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To: Tax Treaties, Transfer Pricing and Financial Transactions Division
OECD/CTPA

Re: **Comments on revised proposals concerning the meaning of "beneficial owner" in Articles 10, 11 and 12 of the OECD Model Tax Convention.**

Dear Sirs,

We highly appreciate an opportunity to provide comments to the revised proposals concerning the meaning of "beneficial owner" in Articles 10, 11 and 12 of the OECD Model Tax Convention. Below we provide our comments on the matter.

Some of our comments may seem to cover more than the drafting issues. However, we believe that all suggestions indicated in our comments below are within the meaning of the "beneficial owner" as it was highlighted in the revised proposals. In our opinion, all suggestions below are aimed purely on rectification of the meaning of the term "beneficial owner" to be assigned to it in the Commentary to the OECD Model Tax Convention and in no way challenge the substance of the term preliminary agreed by the Working Party.

We consider the results of the Working Party's efforts in preparation of the position on the meaning of "beneficial owner" to be balanced and well-grounded. However, in our opinion it is vital to bring more clarity to the meaning of the term as it is described in the Commentary in order to avoid contradictions and discrepancies in application of the term in various states. In particular, we believe that the revised proposals should be amended as described below.

Paragraph 12.1

We agree with the notion of paragraph 12.1 that the term "beneficial owner" should have an autonomous meaning with possible degree of applicability of the term's domestic meaning. It is especially the case for the countries with well-developed case-law on the matter, being in line with the object and purpose of the Model Convention and its requirements. We also agree with the current conclusions of the Working Party that the last sentence of paragraph 12.1 may be potentially confusing and should be deleted.

However, the mere deletion of the sentence will not bring sufficient clarity to the issue of applicability of the domestic meaning of the term "beneficial owner".

The applicability of the domestic meaning of the term "beneficial owner" could be an issue where the domestic meaning is formal or technical (or in any other way contradicts the object and purpose of the Convention). Considering the importance of the understanding of the term for proper application of Articles 10 through 12, we suggest that a special reservation should be made in order to exclude applicability of the technical domestic meaning by explicit statement. As a result, we suggest the following wording:

Revised proposal	Suggested wording
12.1 Since the term "beneficial owner" was added to address potential difficulties arising from the use of the words "paid to … a resident" in paragraph 1, it was intended to be interpreted in this context and not to refer to any technical meaning that it could have had under the domestic law of a specific country (in fact, when it was added to the paragraph, the term did not have a precise meaning in the law of many countries). The term "beneficial owner" is ***therefore*** not used in a narrow technical sense ***(such as the meaning that it has under the trust law of many common law countries[1])***, rather, it 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. ***~~This does not mean, however, that the domestic law meaning of "beneficial owner" is automatically irrelevant for the interpretation of that term in the context of the Article: that domestic law meaning is applicable to the extent that it is consistent with the general guidance included in this Commentary.~~***	***12.1 Since the term "beneficial owner" was added to address potential difficulties arising from the use of the words "paid to … a resident" in paragraph 1, it was intended to be interpreted in this context and not to refer to any technical meaning that it could have had under the domestic law of a specific country (in fact, when it was added to the paragraph, the term did not have a precise meaning in the law of many countries).*** The term "beneficial owner" is ***therefore*** not used in a narrow technical sense ***(such as the meaning that it has under the trust law of many common law countries[1])***, rather, it 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. ***~~This does not mean, however, that the domestic law meaning of "beneficial owner" is automatically irrelevant for the interpretation of that term in the context of the Article: that domestic law meaning is applicable to the extent that it is consistent with the general guidance included in this Commentary.~~ In any event, the domestic law meaning of "beneficial owner" should not apply if such meaning of the term has a narrow technical sense, is based exclusively on formal criteria or in other way undermines or contradicts the object and purpose of the Convention.***

Paragraph 12.4

In our opinion, the issues raised in the paragraph require more detailed elaboration. Especially it concerns potential application of the "beneficial owner" concept with respect to the hybrid financing instruments, obligations to make payments other than the kind of payment received etc. In our opinion, a number of the issues raised by the commentators and highlighted in the discussion draft, need to be separately addressed in the Commentary.

We are also of opinion that special regard should be made in the text of the paragraph to the following:

1) A person should qualify as the beneficial owner if at least one of the following criteria is met: 1) it has powers to dispose of the assets generating income; or 2) it is entitled to decide the future of the income received.

2) Although the legal title to an asset should be considered to determine the beneficial owner of income thereon, it should not be decisive in this respect. It means that a usufructuary also could be a beneficial owner of the income, if it has the capacity to dispose of its usufruct, or is free to decide the future use of income.

3) Special regard should be made in the text of the paragraph to the anti-avoidance nature of the concept. It was outlined by the Working Party that the beneficial owner is an anti-abuse provision and not a mere attribution rule. In such a case, it should be aimed at targeting tax-driven structures not having a proper business purpose. It means that the Commentary should

clarify that the taxpayer should have the right to prove the valid business purpose of its arrangement thus being recognised a beneficial owner of the income.

4) Additionally, considering the anti-abuse character of the concept, it should be further clarified that the special purpose vehicles used in various finance transactions could be eligible to beneficial owner's status. This position is supported at least by two following arguments:

   a. The terms of the Convention should be interpreted in the light of its object and purpose. The Convention is aimed at promotion of international trade and movement of capital. Access to international financial markets forms an integral part of cross-border trade nowadays. However, due to various legal and regulatory reasons, it is either not feasible or impossible for borrowers in certain states to get a direct access to the foreign capital markets. Therefore, establishment of SPVs for access to capital markets facilitates the object and purpose of the Convention. It is clear for us, that no provision of the Convention could be aimed at targeting an arrangement facilitating object and purpose of the Convention. Such an operation of the paragraph would undermine the object of the Convention by denying or reducing access of taxpayers to capital markets in third states.

   b. The beneficial ownership concept is aimed at prevention of fiscal evasion through the treaty shopping. It is widely recognised that an arrangement should not constitute a treaty shopping, if it has a sound commercial reason behind it. This is the case for the SPVs established for access to the capital markets.

   Considering the above, for the purposes of companies' access to foreign capital markets the paragraph should be clarified as follows: **"A fiduciary or administrator of income may be considered the beneficial owner of such income provided that there is a sound commercial reason for establishment of such entity. For example, entities established for public issuance of securities traded on recognised stock exchanges could be beneficial owners of income provided that their establishment was required for access to the stock exchange either for legal or regulatory considerations (and not merely for tax economy purposes)".**

   For the same reasons we believe, that it is vital to exclude corporate entities with business substance, bearing legal and economic risks and earning an arm's length remuneration from the application of the beneficial ownership clause.

Paragraph 12.5

The current wording of the paragraph can be misleading in application of the beneficial ownership concept to conduit companies. The wording of the paragraph may be interpreted as to preclude the application of the beneficial ownership concept to the conduit companies, except for those who are not mere fiduciaries or administrators. However, such operation is not in line with the notion of the working party to establish independence of the beneficial ownership and other anti-abuse concepts. If the respective paragraph is interpreted as to preclude the applicability of the beneficial ownership concept to the conduit companies, it may lead either to an abuse of treaty benefits or to double taxation. The reasons for such a conclusion are as follows:

1) If, in example, an immediate recipient of the income is a conduit company which, at the same time, is not the beneficial owner of such income. It is possible that: (1) the DTT between the source state and the residency state does not contain anti-abuse provisions or anti-abuse wording in the preamble of the convention; and (2) the national legislation of the source state does not contain an anti-abuse provision or preclude application of such provision if it is not explicitly provided for in the tax treaty. In such case, exclusion of conduit companies from

application of the beneficial ownership concept will result in recognition of the conduit company as the beneficial owner and successful treaty shopping. Therefore, the paragraph should explicitly provide that the beneficial ownership concept still should apply to the conduit companies' cases.

2) In the same situation, if tax position of the beneficial owner of income is better than the tax position of the conduit company without entitlement to treaty benefit, it is clear from the Commentary that the tax treatment of the beneficial owner should apply to the payment. The situation, however, is not clear for the application of anti-abuse provisions, which means that, if the beneficial owner concept is not applied to the conduit company's income, it will be over-taxed compared to the tax treatment of the beneficial owner. Therefore, we suggest that the Commentary should also address the issue of applicability of beneficial owner's tax treatment if other anti-abuse provisions are applied to the conduit company. In our opinion, the tax treatment of the income in source state may not be worse for a conduit company than it is if the income is immediately received by the beneficial owner of the income.

We hope that comments above would be useful for the Working Party and that the Working Party will find it possible to implement the positions above into the draft proposals for the Commentary.

Faithfully yours,

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