
5/20/2015

Draft provisions address stateless income, corporate inversions and limitation on benefits

WASHINGTON - Today, the Treasury Department released for public comment draft updates to the U.S. Model Income Tax Convention (the "U.S. Model") — the baseline text used by the Treasury Department when it negotiates tax treaties. The revisions to the U.S. Model text are intended to ensure that the United States is able to maintain the balance of benefits negotiated under its treaty network as the tax laws of our treaty partners change over time, and to deny treaty benefits to companies that change their tax residence in an inversion transaction. The U.S. Model was last updated in 2006.

"The draft provisions we are releasing for comment today reflect the fact that the tax regimes of our treaty partners are more likely to change over time than they have in the past, and that they sometimes change in ways that encourage base erosion and profit shifting or BEPS, by multinational firms. Treaties exist to eliminate double taxation, not to create opportunities for BEPS, and today's updates fully take account of the new international tax environment. The draft provisions also articulate steps that would help prevent our treaty network from encouraging inversion transactions," said Deputy Assistant Secretary for International Tax Affairs Robert B. Stack.

One set of draft provisions address issues arising from so-called "special tax regimes," which provide very low rates of taxation in certain countries in particular to mobile income, such as royalties and interest. This is income that taxpayers can easily shift around the globe through deductible payments that can erode the U.S. tax base. Consistent with the G20/OECD BEPS Project, the proposals are intended to avoid instances of "stateless income" or double non-taxation, whereby a taxpayer uses provisions in the tax treaty, combined with special tax regimes, to pay no or very low tax in the treaty partner countries.

The second set of draft provisions is intended to reduce the tax benefits from a corporate inversion by imposing full withholding taxes on key payments such as dividends and base stripping payments, including interest and royalties, made by U.S. companies that are "expatriated entities" as defined under the Internal Revenue Code.

Finally, and also part of the effort to eliminate BEPS, the proposal makes revisions intended to prevent residents of third-countries from inappropriately obtaining the benefits of a bilateral tax treaty. These include more robust rules on the availability of treaty benefits for income that is not subject to tax by a treaty partner because it is attributable to a permanent establishment located outside the country, and the ability of a company to make excessive base eroding payments.

Recognizing that multinationals often have global operations dispersed through many subsidiaries around the globe, the U.S. model for the first time contains a so-called "derivative benefits" rule. This taxpayer-favorable rule is an additional method of qualifying for treaty benefits based on a broader concept of ownership that includes certain third-country ownership.

While not among the draft treaty provisions that are being released today, the Treasury Department intends to include in the next U.S. Model a new Article to resolve disputes between tax authorities through mandatory binding arbitration.

The Treasury Department invites comments on the proposed treaty rules. Comments received will be taken into account as the Treasury Department works to finalize its revisions.

View the draft provisions here.

###