

SUBMISSION



Submission on the

**Meaning of Beneficial Owner  
in Articles 10, 11 and 12 of  
the OECD Model Tax  
Convention**

15 December 2012

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Submitted online to [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

Tax Treaties, Transfer

**Re: Submission to the Committee on Fiscal Affairs of the OECD on the Revised Proposals Concerning the Meaning of Beneficial Owner in Articles 10, 11 and 12 of the OECD Model Tax Convention**

At this stage of the submission process the Committee is requesting comments on the Discussion Draft focusing on drafting issues rather than on matters of substance. The New Zealand Institute of Chartered Accountant's comments are, first, that they welcome the general approach taken by the OECD, but secondly, feel that the OECD need to focus further on the need to clarify two significant areas. These two areas have the potential for considerable uncertainty and tax associated risk (for revenue administration and taxpayers alike). Careful drafting will certainly assist in reducing the risk of confusion.

***What type of obligation to pass on payment to another constrains the recipient from beneficial ownership? What is a related payment?***

Under the revised proposal new paragraph 12.4 describes the requisite constraining contractual legal obligation to pass on a payment as a type of obligation which must be "related" to the payment received. An example of an unrelated obligation is given such as "those unrelated obligations that the recipient may have as a debtor or as a party to financial transactions" or those 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 to article 1.

With the greatest of respect, neither of these examples provide great insight into what constitutes a related or unrelated obligation. What criteria are used to establish that a payment passed on to a person is "related" to a receipt? The question of "related" may be determined, for example, by the relationship of association (this might be a direct legal connection such as that of a parent company to its subsidiary). Is an unrelated obligation one which is simply owed to an independent third party?

Another form of relationship is based on economic dependence (many transactions are structured so that economically a payment is reliant upon a receipt).<sup>1</sup> An independent third party could certainly have such an economic relationship.

Sometimes the relationship might be one of time (one could envisage an immediately contemporaneous legal obligation, that is a receipt immediately matched with an outgoing obligation or transactions that have an exact durational relationship).

Yet another example is that the relationship between a receipt and a resultant payment may be linked by

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<sup>1</sup> The transactions described in the English Court of Appeal decision, *Indofood International Finance Ltd v JP Morgan Chase Bank NA*, London Branch 8 ITLR 1, have some elements of these types of "related" relationships.

legal risk (so that security arrangements, guarantees and the like result in a high degree of inter-dependence between a receipt and payment).

Apart from the unrelated obligation that a person has as a debtor which is referred to above, the only other example given of "related" and "unrelated" obligations are those expressed as the typical distribution obligations of pension schemes and collective investment vehicles. The obligation of pension schemes and collective investment vehicles may differ widely according to the legal form of such vehicles (trusts or unit trusts governed by trust deed, superannuation funds, closed and open ended companies et cetera) and the jurisdiction concerned. Apart from establishing the fact that distributions from pension funds and collective investment vehicles are intended to outside the concept of a constraining legal obligation, this example is not helpful in clarifying the requisite relationship.

We would recommend giving other more helpful examples. The fact situation from a recent Swiss case *Re Swiss Swaps Case* involving a total return swap may be one such example. In this case, which the Committee will of course be aware, the Swiss Federal Administrative Tribunal considered transactions involving total return swaps over equities issued by Swiss companies with counterparties resident in France, Germany, the UK and the US.<sup>2</sup> The taxpayer, a Danish bank, was under an obligation to make a payment to the counterparty equal to the economic return on the underlying equities over the swap period. This was the product of movements in the market price and any dividends received on the underlying equities. The Danish bank, as a matter of practice, hedged its obligations under the swaps by acquiring the underlying equities using an international broker (and not the counterparty).

The court held that the taxpayer was in any event the beneficial owner of the dividend. This was because the obligation to pass on the income, either contractually, or by way of a de facto duty, was insufficiently binding under these swap arrangements. The critical factor was that the Danish bank still assumed responsibility for the economic return even if no dividend was paid.

Another example could involve a standard securitisation vehicle. What is the Committee's view on the packaging of contractual debt being sold as bonds, pass-through securities, or collateralised mortgage obligations to investors? While these are commonplace techniques for financiers to provide liquidity and reduce the cost of funds is not clear whether the beneficial owner(s) is the securitisation vehicle or the underlying investors.

In short we would recommend the Committee provide guidance on the type of relationship they are suggesting is sufficient to create a constraining legal or contractual obligation, be that one of legal association, economic dependency, temporal or risk related legal necessity. Drafting further examples, including one based on the fact situation in the *Re Swiss Swaps* case would be highly desirable.

### ***The relationship between beneficial ownership and treaty shopping***

The second and related point in the Committee's proposal, when assessing beneficial ownership under paragraph 12.4, is that the contractual or legal obligation to pass on the payment should be viewed through an anti-avoidance frame. The major test of beneficial ownership proposed by the OECD is one based on private law property rights constituting a legal relationship. Under the avoidance analysis the OECD suggest an examination of "facts and circumstances" and an "in substance" enquiry in order to establish whether

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<sup>2</sup> *Re Swiss Swaps Case* I/A 14 ITLR 638.

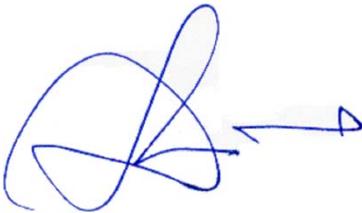
there is an obligation to pass on the payment received to another person. Our concern is that paragraphs 12.4 and 12.5 are contradictory.

The New Zealand Institute of Chartered Accountants endorses the approach of paragraph 12.5 which makes clear that beneficial ownership and treaty shopping are two separate enquiries. Treaty shopping, as paragraph 12.5 indicates, is best dealt with using specific anti-abuse provisions treaties, general anti-avoidance rules, substance-over-form, or an economic substance approach. Accordingly, there is a conceptual inconsistency in embedding an anti-avoidance focus in the approach of paragraph 12.4 which defines beneficial ownership, when it is made clear in paragraph 12.5 that the anti-avoidance rules will apply notwithstanding the beneficial ownership outcome.

We would recommend that the language concerning beneficial ownership remaining firmly fixed in defining legal property rights and not stray into the economic, or in substance, terminology frequently employed in anti-avoidance provisions. Our specific recommendation is to delete references to "facts and circumstances" and "in substance" in paragraph 12.4. It is made very clear in paragraph 12.5 that treaty shopping is not the province of beneficial ownership.

If you have any queries or require clarification of any matters in this submission, please contact Craig Elliffe (c.elliffe@auckland.ac.nz).

Yours sincerely

A handwritten signature in blue ink, consisting of several loops and a long horizontal stroke extending to the right.

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Chair, Tax Advisory Group

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