only in order to fight tax avoidance behaviours that have passed the filter of the BO test.

Such clear conclusions are not very evident when reading the Commentary on Article 29 of the OECD Model (2017). First, some of the general examples in the Commentary of the application of the PPT seem to refer to conduit structures which would hardly pass the BO test.[82]Second, some of the specific conduit examples in paragraph 187 (which refers to factual patterns that could be attacked with specific conduit rules, but that could also be fought with article 29(9) of the OECD Model (2017) also present doubts regarding their interaction with the BO concept.[83]

Thus, many of the examples (PPT and conduits) leave the reader wondering about their relationship with the BO test and whether they are correct, as they seem to refer to situations that would simply not meet such a condition. Alternatively, it might be concluded that the BO concept has an extremely narrow scope (i.e. it only applies to cases functionally equivalent to agents or nominees) and that this is the reason for their inclusion in the Commentary on article 29 (i.e. because they cannot be attacked with the BO concept).[84]Finally, the OECD may have tried to show that article 29(9) of the OECD Model (2017) also

78. For instance, para. 12.1 *OECD Model: Commentary on Article 10* (2017) explains that BO "should be understood in its context, in particular in relation to the words 'paid … to a resident', and in light of the object and purposes of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance". Similar references are included in the Commentaries to articles 11 and 12 of the OECD Model on the meaning of BO with regard to interest and royalties.
79. *See* R.J. Danon, *The Beneficial Ownership Limitation in Articles 10, 11 and 12 OECD Model and Conduit Companies in Pre- and Post-BEPS Tax Treaty Policy: Do We (Still) Need It?*, in *Current Tax Treaty Issues* sec. 15.3.1.2. (G. Maisto ed., IBFD 2020), Books IBFD.
80. Para. 12.5 *OECD Model: Commentary on Article 10* (2017) explains the following: "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 on the dividend to someone else), it does not deal with other cases of abuses, such as certain forms of treaty shopping, that are addressed by these provisions and principles [the reference is to art 29(9) *OECD Model* (2017) and to *OECD Model Tax Convention on Income and on Capital: Commentary on Article 1* (21 Nov. 2017)] and must not, therefore, be considered as restricting in any way the application of other approaches to addressing such cases." In 2014, the paragraph referred only to "other cases of treaty shopping", as art. 29(9) *OECD Model* did not yet exist. A similar statement is included in the Commentaries on articles 11 and 12 of the OECD Model (2017).
81. *See* *OECD Model Tax Convention on Income and on Capital: Commentary on Article 29* para. 187 (21 Nov. 2017).
82. This is the case, for instance, with the example in para. 176 *OECD Model: Commentary on Article 29* (2017) (dealing with the assignment of a receivable by a parent to a subsidiary in a country with a tax treaty with the other subsidiary paying the interest and the first subsidiary left with a minimum spread). It can also be seen with some of the examples in para. 182: (i) Example A (a company assigns the right to receive dividends to an intermediary in a country with a tax treaty with the company paying the dividends); (ii) Example B (where the usufruct of shares is assigned to an intermediary to receive dividends with a reduced withholding tax rate in exchange for an amount that represents the present value of the future dividend stream); and (iii) Example L (where a securitization vehicle which could hardly be regarded as beneficial owner of interest received is established in a country; although these types of vehicles usually seek to obtain treaty benefits, the example is explained in terms of relevant nexus with its country of establishment). Some of the examples are based on specific cases commented in section 5. (e.g. the French decision in *Bank of Scotland* (2006), the Spanish cases on societies for the management of author's rights).
83. This is the case with Example A (an interposed company receives "dividends" that belong to a third party although it retains a minimum spread) and Example C (a loan is assigned to a subsidiary with a favourable tax treaty with the country of the borrower and this intermediary subsidiary retains a minimum spread)
84. S. van Weeghel, *A Deconstruction of the Principal Purposes Test*, 11 World Tax J. 1, pp. 31-32 (2019), Journal Articles & Papers IBFD.

covers cases that could be attacked with the BO concept only, showing that the PPT has a broader scope. No matter the interpretation preferred, there is an atmosphere of ambiguity and contradiction and, therefore, uncertainty.

Probably, the only meaningful explanation for the potential contradictions between the Commentary on Article 29(9) of the OECD Model (2017) and articles 10-12 of the OECD Model (2017) on BO is that the drafters of the Commentary on article 29(9) regarded BO as having a much more limited role than the PPT (or anti-conduit regulations), or as close to irrelevant in comparison to it, and hence did not pay too much attention to it. BO excludes from treaty access only agents or nominees or persons in a strictly analogous situation because the recipient is not the true legal owner of the income, but article 29 of the OECD Model (2017) would permit the interpreter also to take into account economic considerations regarding the ultimate owner of the income or the structure. Regardless of the ambiguities, this would confirm that the concept of BO does not cover all conduit situations. For instance, BO would not apply to conduits where no more than a functional or factual connection is detected between the income received and paid out to the final or economic recipient, as these cases may fall within the scope of article 29(9) of the OECD Model (2017).[85]This is the only interpretation that permits the attribution of a sensible meaning to BO, article 29(9) and/or conduit regulations where they exist, as a broad interpretation of BO would have the effect of rendering article 29(9) of the OECD Model or conduit regulations almost useless.

Even if this interpretation suggests the possibility of harmoniously interpreting the concept of BO and the examples in the Commentary on Article 29 of the OECD Model, it is unfortunate that the policy is not made more explicit and formulated in a clearer manner, as one cannot avoid thinking that, in fact, there is not much coordination between the Commentaries on BO and PPT.[86]A more detailed explanation of the differences between BO and PPT would have been desirable, as the concepts each have a different function and pursue different policy goals. Whereas BO seeks to identify the true owner of the income (no subjective element is needed, only an objective assessment of whether the recipient is really the owner of the dividend, interest or royalty), the PPT stresses the relevance of the subjective element (the tax purpose of the transaction) in deciding whether or not the (conduit) structure only seeks a tax advantage or has commercial validity. In the PPT, an economic reason (valid purpose) can exclude the application of article 29(9) of the OECD Model; whereas, using the BO concept, if a person cannot be allocated an item of income, there is no valid commercial purpose that can save the transaction or be used to justify applying the tax treaty to a person that is not in reality the owner of such item of income.

## 3.4. LOB clauses and BO

The minimum standard set out in the BEPS Action 6 Final Report can be met with LOB clauses instead of a PPT, complemented by rules addressed to conduit arrangements.[87]The function of BO when a tax treaty has a LOB clause might be slightly different: since the effect of the LOB clause is to exclude from the scope of a tax treaty certain persons or items of income (therefore, adding further conditions to those of article 4 of the OECD Model), the BO clause will apply only in connection with persons/income already qualifying for the benefits of the tax treaty under the LOB clause. For those persons and income, as explained in the section 3.3., the BO concept in articles 10-12 does not have the potential to replace broader clauses that are designed to counteract all potential types of conduit structures. And, therefore, similar problems to the ones already indicated in section 3.3. arise: if the BO concept is interpreted strictly, as suggested by its history and evolution and also the Commentaries on articles 10-12 and on article 29(9) of the OECD Model, it will not replace the need for broader conduit legislation (or doctrines) that address this problem in full or in a more holistic manner. If, however, it is interpreted broadly, as a substitute for PPTs (as is done in many countries), there will be no need for conduit rules such as those proposed in the Commentary on Article 29 of the OECD Model (2017) or applicable in the United States (*see* section 5.8.).

## 3.5. BO and transfer pricing rules

The relationship between BO in articles 10-12 of the OECD Model (2017) and, in cases of intra-group transactions, transfer pricing rules (following BEPS Actions 8-10) is also not easy.[88]For instance, could a cash box or a company only providing funding be regarded as the BO for the purposes of articles 10-12 of the OECD Model (2017)? If it provides a loan, the cash box could easily be regarded as the legal owner (i.e. the BO) of interest received if, for instance, it keeps the sums received without making any other payment or retains the payment for sufficient time. As has been established elsewhere,[89]the OECD's answer to the problem of cash boxes, especially in chapter 6 of the OECD Transfer Pricing Guidelines for Multinational

85. Danon (2018), *supra* n. 1, at p. 36.
86. Danon, *supra* n. 79, at sec. 15.3.2.
87. OECD/G20, *Action 6 Final Report*, *supra* n. 74, at paras. 19 and 22.
88. *See*, on this issue, A.J. Martín Jiménez, *Article 12: Royalties (OECD and UN Models) and Article 12A: Technical Services (UN Model (2017)) – Global Tax Treaty Commentaries* sec. 1.1.2.2.2.2., Global Topics IBFD.
89. Id.

Enterprises and Tax Administrations (OECD 2017), is totally different.[90]For the OECD, the transfer pricing value creation framework of the OECD Guidelines is independent from the legal reality, which means that the cash box will be allocated much less income for transfer pricing purposes than if legal arrangements are taken into account. The main tools the OECD puts in the hands of tax administrations to decide on income allocation for MNL groups are the delineation and non-recognition of legal transactions of chapter 1 of the OECD Guidelines (more elements of these tools are developed in other chapters: for example, the DEMPE functions in chapter 6). The OECD's transfer pricing solution is unsatisfactory with regard to BO: if, from a transfer pricing perspective, income cannot be attributed to a person, it is difficult to conclude that the same person is the real and true legal owner of the same income as BO.[91]

Formally, the concept of BO does not have anything to do with transfer pricing rules, but, in substance, deciding on BO also involves taking relevant decisions about functionality and risk control, regardless of whether BO is interpreted broadly, as close to a GAAR,[92]or more narrowly, as a rule on allocation of income to a taxpayer.[93]If BO is interpreted narrowly, that would mean that transfer pricing rules can always correct the attribution of an income flow to the BO, very much as GAARs would. The intention behind BEPS Actions 8-10 and the OECD Guidelines is to eliminate gratuitous intermediaries interposed in low tax jurisdictions (i.e. cash boxes), and many of these may not even be BOs in a strict legal analysis. Therefore, it seems that there is a certain overlap between BO and transfer pricing rules even if the latter is interpreted in a narrow sense.

If BO is interpreted broadly, as a sort of GAAR, the problem would be which rule, transfer pricing or BO, applies first, as both would pursue a similar goal. The order is not irrelevant in terms of procedure, elements to be taken into account (e.g. the subjective element is relevant in GAAR, but not so much in transfer pricing rules), burden of proof, etc. The outcome of applying both rules should be similar, but it may not be totally equal and may sometimes diverge (i.e. the tax savings element is not always relevant in transfer pricing, but is crucial when applying article 29(9) of the OECD Model) .

In fact, regardless of the (narrow or broad) interpretation of BO, there is always some overlap between BO and the transfer pricing delineation and non-recognition tools. It may be asked why two different tools (BO, and delineation and non-recognition for transfer pricing purposes) are needed to achieve similar policy outcomes, and whether this will create uncertainty and give tax administrations two different weapons to attack the same reality, depending on which one is more convenient for them in the specific case.

For instance, in the case of royalties, will the legal owner of an intangible be regarded as the BO of a royalty if it does not perform any DEMPE function? The answer to this question in Example 16 of the Annex to chapter 6 of the OECD Guidelines is very clear. The non-functional entity is disregarded for transfer pricing purposes. Contrary to what the OECD decided, it would not make much sense to regard that entity as the BO of royalties from a legal perspective when, for transfer pricing purposes, it has been concluded that it is not entitled to the intangible-related returns, which are allocated to another company of the same multinational enterprise ( MNE ) group. Therefore, there seems to be more dependency and mutual influence between BO (even if interpreted strictly) and transfer pricing than the OECD seems to have presumed when it declared that both analyses are independent.

The interdependency and mutual influence of transfer pricing rules and BO is shown in some recent judgments (even if they adopt a broad reading of BO). For example, the Spanish *Audiencia Nacional* (National Court, AN ) in Colgate (2018),[94]ruled that a Swiss entity receiving royalties was not the BO, as it did not perform any function or control any risks regarding the intangible in connection with which it received royalties ( *see* section 5.7.2.2. ). The conclusion is interesting because the Court simply applied the transfer pricing analysis to interpret article 12 (royalties) of the Spain-Switzerland Income and Capital Tax Treaty (1966),[95]and excluded the Swiss entity from the benefits of the reduced withholding rates for royalties on the basis that, because of the transfer pricing analysis, it could not be regarded as the BO of the royalty.[96]A similar perspective

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90. *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD 2017), Primary Sources IBFD [hereinafter *OECD Guidelines* ].
91. For a further explanation of the relationship between BO and the transfer pricing framework derived from BEPS, see Martín Jiménez, *supra* n. 88 , at sec. 1.1.2.2.2.2.; and A.J. Martín Jiménez, *Value Creation: A Guiding Light for the Interpretation of Tax Treaties?* , 74 Bulletin for International Taxation 4-5 (2020), Journal Articles & Papers IBFD.
92. Whether the intermediary effectively bears risks is usually a relevant sign of abuse: *see* , for instance, the case law of the ECJ in the Danish cases in section 5.9.
93. The true legal owner of an item of income bears all the risks inherent to dominion and property. An agent or nominee does not bear any risks (apart from those inherent to their commissions).
94. ES: *Audiencia Nacional* (AN), 30 Nov. 2018, Case 643/2015, *Colgate Palmolive España SA* .
95. *Convention between Spain and the Swiss Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income and Capital* (26 Apr. 1966) (amended through 2011) , Treaties & Models IBFD [hereinafter the *Spain-Switz. Income and Capital Tax Treaty* (1966)].
96. It is also worth pointing out that, because the wording of art. 12 *Spain-Switz. Income and Capital Tax Treaty* (1966) followed the *OECD Draft Model* (1963) , it did not refer to the BO concept. However, the AN considered that the concept could be read into the tax treaty in question and was implicit in it. On this particular issue, the judgment has been appealed to the Spanish *Tribunal Supremo* (Supreme Court, TS), which, at the time of writing this article, had not given a decision on the case.

was also adopted by the ECJ in *N Luxembourg 1* ( Case C-115/16 ),[97]when it took into account assumption of risks as a relevant factor that may indicate abuse and exclude an intermediate entity from being regarded as the BO of income received ( *see* section 5.9. ).

It appears, therefore, that BEPS Actions 8-10 and the OECD Guidelines (2017) not only have not been sufficiently coordinated with article 29(9) of the OECD Model (2017) , but also may pose relevant problems in connection with the concept of BO in articles 10-12 of the OECD Model (2017) , no matter whether interpreted broadly or more narrowly. In fact, it can be said that the OECD Guidelines (2017) , especially chapters 1 and 6, with their risk control/DEMPE frameworks, seek to identify the real owner of an item of income in a form that sometimes is similar to a GAAR. BO and transfer pricing rules may sometimes produce the same effects, as the transfer pricing rules can point out that someone is not the real or true owner of specific items of income, but sometimes the outcome of transfer pricing rules can be closer to a GAAR (and transactions are fully recharacterized) and different from BO if interpreted narrowly.

If that is the case, it appears that the BO concept also adds little to the OECD Guidelines or to the PPT in article 29(9) of the OECD Model (2017), as explained in section 3.3. Rather it appears that, especially for countries interpreting BO broadly, there are three different tools that can be used with the same purpose (transfer pricing recharacterization powers, GAARs and BO) without it being clear when the different tools are to be applied and leaving the taxpayers in an uncertain tax position.

## 3.6. Is BO irrelevant in the current OECD Model?

In view of its evolution, it might be questioned whether the concept of BO has any meaningful function in tax treaties. It never had a very clear-cut meaning or functionality in the context of the OECD Model. As a solution to different issues, the OECD's clarifications on BO always came late: (i) in the OECD Model (1977) , the concept was already unnecessary, even for the United Kingdom where it has its origins, due to the changes in article 4.1. of the OECD Model (1977) and the inclusion of the second sentence of that article; (ii) in 2003, the final recognition of the compatibility of GAARs or similar doctrines with tax treaties rendered obsolete and useless the attempt to broaden the meaning of BO as a tool to fight against treaty shopping and conduits in general; (ii) the 2014 efforts to narrow down its meaning came much too late again once different courts in many countries had already expanded it and continue to do so ( *see* section 5. ); and (iv) BEPS Action 6 and Actions 8-10, the MLI and the OECD Model (2017) also show that, as an anti-abuse device, the BO concept is unnecessary and, once again, may create confusion, especially because the concept is not well coordinated with either article 29(9) of the OECD Model (2017) or the OECD Guidelines.

In view of its evolution in the OECD context, the conclusion, for this author, is clear: the BO concept has only increased legal uncertainty. That does not mean that BO performs no function at all in the tax treaty landscape,[98]as, in the end, the idea that income should be attributed to the true legal owner represents a principle that surely has universal acceptance ( *see also* section 6.5. ). As Baker (2008) has argued, "[i]t would be even more helpful if the Commentary explained that a person who receives income or the proceeds of a capital gain, and pays that income or those proceeds on to another person, is the beneficial owner thereof unless the obligations that require the income or the proceeds to be paid on are of such a nature, either in law or in fact, that it has no possibility of benefiting from them and has no alternative other than to pay them on in accordance with those obligations".[99]That is to say, a general explanation in the Commentaries (for instance, on article 1) of the principle that only the true legal owners of income can take advantage of tax conventions would be enough to make the same principle applicable to all articles of the OECD Model and allow the elimination from articles 10-12 of a term (BO) fraught with uncertainty and that has caused protracted litigation. This would also have the advantage of clarifying that such a principle applies to all articles of a tax treaty (since, as practice and case law show, the principle also applies, for instance, in the context of articles 13, 21 and 23 of the OECD Model).

Before expanding on this idea, however, it is convenient to explore the role of BO in the UN context and the different judicial decisions regarding BO in the most representative jurisdictions.

# 4. BO in the UN Model (1980-2020)

The BO concept has also been present in the UN Model since 1980.[100]The UN Model (1980) followed the OECD Model (1977) and its Commentaries with regard to BO, and the 2001 version largely did the same with the updates to the OECD Model up to 1997. Lastly, the 2011 and 2017 updates of the UN Model followed the OECD Model (2010) . Therefore, the

97. DK: ECJ, 26 Feb. 2019, Case C-115/16 , *N Luxembourg 1 v. Skatteministeriet* , Case Law IBFD.
98. The same position is defended by Meindl-Ringler, *supra* n. 1 , p. 383 (citing previous works of the present author).
99. *See* P. Baker, *The United Nations Model Double Taxation Convention between Developed and Developing Countries: Possible Extension of the Beneficial Ownership Concept* , Annex to Comm. of Experts on Intl. Cooperation in Tax Matters, *Note by the Coordinator of the Subcommittee on Improper Use of Treaties: Proposed Amendments* , E/C.18/2008/CRP.2/Add.1 (UN 2008), pp. 35-36, footnote 17.
100. *United Nations Model Double Taxation Convention between Developed and Developing Countries* (1 Jan. 1980) , Treaties & Models IBFD

changes in the Commentaries on articles 10-12 of the OECD Model (2014) were not included in the latest revision of the UN Model in 2017. Strangely, paragraphs 52-59 of the Commentary on Article 12A (fees for technical services) of the UN Model (2017) followed the OECD Model (2014-2017); that is to say, they include the 2014 update of the OECD Model on the meaning of BO. Therefore, there is no consistency between the meaning of BO in articles 10-12 and article 12A of the UN Model (2017). Moreover, paragraph 72 of the Commentary on Article 1 of the UN Model (2017) seems to suggest that BO can be used to fight against treaty shopping more generally and not only in cases of conduits having a function similar to agents or nominees (the reference to "some extent" in para. 72 is rather vague). It is expected that future revisions of the UN Model will eliminate these inconsistencies.

The concept of BO has received more attention in the UN framework than is fully reflected in the Commentaries on articles 10-12A of the UN Model (2017):[101]

- In 2008 the UN Tax Committee decided not to extend the use of BO to other articles of the UN Model until its meaning had been refined further, especially in the OECD context.[102]The decision was linked with the report of Baker (2008), in which different options were explored (a general article on BO or adding the BO concept to other specific articles (i.e. articles 21, 13(6) and 22(4) and (7)), and it was concluded that extending an unclear and vague term to other articles of the UN Model would only transfer the problems of interpreting BO from articles 10-12 of the UN Model to other articles.[103]The UN Tax Committee pointed out that Baker's report could also be included in the UN Manual for the Negotiation of Bilateral Tax Treaties Between Developed and Developing Countries.
- The 2019 version of the UN Manual for the Negotiation of Bilateral Tax Treaties Between Developed and Developing Countries took note of the evolution regarding BO in the Commentaries on the OECD Model after 2014.[104]The previous version of the Manual also referred to the developments in the Commentaries on articles 10-12 of the OECD Model after 2014, and pointed out that it would be useful for treaty negotiators to discuss the interpretation of BO with their counterparts.[105]
- The UN Tax Committee has again decided to carry out further work on BO. Two issues are relevant in this context: whether the term should be defined by reference to domestic or international law, and whether it is a broad or a narrow clause. On the first issue, the works of the UN were inclined to stress that BO is independent from national law,[106]and, on the second, that the OECD's position after 2014 should be followed.[107]It was expressly acknowledged that it may be a waste of resources to apply and focus on BO, which has a controversial meaning, now that developing countries have rules, i.e. article 29 of the OECD Model (2017), that permit them to address treaty shopping in a more holistic manner.[108]
- Finally, the Committee of Experts on International Cooperation[109]has decided the following in connection with the 2021 update of the UN Model: (i) the Commentaries on articles 10-12 of the UN Model are to be amended to align them with the 2014 changes to the Commentaries on the same articles of the OECD Model, and it will be emphasized that BO should be assigned a contextual meaning and not the meaning in the law of the state of source, as per article 3(2) of the UN Model; (ii) the drafting of articles 10(2), 11(2) and 12(2) of the UN Model is to be changed to align them with the wording of articles 10(2), 11(2) and 12(1) of the OECD Model (as modified in 1995, 1997 and 2014: *see* section 2.2.4.), and to emphasize that the reduced withholding taxes will apply even if the recipient of the dividends, interest and royalties is not a resident of the other contracting state but the BO meets that condition; and (iii) the possibility of defining BO in a specific paragraph of article 3(1) of the UN Model is to be rejected, as it would only create further problems and could be interpreted as an attempt to provide a different definition from the one in the Commentaries on articles 10-12A of the UN Model (as updated

101. *See* Comm. of Experts on Intl. Cooperation in Tax Matters, *Eighteenth Session: Update of the UN Model Double Taxation Convention Between Developed and Developing Countries – Beneficial Ownership* , E/C.18/2019/CRP.10 (UN 2019).
102. Comm. of Experts on Intl. Cooperation in Tax Matters, *Report on the Fourth Session (20-24 October 2008)* , E/2008/45-E/C.18/2008/6 (UN 2008), paras. 47-48.
103. Baker, *supra* n. 99 .
104. *See* UN, *Manual for the Negotiation of Bilateral Tax Treaties Between Developed and Developing Countries* (UN 2019), pp. 98-99, 107 and 116.
105. UN, *Manual for the Negotiation of Bilateral Tax Treaties Between Developed and Developing Countries* (UN 2016), p. 91-92 (although referring only to interest).
106. It is proposed that a specific headnote be added to make this clear before the references to BO in the 2017 Commentaries on articles 10-12 of the OECD Model . *See* Comm. of Experts on Intl. Cooperation in Tax Matters, *Nineteenth Session: Update of the UN Model Double Taxation Convention Between Developed and Developing Countries – Beneficial Ownership,* E/C.18/2019/CRP.21, p. 2.
107. Id., at p. 2 et seq.
108. Comm. of Experts on Intl. Cooperation in Tax Matters, *supra* n. 101 , at p. 6; *see also* p. 13 of the same document, which reports that the UN Tax Committee is also discussing whether the UN Model should be aligned with the changes to articles 10 and 11 of the OECD Model (2014) and their respective Commentaries to stress that the reduced rates of such articles also apply in cases of payments to intermediaries in third countries, as long as the BO is resident in the other contracting state. It seems, however, that there are divergent positions on this specific issue.
109. See Comm. of Experts on Intl. Cooperation in Tax Matters, *Twentieth Session: Update of the UN Model Double Taxation Convention between Developed and Developing Countries – Beneficial Ownership – Note by the Subcommittee on the UN Model Tax Convention between Developed and Developing Countries* , E/C.18/2020/CRP.6 (UN 2020).

to bring them in line with the OECD Model). As a result of these changes, once they are made, articles 10-12 of the UN Model will finally recognize the same meaning of BO as article 12A of the UN Model.

From the above, it appears that the BO concept presents in the UN Model almost the same problems as in the OECD Model. The call to "developing countries" to concentrate on broader anti-avoidance tools such as article 29 of the UN Model (2017), which follows article 29 of the OECD Model (2017), is worth stressing, as it reveals that the ambiguity of the term may render it ineffective and lead to protracted litigation (with the inherent waste of time and resources for the taxpayer and tax authorities). It remains to be seen if that advice is followed, also in view of the judicial decisions of developed countries, as for tax administrations in developing countries it is probably easier to apply BO than the equivalent to article 29(9) of the OECD Model (2017).

# 5. Different Positions on BO in Different Countries and in Case Law

## 5.1. Introduction

The experience of some relevant countries reveals a sharp contrast with the Commentaries on articles 10-12 of the OECD Model after 2014. A majority of cases in different courts all over the world, and the positions taken by many tax administrations, have defended a broad reading of BO, whereas only a minority of them (the "market maker" case in the Netherlands, *Prévost* (2008) and (2009) and *Velcro* (2012) in Canada) have defended a different position. It is interesting that the ECJ seems recently to have endorsed the first position, further obscuring the debate on BO, rather than helping to eliminate doubt. As will be shown, it is difficult today to assume a uniform meaning of BO in different jurisdictions.

## 5.2. Netherlands: A narrow interpretation of BO in the "market maker" decision

The Netherlands Supreme Court decision 28.638 of 6 April 1994 ("market maker") is probably the most traditional judgment on BO, often commented on by the specialized literature.[110]The facts are not complex. A UK company, registered as a market maker for shares in different companies, purchased dividend coupons – not the underlying shares – of Royal Dutch Shell, a Dutch company. The coupons were purchased from a Luxembourg company at a price of approximately 80 per 100 of their face value. However, the acquisition took place when the dividends had already been declared but before they were made payable. The paying agent applied a withholding tax of 25 per 100 upon payment, but the UK company applied for a refund of 10 per 100 of the tax withheld, based on the Netherlands-United Kingdom Income and Capital Tax Treaty (1980), which followed the OECD Model (1977).

The Dutch tax authorities refused the application of article 10 of the Netherlands-United Kingdom tax treaty, mainly because the UK company was neither (i) the owner of the shares nor (ii) the owner of the dividend coupons when the dividend was declared. The *Gerechtshof* (Court of Appeal) Amsterdam confirmed that decision. As the UK company had bought an amount of dividends already declared and payable in a few days, for the Court, it was not the BO of the dividends. It was doubtful for the Court that the UK company had received a dividend as such, as it simply purchased a "fixed amount" that was not regarded as a dividend from the UK perspective. It had merely received a commission fee for the provision of a service. Moreover, the UK company was not the owner of the shares to which the dividends were linked.

The *Hoge Raad der Nederlanden* [Supreme Court] reversed the decision of the Amsterdam Court and decided that the UK company was indeed the BO of the dividend. For the Supreme Court, the taxpayer was the owner of the dividend after the purchase of the coupons and had the free disposal thereof. The taxpayer was not acting as agent on behalf of another person. Therefore, the UK company should be regarded as the BO of the dividends received and had access to article 10 of the Netherlands-United Kingdom tax treaty. For the Supreme Court, it was irrelevant in the specific case that the UK company was not the owner of the underlying asset or that the coupons were bought right after the dividend was declared (therefore, BO was to be tested when the stream of income was received, and not before, when the dividend was declared).

It appears that the Supreme Court decision relied heavily on the Advocate General's Opinion.[111]The latter defined a concept of BO that was autonomous from domestic legislation and used as a source the scholarly opinions available at that time. The AG concluded that the UK company was the BO because it became the owner of the coupons and was entitled to freely

110. NL: HR [Supreme Court], 6 Apr. 1994, 28.638, BNB 1994/217, Case Law IBFD. This chapter has benefited from the following works of scholarship in commenting on this decision: Van Weeghel, *supra* n. 1, at p. 75 et seq.; C. Du Toit in Oliver et al., *supra* n. 1, at pp. 32-34; Pijl, *supra* n. 1, at pp. 257-258; De Broe, *supra* n. 1, at pp. 694-697; and D.S. Smit, *The Concept of Beneficial Ownership and Possible Alternative Remedies in Netherlands Case Law*, in *Beneficial Ownership: Recent Trends* p. 51 et seq. (M. Lang et al. eds, IBFD 2013), Books IBFD.

111. *See* Smit, *supra* n. 110, at pp. 65-67.

dispose of them after the distribution. This was so even if the UK company was exposed to a very limited risk (insolvency, currency) for a short period of time.

The Supreme Court followed a very strict interpretation of BO that is very different from broad/economic interpretations in other countries. It is not clear in Dutch scholarship whether the solution would have been the same if the recipient of the dividends had the legal obligation to pass on the income to another person, or whether the Court intended to limit the application of BO to cases of strict agents and nominees.[112]However, if it was crucial for the Court that the recipient had the power to freely dispose of the income received, the legal (not factual) obligation to pass on the income to a third party would probably have had the consequence of excluding the recipient from the category of BO. A factual obligation to pass on the income to another person would not be relevant from the perspective of the Supreme Court.[113]

From a strict legal perspective, probably the Court of Appeal Amsterdam was right in affirming that it is doubtful whether the UK company was receiving a dividend at all, as it was clear that this company was not the shareholder of the payer. However, this issue is not directly relevant to the Supreme Court's construction of BO.

## 5.3. United Kingdom: A not fully clear case (Indofood ) and the HMRC's reaction in establishing a high threshold

On 2 March 2006, the Court of Appeal of England and Wales (Civil Division) gave its decision in (the civil, not tax) case *Indofood* (2006).[114]The facts and reasoning in the judgment are well known and will be only briefly summarized in order to make a short comment on the position adopted by the Court and, later, the tax administration.[115]Indofood is not really about English law – it discusses what an Indonesian court would have done if confronted with the issue. The only connection with English law was the parties chose English courts to resolve any dispute between them. An Indonesian parent company that wanted to raise funds in international markets for its activity, instead of issuing loan notes directly (a 20% withholding tax would have been levied in Indonesia),[116]did so through a Mauritian company,[117]with the effect that the withholding tax on interest paid to the Mauritian company was reduced in Indonesia to 10% under the Indonesia-Mauritius Income Tax Treaty (1996) (no withholding tax was levied in Mauritius on interest paid to the noteholders).

When the Indonesian government denounced the Indonesia–Mauritius Income Tax Treaty (1996) in order to have it terminated with effect from 1 January 2005, the Indonesian parent company attempted to redeem the notes (not only because of the increase in withholding taxes but also due to the, at the time, high interest rate it was paying to the Mauritian company/ noteholders). There was a clause in the agreement permitting the issuer of the notes to redeem them before the date initially foreseen in order to mitigate additional tax charges (the increased withholding tax after the DTC was terminated), unless there were "reasonable measures" which provided for an alternative solution. However, the trustee for the noteholders deemed that a "reasonable measure" would be to interpose a Netherlands company. Therefore, the English court had to decide whether replacement of the Mauritius special purpose vehicle by a Netherlands company was such a measure. Only if the Netherlands company could be regarded as the beneficial owner of interest from Indonesian sources according to the Indonesia-Netherlands Income Tax Treaty (2002) could Indofood not redeem the note.

Some factual circumstances are relevant for understanding the case:

- payments received and made by the Mauritian/Netherlands company were tied, so that interest received by the bondholders was really the money or interest paid by the Indonesian company (in fact, one of the clauses of the contract prohibited the Mauritian company from paying interest with its own funds, other than the interest received from Indonesia). Moreover, there was no difference in the rate of interest on both loans;
- the Mauritian/Netherlands company did not retain a spread that could fully justify the risks assumed; it was remunerated with a sort of "fee" or charge;

112. *See* id., at pp. 66-67, for a summary of the various positions of Dutch scholars.
113. Id., at pp. 67-68.
114. UK: EWCA (Civ.), 2 Mar. 2006, *Indofood International Finance Limited v. JPMorgan Chase Bank NA, London Branch* , [2006] EWCA Civ. 158, [2006] STC 1195, Case Law IBFD.
115. On *Indofood* , *see* , for instance, R. Fraser & J. Oliver, *Treaty shopping and beneficial ownership: Indofood International Finance Limited v. JP Morgan Chase Bank* , N.A., London Branch, Brit. Tax Rev. 4, p. 422 (2006); P. Baker, *Beneficial Ownership: After* Indofood, 6 Grays Inn Tax Chamber Review 1, p. 15 (2007); P. Baker, *United Kingdom: Indofood International Finance Ltd v. JP Morgan Chase Bank NA* , in *Beneficial Ownership: Recent Trends* (M. Lang et al. eds, IBFD 2013), Books IBFD; and L. Sheppard, *Indofood and Bank of Scotland: Who is the Beneficial Owner?* , 45 Tax Notes Intl. 5, p. 406 (2007). *See also* De Broe, *supra* n. 1 , at p. 706 et seq.
116. Interest was paid "net" of taxes (gross-up clause), so the withholding was in fact a cost for the issuer.
117. The Mauritian company issued the bonds and lent on the funds raised to the Indonesian parent company. The Indonesian parent acted as guarantor of the issue.

- on paper, interest received by the Mauritian/Netherlands company was paid on the following day to the bondholders. However, as the Court explained, the parent company paid the sums due to the noteholders directly to their trustee (thus, the Mauritian subsidiary did not receive/make any payment); and
- an answer by the Indonesian Directorate-General for Taxation ( DGT ) of 24 June 2005 to a question by the Indonesian parent concluded that the interposition of a Netherlands company would be a case of improper use of the treaty. The DGT identified the beneficial ownership concept with the substance-over-form principle of Indonesian law, and therefore as an anti-abuse rule. As a consequence, a Netherlands conduit would not be the beneficial owner of interest from Indonesian sources. On 7 July 2005, the DGT issued a circular letter in which it identified BO with "the actual owner of income ... either individual taxpayer or business entity taxpayer that has the full privilege to directly benefit from the income", and, therefore, "'special purpose vehicle' in the form of 'conduit company', 'paper box company', 'pass-through company' or other similar are not included in the 'beneficial owner' definition".[118]

The main findings of the Court were as follows:

- the term "beneficial owner ... is to be given an international fiscal meaning not derived from the domestic laws of the contracting states".[119]This is an important feature of the decision, ruling out attributing to the term the meaning it has under Indonesian (or English) law;[120]
- the concept of BO is "incompatible with that of the formal owner who does not have 'the full privilege to directly benefit from the income'";[121]
- In finding the meaning of BO, the Court looked at the "substance of the matter". Since both loans were tied and the intermediate company (Netherlands or Mauritian) had to pay that which it receives, "in practical terms it is impossible to conceive of any circumstances in which either the Issuer or Newco [the Netherlands company] could derive any 'direct benefit' from the interest payable to the Parent Guarantor except by funding its liability to the Principal Paying Agent or the Issuer respectively". In the Court's view, "[s]uch an exception can hardly be described as the 'full privilege' needed to qualify as the beneficial owner, rather the position of the Issuer and Newco equates to that of an 'administrator of the income'". As a matter of fact, one of the reasons why the Court of Appeal reversed the decision was because the assumption that an arm's length spread would be retained by the Netherlands company was incorrect;[122]and
- the Court also based its conclusion on the fact that this is consistent with the object and purpose of the DTCs (between Indonesia and Mauritius, on the one hand, and between Indonesia and the Netherlands, on the other). For the Court, relief from withholding tax would not have been afforded had they granted the loan directly to the parent company, which is an indication that the transaction fell outside the object and purpose of the DTC at issue.

There is some resemblance between *Indofood* and cases decided in other jurisdictions (e.g. in Spain and Switzerland: *see* sections 5.6. and 5.7. ). The *ratio decidendi* in all cases is that payments received and made were so closely tied that the intermediate company had to pay "that which it received". Like the Spanish and Swiss courts, the Court of Appeal did not look at whether the Mauritian/Netherlands company was paying its own money or the money of others.[123]Probably, there was no real need to do so: (i) from a contractual perspective, it was clear that the Mauritian/Netherlands company did not have any right over the income it received: it had to pay what it received and could not use any other income to discharge its liabilities with the noteholders; (ii) in fact, the Mauritian company did not receive any interest, as the Indonesian parent paid directly to the trustee of the noteholders. It seems to be implicit in the reasoning of the Court that, if there had been any "spread" (which can only be justified if "risks" are assumed by the intermediate company), the conduit could be regarded as beneficial owner. As Baker (2014) puts it, "if beneficial ownership had any meaning at all, surely it would exclude the type of interposed entity which had no function whatsoever but to receive any income and pay on the identical amount of income: in fact, it had so little function that, according to the Court of Appeal, the actual flows of money missed it out completely".[124]

Less justified are some statements by the Court referring to the "substance of the matter" (reminiscent of a substance-over-form analysis), others where the Court resorted to the definition of beneficial ownership by the Indonesian DGT

118. Paras 18-19 *Indofood* (2006).
119. Para. 42 *Indofood* (2006) (citing P. Baker's opinion and the Commentaries on articles 10-12 of the OECD Model (1977-2003), as well as the Conduit Companies Report).
120. Baker (2007), *supra* n. 115 , at p. 23, pointed out in this regard that, if one were to applaud any point in *Indofood* , it is that it construed the term with an international meaning, as opposed to a domestic law meaning.
121. Para. 42 *Indofood* (2006) (citing the Indonesian DGT Circular of 7 July 2005).
122. Para. 40 *Indofood* (2006) (the "substance requirements" under Dutch law would be satisfied with a combination of "handling charges" and "paid-up equity capital").
123. *See* Fraser & Oliver, *supra* n. 115 , at p. 427.
124. Baker (2007), *supra* n. 115 , at p. 25. *See also* De Broe, *supra* n. 1 , at p. 712, for a similar opinion.

(as this definition does not clarify the meaning of BO)[125]or where it judged that the reduction of withholding of taxes by means of interposing an intermediate entity is contrary to the object and purpose of DTCs. The Court did not make clear whether it excluded the intermediate entity as a BO because there was a legal obligation to pass on the income received, or because in considering all facts and circumstances it was concluded that the intermediate entity is not the BO from an economic perspective. These arguments give support to those who defend a broad interpretation of the term BO in the case, as assimilated to a more general anti-avoidance clause. And in fact, these statements were picked up on by the UK tax administration (Her Majesty's Revenue and Customs, HMRC ) in providing its peculiar understanding of the effects of *Indofood* in the United Kingdom. On 6 October 2006, HMRC released draft guidance[126]on the impact of *Indofood* , which was subsequently included in the HMRC International Manual.[127]The guidance acknowledges the international meaning of BO; the problem is that it ultimately assimilates it to a broad anti-treaty shopping device that permits HMRC to attack any reduction of UK withholding taxes by using conduits.[128]It is surprising that the guidance focused its attention on the statements in Indofood regarding the object and purpose of DTCs and tried to draw conclusions from Indofood that go beyond the Court decision (and the "international meaning of the term"), especially because the guidance contradicts UK treaty policy of including specific anti-avoidance provisions in arts. 10-12 of its tax treaties ("main purpose" clauses) as a means of combating treaty shopping.[129]

In sum, it seems that HMRC identified the term "beneficial owner" as a (broad) anti-treaty shopping clause by making an interpretation of Indofood that the English Court did not defend. It is true that some statements in Indofood give support to the position of HMRC, but is no less certain that Indofood merely concerned a single case in which the intermediary could be regarded as an "agent or nominee", and this is what the English Court took into account.

## 5.4. France: BO as equivalent to a GAAR in *Bank of Scotland*

Bank of Scotland *(2006)* [130]is a well-known case of the French Conseil d'État (Supreme Administrative Court, CE ) that caused some concern in the international tax community.[131]In November 1992, a US parent company sold to the Bank of Scotland ( BoS ) the temporary usufruct of a number of preferred non-voting shares of its French fully-owned subsidiary. The conditions of the sale were, as the CE held, the most striking feature of the contract:

- the price paid by BoS would be recovered in 3 years in the form of dividends paid by the French subsidiary. The dividend was predetermined on the date of the initial sale and BoS would receive the price paid plus a certain amount (which was calculated after the French withholding tax was applied and the French avoir fiscal refunded to BoS); and
- BoS did not assume any risk in the transaction, because the US parent company (i) guaranteed that if the French subsidiary could not pay the predetermined dividends, it would do so, plus supplementary compensation if BoS did not receive the refund of the avoir fiscal from the French authorities; (ii) would give full financial support to the French subsidiary so that it could distribute the predetermined amount of dividends; and (iii) was obliged to buy back the shares if the income of the French subsidiary did not reach an also predetermined amount in any trimester.

The aim of the transaction, which resembles a dividend stripping, was to gain access to the France-United Kingdom Income Tax Treaty (1968). If dividends had been received by the US parent, the avoir fiscal would not have been refunded, but by selling the usufruct to BoS the French tax liability was significantly reduced.

First, the French tax administration considered that BoS was not the BO of the dividends paid by the French subsidiary of the US company. The French tax administration deemed the price paid by BoS when purchasing the usufruct right

125. *See* , for the same opinion, Baker (2007), *supra* n. 115 , at p. 25.
126. For a critical review of the Draft Guide, see R. Fraser & J. Oliver, *Beneficial Ownership: HMRC's Draft Guidance on Interpretation of the* Indofood *Decision* , Brit. Tax Rev. 1, p. 39 (2007).
127. *See* HMRC, *International Manual – Double Taxation applications and claims: HMRC reaction to Indofood case* (last updated 1 Sept. 2020) https://www.gov.uk/hmrc-internal-manuals/international-manual/intm332050 (last accessed 30 May 2020).
128. *See* Fraser & Oliver, *supra* n. 126 , for a similar view . Especially controversial is Example 7 of the guidance, in which the use of a Luxembourg company to channel a loan to a UK borrower from a country with no DTC with the United Kingdom is deemed to fall outside the term "beneficial owner" because "it is clear one of the main purposes of the Luxembourg company is to avoid the withholding tax which would be due" if payments were made directly to the company lending the funds to Luxco. In the example, Luxco was set up for this transaction, it has a small "turn" for administering the loan and the interest is "predetermined" to be passed on to the parent in a country with no DTC with the United Kingdom. As Fraser & Oliver point out (at p. 48), one of the problems in Example 7 is that "predetermined" does not indicate anything as to the legal situation of Luxco, and is so general a term that it can be used to attack any "conduit", including those cases in which the conduit is the real owner of the income it receives.
129. Id., at p. 41 et seq.
130. FR: CE [Supreme Administrative Court], 29 Dec. 2006, 283314, *Bank of Scotland* , Case Law IBFD.
131. On *Bank of Scotland* (2006), *see* , for instance, S. Austry, S. Gelin & D. Sorel, *Practical Effectiveness of Beneficial Ownership Clauses in France's Tax Treaties* , 53 Tax Notes Intl. 2, p. 151 et seq. (2009); B. Gibert & Y. Ouamrane, *Beneficial Ownership – A French Perspective* , 48 Eur. Taxn. 1, p. 2 et seq. (2008), Journal Articles & Papers IBFD; Sheppard, *supra* n. 115 , at pp. 409-413; De Broe, *supra* n. 1 , at p. 697. Gibert & Ouamrane (at p. 6) and De Broe (at p. 697 et seq.) also provide references to previous decisions in France.

to be the amount of net dividends guaranteed to BoS. Therefore, according to the French tax administration, BoS granted a loan to the US parent company and the benefit gained by BoS in the transaction was the avoir fiscal. The *Cour Administrative d'Appel* (Administrative Court of Appeals) of Paris ruled for the taxpayer because, inter alia, BoS could not be regarded as an agent or nominee and the tax administration did not show that the distribution of risks in the contract was abnormal.[132]However, the *CE* considered that the distribution of risks in the usufruct contract sought artificially to hide the real transaction, i.e. a loan that would be reimbursed with the dividends paid by the French subsidiary. The main purpose of the contract was, for the *CE* , to gain access to the 1968 France–United Kingdom DTC and, therefore, to obtain the refund of the avoir fiscal in France (which was not available if dividends were directly paid to the US parent company). The *CE* ruled that this use of the DTC was contrary to its object and purpose and that the BO of the dividends was not BoS but the US parent.

What is most interesting in the decision of the *CE* is that:

- the *CE* adopted a factual/economic approach in order to disregard the temporary usufruct contract and convert it into a loan, which is inherent to substance-over-form doctrines.[133]It is obvious in the case that BoS was not legally obliged to pass on the dividends received to any third party and had the full right to use them; and
- the conclusions of the Court are based not only on the BO concept but also on the French general domestic anti-abuse clause (which requires taking into account the purpose of the transaction). It is not entirely clear if this is so because the *CE* considered the BO requirement insufficient to underpin a substance-over-form approach and deny access to the 1968 France–United Kingdom DTC , or, rather, because it treated BO and anti-treaty shopping clauses as equivalents.[134]The latter seems the more accurate explanation, as in his preparatory opinion before the judgment, the Commissaire du Gouvernement (Government Commissioner) had already defended a broad interpretation of the concept of BO to also cover any form of treaty shopping.[135]In fact, this is also how some French commentators read the concept of BO.[136]This position also permitted the Court to avoid the domestic problem that the tax treaty did not expressly provide for the application of domestic anti-avoidance rules.[137]

As a consequence, it seems that in France, at least in the *Bank of Scotland* decision, BO is given a broad anti-abuse meaning equivalent to GAAR . The OECD has signalled that this interpretation of BO is not the right one. Example B of paragraph 182 of the Commentary on Article 29 of the OECD Model (2017) is almost identical to the factual situation in BoS. The OECD used this example to illustrate a case in which the principal purpose of the arrangement is to obtain treaty benefits, and in which article 29(9) of the OECD Model (2017) could be applied to avoid it because the transaction would be contrary to the object and purpose of the treaty. Thus, the Commentary on Article 29 of the OECD Model (2017) confirms that the broad reading of BO by the French CE is not satisfactory, and is not the correct ("international") interpretation of that concept. This basically means that the OECD regards the bank in such a factual pattern as the BO of the dividends, and holds that, if there is treaty shopping, devices other than BO should be used to counteract it.

Some recent decisions of the CE[138]also suggest that the Danish ECJ cases ( *see* section 5.9. ) will be used extensively in that country. The CE has ruled that BO is a condition for applying the exemption from withholding taxes (article 5) of the EU Parent-Subsidiary Directive (2011/96) , which, as explained in section 5.9. , does not explicitly refer to that term. It is also shown below that the so-called Danish cases refer to an interpretation of BO that attributes to it a meaning closer to a GAAR, which is very much in line with the *Bank of Scotland* case.

## 5.5. Canada: A very low threshold for BO in the *Prévost* and *Velcro* cases

### 5.5.1. *Prévost*

The approach to the concept of BO by Canadian courts in the Prévost judgments attracted worldwide interest, mainly because they represent an alternative to theories and interpretations of the same concept in other countries (Spain, France, Switzerland

132. FR: CAA [Administrative Court of Appeals], 23 May 2005, 01PA04068 , Case Law IBFD.
133. Sheppard, *supra* n. 115 , at p. 410 (citing Michel Collet).
134. Gibert & Ouamrane, *supra* n. 131 , at p. 9. For instance, these authors seem to regard BO as a clause that permits attacking treaty shopping in a broad sense.
135. *See* id., at p. 8, for an unofficial translation of the main paragraphs of the opinion.
136. Id.
137. In this regard, D. Gutmann, *Beneficial Ownership as Anti-Abuse Provision: The Bank of Scotland Case* , in *Beneficial Ownership: Recent Trends* p. 172 (M. Lang et al. eds, IBFD 2013), Books IBFD, explains that "[t]he Supreme Administrative Court distorted the meaning of the concept because its goal was to apply the French general anti-avoidance theory without formally departing from the treaty rule. The distortion therefore took place in order to circumvent a purely domestic issue, namely whether the tax authorities may directly apply a general anti-avoidance theory without relying on a specific provision of a tax treaty". It appears the French Court tried to bypass the problem that the tax treaty did not have a specific anti-avoidance provision and the broad reading of the BO concept permitted it to make use of the domestic anti-avoidance approach in the treaty context.
138. FR: CE, 5 June 2020, 423809, 423810, 423811 and 423812, *Eqiom and Enka* .

and, with some nuances, even the United Kingdom). The context of the *Prévost* case is the restrictive approach to treaty shopping defended by Canadian courts in *MIL (Investments)* (2007),[139] in which the Federal Court of Appeal decided that the Canadian GAAR did not apply to "a blatant case of treaty shopping"[140] (a redomiciling of a Cayman Islands company to Luxembourg in order to derive capital gains from shares in a Canadian company without paying any Canadian source tax). There are two Prévost judgments – first, the decision of 22 April 2008 by the Tax Court of Canada ( TCC );[141] and, second, the confirmation of this judgment on 26 February 2009 by the Canadian Federal Court of Appeal ( FCA ).[142]

Both judgments refer to the treatment of holding companies as BO. A Netherlands holding company received dividends from 1996 to 2001 from a Canadian wholly-owned subsidiary. The Canadian tax authorities concluded that it did not have access to the reduced withholding tax rates of the Canada-Netherlands Income Tax Treaty (1986) (as amended by subsequent protocols), because the BOs were the Netherlands company's shareholders, Henlys (a resident of the United Kingdom) and Volvo (a resident of Sweden). Other relevant factual circumstances are the following: (i) there was a shareholders' contract, according to which the Netherlands holding company would distribute at least 80% of its profits; (ii) the substance of the Netherlands holding was minimal but enough to qualify as a resident of the Netherlands; (iii) the Netherlands holding company's single asset was the participation in the Canadian subsidiary; and (iv) the directors of the Netherlands holding were also the directors of the Canadian subsidiary.

*The* Prévost (2008) decision paid special attention to the opinion of two Netherlands expert witnesses (Stef van Weeghel, who has written extensively on improper use of DTCs, and Rogier Raas, specializing in Netherlands corporate law). From the experts' opinions, it was clear to the TCC that the holding company would be the BO of the dividends received under Netherlands commercial and tax law and, notwithstanding the shareholders' contract, there was no legally binding obligation for it to distribute 80% of its dividends. The TCC, after consulting internal law and the OECD materials (the Commentary on Article 10 of the OECD Model (1977) and ( 2003 ) and the Conduit Companies Report), as well as, inter alia, the English Indofood case, ruled in favour of the Netherlands holding, primarily on the basis of the meaning of BO under Canadian law.[143] The TCC gave a narrow definition of BO that was at odds with the jurisprudence of other countries (e.g. France, Spain, Switzerland and the United Kingdom). In practice, Prévost (2008) left the meaning of BO confined to something resembling an attribution-of-income rule.[144] The TCC offered a definition of BO[145] and construed it from the perspective of Netherlands commercial and tax law. As, according to Netherlands legislation, the holding company was the owner of the dividends because it enjoys discretion to use the funds (despite its minimal substance, there being no office or employees, the dividends were included in its profits and loss account, and until distributed they were an asset available to its creditors – there was no predetermined or automatic flow of funds to the Netherlands holding company's shareholders and no legal obligation for the company to pass the dividends on to them), the TCC concluded that it was the beneficial owner for the purposes of article 10(2) of the Canada-Netherlands Income Tax Treaty (1986).[146]

The Canadian tax administration appealed the decision of the TCC. The main arguments it adduced were that the TCC gave the term BO the meaning it has in common law, thereby ignoring the meaning it has in civil and international law. However, on 26 February 2009, the FCA upheld the judgment of the TCC. The FCA, unlike the TCC, did attribute relevance to the OECD materials (the 2003 amendments to the Commentary on Article 10 of the OECD Model ) released after the Canada-Netherlands Income Tax Treaty (1986) in interpreting its article 10(2). For the FCA, these materials are helpful insofar as they "are eliciting [ *sic* elucidating], rather than contradicting, views previously expressed".[147] The FCA stressed that the TCC's

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139. CA: FCA, 13 June 2007, *MIL (Investments) SA v. Her Majesty the Queen* , Case Law IBFD .
140. B.J. Arnold, *The Concept of Beneficial Ownership under Canadian Tax Treaties* , in *Beneficial Ownership – Recent Trends* p. 39 et seq. (M. Lang et al. eds, IBFD 2013), Books IBFD.
141. CA: TCC, 22 Apr. 2008, *Prévost Car Inc. v. Her Majesty the Queen* , 2008 TCJ 231 (TCC), Case Law IBFD. On this decision, *see* B.J. Arnold, *Tax Treaty Monitor: Tax Treaty News* , 62 *Bull. Intl. Taxn.* 7, p. 263 (2008), Journal Articles & Papers IBFD, for a brief but very interesting commentary; and M.N. Kandev, *Treaty Shopping in Canada: The Door is (Still) Open* , 62 *Bull. Intl. Taxn.* 10, p. 463 (2008), Journal Articles & Papers IBFD.
142. CA: FCA, 26 Feb. 2009, *Prévost Car Inc. v. Her Majesty the Queen* , 2009 FCA 57, Case Law IBFD. *See* , on this decision, N. Boidman & M.N. Kandev, *Canadian Taxpayer Wins Prévost Appeal* , 53 *Tax Notes Intl.* 10, p. 862 (2009); J. Bernstein & L. Summerhill, *Canada's Prévost Decision: the World is Watching* , 53 *Tax Notes Intl.* 11, p. 985 (2009); B.J. Arnold, *Tax Treaty Monitor: Tax Treaty News* , 63 *Bull. Intl. Taxn.* 5/6, pp. 175-176 (2009), Journal Articles & Papers IBFD; and Arnold, *supra* n. 140 .
143. The legal basis of the decision is not very clear. The TCC ruled out adopting, in the treaty context, the internal law meaning of BO, because this route might lead to confusion in view of the fact that the interpretation in Canada of the term is not evident; apart from that, however, the decision is not fully based on OECD materials or on any other single source. Arnold, *supra* n. 142 , at p. 175, believes that the TCC "derived the meaning of the term from Canadian domestic law".
144. Arnold, *supra* n. 141 , at p. 263; Arnold, *supra* n. 142 , at p. 175.
145. For the TCC, the BO was "the person who enjoys and assumes all the attributes of ownership": para. 99 *Prévost* (2008). In the case of corporations, the corporate veil should not be lifted "unless the corporation is a conduit for another person and has absolutely no discretion to use or application of funds put through it as conduit, or has agreed to act on someone else's behalf pursuant to that person's instructions without any right to do other than that person instructs it" (para. 100).
146. See especially para. 102 et seq. *Prévost* (2008) .
147. Para. 12 *Prévost* (2009). This statement follows on from the view of the FCA as to when later commentaries are relevant in interpreting prior DTCs, as expressed in para. 11 *Prévost* (2009): "later commentaries [may be used as a guide], when they represent a fair interpretation of the words of the Model

formulation of the concept of BO not only "emerges from the review of the general, technical and legal meanings of the terms", but, "most importantly", it "accords with what is stated in OECD Commentaries and in the Conduit Companies Report".[148]The FCA rejected the the tax administration's proposal to construe the concept as meaning the person "who can, in fact, ultimately benefit from the dividend", because this definition does not "appear anywhere in the OECD documents" and would jeopardize the "certainty and stability that a tax treaty seeks to achieve".[149]

To sum up, the FCA not only approved the concept of BO given by the TCC in Prévost *(2008)* , but also pointed out that it is in conformity with OECD materials (even if some of them are posterior to the treaty being interpreted), and, what is more important, rejected an economic interpretation of the term BO that could have had the effect of turning that concept into a broad anti-avoidance clause.[150]This does not mean that any holding company would have been regarded as the BO: if it had absolutely no discretion on the use of the dividends received, or if there were a predetermined flow of funds, the holding would not be the BO. Therefore, there exists a strict legal reading of the concept which is quite different from the scope of anti-avoidance rules such as article 29(9) of the OECD Model (2017) .[151]

### 5.5.2. *Velcro*

*Velcro* (2012)[152]also referred to a Dutch intermediary company. This was part of a typical royalty structure, in which the final owner of the royalties was a Netherland Antilles company (NA Co) of the Velcro group which had previously assigned the rights under a licence for intellectual property in favour of the Canadian subsidiary to another Dutch company of the group. The Dutch intermediary (Dutch Co) received the royalties paid by the Canadian subsidiary and passed on 90 per 100 of the amount of the royalty to NA Co within 30 days of receiving it. It appears, although many details are missing in the case, that the substance of Dutch Co was minimal or non-existent and that its main income and expense was the royalty stream. Apparently, the royalties received were commingled in the same account with other funds and the same account was used to pay loans, expenses and professional fees. If the royalties had been paid directly from the Canadian subsidiary to NA Co, a 25 per 100 withholding tax rate would have been levied; instead, the interposition of Dutch Co permitted claiming the benefits of the Canada-Netherlands Income Tax Treaty (1986) and the withholding tax was reduced to a rate of 10 per 100.

The TCC applied the BO test of *Prévost* to the specific factual pattern presented above, and checked whether Dutch Co really had discretion to use the royalties received. For the TCC, there was no automatic flow of funds through Dutch Co to NA Co, and Dutch Co had all the attributes of a BO (possession, use, control and risk). This conclusion was based on two main factors: (i) the royalties received were commingled with other funds in the same bank account; and (ii) the amount paid by Dutch Co to NA Co was not the same as the amount received from the Canadian subsidiary. According to the TCC, in view of those circumstances, there was no predetermined flow of funds and the position of Dutch Co could not be equated to that of an agent or nominee because it had discretion as to the use of the funds, assumed risks and controlled them.

As Arnold (2014) has suggested,[153]the reasoning of the TCC is far from convincing and seems to be based on some misunderstandings:

- the fact that the royalties received are comingled for 30 days with other funds in one account does not say anything about whether a person is the BO and leaves it in the hands of the recipient to meet that condition;
- a 30-day period of possession of the funds does not seem sufficient to disregard the fact that, after that period, the royalties were passed on to Dutch Co. Even if, within those 30 days, Dutch Co could use the funds, this seems too little to exclude the conclusion that it had very narrow powers over the royalties received; and
- the amounts received were different from the amounts paid precisely in the amount of tax withheld in Canada (10 per 100). Therefore, Dutch Co did not retain a 10 per 100 share of the royalty, as the TCC concluded; rather, it was obliged to pass on to NA Co the full amount it received from the Canadian subsidiary.

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Convention and do not conflict with Commentaries in existence at the time a specific treaty was entered and when, of course, neither treaty partner has registered an objection to the new Commentaries".

148. Id., at para. 14.
149. Id., at para. 15.
150. Boidman & Kandev, *supra* n. 142 , at p. 864, have noted in this regard that the FCA "has swept aside notions of purposive economic substance analysis in concluding as it did in *Prévost* in favour of merely distinguishing between agents and principals".
151. Some authors have pointed out that the *Prévost* decisions make sense in policy and practical terms ( *see* , for instance, Arnold, *supra* n. 140 , at p. 43). In the present author's view, the policy behind the tax treaty is a relevant argument for deciding whether there is abuse, but not so much when concluding that a person is the BO of the item of income received if the term is interpreted as narrowly as the Canadian courts have done (as a logical requirement for allocating income to a person).
152. CA: TCC , 24 Feb. 2012, *Velcro Canada v. the Queen* , 2012 DTC 1100, 2012 TCC 57, Case Law IBFD.
153. Arnold, *supra* n. 140 , at pp. 47-48.

In view of the facts of the case, it is difficult to conclude that Dutch Co is in a position any different from that of an agent or nominee. The TCC seemed to rely on the *Prevóst* test that a conduit is a company that has "absolutely no discretion" to use the funds received. Because, in *Velcro* , Dutch Co had some (albeit very limited) discretion, it did not meet that test. The decision is too formal, and seems to have emptied the BO test of any meaningful application.[154]

### 5.5.3. A low, almost meaningless, BO threshold in Canada?

Both the *Prévost* and *Velcro* decisions established a very low threshold for BO :[155]one certainly much lower than that established by the OECD Commentaries after 2014. It can even be asked whether the standard is useful at all in view of *Velcro* : it is no longer a test about real legal ownership, but rather a formal test that disregards "legal substance", and one according to which persons having a role almost identical to that of an agent or nominee would qualify as BOs as long as they enjoy a minimum degree of discretion. From the point of view of the Commentaries on Article 12 of the OECD Model (2014) and ( 2017 ), the conclusion of the *Velcro* case would be clearly wrong: it is difficult to conclude that Dutch Co's rights to use and enjoy the royalties are not "constrained by a contractual obligation to pass on the payment received to another person".[156]

## 5.6. Switzerland: A broad "objective substance-over form" test for determining BO?

### 5.6.1. *V. SA* : A high threshold for the interpretation of BO

The Swiss Federal Tax Appeal Commission ( CRC ) decided on BO in a judgment of 28 February 2001, V. SA (2001).[157]The facts of the case were relatively straightforward. A Luxembourg company (Luxco), which was controlled by two British companies, purchased from a US resident the full capital of a Swiss company. The purchase was financed (almost in full) with a loan obtained from one of its shareholders. Such participation was the only relevant asset of Luxco. In 1996 and 1997, it received dividends from the Swiss company and, when it applied for the refund of taxes withheld at source, the Swiss tax authorities denied access to the reduced withholding tax rates of the Luxembourg-Switzerland Income and Capital Tax Treaty (1993). Other relevant facts are: (i) Luxco was not a holding company in Luxembourg benefiting from any special tax regime; (ii) all revenues received from the Swiss subsidiary were used to pay interest and other charges; and (iii) when asked by the Swiss authorities, surprisingly Luxco responded that it was not the BO of the dividends received.

The CRC noted that article 10(2)(b) of the Luxembourg-Switzerland Income and Capital Tax Treaty (1993) did not use the term BO but referred only to "beneficiary". Using a grammatical interpretation, the CRC concluded that a company that transfers the dividends it receives to a third person, in the form of deductible interest and charges, without having the power to fully dispose of them, is not the "beneficiary" of income. This definition of beneficiary, the CRC noted, citing the Conduit Companies Report, is close to the concept of BO, which is the "person who economically has the benefit of an item of income". Such a concept "is not applicable to conduit companies like intermediaries between the debtor and the person who will ultimately receive the item of income". Thus, Luxco could not be granted the refund requested, as it was not a beneficiary or BO for the purposes of the DTC .

The *V. SA* decision is interesting for several reasons. First, although starting with a grammatical interpretation, the CRC, in line with the Swiss tradition of treaty interpretation, followed all the steps of the Vienna Convention on the Law of Treaties and confirmed that the object and purpose of the treaty as well as its context bore the grammatical conclusion. It appears that the CRC tried to deduce a truly international meaning of the term without referring to domestic law. Second, it is interesting that the CRC seemed to consider at the same level the problem of BO and the broader problem of treaty shopping or abuse in general, which may mean that it was accepting a certain equivalence between the two concepts. That is to say, BO seems to have been interpreted broadly.

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154. Id., at p. 48.
155. Id.
156. Para. 4.3. *OECD Model: Commentary on Article 12* (2017) ; id., at p. 49.
157. CH: CRC [Federal Tax Appeal Commission], 28 Feb. 2001, VPB 65.86, *V. SA* , Case Law IBFD. The judgment is commented on in detail by Danon (2007), *supra* n. 1 , at p. 58 et seq. Danon reads this decision from the point of view of his theory on beneficial ownership, defended in Danon (2004), *supra* n. 1 , at p. 326 et seq.

### 5.6.2. *X Holding ApS*

Some years later, on 3 March 2005, the CRC released another decision on BO: X Holding ApS, which was confirmed by the Federal Supreme Court on 28 November 2005.[158] This time the case referred to a direct conduit – a Danish holding company – which was set up in Denmark and controlled by a Guernsey company, in turn fully owned by a Bahamian company. The director and final shareholder of all of these was a resident of the Bahamas. The Swiss Court concluded that the Danish company was the BO of the dividends (it did not pay "deductible income" to third parties), but denied access to the nil withholding tax rate for dividends under the Denmark-Switzerland Income and Capital Tax Treaty (1973) by using Swiss internal anti-avoidance norms as a legal basis (therefore, confirming they can be applied in a tax treaty context). The case is also interesting as it seemed to clearly differentiate between BO and abuse, an aspect that was not so clear in the previous *V. SA* case nor in subsequent Swiss practice. It also confirmed that, even if the BO requirement is not explicitly mentioned in the text of the tax treaty, it is implicit in it.

### 5.6.3. The swap cases

In a series of swap cases, the Swiss courts further refined the Swiss position on BO. The first case, *Bank A* (2012),[159] referred to a total return swap in which the intermediary entity was a Danish bank, which received dividends from Swiss sources and made payments under the swap agreements to third parties resident in countries other than Denmark. The Federal Administrative Court defined BO as an objective requirement for treaty access, "a condition of entitlement like, say, the concept of residence". However, the Court interpreted such a condition with a "substance-over-form" flavour: it was relevant to determine not only whether the recipient of the income was contractually bound to pass the dividends on to third parties, but also whether the payments would, de facto, flow through the intermediary towards its ultimate recipient ("economic perspective"). The difference between abuse and beneficial ownership would be that, whereas the former requires an inquiry into the motives of the specific arrangement or transaction, the latter does not: it only requires establishing the factual (or legal) connection between the stream of income at the level of the intermediary. Although the decision was reversed on appeal by the Federal Supreme Court,[160] the main reasoning on the concept of BO was confirmed (also in subsequent judgments of the Swiss Supreme Court).[161] As Danon has remarked:

> for the Federal Supreme Court, beneficial ownership should be examined from the perspective of economic control and focuses on the criterion of interdependence between income and the obligation to transfer such income to non-residents on the basis of a legal arrangement or, more importantly in practice, simply factual circumstances. The Supreme Court generally considers that economic control fails to exist where, on the basis of a legal or factual obligation, all or even just an essential portion of the treaty protected income is being transferred to non-residents.[162]

Controversially, this line of reasoning has even led the Federal Supreme Court to exclude from the scope of tax treaties intermediaries that did not provide any tax benefit to the taxpayer in terms of reduction to withholding taxes.[163] However, this would be a natural consequence of interpreting BO as a true legal ownership requirement, as, in the end, the Court should inquire whether the income belongs to the person receiving it. It does not, however, make any sense to interpret BO economically (de facto), as the Swiss courts do, without linking this interpretation to a tax advantage for the final owner of the income.

It also appears that the Federal Supreme Court reads the "legal obligation" to pass income to a third party, which would exclude BO status, quite broadly, in order to avoid any conflict with the Commentaries on articles 10-12 of the OECD Model (2014-2017). For the Swiss Court, BO is excluded if there is the legal or de facto obligation to pass on the income to a third party, but the OECD concludes only that the recipient will not be the BO if a legal obligation to pass the income is established. The Federal Supreme Court has so far fended off the debate over whether its position on de facto obligations is contrary to the OECD's Commentary by simply enlarging the concept of "legal obligation", and interpreting it to cover any legal or de facto obligation to pass on the income to a third party. This is at odds with the meaning of BO derived from the Commentaries on articles 10-12 of the OECD Model (2014).

158. CH: BGer/TF [Federal Supreme Court], 28 Nov. 2005, Case 2A.239/2005, *X Holding Aps*, Case Law IBFD. On the factual circumstances and legal reasoning of the judgments, I have followed Danon (2007), *supra* n. 1, at p. 46 et seq., and Danon (2008), *supra* n. 1. The English translation of the Federal Supreme Court judgment is published in 8 Intl. Tax Law Reports, p. 536 (2005).
159. CH: BVGer/TAF [Federal Administrative Court], 7 Mar. 2012, Case A-6537/2010, *Bank A*, Case Law IBFD.
160. CH: BGer/TF [Federal Supreme Court], 5 May 2015, Case 2C_895/2012, Case Law IBFD.
161. *See*, for instance, CH: Bger/TF [Federal Supreme Court], 19 May 2020, Case C_880/2018 (also arguing that a small spread retained by the conduit is simply compensation for forwarding income).
162. Danon, *supra* n. 79, at sec. 15.2.5.3.1.
163. CH: BGer/TF [Federal Supreme Court], 19 Dec. 2019, Case 2C_209/2017, Case Law IBFD, published in 22 Intl. Tax Law Reports, p. 435 (2019), with a commentary by B. Malek. Malek, at p. 441, regrets that "[t]he Federal Supreme Court has adopted a regrettably formalistic approach which serves the rather obscure purpose of denying treaty benefits in the absence of treaty abuse".

The Federal Supreme Court's position was also applied in the most recent decision of the Swiss Federal Administrative Court[164]to a case of reception of dividends by an Italian broker in the context of a swaps / futures and stock lending contracts.

### 5.6.4. An "economic" interpretation of BO?

It is interesting that the Swiss position has progressively evolved towards clearly differentiating the concept of BO from that of abuse and further enlarging its meaning without relying on the "subjective criteria" inherent to GAARs. The main difference between BO and a GAAR in Swiss case law is that, whereas the first is an objective requirement to which the intention of the taxpayer is irrelevant, the second calls for an inquiry into the (tax) purposes of the taxpayer. In practice, however, the Swiss approach has managed to achieve with BO an outcome that is similar to a GAAR, without all the inherent problems in the application of the subjective element.

Although the concept of BO in Switzerland appears to be, on its face, more aligned with the OECD position after 2014, in fact, its effects are broader, as the 'factual' connection between the income received by the intermediary and that passed on to other persons permits the Swiss tax administration and courts to squeeze into the BO requirement an economic result or concept of ownership similar to the one that GAARs achieve. The Swiss position seems to have a very relevant connection or alignment with the OECD 2011 Discussion Draft, which caused turmoil especially (but not exclusively) for financial institutions, and forced the OECD to react to limit the effects of the BO clauses in cases in which there was a factual (not legal) connection between the income received and paid ( *see* section 2.2.8.). As explained in section 5.6.3., the Swiss courts' broad understanding of BO can lead, paradoxically, to the exclusion from treaty benefits of certain taxpayers in cases in which no tax advantage or tax motive is identified as the reason for interposing an intermediary company. This outcome would be consistent with a narrow interpretation of BO that identifies this term with the true legal owner, but there is no reason to allocate income with economic criteria to other taxpayers where tax purposes cannot be identified in a specific structure or transaction. This broad reading of BO may lead to exclusion from treaty benefits in cases in which the application of article 29(9) of the OECD Model would not have excluded the taxpayer from the scope of a tax treaty either and the taxpayer is still the legal owner of the income received. Therefore, the Swiss position is probably not in line with the main reason for the inclusion of BO in tax treaties, and is also not fully consistent with article 29(9) of the OECD Model.[165]

## 5.7. Spain: Identification of BO with a GAAR and application of BO to other treaty articles (residence country perspective)

### 5.7.1. Introduction

The Spanish courts have issued a great variety of judgments on BO, referring to different factual patterns. All of them reflect a tendency on the part of the tax administration and the courts to interpret BO broadly as a substitute for GAARs; and, even if attention is paid by the Spanish authorities to the OECD Commentaries and their evolution, it appears that the concept is used to bypass the nuisance of activating the cumbersome procedures for applying the domestic GAAR, and that too much credit is given to the 2003 Commentaries on the OECD Model. To the author's knowledge, it is the first country to have applied the so-called Danish judgments of the ECJ in order to interpret the BO concept again with a much broader meaning than the one it has in the Commentaries on articles 10-12 of the OECD Model (2014-2017) – which shows the damage that the ambiguous and probably wrong case law of the ECJ may cause for the smooth application of tax treaties.

### 5.7.2. BO from a source country perspective

#### 5.7.2.1. BO and collective management organizations for authors' rights

The judgment of the *Tribunal Económico-Administrativo Central* (Central Economic-Administrative Court, TEAC) of 22 September 2000, RG 6294/1996, was the first decision in Spain in which the concept of BO was an issue.[166]It was later confirmed by the AN, a central court of justice, on 19 June 2003. In both cases, the Spanish TEAC and AN had to decide whether foreign societies for the management of copyrights and authors' rights were BOs, and thus entitled to apply the reduced withholding tax rates for royalties provided for in several Spanish DTCs.[167]The TEAC and AN ruled that foreign societies for the management of copyrights or authors' rights are "intermediaries or agents acting in the name of the holders of

164. CH: BVGer/TAF [Federal Administrative Court], 29 May 2020, Case A-2516/2018, *A v. Administration Federal* .
165. For a very clear summary of the Swiss position and why it can be criticized, *see* Danon (2020), *supra* n. 1 , at pp. 413-446. The author would like to thank R. Danon and B. Malek, of the University of Lausanne, for their help in identifying the relevant Swiss case law and for forwarding to him the most recent judgments with their English translations.
166. ES: TEAC [Central Economic-Administrative Court], 22 Sept. 2000, Case RG 6294/1996 , Case Law IBFD.
167. It is not very clear from the judgments to which DTCs they refer, but one of them was the *Convention between the United States of America and the Kingdom of Spain for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* (22 Feb. 1990) , Treaties & Models IBFD [hereinafter *Spain-US Income Tax Treaty* ].

the right (the authors) and, since they do act on behalf of copyright holders, they cannot be beneficial owners for the purposes of Spanish DTCs" (unless they prove that the authors in the names of whom they act are residents of the same state as the societies).

The decisions of the TEAC and AN are technically correct, but some points are worth stressing:

- the TEAC and AN did not refer to the OECD Model or the Commentaries on articles 10-12 in discussing BO. It is likely that the courts used OECD materials, but there is no reference to where they found the meaning of BO that they used. It is clear, though, that attention was paid to the function of entities for management of copyrights and authors' rights under Spanish domestic law;
- the concept of BO that the TEAC and AN used revolves around the idea of "ultimate owner of the income". The facts of the case probably led the TEAC and AN to focus on the "ultimate owner" of income, but it is likely they did not mean to convey the idea that the concept should be given an economic, as opposed to a legal, meaning: it was clear from the facts that the societies did not have any right upon the royalties they received and that they acted in the name of the holder of the rights; and
- the TEAC and AN stressed that the organizations receiving the royalties had no power to dispose of the income received – they could only manage the rights of other parties (the authors), and the real owners of the rights had not attributed further powers to the societies apart from those related to receiving the income in their name. It is interesting that the Spanish courts studied the powers of the societies from the point of view of the Spanish legislation on authors' rights. Most likely, the Courts simply sought a way to facilitate their decision: they studied the contracts between the societies and the authors and concluded that the structure of the societies and the powers they had are analogous to those that similar Spanish societies and organizations have under domestic legislation. The courts probably did not mean that, when searching for the BO, the legislation of the source state is relevant.

To sum up, it seems that these decisions regard BO as a sort of rule on attribution of income: the income was obtained by the authors and not the societies or organizations who received it, and, therefore, the residence of the owner of the income, not of the organization, should be proved to have access to the reduced withholding tax rates under tax treaties.

It is strange that Example I of the Commentary on Article 29 of the OECD Model (2017) uses a very similar factual pattern, and concludes that the organizations are not interposed for treaty shopping reasons, but to make sure of the correct and efficient application of tax treaties. The OECD's conclusion is surprising, as the problem is not about treaty-shopping, but about BO: societies or organizations for the management of authors' rights are never BOs of the income they receive on behalf of authors. The OECD's example is, therefore, completely misplaced: it refers to a problem of BO, as the Spanish judgments show, and not one of treaty-shopping as presented by the example used by the OECD.

### 5.7.2.2. Royalties and BO: The *Real Madrid* and *Colgate* cases

On royalties and BOs, two groups of cases stand out: the older *Real Madrid* and the newer *Colgate* cases.

#### *Real Madrid* cases

The *Real Madrid* cases are a group of judgments of the AN ,[168]which refer to very similar structures used by well-known soccer players of Real Madrid (RM) in order to receive part of their wages without paying Spanish personal income tax. RM paid certain amounts to several Hungarian entities for the use of, or the right to use, the "image rights" of some soccer players with whom RM had a work contract; or, if the player had registered his name as a brand, for the use of or the right to use such brand.[169]The Hungarian entities, in turn, transferred almost the full income received[170]to entities that were residents of the Netherlands or Cyprus. The use of the Hungarian entities had a clear goal: the DTC between Hungary and Spain was a well-known exit route for royalties, because, at that time, it was (together with the DTC with Bulgaria) the only DTC in the Spanish treaty network with no withholding tax for royalties at source.[171]

168. ES: AN [National Court], 18 July 2006, Case 1110/2003, JUR/2006/204307 , Case Law IBFD; similar and associated cases are ES: AN [National Court], 18 July 2006, JUR\2007\8915 and JUR\2007\16549; ES: AN [National Court], 10 Nov. 2006, JUR\2006\284679; ES: AN [National Court], 20 July 2006, JUR \2007\16526; ES: AN [National Court], 13 Nov. 2006, JUR\2006\284618; and ES: AN [National Court], 26 Mar. 2007, JUR\2007\101877. All of these AN judgments follow literally, by copying his arguments, the position of F.A. Vega Borrego, *El concepto de beneficiario efectivo en los Convenios para Evitar la Doble Imposición* , Documentos del Instituto de Estudios Fiscales 8 (2005), and F.A. Vega Borrego, *Las medidas contra el "treaty Shopping"* (Instituto de Estudios Fiscales 2003).
169. Because, in the context of these judgments, both categories of income present almost the same problems, no differentiation is made here between the two types of income flows.
170. The percentage of income paid out by the Hungarian companies to the Netherlands or Cypriot final recipients ranged between 98% and 99.5% of the payments received from RM.
171. In the view of the present author, it is clear that payments for "image rights" cannot be characterized as royalties under art. 12 *OECD Model* . But, at that time, the Spanish tax administration believed that royalties could encompass image rights.

In all the judgments, the main issue was whether the Hungarian entity receiving and making payments could be regarded as BO for the purposes of the Hungary-Spain Income and Capital Tax Treaty (1984). The Spanish tax administration concluded that the interposed entity in Hungary was not a BO, because it paid almost all the "royalties" received to non-Hungarian (Netherlands or Cypriot) resident companies.[172]The fact that the Hungarian entity retained only a small part of the royalty (between 2% and 0.5%), and the clear link between the payments received and made (payments were made consistently on the same date or one day after receiving the payment) were crucial for the tax administration in concluding that the Hungarian entity was not the beneficial owner of the payments. Some of the circumstances that the tax administration established clearly indicated that the position of the Hungarian conduits was very weak: for example, (i) there were no invoices between the principal companies and the Hungarian entities; (ii) despite having no invoices, the royalty payments were made, sometimes at dates prior to those established in the contract, sometimes in amounts that were different from those foreseen in the contract; (iii) in some cases, the date of signature of the contract between the Netherlands/Cypriot company and the Hungarian entity was later in time than the date of the contract between the Hungarian entity and RM; etc.

RM (the appellant) claimed that the tax administration founded its decision on the fact that most of the income received by the Hungarian conduits was paid to a third party, but did not give any argument as to whether (or not) the Hungarian entities were the legal owners of the royalties received. Therefore, the fact that most of the income received was paid to a third party, RM contended, could not leave the Hungarian entities outside the scope of BO as in the DTC between Hungary and Spain.

The arguments the AN gave for excluding the Hungarian entities from the BO concept of article 12 of the Hungary-Spain DTC were the following:

- the main purpose of the concept of BO is to prevent treaty shopping. In fact, the AN conceived of BO as a clause with a (very) broad anti-treaty shopping effect. In the AN's opinion, its meaning and impact was analogous to the GAAR in the Spanish General Tax Law. As a consequence, for the AN, the BO requirement permitted the source country to exclude from the royalties article any situation in which avoidance can be singled out, without the "bother" involved in applying the internal law procedure for these cases;[173]
- for the AN, BO was a term with an autonomous international meaning. That is to say, this was a case in which "context otherwise requires", and reference to internal law, according to article 3(2) of the OECD Model, must be excluded. The way in which the AN found such an international meaning was, to say the least, a little peculiar. The AN followed the evolution of the concept of BO in the OECD Model and its Commentaries, as well as Conduit Companies Report. However, it misunderstood this evolution. In the view of the AN, the 2003 changes to the OECD Commentaries on articles 10-12 confirmed the "clear" goal of the concept of BO, i.e. its function as a broad anti-treaty shopping device, oriented towards tackling any form of treaty shopping. Following the 2003 changes to the OECD Commentaries on articles 10-12, according to the AN, an "economic interpretation" can be used to seek the "real owner" of income[174](and, therefore, to disregard the legal owner thereof). In fact, the AN assimilates BO to a "business purpose test": if there is a business reason to place an entity between the payer and the final recipient of the income, beyond reduction of withholding taxes in Spain, the intermediary will be the BO; whereas, if the conduit has only the goal of reducing withholding taxes, it will fall outside that concept. In view of the effects of the 2003 changes to the Commentaries on the OECD Model, the AN cannot be blamed for the position it took – as, in the end, the OECD, as shown in section 2.2., contributed to the confusion;
- the AN did not take into account any legal powers the recipient may have had over the royalties received. Rather, it presumed that, as the Hungarian entities received and immediately paid "royalties" out to Netherlands or Cypriot companies, they did not have any control over the income. Therefore, the decisions lack any analysis of whether the Hungarian entities could be the legal owners of the income, whether (or not) the royalties could be legally attributed to them or whether they assumed any risk or had any control of the income in the transactions at issue, no matter the legal obligations that they had with third parties; and
- the AN applied the 2003 OECD Commentaries and the 1986 Conduit Companies Report, to the 1984 Hungary-Spain DTC, but did not explain how subsequent Commentaries or OECD materials could be used in this way to interpret prior DTCs.

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172. The consequences of the tax administration's decision were different depending on the use of Dutch or Cypriot entities. In the cases of structures with Dutch entities, the tax administration decided to levy the 6% withholding tax applicable to royalties in the *Neth.-Spain Income and Capital Tax Treaty* (1971). Quite incomprehensibly, therefore, the tax administration disregarded the Hungarian entity and concluded that the Dutch entity was the BO for the purposes of the Netherlands-Spain DTC. Such DTC does not have a BO requirement in articles 10-12, so it is not clear whether the tax administration was concluding that BO is not implicit in tax treaties that do not refer to that term or whether there was evidence that the Dutch entity was the BO of the "royalties". Regarding the structures with Cypriot entities, there was at that time no DTC between Cyprus and Spain (in fact, Cyprus was blacklisted, as a tax haven), and the domestic withholding tax rate in force at the time the facts took place (25%) was applied.
173. In both the old and new Spanish General Tax Laws, declarations of tax avoidance had to follow a special procedure. As of 2003, that procedure requires the tax inspector to stop the tax audit and refer the case to a central commission, which will decide whether or not there is avoidance: ES: Ley General Tributaria [General Tax Law], Law 58/2003 of 17 Dec. 2003 , arts. 15 and 159, Primary Sources IBFD.
174. For the AN, the ownership of the income-generating asset is not relevant – what is important is the link between the recipient and the income.

The main conclusion that can be drawn from the *Real Madrid* judgments is that the Spanish tax administration and courts aligned (without citing any foreign decisions) with the trend to identify BO with a broad anti-fraud or anti-avoidance clause. The basis of the reasoning of the AN is an economic/substance-over-form analysis of the kind often found when applying GAARs. The AN could have reached the same conclusion by simply analysing the legal position of the Hungarian companies, and without assimilating the concept of BO to a broad anti-abuse provision ( *see* section 6.3. ). It is questionable to what extent the AN can be blamed for this, as, in the end, the confusion is largely derived from the 2003 changes to the OECD Commentaries.

### *Colgate* cases

As a consequence of the restructuring of the US Colgate group to operate with a principal/limited risk distributor model, its Spanish subsidiaries were audited. One of the tax assessments that closed the audit referred to royalties “paid” from the Spanish subsidiaries to the Swiss “principal” of the group. This assessment was the object of a judgment by the AN of 30 November 2018[175](the transfer pricing aspects of the restructuring itself were considered in a different judgment, which does not refer to BO). Before the restructuring, a royalty had been paid by the Spanish distributors to the parent company in the United States for the use of the brand, know-how and commercial name. After the restructuring, the Spanish subsidiaries ceased to pay that royalty, and paid to the Swiss principal only the price of the goods that were distributed in Spain. However, after 2005, the Swiss principal itself paid a royalty to the US parent under a licence agreement. The Spanish tax auditors concluded that, as there was no royalty payment by the Spanish subsidiaries to the Swiss principal but, nevertheless, the Spanish subsidiaries were using the Colgate name, brand and know-how in the Spanish market, and were also contributing through marketing campaigns to the value of these intangibles, the royalty was implicit in the price paid for the goods sold by the Swiss principal to the Spanish companies. However, the auditors considered that the Swiss principal was not the BO of the royalty, although article 12 of the Spain-Switzerland Income and Capital Tax Treaty (1966) (as amended through 2011) does not refer to BO, and they applied the domestic withholding taxes to the “royalty” (and not the withholding rates under the Spain-United States Income Tax Treaty (1990)).

The AN concluded that the Swiss company did not perform any function or control any risk or asset regarding the intangibles (despite the fact that it had a licence from the US owner of the intangibles). Therefore, it could not be regarded as the BO of the royalty. Further, the AN confirmed the conclusion of the tax auditor that the Spain-United States tax treaty could not be applied either, because, as the “‘flow followed by the rent is unknown, for these purposes it must be taken into account that it could have well been channelled through (or located in) any jurisdiction”. The AN did not rule out the possibility of applying the US tax treaty to the royalty; it merely remarked that, for this to happen, the Colgate group had the burden of proving the flow of the royalty from Switzerland to the United States, and that otherwise it did not meet the requirements for access to the Spain-United States tax treaty. This conclusion is controversial, as no payments to other entities were mentioned in the cases, and it gives the impression that it is merely an excuse to interpret BO as a GAAR while at the same time avoiding fully recharacterizing the transactions.

The conclusion of the AN is also interesting because deciding about BO may entail a careful pondering of whether the person receiving the income performs any function, controls an asset or assumes any risks in connection with the income received. That is no different from deciding whether the recipient is the true owner of the item of income received. In the end, if the BO is the person that has the power to decide what to do with the income received, an intermediary does not assume any risk and does not perform any substantial function in connection with it (apart from the usual competences of a mere intermediary).

It is undeniable that a person that does not have the legal obligation to pass on the income to another and instead can retain it performs functions and risks as an owner, but a full functional and delineation analysis of the kind required by chapter 1 or 6 of the OECD Guidelines has more in common with a GAAR and an economic analysis than with a strict concept of BO. The functional analysis can lead the interpreter to the conclusion that the recipient of a royalty is not the legal owner of income and, therefore, is not the BO either. But, on the other hand, it can also be the case that the legal analysis and the economic one proposed by the OECD Guidelines do not produce the same outcomes. Even if deciding whether a person is the legal owner and whether they exert relevant functions or risks may be two sides of the same coin in many cases, the AN seemed to use the functional analysis in a form closer to a GAAR and fully in line with the OECD Guidelines: the Swiss principal, the AN concluded, was not the BO because it did not perform functions or control relevant risks, despite the fact that it was unclear where the “deemed royalty” ended up (i.e. the United States or any other country) or if it was even retained by the principal. In fact, it is quite contradictory to find that there was no proven link between the deemed Spanish-sourced royalty paid to the principal and the payment made by the principal to the US parent to exclude the application of the Spain-United States treaty, and yet to conclude that the Swiss principal is not the BO because it is unknown where the item of income ended up. It appears, as already mentioned, that the AN reasoned with arguments closer to a GAAR but used the BO concept to avoid a full recharacterization of the Swiss principal.

175. *Colgate* (2018).

Therefore, the *Colgate* case is relevant for three reasons: (i) it read the BO concept into a provision that did not include it; (ii) it permitted in theory the application of the tax treaty with the country where the BO is resident (although disallowed it because proof was not provided of a connection between the different flows of royalties); and (iii) it applied a functional analysis to establish whether or not the intermediate recipient of the income is the BO (even if this analysis is closer to that of a GAAR and leaves the taxpayer in an uncertain position as a result of the recharacterization of the transactions). The judgment of the AN has been appealed before the Spanish *Tribunal Supremo* (Supreme Court, TS) with reference only to point (1); that is to say, the company maintains that the BO concept cannot be read into a treaty that does not refer to it.[176]

### 5.7.2.3. BO and dividends paid to an "intermediate holding"

The TEAC, in its judgment of 28 September 2009 (Case RG 1481/2007)[177]applied the BO concept derived from the *Real Madrid* case to a UK intermediate holding controlled by a resident of the United Arab Emirates. On 30 October 2002, a Spanish resident company distributed a dividend in the amount of EUR 1.8 million to its UK parent. On 7 March 2003, the UK parent distributed a dividend in the amount of EUR 1.45 million to its shareholder in the United Arab Emirates. The Spanish tax authorities rejected the application of the Parent-Subsidiary Directive (2011/96) to the dividend distribution by the Spanish subsidiary, on the basis of the anti-abuse clause of article 14(1)(h) of the Law on Income Tax on Non-Residents, which implemented article 1(2) of the Parent-Subsidiary Directive.[178]The tax authorities considered that none of the escape clauses in the anti-abuse provision were applicable. However, they took the position that the withholding tax rate of 10% under article 10(1)(a) of the Spain-United Kingdom Income and Capital Tax Treaty (1975) (as amended through 1993) could be imposed on the dividend distribution. That is to say, the Spanish tax authorities regarded the UK conduit as the BO of the dividends received for the purposes of the Spain-United Kingdom tax treaty. The TEAC confirmed the decision of the Spanish tax authorities on the non-application of the anti-abuse clause of the Parent-Subsidiary Directive in this specific case, but added that the UK company should not have been regarded as the BO for the purposes of the tax treaty either .

The following data were regarded as relevant by the TEAC in deciding the case:

- the UK company was managed and effectively controlled by the individual resident in the United Arab Emirates;
- the Spanish company did not conduct any business activities. It simply bought a piece of land, which it sold after some time with a considerable capital gain. It was domiciled in a law firm and liquidated in 2004, shortly after the sale. The UK parent did not conduct any business either, and its only asset was the participation in the Spanish company. Neither the Spanish subsidiary nor the UK parent ever had any employee. There was no evidence whatsoever that the UK company managed the Spanish subsidiary;
- the Spanish company had entered into a participating loan with another UK company, also controlled by the individual resident in the United Arab Emirates, with the sole purpose of reducing the taxable base of the capital gain obtained by the Spanish subsidiary; and
- no tax was paid in Spain on the dividends paid to the UK parent company, whereas the other amounts paid to the UK companies were deductible in Spain and taxed in the United Kingdom at the very low rate of 7%.

The TEAC concluded, on the basis of these facts, that the UK parent company was instrumental in obtaining the exemption of the dividends in Spain, and it applied the Spanish anti-abuse clause of the Parent-Subsidiary Directive. The TEAC rejected the argument that application of the clause might be contrary to primary EU law because (i) the ultimate beneficiary of the dividends was a resident outside the European Union, and (ii) there was no valid economic reason for investing in Spain through the UK company.

Then, the TEAC considered ex officio whether article 10(1)(a) of the Spain-United Kingdom tax treaty should have been applied in this case. The TEAC observed that the UK company was not the beneficial owner of the dividends because it acted as an intermediary, a trustee or a person receiving income that belongs to someone else: the ultimate owner, i.e. in the pertinent case the individual shareholder in the UAE. For the TEAC, the BO requirement acts as an anti-abuse measure that stops the non-resident from abusing a DTC, insofar as it prevents the application of reduced withholding tax rates through intermediaries located in one of the signatory states with the sole intention of illegitimately gaining access to a reduced rate. As the attribution rules for dividends in article 10 of the treaty apply only if the treaty resident receiving the dividends is the beneficial owner, in the TEAC's opinion no reduction of withholding tax should have been granted under the treaty and, consequently, the domestic withholding tax rates should have been applied (no tax treaty between Spain and the UAE existed during the years in dispute).

176. ES: TS [Supreme Court], Order of 6 June 2019, Case 1996/2019 (not yet decided by the Supreme Court).
177. ES: TEAC [Central Economic-Administrative Court], 28 Sept. 2009, Case RG 1481/2007 , Case Law IBFD.
178. ES: Ley del Impuesto sobre la Renta de No Residentes [Law on Income Tax on Non-Residents], Royal Legislative Decree 5/2004 of 5 March 2004 , art. 14(1)(h), Primary Sources IBFD.

However, the prohibition of a *reformatio in peius* as a consequence of an appeal, a principle that is strictly observed by Spanish courts, prevented application of the higher domestic withholding tax rate to the dividends distributed by the Spanish subsidiary.

The TEAC did not analyse whether the UK company was the "legal owner of the dividends", but instead rushed to conclude that it acted as an intermediary, in the name of and for the account of the resident in the United Arab Emirates, simply because the UK company had no substance. In fact, the TEAC's position is fully in line with the AN decisions in the *Real Madrid* cases (in which the BO analysis was assimilated to a broad anti-abuse clause). Attention should be drawn, however, to the facts that the amounts received (EUR 1.8 million) and paid (EUR 1.45 million) by the UK holding were not equal, and that more than 4 months elapsed between receipt and payment. In later cases regarding holding companies and also interest, and following the decision of the ECJ in the Danish cases, the TEAC reiterated its position with renewed vigour ( *see* section 5.7.2.4. ).

### 5.7.2.4. Application of the EU interpretation of BO to DTCs between Member States

After the judgments discussed in sections 5.7.2.1.-5.7.2.3., the Spanish tax administration lost several cases connected with "conduit structures" set up within the European Union in the 2000s in order to avoid the application of Spanish thin capitalization provisions.[179]At that time, in order to avoid problems under EU law (i.e. discrimination), Spanish tax legislation excluded the application of thin capitalization provisions to EU residents (thus residents of Spain and of EU Member States would not be subject to those rules, unlike residents of non-EU states). Non-EU MNE groups often set up companies within the EU that would fund Spanish subsidiaries in leveraged acquisitions, not only to avoid the thin capitalization rules, but also to erode the Spanish corporate tax base and avoid withholding taxes on interest (due to exemptions in Spanish domestic law that would not apply to loans granted by non-EU residents).

The non-EU purchasers of the Spanish Colomer Group (in the context of the purchase by a capital venture fund of part of the Revlon Group) had such a structure, which was challenged by the Spanish tax administration. The purchase of the Spanish division of the group was funded by two companies in Luxembourg and Madeira, which lent funds to the Spanish subsidiaries and, in turn, received loans from non-EU companies of the MNE group of the purchaser. Therefore, the interest received by the Luxembourg and Madeira companies was repaid almost in full to the non-EU companies that had originally granted the loans to the Luxembourg and Madeira companies. To attack that structure, the Spanish tax administration simply disregarded the intermediate entity and applied the domestic withholding taxes (not the domestic exemption for EU residents or the reduced rate of the Luxembourg-Spain Income and Capital Tax Treaty (1986); for some reason, the Madeira entity was not included in the assessment). One of the main reasons for piercing the veil of the intermediate company was that it lacked any assets or relevant business activity apart from the loans. The tax assessment, however, applied the Spain-United States Income Tax Treaty (1990) (as amended through 2013) in connection with the part of the interest that was allocated to US entities. The Spanish courts, however, set aside the assessments of the Spanish tax administration, because the veil of the Luxembourg company could be lifted only if the Spanish GAAR and its specific procedure was used as a legal basis.

In the AN judgment of 31 October 2017 (Case 24/2016), the Court suggested that a specific anti-avoidance clause such as BO could have been used in the tax assessments, with the consequence that interest paid to the Luxembourg company would not have access to the exemption in domestic law for interest paid to EU residents or to the tax treaty with Luxembourg (the ultimate BOs were entities resident in Jersey and the United States). The conclusion of the AN reflects its traditional position that BO should be interpreted broadly, with a similar meaning to a GAAR, as it did not consider whether the intermediate companies were the real owners of the interest received or had any discretionary powers over it. It may well be the case, based on the factual information, that the interposed companies had a legal obligation to pass all the interest received to the ultimate BOs, but the analysis of the AN focused on the substance of the "conduits". Further, the AN considered that the BO requirement was implicit in the domestic exemption for interest (the exemption implemented, with a broader scope, the Interest and Royalties Directive (2003/49), but without requiring that the recipient be the BO of the interest received).

Later, and in line with the recommendations of the AN, the so-called Danish cases decided by the ECJ[180]( *see* section 5.9. ) have been used ex officio by the TEAC in direct support of the position of the tax administration. Shortly after the ECJ released the Danish judgments, the TEAC used them extensively in two decisions of 8 October 2019 (Case 185/2017 and Case 2188/2017)[181]that refer respectively to payments of interest to a Dutch BV with an ultimate Andorran shareholder and to a Luxembourg holding company controlled by a Qatari investment group (ultimately belonging to the Qatar Investment Fund). The facts of both cases are different, but the reasoning is basically identical despite some very relevant dissimilarities regarding the applicable legislation. The facts of the cases will first be summarized, before the reasoning of the TEAC is discussed.

179. The main cases are ES: TS [Supreme Court], 26 Jan. 2015, Case 2945/2013; and ES: AN [National Court], 31 Oct. 2017, Case 24/2016.
180. DK: ECJ, 26 Feb. 2019, Case C-115/16 , *N Luxembourg 1 v. Skatteministeriet* , Case Law IBFD (referring to the Interest and Royalties Directive ); and DK: ECJ, 26 Feb. 2019, Case C-116/16 , *Skatteministeriet v. T Danmark* , Case Law IBFD (on the Parent-Subsidiary Directive).
181. ES: TEAC [Central Economic-Administrative Court], 8 Oct. 2019, Case 185/2017; ES: TEAC [Central Economic-Administrative Court], 8 Oct. 2019, Case 2188/2017.

The TEAC decision in Case 185/2017 refers to a structure in which an Andorran company, controlled by an individual shareholder also resident of Andorra, set up a Netherlands Antilles BV which, in turn, controlled a Dutch BV. The latter was the sole shareholder of a Spanish operative company. The ultimate Andorran shareholder made loans that went all the way down the chain of companies from Andorra to the Spanish company. The Spanish company also paid interest in 2012 and 2014 to the Dutch BV, which was repaid at the different levels until it reached the Andorran company. The loans were made and the interest was paid from one level to another either on the same or on very close dates. Apparently, the Netherlands Antilles and Dutch BVs did not have any substance or relevant activity.

The Spanish tax auditors had refused access to the Interest and Royalties Directive (2003/49) and to the interest article of the Netherlands-Spain Income and Capital Tax Treaty (1971) in connection with interest paid by a Spanish company to a Dutch BV. From the perspective of the Netherlands-Spain DTC, it was clear at the audit level that the Dutch BV was not the BO of the interest, as the same interest received was immediately repaid to the next level.

However, the Spanish company paying the interest appealed the assessment, with the argument that the Spanish implementation of the Interest and Royalties Directive does not refer to the concept of BO. For the TEAC, although the Spanish domestic law exemption for interest paid to EU residents did not include any reference to BO, this concept was implicit in the domestic legislation implementing the Interest and Royalties Directive and the Danish cases of the ECJ supported this reasoning.

The other decision of the TEAC of 8 October 2019 (Case 2188/2017) used the same exact reasoning and the Danish judgments of the ECJ to exclude not only the application of the Parent-Subsidiary Directive (2011/96) but also the Luxembourg-Spain Income and Capital Tax Treaty (1986) to a Luxembourg holding company ("Lux Holdco") which was set up by a Qatari investor. Lux Holdco had almost 10 per 100 of the participation of a Spanish operative company in the years 2013-2014 (in Spain the Parent-Subsidiary Directive applies to participations above a 5 per 100 threshold, to avoid discrimination from domestic rules on relief for economic double taxation applicable to dividends). The Spanish company paid dividends to Lux Holdco, but the dividends were not immediately repaid to the Qatari shareholder. However, there was a financial instrument between the Lux Holdco and its shareholder whereby the latter would make payments of interest to the former, but, from the factual description, there was no correspondence or direct link between dividends received and interest paid to the ultimate shareholder. In this case, contrary to what happened in the one described in section7.2.3., the Lux Holdco had, at least, some, even if minimal, substance: although it had investments in other companies and received income other than the Spanish-sourced dividends, it lacked employees or premises and was domiciled at the address of a legal services company, which also provided directors to the board of Lux Holdco.

The legal issues considered by the TEAC were, however, different from the case of the Andorran company. Under the clause addressing abuse of the Parent-Subsidiary Directive in Spanish domestic legislation, the TEAC concluded that the Lux Holdco was not entitled to the benefits of the Parent-Subsidiary Directive (the anti-abuse clause applied was very similar to the French clause that the ECJ concluded was contrary to EU Law in *Eqiom and Enka* ( Case C-6/16 ),[182]and had similar effects to the German rules also held to be in violation of EU law in *Deister Holding* (Joined Cases C-504/16 and C-613/16)[183]and *GS* ( Case C-440/17 )).[184]Moreover, the TEAC also denied access to the Luxembourg-Spain DTC because the Lux Holdco could not be regarded as the BO of the interest. This shows that, for the TEAC, BO was equivalent to a broad prohibition of abuse, and this is why this concept for tax treaty purposes and the specific anti-abuse clause in the Spanish legislation excluding access to the Parent-Subsidiary Directive could be interpreted interchangeably (the same would have been true if the Spanish GAAR had been applied).

In both cases of 8 October 2019, the TEAC referred at length to the Danish judgments of the ECJ, but incorrectly. In fact, the reasoning is copy-pasted from one case to the other, and probably the application of the reasoning in the case of the Lux Holdco is more interesting. The TEAC explicitly affirmed that it regards the Danish judgments of the ECJ as the ECJ taking a stricter position on "holding companies" controlled by non-EU residents, which, for the TEAC, means less tolerance for the conclusion that such holdings or intermediate companies can be BOs of income received from Spanish sources or can be interposed without being regarded as abusive structures or transactions. For the TEAC, the absence of any reference to previous case law in the Danish cases (that is to say, to *Eqiom and Enka* , *Deister Holding* or *GS* ) means a change in direction in the definition of abuse by the ECJ and a less strict anti-abuse standard. If the indicia identified by the ECJ in the Danish cases were present, or any other tax reason for the interposition of the company, the application of the Interest and Royalties Directive or the Parent-Subsidiary Directive could be excluded unless the taxpayer shows a valid commercial reason for interposing the intermediate company. This reasoning was extended by the TEAC to the tax treaty domain, where the BO concept permitted it to achieve similar results in excluding access to tax treaties between Spain and other EU Member States

182. FR: ECJ, 7 Sept. 2017, Case C-6/16 , *Eqiom and Enka* , Case Law IBFD.
183. DE: ECJ, 20 Dec. 2017, Joined Cases C-504/16 and C-613/16, *Deister Holding and Juhler Holding A/S* , Case Law IBFD.
184. DE: ECJ, 14 June 2018, Case C-440/17 , *GS* , Case Law IBFD.

for intermediate companies of non-EU investors. In practice, this also implies that the TEAC will not hesitate to extend the same interpretation of BO to treaties with non-EU countries and that the concept of BO will continue to be interpreted broadly in Spain.

Although the reasoning of the TEAC presents many problems in terms of EU law,[185]this section will limit its comments to the interaction of the TEAC's reasoning with tax treaties. First, the requirements of substance in order for intermediate companies to validly invoke the benefits of Directives or tax treaties seem to be rather high from the perspective of the TEAC. At least in Case 2188/2017, Lux Holdco seemed to derive substantial income from sources other than the Spanish dividends and had other investments (even if some link could be established between those other investments and the stake in the Spanish company). However, despite the minimal substance of Lux Holdco, the TEAC denied Lux Holdco access to the Parent-Subsidiary Directive and the DTC with Luxembourg. This means that, for the TEAC, the BO concept in that treaty has a substance requirement that cannot be found anywhere in the Commentaries on articles 10-12 of the OECD Model.

Second, the confusion between BO and the principle of prohibition of abuse in the Danish cases ( *see* section 5.9. ) also permitted the TEAC to interpret the concept of BO in tax treaties in line with the conclusions of the ECJ. This is also a leap too far and suggests that, at least for the TEAC, the Danish cases are relevant for interpreting the concept of BO in tax treaties between Member States, but also between Member States and third countries. This is so even if it is clear that the economic concept of BO in the Danish cases is stricter than the legal one derived from the Commentaries on articles 10-12 of the OECD Model (2014-2017). It appears also that the TEAC, as the AN did in the *Colgate* case, is ready to apply the BO concept in cases in which there is no reference to this requirement and regards it as implicit in provisions implementing a Directive or a tax treaty.

Finally, with regard to the non-application of the Luxembourg-Spain DTC to Lux Holdco, the TEAC is making an instrumental use of the Danish cases that permits it to avoid or disregard the clear case law of the Spanish Supreme Court (as in the *Colomer* cases cited above) that requires the tax administration to resort to a special procedure when the Spanish GAARs are applied (the Spanish regulation on the GAAR requires initiating a special procedure to safeguard the rights of the taxpayer and certain uniformity throughout the national territory in its interpretation). Because the Luxembourg-Spain DTC did not have any specific or general anti-abuse clause, the only means of excluding Lux Holdco from the treaty was to apply the Spanish GAAR, which required opening a specific procedure. The extension of the ample concept of BO of the Danish cases to the interpretation of the same concept in the Luxembourg-Spain DTC permitted the TEAC to argue that there was no need to resort to the Spanish GAAR to exclude the Lux Holdco from tax treaty benefits.

In a nutshell, the decisions of the TEAC in both cases seem to be an open invitation to the Spanish tax administration to use the concept of BO in tax treaties (or the clauses prohibiting abuse of the Directive) aggressively. However, the reasoning in both decisions is deficient in terms of EU law and tax treaty interpretation, so more cases (including preliminary rulings of the ECJ) are likely to arise if the tax administration follows the TEAC's lead. It is also likely, although not yet publicly known, that the TEAC decision in Case 2188/2017 has been appealed before the Spanish courts.

### 5.7.3. BO from a residence country perspective and the elimination of double taxation in DTCs

Two decisions by the AN in 2010 and 2012 considered whether a company resident in Spain and receiving dividends from the United Kingdom could be regarded as the BO of this income for the purposes of the Spanish direct and indirect tax credit.[186]In the context of a complex transaction, a Spanish entity (Mobel Linea) bought from Goldman Sachs 13 million "value added shares" issued by the Royal Bank of Scotland. The value added shares granted the shareholder the right to receive a predetermined flow of dividends between the date of subscription – July 2002 in the case at issue – and December 2003. After a pound sterling per share had been paid to the shareholder (in December 2003), the shares would be withdrawn from the stock exchange and cancelled.

However, on the date of purchase of the shares, Mobel Linea entered into a complex set of forward and swap contracts with Goldman Sachs, whereby Goldman Sachs would repurchase the shares before November 2003 and, although the dividends would have been paid to Mobel Linea, that company would have the contractual obligation to repay the amounts received to Goldman Sachs.[187]

The aim of the transactions is not evident from the record, but it seems the tax administration considered that there may have been simulation (which, in the present author's view, is highly unlikely). From the record of the case, it appears that no

185. The conclusion that the Danish cases overrule *Eqiom* , *Deister Holding* and *GS* is probably wrong: the reversal of the burden of the proof against the taxpayer in the TEAC decisions is contrary to EU law (the tax authorities must provide indicia of abuse; it is not up to the taxpayer to prove valid economic reasons without those indicia).
186. ES: AN [National Court], 23 Feb. 2012, Case 182/2009; ES: AN [National Court], 25 Nov. 2010, Case 389/2007.
187. The "forward contract" obliged Goldman Sachs to repurchase the shares on a certain date, whereas the swap agreement had the consequence that the dividends were transferred to Goldman Sachs.

withholding tax was levied in the United Kingdom upon payment of dividends to the Spanish company. Therefore, it is likely that the Spanish company was seeking the benefits of the Spanish provisions to eliminate double (economic) taxation, as article 24(2)(b) of the Spain-United Kingdom Income and Capital Tax Treaty (1975) granted the participation in UK companies a national treatment (the cases refer to the 1975 tax treaty, which is no longer in force, and to domestic legislation that at that time differentiated between international and national dividends). That is to say, the Spanish company could gain access to either the 100 per 100 or 50 per 100 credit under domestic legislation for domestic dividends, depending on whether the participation was equal or higher than 5 per 100 of the share capital of the UK company or lower than that percentage.[188]The effect of the transaction was interesting for Mobel Linea, as, in connection with the dividends received, it permitted the company to reduce its corporate tax base in Spain to zero (dividend income was compensated with payments to Goldman Sachs under the swap contract, which were treated as deductible expenses), while the 50 per 100 or 100 per 100 credit (or the notional credit it claimed) still remained and could be used to compensate tax linked to other income obtained by the Spanish company. It is, however, confusing in the case that, according to the AN, Mobel Linea applied a credit only for taxes withheld in the United Kingdom, and the AN referred only to the domestic provisions granting direct and indirect tax credits for dividends received from abroad instead of to the domestic provisions regulating credits for dividends received from Spanish companies (which, according to article 24(2)(b) of the Spain-United Kingdom tax treaty, should have applied to the case of Mobel Linea).

The AN ruled that Mobel Linea was not the BO of the income because it was not the real and effective owner of the dividends received. The AN explained that this conclusion was based on the fact that as a consequence of the swap contract, the dividends were transferred to Goldman Sachs the day after they were received by Mobel Linea, no double taxation was suffered by Mobel Linea and it should not have the right to apply the credits to relieve legal and economic double taxation.

It is not evident that this case presented a problem relating to BO, even though that concept was used by the Spanish court. The AN reasoned that the swap contract caused the income to be excluded from the tax base of the Spanish company, and, therefore, from a technical point of view, it did not make sense to permit application of the direct and indirect tax credits, because the Spanish company did not suffer any double taxation. For the AN, even if it was not contested that the entity was the owner of the shares, a problem arose with the dividends, as, in view of the swap contract signed with Goldman Sachs, this entity was the real owner of the income paid by the Royal Bank of Scotland. For the AN, the obligation under the swap agreement to pass on the dividends received to Goldman Sachs was fatal, and should exclude the Spanish company from being the real owner. But, in the present author's view, in order to reach the conclusion that the Spanish company was not the BO, the AN should have demonstrated that its position was closer to that of a custodian or agent of the dividends received, which would have required a careful consideration of the legal rights and obligations of the Spanish company in connection with the dividends obtained – i.e. whether the Spanish company could freely dispose of the amount received, whether it was obliged to repay the same amount it received without having any power over that income, whether there was any risk assumed by the Spanish company in the transaction with regard to the dividends/share capital and whether Goldman Sachs assumed any risk (e.g. non-payment of the dividends, the possibility of paying less for the shares than the amount paid by the Spanish company), etc.).

It is interesting that the AN claims to have reached its conclusion "from a strict legal, and not economic, standpoint" and that it read a BO clause into article 23 of the OECD Model (although this article does not include any reference to BO). Indeed, it would make sense to give relief from double taxation to the legal owner of the income, i.e. to the person to whom income can be attributed in the state of residence if that person is a resident of such state. There is, therefore, a close link between the BO requirement in articles 10-12 and article 23 of the OECD Model: to the extent that a person has access to the reduced withholding tax rates in the treaty, it should also have double taxation removed in the state of residence in accordance with the provisions of article 23 of the OECD Model. Conversely, to the extent that income cannot be attributed to the person receiving it in the state of residence (according to the rules of the state of residence), it makes sense to exclude the application of articles 10-12 of the OECD Model if the true owner of the income is not a resident of the same state as the person receiving the income. To achieve that result, there is no need to include an explicit reference to BO in article 23 (A or B) of the OECD Model, as the drafting of the article reveals that close link between article 23 and articles 10-12.

In order to conclude that the Spanish company could benefit from article 24 of the 1975 Spain-United Kingdom tax treaty (methods for the elimination of double taxation), it was also relevant to know whether the Spanish company was the real/legal owner of the participation held in the UK company and the dividends received from it. By focusing on the obligation to repay, the AN was not conducting the sort of legal analysis it claimed to exert, but was closer to employing a form of reasoning that is often found at the core of anti-avoidance clauses: because the whole transaction seemed artificial, as shown by the

188. It was common at that time to argue that the direct and indirect credits recognized in the old tax treaty with the United Kingdom could be applied simultaneously, even though no tax was effectively paid in the United Kingdom by the recipient of the dividends. Due to the particularities of the advance corporation tax (ACT) system and its later derogation, the direct tax credit was, in reality, a notional credit for unpaid taxes. It may also be the case that the company sought the benefit of the notional credit. This issue led to litigation in some Spanish cases, e.g. ES: TS [Supreme Court], 2 Mar. 2015, Case 645/2013; and ES: AN [National Court], 17 Nov. 2016, Case 494/2014. In later cases, however, the issue of BO was not raised.

obligation to pass on income received, the AN concluded that the Spanish company was not the real owner of the income, and, as a consequence, was not entitled to any (direct or indirect) tax credit in Spain. As explained above, to carry out a true legal analysis, the AN should have established what the legal position of the Spanish company was, the obligations it assumed, the powers and control it had over the income received, etc. But the AN did not undertake that kind of analysis, with the consequence that it ended up characterizing as a problem of BO/legal attribution of income an issue that should have been decided by resorting to domestic GAARs (i.e. under article 15 of the Spanish General Tax Law). The analysis of the AN was not so much legal as factual, and, as such, closer to the analysis employed under a GAAR.

In short, the AN was not doing anything different from an economic/substance-over-form interpretation, even if it claimed to be merely making a legal determination of the positions of the parties.

### 5.7.4. Conclusions: BO equivalent to a GAAR

The various cases decided in Spain present some common features. First, the Spanish tax administration and courts have a strong tendency to interpret BO as equivalent to a GAAR. Rather than focusing on whether the recipient of income is the real legal owner of the item of income received, they tend to put emphasis on factual circumstances that are more in line with a typical GAAR analysis: the substance of the entity receiving the income, or whether there is a tax motive or saving, or whether the intermediate entity carries on a business activity. Further, the *Colgate* cases also show that typical transfer pricing functional analysis (delineation) of control of risks can also be used to exclude the condition of BO, adding more confusion to the meaning of the term. This trend is reinforced by the interpretation offered by the TEAC, that an expansive reading of BO is required by the case law of the ECJ, and which applies equally to the provisions implementing EU direct tax directives and to tax treaties. In many of the cases, it is likely that, if the BO clause were given a less broad meaning, more in line with the Commentaries on articles 10-12 of the OECD Model after 2014, the outcome of the cases would not have been different. However, the reasoning of the Spanish courts permits the tax administration to attack structures without the burdensome procedures that the Spanish GAAR would require, without an analysis of whether the recipient is the true legal owner of the income and reversing the burden of the proof against the taxpayers. It is also in contradiction with the string of cases in the Spanish courts that have required the strict use of GAAR procedures when abuse could be identified.

There is also a tendency to presume the BO requirement in two different scenarios: (i) passive income provisions for dividends, interest and royalties in domestic legislation or tax treaties (although the Supreme Court still has to render a decision on this); and (ii) from a residence country perspective (article 23 of the OECD Model). Both presumptions make sense if the BO concept is regarded as a rule for the proper allocation of income, but not so much if, in the end, it is regarded as a handy substitute for GAARs. Hopefully, the future decision of the Supreme Court in the *Colgate* case will shed some light into the BO debate in Spain.

## 5.8 United States: A source country perspective on BO and no substantial use of the concept

The debate and meaning over BO has special features in the United States in comparison with the OECD or other countries. First, although the United STates makes a more extensive use of BO in its treaties than does the OECD Model (BO is usually included in article 21, Other Income, as well as in articles 10-12), the relevance of this expression from the US perspective is very different in comparison with other countries.

The US position on treaty shopping is well known.[189]It uses LOB clauses as a limitation on the effects of article 4 (residence). General and subjective anti-abuse clauses (GAARs) have not been favoured by the US, which has preferred objective limits to tax treaty access such as those defined in LOB clauses. But while LOB clauses are supposedly simpler and more objective than GAARs, in practice they open up tax planning opportunities with well-known structures and are not easy to interpret.

LOB clauses therefore need to be supplemented with “anti-conduit regulations”.[190]From a US source perspective, the anti-conduit regulations refuse access to tax treaties in certain back-to-back loans and financing transactions. If the person immediately receiving the income, interest and rents of a financing arrangement is regarded as a conduit, the United States will refuse tax treaty access, because the conduit is not regarded as the BO of the income. Rather than an inquiry into whether the recipient of interest or rents is the legal owner of the income, the anti-conduit regulations are a SAAR that requires taking into account whether there is a “tax avoidance plan” (based on a PPT and a number of elements) and a tax reason – as defined in the regulations – that transforms the recipient in a “conduit company”. Because of this, the concept of conduit under the regulations does not fully match, being broader than, the same concept as used in connection with BO. It is not only conduits

189. For a good and succinct review of this policy, *see* Y. Brauner, *Beneficial Ownership in and outside US Tax Treaties* , in *Beneficial Ownership: Recent Trends* pp. 143 et seq. (M. Lang et al. eds, IBFD 2013). *See also* Meindl-Ringler, *supra* n. 1 , at p. 194 et seq.
190. 26 CFR § 1.881-3 – Conduit financing arrangements.

acting as fiduciaries, agents or nominees that are attacked under the US anti-conduit regulations, but also those that are real owners but exist for tax reasons as identified in the anti-conduit regulations.

The anti-conduit regulations have very much influenced the meaning attributed to BO under the US Model Income Tax Convention .[191]Since 2006, unlike the OECD Model, the US Model has argued that BO should be construed from the perspective of the source country legislation.[192]However, the meaning attributed to BO under previous versions of the US Model was totally different, being construed from the residence country perspective.[193]The change of position sought to justify the anti-conduit regulations and their compatibility with tax treaties. The shift from a residence to a source perspective was intended to avoid alleged treaty overrides with the anti-conduit regulations: the "source country" perspective was the excuse used by the United States to justify source country SAARs that interpreted BO differently from the OECD Model. Now that anti-conduit regulations are permitted under the BEPS anti-avoidance minimum standard and the Commentary on Article 29 of the OECD Model (2017) as a complement to LOB clauses,[194]it can be argued that the broad US interpretation of BO as a source country concept is unnecessary (the anti-abuse standard and elements of the anti-conduit regulations should be aligned with article 29(9) of the OECD Model).

It is not clear whether the special US position and approval of anti-conduit regulations was motivated by the scant attention paid to BO in US case law on tax treaties and its narrow construction in the courts,[195]or whether US case law does not use BO because there are better alternatives for fighting against treaty shopping in the US legal order. Regardless of the reason, SAARs such as the US anti-conduit rules are now admitted to be universally acceptable as part of the anti-abuse treaty standard. In this context, it can be argued that a broad source country-oriented interpretation of BO does not make sense today in the light of BEPS, the MLI and the Commentary on Article 29 of the OECD Model (2017) .

## 5.9. BO according to the ECJ (the Danish cases)

The ECJ decisions in the so-called Danish withholding cases – *N Luxembourg 1* ( Case C-115/16 ) and *T Danmark* ( Case C-116/16 ) – are highly relevant to the meaning of BO from the perspective of EU law and, in particular, in the context of the Interest and Royalties Directive (2003/49) and the Parent-Subsidiary Directive (2011/96) (in the latter the concept was regarded as implicit).[196]Although the facts and legal issues in *N Luxembourg 1* are complex, they boil down to whether payments of interest from Denmark could benefit from the Interest and Royalties Directive when received by companies in Luxembourg or Sweden, which retained a spread before it was passed on to non-EU lenders (shareholders). The facts in *T Danmark* are similar and refer to payments of dividends from Danish subsidiaries to intermediate holdings in Luxembourg and Cyprus. Both cases make fully clear that, regardless of their wording, the anti-abuse rules in article 5 of the Interest and Royalties Directive and article 1(2) of the Parent-Subsidiary Directive must be interpreted in line with the meaning of the general principle of prohibition of abuse in EU law as developed by the ECJ. In particular, with regard to the concept of BO, the *N Luxembourg 1* decision noted the following:

> The concept of "beneficial owner of the interest", within the meaning of Directive 2003/49 , must therefore be interpreted as designating an entity which *actually benefits* from the interest that is paid to it. Article 1(4) of the directive confirms that reference to *economic reality* by stating that a company of a Member State is to be treated as the beneficial owner

191. *US Model Income Tax Convention* (17 Feb. 2016) , Treaties & Models IBFD.
192. The *US Model* (2016) has no Technical Explanation, but the *Technical Explanation to the 2006 US Model Income Tax Convention* art. 10 (15 Nov. 2006) , Treaties & Models IBFD, reasoned as follows (the same explanation was provided in the Technical Explanation to articles 11, 12 and 21):
The term 'beneficial owner' is not defined in the Convention, and is, therefore, defined as under the internal law of the country imposing tax ( *i.e.* , the source country). The beneficial owner of the dividend for purposes of Article 10 is the person to which the income is attributable under the laws of the source State. Thus, if a dividend paid by a corporation that is a resident of one of the States (as determined under Article 4 (Residence)) is received by a nominee or agent that is a resident of the other State on behalf of a person that is not a resident of that other State, the dividend is not entitled to the benefits of this Article. However, a dividend received by a nominee on behalf of a resident of that other State would be entitled to benefits. These limitations are confirmed by paragraph 12 of the Commentary to Article 10 of the OECD Model. See also paragraph 24 of the Commentary to Article 1 of the OECD Model.
193. The *Technical Explanation to the 1996 US Model Income Convention* art. 10 (20 Sept. 1996) explained that:
[t]he 'beneficial owner' of a [dividend, interest or royalty] is understood generally to refer to any person resident in Contracting State to whom that State attributes the dividend for purposes of its tax. Paragraph 1(d) of Article 4 (Residence) makes this point explicitly with regard to income derived by fiscally transparent persons. Further, in accordance with paragraph 12 of the OECD Commentaries to Article 10 [or the corresponding paragraphs of articles 11 and 12], the source State may disregard as beneficial owner certain persons that nominally may receive a dividend but in substance do not control it.
194. *See* para. 187 *OECD Model: Commentary on Article 29* (2017) and sec. 2.
195. This seems to be the origin of the legislative approach to BO in the United States, as explained by Brauner, *supra* . n. 189 , at p. 148. It appears that the "legislative reaction" was triggered because the US Tax Court gave BO a very narrow reading in US: USTC, 5 Aug. 1971, *Aiken Industries v. Commissioner of Internal Revenue* , 56 TC 925 , Case Law IBFD: a recipient of income would not be its "true owner" if it "was committed to pay out exactly what it collected, and it made no profit". As the recipient had no dominon or control over the income, it could not be attributed to the intermediary. For the evolution of the US case law, see Brauner, *supra* n. 189 , at pp. 146 et seq.: Brauner, however, seems to believe that BO is a broad anti-avoidance clause when complaining that "[l]ittle risk taking and some independent function may suffice for an intermediary to overcome its bite".
196. On the effects of the interpretation of the concept of BO in the Danish cases for the Member States and the problems with the reasoning of the ECJ in these cases, *see* L. De Broe, *Should Courts in EU Member States Take Account of the ECJ's Judgment in the Danish Beneficial Ownership Cases When Interpreting the Beneficial Ownership Requirement in Tax Treaties?* , in *Current Tax Treaty Issues* (G. Maisto ed., IBFD 2020), Books IBFD.

> 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.
>
> ... The use of those various expressions [in the translation of BO into different official languages and versions of the EU Interest and Royalties Directive] underscores that the term "beneficial owner" concerns not a formally identified recipient but rather the entity which benefits *economically* from the interest received and accordingly has the power freely to determine the use to which it is put.[197][Emphasis added.]

From that paragraph it appears that, although the ECJ refers to the OECD Model (without making explicit to which version), it is certainly using a concept of BO that has a broader scope than the Commentaries on articles 10-12 of the OECD Model (2014-2017). This concept of BO includes not only legal but also factual obligations to pass on the income to a third party, as well as consideration of the economic reality of the specific fact pattern. Although claiming that it followed the OECD understanding of BO, the judgment offers a (rather unclear) concept of BO that is at odds with the one admitted by the current version of the OECD Commentaries after the changes in 2014. It appears that the ECJ is identifying abuse with the fact that the entity receiving the stream of interest (or royalties) does not meet the BO condition from an economic and not a legal standpoint. In order to decide whether there is such an abuse or a conduit situation that excludes the condition of BO, the ECJ takes into account all the indicators of abuse it has defined and not whether the entity is the legal owner of the income.[198]The *T Danmark* case confirmed this interpretation when the ECJ treated the concept of BO as implicit in the Parent-Subsidiary Directive with the stated aim of preventing abuse in the context of this norm, as defined by the case law of the ECJ, despite the fact that the Directive does not refer at all to the concept of BO (although it has an anti-abuse clause in article 1).

The main difficulty with the interpretation of BO in the Danish cases is not only that its consequences and the contours of BO are unclear, but also that there is a high risk that the "economic interpretation" defended by the ECJ will interfere with the interpretation of tax treaties between the Member States or between Member States and third states.[199]As an example, the broad interpretation of BO by the ECJ is already having consequences in the Member States, as shown by the judgments of the TEAC in Spain of 8 October 2019 ( *see* section 5.7.2.4. ). These judgments transferred the interpretation of BO in the Danish cases to Spain's tax treaty with Luxembourg (and, indirectly, with the Netherlands). It is unfortunate that the unclear, broad interpretation of BO given by the ECJ, which completely disregards the efforts of the OECD to narrow down the scope of this concept, has come to be used against taxpayers by tax administrations in the EU Member States. This does not improve legal certainty and has a potentially enormous impact upon the smooth application of tax treaties within the EU and in connection with third states. Even within EU law, the Danish decisions undermine the uniform application of the EU GAAR in article 6 of the Anti-Tax Avoidance Directive (2016/1164) if the EU Member States can take BO as a clause that could be used to apply their own interpretation of the EU GAAR, without paying any attention to its structural elements or the rights and burdens it establishes in favour of or against the taxpayer.[200]

## 5.10. BO in other countries

The experience of other countries does not much differ from the cases studied in previous sections. A general trend to attribute to BO the meaning of a GAAR prevails in most countries, either in the practice of tax administrations or case law.

For instance, Italy has had cases in which BO (i) was regarded as equivalent to a broad anti-abuse clause that requires taking into account the legal and economic entitlement of the intermediate company to the income received;[201]or (ii) was

197. Paras. 88-89 *N Luxembourg 1* ( C-115/16 ); similar statements can be found in para. 122.
198. These are the following:
-taxes are avoided by interposing the conduit in comparison with a direct payment to the final beneficial owner;
-the interest or dividend is passed on quickly by the intermediary to persons that do not fulfil the conditions for the application of the Directives. A careful assessment of the contracts and the relations between all the parties involved is needed in order to know whether the conduit receiving the funds, in substance, is not entitled to use them;
-the intermediary conduit company makes only a marginal taxable profit in order to enable the flow of funds to the final beneficial owner;
-the conduit company does not have any other economic activity (apart from receiving interest or dividends). The absence of economic activity can be inferred from an analysis of factors relating to the management of the company, its balance sheet, its cost structure and expenditure, its employees, and its premises and equipment. This seems similar to assessing whether the conduit assumes any relevant risks; and
-the timing of establishment of an avoidance structure in relation to the adoption of legislation that the structure is intended to avoid.
199. For a more detailed study of the inconsistencies of the ECJ's Danish judgments with regard to the concept of BO, *see* De Broe, *supra* n. 196 .
200. On the EU GAAR standard, *see* A.J. Martín Jiménez, *The Prohibition of Abuse of EU Tax Law and the codification of the EU GAAR* , in *The General Anti-Avoidance Rule: Past, Present, and Future* (B. Arnold ed., Canadian Tax Foundation 2020), and the bibliography cited there.
201. IT: Cass. [Supreme Court], 25 May 2016, Case 10792/2016 , Case Law IBFD; IT: Cass. [Supreme Court], 19 Dec. 2018, Case 32840; IT: Cass. [Supreme Court], 19 Dec. 2018, Case 32842 , Case Law IBFD. For a comment on the first case, *see* P. Pistone, *Italy: the Concept of Beneficial Ownership in Tax Treaties and its General Antiavoidance Function* , in *Tax Treaty Case Law Around the Globe 2017* , pp. 185 et seq. (M. Lang et al. eds, Linde 2018). The judgment in IT: Cass. [Supreme Court], 28 Dec. 2016, Case 27113/16 , Case Law IBFD, was more nuanced regarding a passive holding company, and only required demonstration of the right to retain the dividends and use them, but, as it refers to legal and economic entitlement, the concept goes beyond the OECD's.

relevant from a residence country perspective in factual situations closely resembling the Spanish Mobel Linea cases ( *see* section 5.7.3. ) or the Swiss swap cases ( *see* section 5.6.3. ).[202]

Russia has a very active tax administration that often provides guidance on BO. Again, their interpretation is closer to GAARs than to a strict or narrow threshold for BO, with the tax administration and courts taking into account not only legal factors but also the economic activity of the intermediate company and the economic reasons for interposing it, its assets, structure and accounts, and payments made to other parties even if they are not legally linked with the payment received by the conduit. The withholding agent must also have documentation that proves BO (a confirmation letter and a "defence file").[203]Like other countries, Russia regards the BO concept as applying not only to dividends, interest and royalties but also to other treaty articles.

In China, the State Taxation Administration released Public Notice [2018] 9 on 3 February 2018,[204]updating the rules on BO in tax treaties. Generally, according to this Notice, BO must be determined on the basis of factual circumstances, and the SAT's understanding of the concept is certainly broader than in the OECD context after 2014 and is closer to a GAAR.[205]

In Argentina, the *Molinos* cases (2013 and 2016)[206]are interesting and revealing regarding the confusion or interchangeability in some countries between BO and GAARs. The facts of the cases are simple. Some operative subsidiaries in Latin American countries of an Argentinian parent company were controlled through a holding company in Chile. The holding company permitted the parent of the group to receive untaxed dividends in Argentina, whereas, if they had been received directly from the subsidiaries in Uruguay and Peru, they would have been included in the corporate income tax base in Argentina. The Chilean holding company permitted the group to take advantage of the DTC between Argentina and Chile, which followed the Andean Community Income and Capital Model Tax Treaty (1971)[207]and did not permit the residence country, i.e. Argentina, to tax the dividends distributed by the holding company in Chile. The dividends were not taxable in Chile, neither when received nor when distributed by the holding to its Argentinean parent company.

Both the lower court and the *Cámara Nacional de Apelaciones en lo Contencioso Administrativo Federal* (Federal Court of Appeal) in Argentina applied the domestic GAAR (principle of economic reality) to disregard the Chilean holding, because it did not have any nexus with Chile or with the activities of the subsidiaries. Both Courts regarded the holding as a conduit and made extensive use of OECD materials on conduits so that they somehow read the BO concept into the Argentina domestic GAAR, but with an understanding of the meaning of "conduit" and BO that pays attention not only to legal realities but also to the "economic substance" of the factual pattern presented. Attention was paid to the fact that dividends were distributed by the Chilean holding company immediately after received, but not to whether there was a predetermined legal obligation to do so. Therefore, from this case it can be derived that both Courts, especially the lower one, considered the BO concept, and obviously the GAAR, to allow fighting any type of conduit company. The two concepts, as in many countries, were regarded as nearly equivalent and as having similar effects. The applicable treaty between Argentina and Chile, apart from following the Andean Model (1971), did not refer to BO, so the Courts seem to have used the domestic GAAR to enshrine the BO concept in the treaty unnecessarily – as the use of the GAAR, as such, was enough to attain the same outcome. The case is pending before the Supreme Court in Argentina.

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202. *See* P. Pistone, *Italy: Beneficial Ownership as Anti-Abuse Provision in International Taxation* , in *Beneficial Ownership: Recent Trends* , p. 175 et seq. (M. Lang et al. eds, IBFD 2013), Books IBFD, commenting on the judgment IT: CTP [First Instance Tax Court] Reggio Emilia, 29 Nov. 2010, N.242-01-10.
203. Federal Tax Service, Letter No. CA-4-9/8285 (28 April 2018); N. Milogolov, *Summary of court practice regarding application of beneficial owner concept – FTS clarifications* (5 June 2018), News IBFD (summarizing the practice of Russian courts; subsequent practice has not varied from the principles expressed in the Letter); and KPMG, *Russia: Concept of "beneficial ownership" and implications for withholding tax* (3 Sept. 2019), available at https://home.kpmg/us/en/home/insights/2019/09/tnf-russia-concept-beneficial-ownership-implications-withholding-tax.html (last accessed 27 May 2020).
204. State Taxation Administration, Public Notice [2018] 9 (3 Feb. 2018); *see* S. Ma, *New Notice on Beneficial Ownership Published* (9 Feb. 2018), News IBFD.
205. The following factors will have an adverse effect in determining BO status: (i) the recipient has the obligation (contractually or de facto) to pass on more than 50% of the received payments to a resident of a third country (or region) within 12 months; (ii) activities conducted by the recipient do not constitute substantial business activities (substantial business activities include substantial manufacture and sales and management activities, and substance must be determined by reference to functions performed and risks assumed); (iii) the income of the recipient is not subject to tax, is exempt from tax or is taxed at a very low effective tax rate in the jurisdiction in which the recipient resides; (iv) in addition to the loan agreement from which the interest income is derived, there is (are) other similar (in terms of amount, interest rate and time) loan or deposit agreement(s) with a third party; and (v) in addition to the contracts on copyright, patent and know-how in which royalties arise, there is (are) other contracts on copyright, patents and know-how with a third party. The Public Notice also includes safe harbours for certain categories of taxpayers: (i) the government of the recipient's country jurisdiction; (ii) a resident company listed in the recipient's jurisdiction; (iii) an individual resident of the recipient's country; and (iv) a direct or indirect 100%-owned subsidiary of the above-mentioned (in the case of indirect shareholding, the intermediate company must be a resident of China or the recipient's jurisdiction).
206. AR: CNACAF [Federal Court of Appeal], 19 May 2016, *Molinos Rio de la Plata v. DGI* , which confirmed the first instance judgment AR: TFN [Federal Tax Court], 14 Aug. 2013, Case 34.739-I to 35.783-I, *Molinos Rio de la Plata v. DGI* , Case Law IBFD. A comment on the Federal Court of Appeal decision can be found in M. Screpante, *Argentina: Treaty Abuse and Beneficial Ownership – the Molinos Case* , in *Tax Treaty Case Law Around the Globe 2017* p. 115 (M. Lang et al. (eds), Linde/IBFD 2018), Books IBFD. The author would like to thank M. Screpante for sending him the original texts of the two judgments.
207. *Andean Community Income and Capital Model Tax Treaty* (16 Nov. 1971) , Treaties & Models IBFD.

## 5.11. Conclusions on the trends in different countries

Although the changes to the Commentaries on articles 10-12 of the OECD Model in 2014 sought to clarify the meaning of BO, their impact on the case law and administrative positions of different countries has been limited. Before and after 2014, most countries (with the notable exceptions of Canada and the Netherlands) have preferred to construe BO broadly, as an alternative to or replacement for domestic GAARs, or have even decided to pass their own SAARs to interpret the concept broadly (e.g. the United States). The ECJ judgments in the Danish cases will probably reinforce this trend and lead to the extension to tax treaties of the broad interpretation it gave to the concept of BO in EU law (as has already been done by the Spanish TEAC: *see* section 5.7.2.4.).

The trend towards construiung BO broadly, as equivalent to a GAAR, has historically sought to overcome two difficulties: (i) BO has been a handy tool for overcoming the domestic difficulty experienced by some countries in applying GAARs in a tax treaty context (e.g. France in *Bank of Scotland*); and (ii) it has also been used by tax administrations and courts to avoid the often burdensome application of GAARs, with their specific procedures in some countries, and in particular the need to prove the "subjective element" (application of a GAAR is usually more difficult and cumbersome than using an undefined and ambiguous concept as BO to attack treaty shopping). In this context, the Swiss experience is especially interesting: by objectivizing the "subjective element" of the GAARs and reading it into BO, the Swiss courts could read a GAAR into the BO concept without all the inconveniences and burden of proof issues that application of GAARs and their subjective elements often present for tax administrations. This is similar to what courts and administrations in other countries are doing, and the ECJ likewise, in taking into account factual (and not only legal, as the OECD suggests) elements when applying BO.

The trend towards interpreting BO as a sort of GAAR in a majority of countries is in sharp contrast with the parallel move, sometimes in the same countries (e.g. Argentina, Italy, Spain and Switzerland),[208]towards regarding this concept as implicit in tax treaty provisions that do not refer to BO, whether because they follow the OECD Draft Model (1963) or for other reasons. It would be natural to consider the concept as implicit in any provision of tax treaties if it were interpreted narrowly (as true legal ownership), but not in other cases, as "economic ownership" cannot be a useful benchmark for allocating income without using specific GAAR procedures. If interpreted as equivalent to ultimate economic beneficiary, the conclusion that BO is implicit in tax treaties in which the term is not used poses obvious problems of uncertainty.

It appears that the effect of introducing article 29(9) of the OECD Model (2017) has not contributed to reducing this trend or the speed with which the expansive use of BO seems to be spreading. Moreover, the transfer pricing framework derived from the BEPS Project, which clearly has an anti-abuse flavour, with so much emphasis placed on control of risks and DEMPE functions in the OECD Guidelines, will cause further uncertainty (the Spanish *Colgate* case shows this further element of confusion). Probably it is too early to say, but there are hints in the position of some tax administrations and court judgments (i.e. by the ECJ, in Spain and Switzerland) that suggest that BO will be more relevant than it should in a post-BEPS context. This is yet another contradiction in the unfortunately long life of BO, as the BEPS changes (the MLI and the OECD Model (2017) in particular) clearly situate this concept as a prime candidate for elimination from the international tax landscape.

# 6. Conceptual Issues

## 6.1. Introduction

From the previous section it is clear that there is a prevailing trend towards interpreting BO as equivalent or almost equivalent to a GAAR, despite the OECD's efforts to narrow down its scope in 2014 (following the OECD's own move to enlarge it in 2003).

At first glance, it is tempting to conclude that BO is interpreted differently by tax administrations and courts in the countries studied. In the present author's view, however, this conclusion would be erroneous, because there are common points in those decisions that should be stressed and that add important nuances to the (never-ending) discussion about the meaning of BO. In fact, as long as there are more similarities than divergences, some common understanding of the term may be found. It is curious, however, that convergence has not taken place in the direction of the OECD's apparent interpretation of BO after 2014, which suggests that the 2014 changes to the Commentaries on the OECD Model were not sufficient and that some further action may be needed regarding BO to take into account the new situation derived from the BEPS Action 6 Final Report, the MLI and the introduction of article 29 of the OECD Model (2017). The conceptual issues that present problems are studied further in the following sections, along with the commonalities and differences in interpreting the concept in the countries studied.

208. This is also the case in the so-called Danish judgments of the ECJ.

## 6.2. Towards an international meaning of the concept of BO?

Almost all of the cases (and administrative positions) in the jurisdictions studied attribute an "international meaning" to the BO concept or refer to such a meaning. In order to establish what its content is, the courts usually resort to international law (e.g. the Swiss courts) or to the OECD Model and the Conduit Companies Report, accepting (at least in some jurisdictions: e.g. Spain, Canada and England) the retroactive effect of either the 1986 Conduit Companies Report or the discussions of BO in the 2003 Commentaries on articles 10-12 of the OECD Model.[209]However, the Commentaries on the OECD Model (2014-2017) have been utilized much less in decisions rendered after they were published, despite the fact that they reinforce the international meaning of BO by, for instance, explicitly affirming the independence of BO from the same domestic concept in the law of trusts.[210]Some courts (e.g. in Switzerland) have even forced an interpretation of the newer Commentaries that is more in line with their 2003 versions.

It is not fully clear to what extent statements in judicial decisions about the international meaning of BO have been influenced by the discussions of BO in the Commentaries on arts. 10-12 of the OECD Model (2003) ,[211]by the lack of any domestic law definition (or agreement in internal law on the meaning) of BO, or by the law of treaties and the need to interpret DTCs symmetrically in both contracting states. In some countries (e.g. Spain), it appears that the 2003 Commentaries had a decisive impact on the meaning attributed to BO.

A quick reading of the cases may lead the interpreter to conclude that the focus of discussion about BO has shifted from internal to international law and that this concept, when used in tax treaties, may have forever abandoned its link with the law of trusts or the law of the source state (this is a case in which "context otherwise requires", and so the rule of article 3(2) of the OECD Model cannot be applied).[212]It is surprising to see, however, that, although courts in different countries speak about the international meaning of the concept of BO, it has not fully lost its nexus with internal law (of the source or the residence state). In fact, most of the decisions apply source country anti-abuse standards in order to attribute a meaning to BO. Confronted with this situation, a cynic would say that, even if there were an international meaning of BO, courts and tax administrations in the countries studied are speaking different dialects that are so dissimilar from each other that mutual understanding may not be facilitated. An even greater cynic might even say that convergence on the meaning of BO, if any, has centred around parameters other than those taken into account by the OECD in the Commentaries on articles 10-12 of the OECD Model (2014-2017) – with the result there are different international meanings of BO in the Commentaries and in domestic case law. Despite their differences, the positions on BO in the countries studied have more in common than it may seem at first sight.

## 6.3. Beneficial ownership: an economic or legal concept? Broad or narrow anti-abuse clause?

It is interesting that most of the administrative positions and judgments studied (with the important exception of the Dutch "market maker" and the Canadian *Prévost* and *Velcro* cases) adopted an economic/substance-over-form approach to decide who the BO of income is. There are nuances in the different approaches followed. Some tax administrations and courts tend to apply in the context of BO the same indicators they would use to find abuse when applying a GAAR (e.g. China, the ECJ, Italy, Spain, Russia and the United Kingdom).

Others (e.g. Switzerland) follow a so-called "forwarding approach",[213]which uses fewer factors (primarily the legal or factual connection between payments received and made) and is narrower than the broad anti-abuse approach (no need to identify "motives" or "tax reasons"). However, the forwarding approach produces very similar outcomes and is substantially equivalent to the broad anti-abuse interpretation of BO: forwarding the payments is always a relevant factor in deciding whether there is abuse. It can be argued that, in the forwarding approach, there is no search for a "subjective element", which is inherent in the application of GAARs. In practice, the search for a connection between the payments received and made is a handy substitute

209. The reason why the Commentaries on articles 10-12 of the OECD Model (2003) and the Conduit Companies Report are granted retroactive effect is not obvious in all jurisdictions: in Spain nothing is explained by the AN in this respect, and in Canada the FCA explicitly mentions their clarifying effect. The retroactivity of the 1977 Commentaries with regard to previous DTCs that do not contain the term BO is also widely accepted; *see* , for instance, Walser, *supra* n. 1 , at pp. 30-32. This issue is pending before the Spanish Supreme Court in the *Colgate* case: *see* sec. 5.7.4.
210. *See* paras. 12.1, 9.1. and 4 respectively of the Commentaries to articles 10, 11 and 12 of the OECD Model (2014-2017).
211. Para. 12 *OECD Model: Commentary on Art. 10* (2003) : "The term 'beneficial owner' is not used in a narrow technical sense, rather, it should be understood in its context and in light of the object and purposes of the convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance" (similar statements can be found in the Commentaries on articles 11 and 12).
212. The issue of whether or not BO takes its meaning from internal law under art. 3(2) of the OECD Model has attracted much academic attention. In particular, Du Toit, *supra* n. 1 , has been an ardent defender of the claim that the term takes its meaning from the domestic law of common law states (even if he argues that it is a term of international tax law); *see also* Pijl (2003), *supra* n. 1 , at p. 357. Other commentators have argued the contrary: *see* , for instance, S. van Weeghel, in Oliver et al, *supra* n. 1 , at pp. 43-46; J.B. Libin, in Oliver et al, *supra* n. 1 , at pp. 46-48; Danon (2004), *supra* n. 1 , at pp. 332-334; Avery Jones et al., *supra* n. 13 , at p. 247; and De Broe, *supra* n. 1 , at p. 668 et seq., all of whom are in favour of giving the term a "contextual" meaning.
213. On the forwarding approach, *see* Meindl-Ringler, *supra* n. 1 , at p. 325 et seq.

or proxy for the subjective element, as the intention of a taxpayer can only be proved with objective indicators of abuse. This is the role that "forwarding" plays.

Therefore, for tax administrations and courts in all the countries studied except Canada and the Netherlands, the concept of BO requires a search for the person who ultimately and economically enjoys the specific item of income. Sometimes the courts state it more overtly (e.g. the ECJ, Spain, Switzerland in the *V. SA* case); sometimes it is more implicit in the decision (e.g. *Indofood* , with its references to the "substance of the matter" and tied payments; the CE in *Bank of Scotland* and its substance-over-form analysis; or the Swiss total return swap cases and their forwarding approach). An economic approach to BO has also been defended by some legal scholars,[214]who consider the Commentaries on articles 10-12 of the OECD Model (2003) to support this position.[215]

However, despite the plain words in many of the judgments, it is possible to dispute that all of them carried out an economic/substance-over-form analysis. At first sight they mention that BO should be interpreted economically, applying various different tests (correlation between income received and paid; powers of the intermediate vehicle; whether or not the income flowed through the intermediary, etc.). In the present author's view, however, what all the judgments (including *Prévost* , *Velcro* and the "market maker" judgment, but with the possible exception of *Bank of Scotland* ) ultimately carried out was a legal analysis of the factual circumstances: facts – and especially legal arrangements between the parties – were scrutinized in order to conclude in most of the cases (excluding "market maker", *Prévost* and *Velcro* ) that the recipient's position was no different from that of an agent/nominee, and was not that of a legal owner of the income with dominion over the income received.

If one steps back for a moment and thinks about the outcome of the cases (except, as mentioned, *Prévost* , *Velcro* , "market maker" and, for other reasons, *Bank of Scotland* ), it is difficult to conclude that the Hungarian companies in the Spanish cases, the interposed conduits in the Swiss cases or the intermediate Mauritian/Netherlands company in *Indofood* are more than agents or nominees from a legal (as opposed to economic) point of view.[216]No "economic" or "substance over form" analysis is needed to reach this conclusion, because a recharacterization of the legal relations or the analysis inherent to simulation cases is enough to conclude that what the parties are saying (i.e. that income can be attributed to the "intermediary") is different from what they in fact do (i.e. there is an agency–administration or analogous relationship rather than a legal entitlement of the intermediary to the income).[217]In the present author's view, BO is a legal issue,[218]not an economic one.[219]If economic analysis of the facts is introduced into the determination of the BO of income, the concept will be so broad as to make it barely distinguishable from a general anti-avoidance measure. The *Bank of Scotland* decision by the CE is blatant proof of this: the French Court resorted to the BO concept, but the OECD used almost the same factual situation as an example of abuse in the Commentary on article 29 of the OECD Model. As explained in sections 2.2. and 2.3. , despite the Commentaries on the OECD Model (2003) , neither history nor a contextual interpretation of the expression (all the more so after BEPS , the MLI and article 29(9) of the OECD Model (2017) ) supports the construction of BO in a broad economic, as opposed to a legal, fashion.

In this regard, it is not fully clear to what extent the original meaning of the concept in common law systems has led to misunderstandings in civil law legal orders, in which the idea of full ownership has been (erroneously) identified with "economic interpretation". However, in many jurisdictions the confusion was exploited by tax administrations, who used the concept of BO as a means of applying domestic GAARs or anti-abuse doctrines in a treaty context when the latter presented domestic

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214. *See* , for instance, Danon (2004), *supra* n. 1 (although Danon has moved to a legal approach in his more recent works: *see* , for instance, Danon (2020), *supra* n. 1 ). Pijl, *supra* n. 1 , at pp. 256-257, explains that this is the approach followed by Dutch tax authorities. The approach of Vogel, *supra* n. 1 , at paras. 9-10, is closer to the economic interpretation, as he refers to beneficial owner as a question of "substance over form" and his test to determine beneficial ownership is not only "legal" but also "factual".
215. *See* sec. 2.5. on the 2003 changes to the Commentaries on articles 10-12 of the OECD Model. Other OECD materials can also be used to defend this interpretation, as also explained in sec. 2.
216. The Swiss position neatly illustrates the kind of analysis undertaken, when it is concluded that the "spread" of the conduit can be regarded as remuneration for the "forwarding", which in legal terms is basically a commission for a role as agent or nominee. *See* , in this respect, CH: BGer/TF [Federal Supreme Court], 19 May 2020, 2C_880/2018.
217. As pointed out by F. Zimmer, *General Report* , in *Form and Substance in Tax Law* pp. 24-25 (IFA Cahiers vol. 87A, 2002) Books IBFD, points out, "legal substance" is not to be assimilated to the "economic substance" of a transaction, as "the concept of legal substance most often refers to the characterisation which emerges from a close study of the rights and obligations in a legal relation ... The main function of the concept of legal substance is to point out that sham or simulation transactions and wrong legal characterisations by the taxpayer will be disregarded for tax purposes". Economic substance" is to be assessed by applying anti-avoidance rules or doctrines.
218. *See also* the conclusions of J.D.B. Oliver in Oliver et al., *supra* n. 1 , at p. 68; Du Toit, *supra* n. 1 , at p. 227; and Walser, *supra* n. 1 , at pp. 17-18. In this context, the tests some authors have proposed for deciding on BO (e.g. the bankruptcy or catastrophe scenario: *see* Baker, *supra* n. 1 , at para. 10B-15) are merely tools for deciding whether the recipient of dividends, interest or royalties is the "legal/real owner" (and not an intermediary or administrator, such as an agent or nominee) of income.
219. *See* Arnold, *supra* n. 142 , at pp. 175-176; De Broe, *supra* n. 1 , at p. 687 (on conduits); Walser, *supra* n. 1 , at pp. 27-29; and the comments by B. Gouthière in Walser, *supra* n. 1 , at p. 24. The position that BO is an "economic concept" has widespread acceptance: *see* , for instance, C. HJI Panayi, *Double Taxation, Tax Treaties, Treaty-Shopping and the European Community* p. 44 et seq. (Kluwer Law International 2007); Pijl, *supra* n. 1 ; Danon (2004), *supra* n. 1 , especially at p. 336 et seq. Danon seems however to have changed his views in more recent works, in which he argues that BO should be interpreted legally: *see* Danon (2018), *supra* n. 1 , and Danon (2020), *supra* n. 1 .

difficulties. It is also clear that the main source of the confusion was the updates to the Commentary on the OECD Model (2003), which expanded the meaning of BO in an unprecedented manner, prompting tax administrations and courts to apply BO with a meaning closer to anti-avoidance rules than it had previously had. It is notable that, in most of the cases, a "legal substance" approach would have sufficed to achieve similar outcomes. This approach would have also corrected the excessive formalism that appears in other cases, such as *Velcro* in Canada or the "market maker" judgment in the Netherlands.

The OECD's attempt to reduce the scope of BO in 2014 has not so far been successful in reducing the broad scope granted to BO in different jurisdictions. First, it probably came too late, after the meaning of BO had already been established in many countries. Second, the limited forwarding approach taken by the OECD in 2014 has limitations, because it is not fully clear what it means and still leaves some room for "economic interpretation" (see section 2.2.8.), rather than making clear that BO refers to a full dominion test and the circumstances in which an interposed intermediary might not be considered to have legal dominion over the income. Implicitly, the inclusion of article 29(9) of the OECD Model (2017) adds further impetus to a reduction of the scope of BO, but decisions such as the Danish cases of the ECJ may affect the position of EU countries (most of them members of the OECD) by expanding the concept of BO, and so further contribute to the confusion (*see* the Spanish TEAC decisions applying the Danish cases, section 5.9.). The "economic substance approach" of the OECD Guidelines, as derived from BEPS Actions 8-10, and which applies in parallel, also fails to increase legal certainty (*see* section 3.5.), and any coordination between BO and the delineation/non-recognition approach of chapter 1 of the OECD Guidelines is still pending.

It is also surprising that many jurisdictions (e.g. the ECJ, Italy, Spain and Switzerland), even while granting to BO a broad economic meaning, still regard it as implicit in tax treaties (and norms) that do not use this term. That conclusion would be understandable if BO were interpreted narrowly, but not in the case of interpretation of the term as closer to a GAAR.

## 6.4. BO: An anti-avoidance or attribution-of-income rule? Of which state – source or residence?

As explained sections 6.1.-6.3., (i) although BO has been assigned an international meaning in all the countries discussed, in reality they were using domestic (anti-abuse) standards to interpret this term; and (ii) even if it made more sense to interpret BO with a legal substance meaning, the majority of countries have attributed to BO the function of a rule (almost) equivalent to a GAAR. Both points entail relevant decisions about the benchmark (i.e. source or residence country tax and legal orders) that is relevant in deciding whether or not a person is a BO.

Interpreting BO as a broad anti-avoidance rule means that the standards and indicators regarded as relevant in the source state will be used to decide on BO. This is very clear in all the administrative positions (e.g. China and Russia) and court decisions (all countries) studied in section 5. It is most evident in the United States, which also attributes to BO the meaning of the source country legislation in order also to justify the application of the anti-conduit regulations in a treaty context (*see* section 5.8.). Now that a common anti-abuse standard has been established in article 29 of the OECD Model (2017), application of source state standards is less justified, although still likely, as the PPT in particular (article 29(9) of the OECD Model (2017)) is very vague and lends itself to different interpretations. It would be unfortunate if BO, in the post- BEPS context, should take on the role of a safety valve allowing the application of source country anti-abuse standards while the almost brand new OECD ones in article 29 of the OECD Model (2017) are disregarded. This is, however, a tangible risk (*see* section 5.7.2.3. on the reaction of the Spanish TEAC to the ECJ's Danish cases). Further clarification of the BO test seems warranted, not only to improve the application of articles 10-12 of the OECD Model but also the brand new common anti-avoidance standard as represented by article 29 of the OECD Model (2017) (LOB plus anti-conduit regulations or the PPT).

The interpretation of BO as an attribution of income rule under the tax laws of the residence state is probably more justified, and a better approach if a number of factors is taken into account.[220] The origins of the expression, as a concept intended to satisfy a UK need, points in this direction. As explained in section 2.1., BO was intended to correct the effect of UK rules that attributed income to UK trusts, in order to exclude from the scope of tax treaties cases in which foreign income was paid to a UK trustee acting in the name of a non-UK settlor. The unusual outcome produced by the United Kingdom's domestic attribution of income rule in the specific case of non-UK resident settlors deriving non-UK income facilitated a very specific form of treaty shopping (interposition of persons that had no direct relationship with the income received and that were not taxed upon receipt of such income). The correction made to domestic attribution rules in the United Kingdom by adding the BO concept was also in itself an attribution rule, which placed income in the hands of the real owner where there was a risk of a treaty shopping (and certainly there was no risk whatsoever of double taxation).

220. *See* Meindl-Ringler, *supra* n. 1, at ch. 10.

The interpretation of BO as a rule of attribution of income under the tax laws of the residence state also finds support in OECD materials, and best accommodates the object and purpose of DTCs (i.e. limitations on source country taxation in DTCs make sense only if income accrues to a resident of the other contracting state under its own legislation).[221]The fact that the Commentaries on articles 10-12 of the OECD Model devote some attention to BO and do not refer to the general rule under article 3(2) (advising reference to source state legislation) is also indicative that this is a case where "context otherwise requires",[222]and in this case "context" may require looking at the residence state legislation on attribution of income.[223]Moreover, this approach, which directly derives from the OECD's Partnerships Report , had a relevant impact in the Commentaries on articles 10-12 of the OECD Model already in 2003, and has not been modified in the current OECD Model, which states that "[t]he direct recipient of the income in this situation qualifies as a resident but no potential double taxation arises as a consequence of that status *since the recipient is not treated as the owner of income for tax purposes in the State of residence* " [emphasis added].[224]That is to say, it appears that the current Commentaries lend support to the interpretation of BO as an attribution of income rule from the perspective of the state of residence.

Needless to say, this interpretation is also not indisputable. None of the decisions commented on in this article (with the possible exception of *Prévost* and, to a certain extent, *Velcro* ) consider in detail what happens in the tax/commercial law legislation of the state of residence. Rather, they focus on the source state position. Practicability and difficulties in the application of residence country legislation by the source country are one of the Achilles heels of the attribution of income approach. In addition, the United States has argued that BO is an attribution-of-income rule under the source state legislation, with the anti-avoidance arsenal of the source state (including, among others, the anti-conduit regulations) being an integral part of the attribution of income.[225]While the Commentaries on articles 10-12 of the OECD Model (2003-2017) provide some support for the construction of the BO clause as a rule of attribution of income according to the legislation of the state of residence,[226]the Commentary on Article 1 of the OECD Model (2003-2017), on improper use of DTCs, can also be used to defend the contrary (i.e. the US position),[227]as can some OECD work.[228]

Although the idea of the guiding principle in the Commentary on Article 1 of the OECD Model after 2003 was to establish a common anti-avoidance standard, it gave a certain margin to states to establish their own anti-abuse principles. The addition of article 29 of the OECD Model (2017) and article 7 of the MLI somewhat reduces this margin and further refines the common anti-avoidance standard to be applied by both contracting states, but the PPT remains vague in some aspects and, again, lends itself to different interpretations and standards that may permit the source state to apply special anti-avoidance rules. Moreover, as explained, the Commentary on Article 29 of the OECD Model (2017) admits anti-conduit regulations to complement LOB clauses, which may also be taken as explicit support for a source country BO standard (although after 2017 it must conform with the common anti-abuse standard of article 29(9) or the guiding principle of paragraph 61 of the Commentary on Article 1 of the OECD Model).

Some challenges and contradictions are also evident in the construction of BO as an attribution-of-income rule according to the laws of the state of residence:

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221. This was the position defended by H.J. Ault when commenting on BO; *see* Walser, *supra* n. 1 , at pp. 21-22. *See* *Partnerships Report* , *supra* n. 41 , at para. 52, where this principle is regarded as inherent in DTCs. Example 4, paras. 59-62 *Partnerships Report* , also interprets the BO requirement as a rule on attribution of income in the state of residence. This position was also upheld by J.B. Libin and J.D.B. Oliver, although not by the other authors, in Oliver et al., *supra* n. 1 , at pp. 60-65; *see also* De Broe, *supra* n. 1 , at p. 693. The interpretation of BO as an attribution-of-income rule would also permit "trusts/ trustees", partnerships subject to tax in their state of residence and other "entities" subject to tax to have access to a DTC when excluding them from a DTC may cause double taxation. *See* , with regard to trusts, J. Prebble, *Trusts and Double Taxation Agreements* , 2 eJournal of Tax Research 2, p. 192 et seq. (2004); J. Prebble, *Accumulation Trusts and Double Tax Conventions* , Brit. Tax Rev. 1, p. 69 et seq. (2001); and Danon (2004), *supra* n. 1 , especially at ch. 3.
222. *See* Walser, *supra* n. 1 , at p. 16, for a similar opinion.
223. H.J. Ault, commenting on Walser, *supra* n. 1 , at p. 17, pointed out that this result can be inferred either from a "contextual" interpretation of BO or from a special rule "where it would be appropriate for the source country to look to the residence country treatment of beneficial ownership".
224. Para. 12.1. *OECD Model: Commentary on Article 10* (2003) ; now included in para. 12.2 *OECD Model: Commentary on Article 10* (2017) . Corresponding paragraphs can also be found in para. 10 *OECD Model: Commentary on Article 11* (2017) and para. 4.1. *OECD Model: Commentary on Article 12* (2017).
225. *See* sec. 5.8 .
226. Wheeler (2005), *supra* n. 1 , at p. 481, suggests that this reference may be to the law of the "intermediary's state". In the present author's view, if the sentence is read *a contrario* , it is referring to the state of residence of the owner of income, but it must be acknowledged that problems may arise if the attribution-of-income rules differ between the state of the intermediary and the state of residence of the "beneficial owner".
227. *See* para. 9.2 *OECD Model: Commentary on Article 1* (2003) , where it was stated that, since domestic anti-abuse rules are part of the internal rules which determine tax liability, they are not affected by DTCs; the same statement also appears in para. 58 *OECD Model: Commentary on Article 1* (2017) . For criticism of this position, *see* F. Zimmer, *Domestic Anti-Avoidance Rules and Tax Treaties – Comment on Brian Arnold's Article* , 59 Bull. Intl. Fisc. Docn. 1, p. 25 (2005), Journal Articles & Papers IBFD; and Wheeler (2005), *supra* n. 1 , at p. 487. It can also be argued the use of domestic anti-avoidance rules in a treaty context is a tool of last resort ( *see* para. 9.5 *OECD Model: Commentaries on Article 1* (2003-2014), para. 61 *OECD Model: Commentary on Article 1* (2017) , whereas the exclusion of intermediaries from agents and nominees is a primary rule in DTCs, so not all the rules on attribution of income of the source state can be applied immediately in treaty situations.
228. *See* *ICG Report* , *supra* n. 50 , at para. 34, in which it is assumed that the residence country and the source country can apply different concepts of beneficial ownership; or at para. 93, in which a source country BO concept is mentioned.

- Some persons subject to tax in the state of residence may be regarded as BOs and have access to DTCs even if, for civil or commercial law purposes, income does not accrue to them.[229]It may make sense to give treaty benefits to persons who are liable to tax in the state of residence, but it would be strange to regard as BO a person who is not in civil law terms the owner of income, even if for tax purposes that income is attributed to such a person. However, if BO is interpreted as an attribution-of-income rule for tax purposes of the state of residence, then, regardless of what happens with civil or commercial law rules, persons taxed in the state of residence would not be excluded from the protection of DTCs and the objective of eliminating double taxation may be achieved. Special cases in which the person taxed is not the BO from a commercial or civil law point of view, if this creates any problems, might best be dealt with by the contracting states through special rules or articles in DTCs (or, alternatively, through interpretative mutual agreement procedures). It should not be forgotten that, when BO was introduced, it was fully acknowledged that persons who could not be attributed income from a civil law perspective (e.g. trusts) could have access to tax treaties because tax law allocated income to them (as in the case of trusts under UK law). In fact, BO was originally intended to correct the unusual outcome caused by the peculiar UK rule for the taxation of trusts in cases in which a UK trustee received offshore income in the name of a non-UK resident. That is to say, in its origins, the BO concept allowed for the different outcomes that tax law and civil law can create and indeed resulted from the explicit recognition that in some specific cases the tax rules can produce strange outcomes that need to be corrected to ensure that the application of tax treaties is more in line with its fundamental goals.
- Some entities/persons with legal personality, but treated as transparent or exempt for tax purposes in the state of residence or some specific agreements (e.g. partnerships, trusts, specific types of company, CIVs, etc.), may not have access to DTCs even if they are legally (from a civil or commercial law perspective) entitled to the income received. Once again it should be remembered in this connection that, besides ts anti-treaty shopping function, BO found its way into UK DTCs as a way to eliminate the rigours of subject-to-tax clauses and allow pension funds and charities, which were usually exempt from taxation, access to articles 10 and 11.[230]Therefore, as a matter of principle, the fact that a person is exempt from tax should not preclude it from being considered the BO if it is the true legal owner, having the relevant dominion over the income.

  The same reasoning may apply to some transparent entities/arrangements, although here the problem is solved at the level of article 1(2) of the OECD Model (2017), because such entities/agreements are probably BOs in the context of articles 10-12 of the OECD Model.[231]Including them within the scope of a tax treaty is likely to require some additional specifications in article 1 (e.g. a clause similar to article 1(2) of the OECD Model (2017)) or in the definition of "person" and "residence" in articles 3(1)(a) and 4 (e.g. CIVs).[232]In fact, the addition of article 1(2) of the OECD Model (2017) and the extension of the principles of the Partnerships Report to other entities (e.g. trusts)[233]has eased the pressure on BO in the special case of transparent entities, as problems of access to tax treaties on the part of entities that are not subject to tax or fully exempt should not now be addressed with the BO concept but, rather, with articles 1 (mainly), 3 or 4 of the OECD Model.[234]As the Commentaries clearly indicate, the issue of "transparency" is completely different from BO. However, the fact that the former is to be resolved through other articles of the tax treaty does not preclude the application of BO by the source state.[235]With regard to CIVs, the Commentary on Article 1 of the OECD Model already gives indications along the lines of the controversial approach defended by the CIVs Report,[236]and here the problem is not BO but whether, for policy

229. *See*, for instance, the example Danon (2004), *supra* n. 1, at p. 347, uses of "grantor trusts" in the United States and Canada, in which income is attributed for tax purposes to the settlor even if the beneficiaries have a fixed right to receive the income on an arising basis. For other examples, *see* Wheeler (2007), *supra* n. 1, at pp. 56-57.
230. Avery Jones et al., *supra* n. 13, at p. 249.
231. For an argument in favour of considering non-taxable entities as residents for the purposes of art. 4(1) *OECD Model*, *see* M. Lang, *Taxation of Income in the Hands of Different Taxpayers from the Viewpoint of Tax Treaty Law*, 55 Bull. Intl. Fisc. Docn. 12, p. 597 (2001), Journal Articles & Papers IBFD. However, while defending the pre-eminence of the law of the state of residence under art. 4(1) *OECD Model*, Lang holds that arts. 6 to 22 should follow the attribution-of-income rules of the state of source – a position the present author does not share. *See* Danon (2004), *supra* n. 1, at p. 319 et seq., for a convincing criticism of Lang's opinion.
232. This is the approach to CIVs adopted by the *OECD Model: Commentary on Article 1* (2010-2017), following the *CIVs Report*, *supra* n. 47, especially at paras. 22 et seq. However, another solution is also explored in these Commentaries and in the *CIVs Report* (at para. 36 et seq.): if the CIV does not have access to a DTC, investors of the CIV residing in countries with a treaty with the source country should be able to claim its benefits. The same solution should apply to cases of BO (tax treaties to which BO is entitled should be applied).
233. Para. 4 *OECD Model: Commentary on Article 1* (2017).
234. This was the position this author defended before the addition of the new art. 1(2) *OECD Model* (2017): *see* Martín Jiménez, *supra* n. 1. The discussion of CIVs in the Commentaries on Article 1 of the OECD Model after 2010 are also helpful with regard to these specific vehicles.
235. Para. 13 *OECD Model: Commentary on Article 1* (2017) states the following: "Whilst the paragraph ensures that the various allocative rules of the Convention are applied to the extent that income of fiscally transparent entities is treated, under domestic law, as income of a resident of a Contracting State, the paragraph does not prejudge the issue of whether the recipient is the beneficial owner of the relevant income. Where, for example, a fiscally transparent partnership receives the dividends as an agent or nominee for a person who is not a partner, the fact that the dividend may be considered as income of a resident of a contracting State under the domestic law of that State will not preclude the State of source from considering that neither the partnership nor the partners are the beneficial owners of the dividend."
236. *See* sec. 2.2.6.2. for the criticism that this report extends BO status only to widely held CIVs.

reasons or reasons of “reciprocity”, (“transparent” or “exempt”) CIVs should have access to tax treaties.[237]It can even be said that the BEPS Action 2 Final Report,[238]with its rules for counteracting hybrid agreements and hybrid entities, has also reduced the need to apply the BO; and, unless this is acknowledged, a certain overlap may result between the defensive rules and the exclusion of access to articles 10-12 of the OECD Model.

- Another version of the problem arises when looking at (general or specific) anti-avoidance clauses in the state of residence: should the source state accept the application of treaty relief when, for instance, CFC clauses of a third state of residence produce the effect of attributing income to one of its residents, even if that item of income was paid to a third person resident of another state (to whom that income is attributed for tax and civil law purposes in that state)? The answer to this question is probably that the source state should look to what the state of residence of the recipient of income does, not to the effects of CFC rules of other countries. However, under the approach to the BO as the person to whom income is attributed under the laws of its state of residence, it is unclear whether the source state should apply the DTC with the state where the recipient of income is a resident, or the DTC with the state that attributes the income to one of its residents (the interpretation of “paid to” in the DTC between the state of the payor and that of the recipient of income will probably lead to the application of that DTC).[239]Something similar occurs if Pillar II of the OECD’s Unified Approach is adopted: the fact that one jurisdiction attracts income allocated to another jurisdiction should not affect the source country’s application of the tax treaty with the country of residence of the true legal owner.

As Wheeler has pointed out, it should be acknowledged that treaty entitlement is a completely different issue from attribution of income under domestic law. With regard to treaty access, it is not yet clear what the role of tax or civil law, or both, should be. It is also unclear, she adds, what the role of BO, if any, should be, in the search for general rules on treaty entitlement.[240]In the present author’s opinion, the BO concept should not be expected either to resolve all the conflicts of attribution of income and treaty access – articles 1, 3 and 4 are the best candidates here – or to create exceptions to the rule that it makes sense to grant treaty access where income may be subject to tax (even if not actually taxed) in the state of residence – special clauses should be used for this purpose – as long as the recipient of income is not an intermediary, such as an agent or nominee.
To a certain extent, the OECD Model has recognized this in the updates of 2010 (CIVs) and 2017 (transparent entities); but, surprisingly, this has had no meaningful effect in the drafting of the Commentaries on articles 10-12 of the OECD Model.
Originally, the purpose of BO was both modest and very basic: excluding from articles 10-12 of the OECD Model persons with access to DTCs whose (legal or factual) nexus with the income received was too weak. This should be a basic rule permeating all attribution-of-income articles in tax treaties: only those taxpayers with a real nexus with income should be allowed to invoke the benefits of those articles.

For these purposes, provided it is undisputed that the recipient of an item of income is entitled to treaty benefits, the pragmatic approach of the Canadian courts in *Prévost* of looking at whether income could (in legal and tax terms) be attributed to the Netherlands holding company should be applauded.[241]This approach of excluding BO only where there is absolutely no discretion to use the funds received, however, has been revealed as too formal, and may produce strange outcomes, as in *Velcro*. Therefore, a certain dose of flexibility should probably be added, so that in cases in which the recipient has minimal or very limited discretion, the recipient of an item of income would not be regarded as BO. Minimal or limited discretion should be defined using objective factors, which, rather than referring to conduit situations in general, should define cases in which the recipient has a similar function to that of an agent or nominee. Additionally, this approach has the advantage that the ghost of economic interpretation is definitively expelled from the body of BO, which may also help to reduce conflicts of attribution or, at least, will return the conflict in the application of the anti-abuse rules of the state of source to where it belongs, namely in the discussion about application of anti-avoidance rules in a treaty context and the standard permitted by article 29 of the OECD Model (2017) (and in the Commentary on Article 1 of the OECD Model).

Therefore, the historical evolution of the term BO, and of the relevant articles of the OECD Model and their Commentaries, seems to favour the attribution of income approach according to the laws of the state of residence, rather than the economic approach and the application of source state standards. The evolution of the OECD materials seems also to clearly separate the problem of BO from the issues connected with treaty entitlement.

237. *See* , for a similar idea, Meindl-Ringler, *supra* n. 1 , at pp. 356-357.
238. OECD/G20, *Neutralising the Effects of Hybrid Mismatch Arrangements – Action 2: 2015 Final Report* (OECD 2015), Primary Sources IBFD.
239. On conflicts of attribution from the perspective of the state of residence, *see* Wheeler (2005), *supra* n. 1 , at p. 485 et seq.; and Wheeler (2007), *supra* n. 1 , at p. 50 et seq.
240. Wheeler (2007), *supra* n. 1 , at p. 56.
241. After all, in a domestic context, few would dispute that, if the recipient of an item of income is not really entitled to it on account of its status (e.g. it lacks legal personality) or its contractual obligations (e.g. it is clear that he acts as a de facto or legal administrator), then that item of income should be included in the tax base of its real owner.

## 6.5. Should the BO concept be extended to other articles of the OECD Model? Should it be deleted?

In view of the problems the interpretation of BO presents, the answer to the first question in the title of this section should probably be “no”, and the reader may be tempted to respond promptly to the second one with a firm “yes” ( *see* section 3.6. ). Indeed, as explained in section 4. , the possibility of extending the BO ownership requirement to other articles of the UN Model (i.e. articles 21, 13.6, 22, 7 and 14)[242]or of adding an article on BO (even in the form of an alternative clause in the Commentary on Article 1) was considered in the UN context, but rejected.

In this author’s view, instead of extending the concept of BO, it would simplify matters to eliminate any reference to it in articles 10-12 of the OECD and UN Models. After all, the term adds very little to the words “paid to” in articles 10-12, and doubts about its interpretation are giving rise to uncertainty in the application of DTCs. This solution makes even more sense if it is taken into account that (i) tax administrations and courts in various countries tend to read a BO clause into treaties and treaty provisions even where no reference is made to that term: if, as this suggests, it is a fundamental principle of internal or treaty law and is inherent in the interpretation and application of DTCs, there is no need to confine the principle to articles 10-12; and (ii) the interests of source countries are sufficiently protected following the addition of the new Commentary on Article 1 of the OECD Model (2003) or article 29 of the OECD Model (2017) : once the application of domestic or treaty based anti-abuse clauses in the form of a PPT or anti-conduit regulations is permitted in a treaty context, there is no need to bring them into a tax treaty through the BO concept.

However, elimination of BO from the international tax landscape may not be completely desirable. Interpreted as an attribution of income rule from the residence state perspective, which denies tax treaty access to agents, nominees or persons playing an analogous role and having no real dominion over the income received, it is a truly fundamental principle that should find some recognition in international materials. It would probably be enough to mention in the Commentary on Article 1 of the OECD (or UN) Model that, as a matter of principle, a “special nexus” in tax terms is required between the person having access to a tax treaty and the income received (an independent treaty provision on “nexus”/attribution of income may also help clarify this issue). Therefore, elimination of BO in articles 10-12 of the OECD Model would avoid maximizing the effects of article 29 of the OECD Model (and domestic GAARs), and would prevent the concept from being used as a handy substitute to bypass or avoid the usual problems encountered when applying a GAAR or the “international standard of prohibition of abuse” represented by article 29. In the end, the original meaning of BO represents a truly fundamental principle in domestic and tax treaty law, and one that deserves recognition: income should only be attributed to its true legal owner, and double taxation should be avoided only for the true owner of the income for tax purposes.[243]

## 6.6. BO and withholding agents

### 6.6.1. BO and withholding agents in general

Some of the administrative positions (e.g. that of Russia: *see* section 5.10. ) and judgments (e.g. the Spanish *Real Madrid* and *Colgate* cases: *see* section 5.7.2.2. ) discussed in this chapter touch upon an important administrative issue connected with BO . If the source country decides that the person receiving dividends, interest or royalties is not the BO, can the source country collect the increased withholding tax rates (as compared to those in the DTC that are deemed not applicable) from the withholding agent, or even apply penalties to withholding agents if, in a tax audit, it is eventually found that the recipient of an item of income is not the BO? The administrative positions and judgments that consider this issue make the withholding agent liable for the taxes not withheld because the tax treaty was unduly applied. Penalties may also be applicable to the withholding agent.

This poses problems. If BO is interpreted broadly, a defence file may need to be compiled by the withholding agent before making the payment ( *see* , for instance, the position of the Russian tax administration, in section 5.10. ). Even if the defence file is not required by law, it may be convenient for the withholding agent to have it in order to avoid any potential liability (issues of distribution of burden of proof are also truly crucial: *see* the Danish cases of the ECJ, in section 5.9. ). If, on the other hand, BO is interpreted as an attribution of income rule according to the state of residence, proof of attribution of income to the recipient in the state of residence may also be required by the withholding agent to the BO. This would also mean that a defence file may be needed, regardless of the broad or narrow interpretation of BO, to show that income has been attributed in the state of residence to its recipient.

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242. Some cases in Spain and Italy ( *see* secs. 5.7.3. and 5. 10 respectively) have considered the problem of BO from the perspective of the equivalent to art. 23 *OECD Model* .

243. A similar view is held by Meindl-Ringler, *supra* n. 1 , at p. 383: “[e]ven if one understood beneficial ownership to be implicit in tax treaties, this would not make the concept superfluous. Rather, it would have to be fulfilled even if not explicitly mentioned” [footnotes omitted].

Second, if countries apply different standards of diligence/negligence and documentation in making the withholding agent liable for the unpaid withholding taxes if the recipient turns out not to be the BO, this may hinder the smooth application of tax treaties. In many cases, if the standard of diligence (and documentation) required of the withholding agent is too high, they may opt for withholding under domestic legislation and transfer the problem of obtaining refunds and applying the tax treaty to the BO. It is obvious in this regard that the fact that the withholding agent is in possession of a certificate of residence in the other country of the recipient of income does not prove much about BO and the conditions under which the recipient receives income from the withholding agent. Some countries issue certificates of BO, but these may not be very reliable or useful from the source country perspective (e.g. if the source country does not pay attention to the definition of BO in the state of residence). Some countries (e.g. Russia) require that a letter of confirmation from the recipient of income is provided to the withholding agent. Such self-declarations may have a deterrent effect. Certificates can also be requested from auditors.[244]

But different requirements in terms of documentation or standard of diligence for the withholding agent may hinder the smooth application of tax treaties, especially in the absence of a certain degree of harmonization or standardization. In this respect, some action should be taken to make sure that articles 10-12 of the OECD Model are correctly applied, without too many administrative burdens or obstacles (so far the only experience reported is in the context of the TRACE project, as discussed in section 6.6.2. ).[245]Some common guidelines of general application on these administrative issues (tax liability, standard of due diligence by the withholding agent when assessing BO, consequences in the case of incorrect assessment, etc.) should be provided by the OECD (or the UN).

The administrative issues relevant for BO are not very different from those arising in the application of article 29 of the OECD Model, regardless of whether BO is interpreted broadly or more narrowly. If this administrative aspect is taken into account, it would be easier to discard one of the common problems of treating BO as equivalent to an attribution of income rule by the state of residence: the application of BO as such or as a broad anti-abuse rule requires a specific standard of diligence on the part of the withholding agent in the state of source that is probably easier to meet if BO is interpreted narrowly than if interpreted broadly. In the latter case (broad interpretation of BO), withholding agents should have not only documentation proving that income is legally attributable to the resident of the other state for tax purposes in that state, but also evidence excluding that the income can be economically allocated to another party and showing that the recipient is not a conduit in the broad sense.

Likewise, these administrative aspects prove that, once tax treaties incorporate a specific anti-abuse standard, i.e. the PPT , it does not make much sense to differentiate between BO and the application of the PPT in terms of the documentation to be kept by the withholding agent. This is an additional argument in favour of eliminating BO from the tax treaty landscape, so as to avoid unnecessary duplication in administrative requirements (e.g. a self certification or certificate by auditors of BO plus a defence file in connection with the application of the PPT, showing that the recipient of the income is not only the legal but also the ultimate economic owner of the income).

The considerations in this section are only useful for relatively static and non-massive relations (e.g. between a holding company and its subsidiaries, or the case of a licence or loan from the parent company to a subsidiary or between two subsidiaries), but requirements for self-certification, certificates of residence and BO or certificates from auditors become largely impractical if there are a great number of investors and relations between payments of dividends or interest. It should also be explored what happens in these cases and if some of the experience acquired by the OECD through TRACE could be extended more generally.

## 6.6.2. BO and financial intermediaries (the TRACE project)

The issue dealt with in section 6.6.1. is directly connected with the OECD's work in the ICG Report on access to DTC relief for investors operating through (professional) intermediaries.[246]The ICG Report is aimed at facilitating treaty access to (mainly) portfolio investors who use professional intermediaries. It does not, however, deal in any great detail with the crucial issue of BO , even where it touches upon the liability of intermediaries for under-reporting of withholding taxes in the source state.[247]Despite its conclusions that "much work needs to be done" before "a sufficiently reliable, practical solution to the problem of collection of underwithholding" is found (paragraph 109), it suggests that the liability of the withholding agent or intermediary should depend on "industry standards", "good faith" and "reason to know" rules with respect to the specific function the intermediary performs (e.g. the liability of an intermediary in direct contact with the client cannot be the same as

244. These certificates do not replace the need of the tax administration to confirm the facts and, for these purposes, possessing information regarding the taxpayer identification numbers (TINs) used by the company in the state of residence will alert the recipient company that exchange of information procedures may be activated. *See* J. Wheeler, *Persons Qualifying for Treaty Benefits* , in *UN Handbook on Selected Issues in Administration of Tax Treaties* pp. 82 and 88 (A. Trepelkov, H. Tonino & D. Halka eds., UN 2013).
245. On the problems of certificates of residence and BO, *see ICG Report* , *supra* n. 50 , at para. 29 et seq.
246. Id.
247. Id., at para. 101 et seq.

that of an intermediary that relies on the information provided by the last intermediary in the chain) (paragraph 110 et seq.). The statements on liability refer to chains of intermediaries in the financial markets, in which there are different layers of intermediaries between the intermediary in direct contact with the client and that dealing with the payer of the income. In this context, it is affirmed that the liability of each intermediary in the chain should be assessed by standards of "good faith" and "reason to know" rules. The idea is to eliminate the need for each intermediary to provide certificates of residence and/or BO and move them down the chain of intermediaries. They should be replaced by self certifications with taxpayer identification numbers (TINs) signed by the final owner of the income and complemented by the "good faith"/"reason to know" standard. In this context, the intermediary in the chain closest to the payer should report to the source state the details of the BO, so that the source state can check all the information and, if needed, exchange information with the state of residence of the BO.[248]

An intermediary wanting to claim benefits on a pooled basis must provide the source state investor with specific information regarding the BO, details of the income received on behalf of such BO, names and addresses of the BOs and, if the investor country has TINs, that TIN or such other information the residence country uses to identify individual taxpayers.[249]

In such a system, a "strict liability" standard for under-withholding is not the rule that triggers the liability of intermediaries if the ultimate owner of the income (interest, dividends) does not have any right to apply the relevant DTC.[250]A minimum standard of diligence would apply instead. Moreover, in this context, the penalty should not always be, although it may include, the payment of the tax under-withheld (it can be even more severe – e.g. withdrawal of the licence to operate in a country could also be an effective sanction in relevant cases – or less severe, depending on the behaviour of the intermediary).[251]

If the whole system is to work smoothly, a financial intermediary in direct contact with the client and the source country should know what BO means, how it should be established and according to the laws of which state.[252]In this regard, however, the TRACE project and its Implementation Package has opted for a broader definition of BO than is found in articles 10-12 of the OECD Model in its self-certification, requiring it to state that the investor is not acting as an "agent, nominee or conduit".[253]The term BO, however, is defined in an ambiguous manner for these purposes, as explained in section 2.6.2, without opting for the source or residence country legislation and without recognizing that countries' legislation may vary on the meaning of this term.

The idea of not always imposing a strict liability standard on withholding agents and using self-certifications with TINs of the state of residence may also deserve more general consideration, for application outside of portfolio investments in financial markets. This would help to mitigate uncertainty for the withholding agent and facilitate the harmonization of the documentation standards they are required to meet.

## 6.6.3. Conclusions on administrative aspects of BO

A non-uniform definition of BO adds a layer of complication to the application of tax treaties, as the withholding agent may be tempted to withhold with domestic tax treaty rates and leave all the burden and difficulties of applying this requirement to the taxpayer. Some work may be needed in this respect. First, the idea of self-certification and establishing a clear standard of diligence for the withholding agent can be a helpful starting point in defining the documentation that the BO should gather in order to avoid any liability. The TRACE project already has ideas that may be generalized to all withholding agents (self-certifications with TINs or the equivalents, and reducing the number of cases where the withholding agent will be held strictly liable for under-withholding). Second, if communication between the withholding agent and the taxpayer is taken into account and regulated, the position that BO should be defined according to the laws of the state of residence is easier to apply and reduces the problems the withholding agent may encounter. Third, the addition of the PPT to tax treaties makes the BO requirement redundant from an administrative perspective: the withholding agent should be sure not only that income paid should be attributed to the taxpayer from the legal perspective of the residence state, but also that the same conclusion is valid economically. This means that, in order to exclude any liability, it would be good practice for the withholding agent to gather information not only on BO and legal attribution from the perspective of the state of residence, but also on economic ownership of the income paid to the immediate recipient.

248. *See also* in this respect the "outline of the streamlined system" for claiming reduced withholding taxes in *TRACE Implementation Package* , *supra* n. 51 .
249. The system is supplemented by an exchange of information limb, the intermediary will report the information to the source country, this will exchange it automatically with the residence country of the BO and the latter will report the source country if the person is not resident in its territory.
250. On the different systems, *see TRACE Implementation Package* , *supra* n. 51 , at pp. 8-9.
251. On the procedures to be established to correctly apply the tax treaties in these cases of portfolio investment through intermediaries, *see ICG Report* , *supra* n. 50 , at paras. 135-136.
252. Id., at paras. 142-144, recommends that (i) beneficial ownership be established on the basis of self-declarations by the "clients" in a standardized format that would be accepted by all or a large number of source countries; and (ii) certificates issued by the residence country of the investor should not address questions of treaty qualification (such as BO). Models for self-certifications and certificates can be found in the TRACE Implementation Package.
253. *TRACE Implementation Package* , *supra* n. 51 , at p.47.

# 7. Conclusions on BO: The Way Ahead

At this point, it should be clear that BO has been an unfortunate episode of international tax law since its introduction into the OECD Model, and its evolution has been a sucession of mistakes and misunderstandings that have caused unnecessary uncertainty and confusion. This is mainly due to the erratic position of the OECD over the years on BO and the interaction of domestic anti-abuse clauses with tax treaties ( *see* sections 2.2. and 2.3. on this issue, with special reference to the 1977, 2003 and 2014 changes). The use of BO in other areas of tax law (i.e. exchange of information, registries of BOs) with a different meaning is also unhelpful.

National tax administrations have taken advantage of this evolution and used the BO concept as a handy replament for the more difficult to apply GAARs (or equivalent rules), to the point that it is challenging to reconcile the position of many countries with the OECD's attempt to narrow down the expanded 2003 concept of BO in the Commentaries to articles 10-12 of the OECD Model (2014-2017). The BEPS outputs and the further evolution of the OECD Model and the MLI in adopting these outputs have added a further element of confusion.

As a broad understanding of BO seems prevalent in domestic tax systems and has received the powerful support of the Danish cases of the ECJ, the influence of the Commentaries on articles 10-12 of the OECD Model (2014-2017) has been diminished, and they risk becoming irrelevant. Now that the OECD Model (2017) and the MLI have an anti-abuse standard, the legal certainty principle would probably recommend deleting BO from articles 10-12 of the OECD Model, although this should not mean that the fundamental principle originally represented by BO (that income should be attributed to its real and true legal owner) should disappear. This should be recognized in the Commentary on Article 1 of the OECD Model as a fundamental principle of treaty interpretation and application, or in a specific multilateral interpretative agreement (which would not be difficult to implement). In view of the current international tax scene, a review of the status and meaning of BO would be an excellent item to add to the agenda of the OECD's project on tax certainty.[254]Some further work on the position of withholding agents could complement this project or, at least, be a second best if there is no appetite for deleting BO from the wording of articles 10-12 of the OECD MC or reducing its unduly enlarged scope.

# 8. Relationship to Other Chapters

## 8.1. Express provisions: Articles 10, 11 and 12 of the OECD and UN Models

As mentioned repeatedly in this chapter, the concept of BO is used only in articles 10, 11 and 12 of the OECD and UN Models. Sections of the respective chapters on article 10, 11 and 12 of the Global Tax Treaty Commentaries expressly refer to this term: *see* Article 10: Dividends – Global Tax Treaty Commentaries sections 3.1.3.1. and 3.2.4.3.1.; Article 11: Interest – Global Tax Treaty Commentaries section 3.2.3.3.; and Article 12: Royalties (OECD and UN Models) and Article 12A: Technical Services (UN Model (2017)) – Global Tax Treaty Commentaries sections 2.1.1.2.3., 3.1.2.4. and 3.2.2.1.3.; but note that all of them leave the development of the meaning to this metachapter.

## 8.2 Metachapters

The metachapter Treaty Interpretation – Global Tax Treaty Commentaries section 5.1.2.4.2.2. refers to BO, expressly defending the position that the term should be commonly understood in both contracting states.

254. On the origins and status of this project, *see* IMF/OECD, *2019 Progress Report on Tax Certainty* (IMF/OECD 2019) available at https://www.oecd.org/tax/tax-policy/imf-oecd-2019-progress-report-on-tax-certainty.pdf (last accessed 1 July 2020).