CHAPTER 6

BENEFICIAL OWNERSHIP:
INTERNATIONAL MEANING

6.1. INTRODUCTION

Following on Chapter 5, which investigated the domestic meaning of beneficial ownership, the current chapter investigates the international tax meaning of the term, which is the main focus of this study.

The chapter is structured in two parts. Part one analyses the current available information, such as decisions by the courts, opinions by commentators and governments, and information from the OECD on the international tax meaning of beneficial ownership. In part two, this study makes its own interpretation of the term.

Part one

6.2. STATUS QUO

For a term that is supposed to play such an important role in the allocation of treaty benefits and which is used in so many bilateral tax treaties, there are remarkably few court decisions on the international tax meaning of beneficial ownership.

The meaning thereof has been considered by the courts, though, and in addition various commentators and governments have provided their views. As the organization responsible for introducing the term into the wide\textsuperscript{325} international tax arena, any information from the OECD on its meaning is of major importance. A good starting point for the investigation in the current chapter is therefore to study the material from the aforementioned sources.

\textsuperscript{325} The word “wide” is used because, as is seen from the discussion in 6.3.2.2., beneficial ownership was used in certain tax treaties before its introduction into the OECD Model in 1977.
As is evident from this investigation, there has so far been no clear and unqualified answer to the question of the international tax meaning of beneficial ownership. There appears to be a consensus that the exact meaning that the term was intended to have on incorporation into the OECD Model has not been made clear at all, neither in the OECD Model nor in the MC Commentary. Neither could an unambiguous meaning so far been deduced from the context of the OECD Model as a whole. In addition, only a few actual bilateral treaties provide a definition of the term.

Importantly, when considering the interpretation by others, is to determine the sources they use for the meaning of beneficial ownership, as well as to determine their interpretation methodology. Of particular importance is to see whether the steps for interpretation of treaty terms as prescribed by the Vienna Convention were followed.

In the first section below the international opinions, not made from the perspective of a specific state, are considered. In the next sections the international meaning of the term, viewed from the perspective of specific states, is investigated. The states discussed below have not been selected for any particular reason. The analyses represent all the states on which any information on the international tax meaning of beneficial ownership could be found.

6.2.1. Global

The “beneficial owner” requirement was added when the text of the OECD Model was revised in 1977. Almost without exception, commentators mention the scarcity of information, either formally or informally, on the intended meaning of beneficial ownership. One also struggles to find any articles with in-depth discussions on the issue around the time of its introduction in 1977. One article which does refer to the amendments is that by Lukoff, who is probably one of the first to be somewhat unflattering as to the vagueness of the new terminology. He points out that the only explanation is the very

326. A discussion on the meaning of beneficial ownership at the 1998 IFA Congress in London confirmed the uncertainty and disagreement as to the meaning thereof. See supra note 8.
short comment concerning agents or nominees interposed between the beneficiary and the payer and then concludes that “the new treaty language in these articles, if adopted, could substantially vitiate the certainty of tax treatment that is one of the goals of tax treaty networks”.

The OECD provides the following information: paragraph 4 of the MC Commentary on Article 12, after the 1997 amendments, reads as follows:

Under paragraph 1, the exemption from 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.

The reference to agents or nominees, and questions such as whether it can be regarded as a complete definition of beneficial ownership, has been the topic of much debate and is further discussed in 6.3.2.9.1. It is important, though, also not to underestimate the importance of the last sentence of the above quotation. States which are not satisfied with the information provided in the OECD Model and MC Commentary on beneficial ownership are provided the opportunity to determine their own definition of the term.

In the OECD Conduit Companies Report, adopted by the OECD in 1986, there is the following elaboration on the meaning of beneficial ownership:

The Commentaries mention the case of a nominee or agent. The provisions would, 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).

328. At paragraph 14(b).
The reference to “narrow powers” is in line with the conclusion in Chapter 5 that the (domestic) meaning of beneficial ownership involves an investigation into the nature and extent of the rights held by the different parties.

According to Vogel, the purpose for introducing the beneficial owner requirement was to help prevent tax avoidance. Persons not entitled to protection by a particular treaty were to be prevented from obtaining its benefits with the help of interposed persons. He further mentions that, before agreeing on the beneficial ownership wording, the OECD considered making treaty benefits dependent on the payments being liable to tax in the state of residence, or to use the wording “final recipient”.

As far as his interpretation of the term is concerned, it is best to quote directly from Vogel:

Treaty benefits should not be granted with a view to a formal title to dividends, interest, or royalties, but to the “real” title. In other words, the old dispute of “form versus substance” should be decided in favour of “substance”...

The “substance” of the right to receive certain yields has a dual aspect. The first is the right to decide whether or not a yield should be realized – i.e., whether the capital or other assets should be used or made available for use – the second is the right to dispose of the yield. Ownership is merely formal, if the owner is fettered in regard to both aspects either in law or in fact. On the other hand, recourse to the treaty is justified – i.e., is not improper – if he who is entitled under the private law is free to wield at least one of the powers referred to. Hence, the “beneficial owner” is he who is free to decide (1) whether or not the capital or other assets should be used or made available for use by others or (2) on how the yields therefrom should be used or (3) both.

It appears that the issue of control is regarded by Vogel as the most important factor to determine beneficial ownership. But “control” on its own is seen as the important factor, which means that the control is not necessarily for the benefit of the person controlling. This is confirmed a few lines further by Vogel when he states that a

330. Id. at 562.
trustee with corresponding powers is also a beneficial owner. A
trustee, of course, does not exercise his powers for his own benefit,
but for the benefit of the beneficiaries. Vogel’s approach is con­
trary331 to the conclusion in Chapter 5 on the domestic meaning of
beneficial ownership, namely that only control for the benefit of the
person controlling constitutes beneficial ownership. In Sainsbury in
England (see 5.2.2.) it was held that the important issue is not
whether the taxpayer can cause the dividend to be declared, but
whether he will receive it if it is declared. In terms of this decision it
can be said that the benefit of receiving is more important than the
control over the decision to declare the dividend.

The important question is what happens under Vogel’s approach
when the control and benefit are in different persons. A trust is a
good example. Say, a trustee with total discretionary powers under a
trust, allocates the royalty to a beneficiary. Who of the trustee or the
beneficiary is then the beneficial owner?

Also Vogel’s splitting of powers (1) and (2) can be questioned.
What happens if his powers (1) and (2) are in different persons, for
example the right to decide on whether a licence can be granted and
the right to freely deal with the royalties. Who is then the beneficial
owner? This issue was discussed in detail in 4.7., namely whether
the investigation into beneficial ownership should focus only on
rights in respect of the actual payment, or whether the rights in
respect of licensing can or should also be considered. It was con­
cluded that the focus should be on the payment (Vogel’s test (2)).

Lastly, Vogel mentions that the fetters that exclude beneficial
ownership may be legal or merely factual. The case law discussed in
Chapter 5 (see, for example, the summary of English decisions in
5.2.4. See also 5.2.6.) shows that beneficial ownership is a question
of law.

The IBFD seems to equate the meaning of beneficial owner with
that of economic owner:

331. In terms of the hypothesis of this study, stated in 6.3.2.1., the meaning of be­
neficial ownership in the common law states should be taken as the starting point
for the interpretation of its international tax meaning.
The term “beneficial ownership” is used to indicate a situation where a person is really entitled to income which is actually received on his behalf by another person who may or may not be the owner in the formal, i.e. legal, sense and whose ownership may be qualified as fictitious.

In a treaty context, this principle operates such that the advantageous tax treatment of income under the treaty is only available if the recipient of the income is not just the “legal”, but also the “economic” or beneficial owner of the income.\(^{332}\)

The discussion in 5.6. of a Dutch Supreme Court decision has shown that it is not inappropriate to compare beneficial ownership with economic ownership.

Baker properly sums up the main issue surrounding the international meaning of beneficial ownership:

It remains open whether a company under the control of a resident of another Contracting State – and therefore likely (though not legally obliged) to pay to its ultimate owner any sums received – could be regarded as beneficial owner of the dividends it receives. That is, whether the beneficial owner requirements in articles 10, 11 and 12 exclude only agents, mere nominees and bare trustees or have a general function of excluding entities imposed for the sole purpose of enjoying treaty benefits not otherwise available to the recipient of the dividends, interest or royalties.\(^{333}\)

6.2.2. The Netherlands

The Netherlands is one state where the meaning of beneficial owner, or the Dutch translation thereof, uiteindelijk gerechtigde, has been considered in some detail by the court and commentators.

The Underminister of Finance was requested on a few occasions during the eighties to comment on the purpose and meaning of the

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332. “Further Attacks on Treaty Shopping”, *European Taxation* 1981/5-6, at 143.
term “beneficial ownership”. On the purpose of the term the Underminister responded as follows:

The use of this term has as its purpose to lay down in tax treaties the intention of the contracting parties that application of certain treaty provisions is not always warranted based on apparent circumstances, but that these provisions are only applicable if the taxpayer is the ultimate, i.e. the real, beneficiary of the income.

On the question of whether it would not be appropriate to provide for a more precise description of the term, because taxpayers would otherwise try to benefit from the facility by using back-to-back structures, the Underminister responded:

Back-to-back structures do not result in entitlement to treaty application. In that light it is not necessary to provide for a more precise description of the term “beneficial ownership”. Incidentally, in such cases, the factual circumstances of each individual case are of crucial importance, which makes it difficult to provide for more precise description.

On a further question as to whether the government believes it useful to further specify the term, inter alia, with a view to counter “treaty shopping”, the answer was:

[The meaning of] the term “beneficial owner” in international tax law is strongly determined by factual circumstances. It is therefore not possible to give further meaning to this term in a general manner. Recommendations in this area are therefore completely lacking in the OECD-model convention.

The Underminister also stated the following:

The Netherlands takes the viewpoint that a person cannot be considered the beneficial owner if he is, for example, contractually obliged to pay the largest part of the income to third parties.

The leading case on beneficial ownership is that by the Supreme Court (Hoge Raad) concerning dividends. There is no reason why the finding in this case should not apply to royalties as well.

334. All answers by the Underminister are quoted by Stef van Weeghel, The Improper Use of Tax Treaties, 1998, at 74-75.
The facts were that the taxpayer, a stockbroker resident in the United Kingdom, bought dividend coupons of Royal Dutch Oil shares. The stockbroker did not possess or acquire the underlying shares. At the time of the purchase, the dividends had been declared but not yet made payable. The stockbroker paid approximately 80% of the face value of the coupons. The dividend was paid to the stockbroker, subject to 25% withholding tax, the full statutory rate, which was withheld by the paying agent. Subsequently, the stockbroker filed for a refund of 10% of the gross dividend, based upon Article 10(2) of the 1980 Netherlands-United Kingdom tax treaty. Under Article 10(2) of the treaty, dividend withholding tax will only be refunded to the “beneficial owner” of the dividend. The tax inspector denied the refund and asserted that ownership of the shares was a prerequisite for refund of the withholding tax. The lower court, on appeal by the stockbroker, ruled that the taxpayer did not qualify as the beneficial owner of the dividends.

The Hoge Raad, whose decision, in typical civil law fashion, is very brief without many explanations, reversed the decision by the lower court, finding as follows:

The taxpayer became the owner of the dividend coupons as a result of purchase thereof. It can further be assumed that subsequent to the purchase the taxpayer could freely avail of those coupons and, subsequent to the cashing thereof, could freely avail of the distribution, and in cashing the coupons the taxpayer did not act as voluntary agent (zaakwaarnemer) or for the account of the principal (lasthebber). Under those circumstances the taxpayer is the beneficial owner of the dividend. The tax treaty does not contain the condition that the beneficial owner of the dividend must also be the owner of the shares and further it is irrelevant that the taxpayer purchased the coupons at the time the dividend had already been announced, because the question who is the beneficial owner must not be answered at the time the dividend is announced, but at the time the dividend is made payable.\footnote{336. Translation by Van Weeghel, supra note 334, at 76.}

In the opinion of this study the above case should be regarded as the most authoritative decision on the international tax meaning of beneficial owner to date. First, the court focused only on the issue to be decided, that is beneficial ownership, and did not apply any other
tests, such as whether the sole reason for the scheme was to obtain a tax benefit. Second, the court focused on the rights in respect of the coupons and payment to conclude that the taxpayer was the beneficial owner of the dividends because he could freely deal with both the coupons and payment. Third, the court confirmed that there is no need to be the owner of the underlying property. Fourth, the court ruled that beneficial ownership must be determined at the time when payment takes place. Fifth, the court supported its finding on beneficial ownership by stating that the taxpayer did not act as an agent.\footnote{337}

The decision by the \textit{Hoge Raad} is supported by the opinion of advocate-general Van Soest, which was provided as part of the court procedures. As part of the motivation for his opinion, Van Soest points out that the purchase price for the coupons were determined in an arm's length transaction and that the purchaser did carry the risks, such as currency and solvency, in respect of the coupons, although only for a short period.\footnote{338}

Van Brunschot concludes that anyone who, after purchasing the rights to dividend distributions, interest payments or royalties, can freely avail of those rights and the payments therefrom, is the beneficial owner of the payments for treaty purposes.\footnote{339}

The question as to what the position is if a person can avail freely of only one of the coupons, or the payments therefrom, remains unanswered. In practice, however, it is difficult to think of situations where these two rights are severed.

A last observation is that there can be little doubt that this whole transaction was motivated by tax reasons. Judging by the \textit{Hoge Raad} decision, the beneficial ownership test is therefore not a “for the main or sole reason to obtain a tax benefit” test. Sporken comments as follows on this issue:

\footnote{337. F.W. van Brunschot, whose commentary is attached to the case, comments (at 1 645), correctly in the view of this study, that the reference to zaakwaarnemer and lasthebber should not be seen as a separate test, because such persons by definition cannot freely deal with the payments.}
\footnote{338. \textit{Supra} note 335, at 1 635.}
\footnote{339. \textit{Supra} note 335, at 1 635.}
It should be borne in mind that in the above case, the Supreme Court held only in respect of the beneficial ownership test and left for another day the question of whether it would have granted the refund after a treaty-abuse test, since this issue was not brought up by the Netherlands Revenue. ... Both the above Supreme Court case law and other jurisprudence relating to tax treaties with Belgium ..., the United States ..., and Spain ..., demonstrate that the Supreme Court will not find anti-abuse if neither the tax treaty nor the explanatory notes given by the contracting states evidence that these contracting states shared an intention to disallow abuse.\textsuperscript{340}

The above case is often referred to by commentators when discussing conduit entities. Van Brunschot comments that the decision by the Hoge Raad negates the view of the Underminister (quoted above) that a person cannot be considered the beneficial owner if he is, for example, contractually obliged to pay the largest part of the income to third parties.\textsuperscript{341} This study deals with conduit entities in 6.3.2.10. At this stage, though, it can be observed that in this case (on the information available) there was no legal obligation on the stockbroker to pay on the distribution received to his creditor. This can therefore not be seen as a decision providing unqualified sanctioning for the use of conduit entities in situations where there is a legal obligation on the conduit entity to pay on the distributions received.

Lastly, a person often quoted in the Netherlands on the subject of beneficial ownership is Romyn, who concludes as follows:

In my opinion neither text nor the commentary of the OECD Model Convention allows leeway for applying the provision at issue [beneficial ownership] outside formal “agency” and “nominee” relationships.\textsuperscript{342} [translation – CdT]


\textsuperscript{341} \textit{Supra} note 335, at 1 635.

\textsuperscript{342} M. Romyn, “De uiteindelijk gerechtigde; Wie geniet inkomsten voor verdragsdoeleinden?”, in \textit{Van Dijck Bundel}, 1988, at 319.
6.2.3. United States

There appears to be no reported case law pertaining to the term “beneficial owner” in the treaty area in the United States.\(^{343}\)

At the 1998 IFA Congress in London,\(^{344}\) a United States member of the panel discussion on the meaning of beneficial ownership, said the following:

In principle a person should be considered a mere nominee or agent and thus not a beneficial owner from the treaty perspective if he has only title to property but no other economic, legal or practical attributes of ownership. To be a beneficial owner one must have the right to deal with the property or income at least to some extent as his own. This is often referred to as dominion and control over the property. In addition to dominion and control another important component of beneficial ownership, or what the Model apparently envisages as beneficial ownership, is some economic interest in the property. That is, some interest in the risks and rewards of its fluctuating value and, or the value of the income that it generates.

The views expressed above are in line with that on the domestic meaning of beneficial ownership, as discussed in Chapter 5.

In the Technical Explanation of the 1996 United States Model Convention, the following is said on the meaning of beneficial ownership of royalties in Article 12:

The “beneficial owner” of a royalty payment is understood generally to refer to any person resident in a Contracting State to whom that State attributes the payment for purposes of its tax.\(^{345}\)

The Technical Explanation also deals with beneficial ownership in its discussion of Article 22 of the United States Model Convention, dealing with limitation on benefits. It says the following:

\(^{343}\) Two cases often quoted in the context of beneficial ownership, namely *Aiken Industries, Inc. v. Commissioner*, 56 T.C. 925 (1971) and *SDI Netherlands B.V. v. Commissioner*, 107 T.C. 161 (1996), do not deal with beneficial ownership, but with the meaning of “received by” and the “cascading royalty” theory respectively.

\(^{344}\) See supra note 8.

\(^{345}\) Note the difference between this “definition” and that provided on Form 1001 – see 6.2.13.
Article 22 and the anti-abuse provisions of domestic law complement each other, as Article 22 effectively determines whether an entity has a sufficient nexus to the Contracting State to be treated as a resident for treaty purposes, while domestic anti-abuse provisions (e.g., business purpose, substance-over-form, step transaction or conduit principles) determine whether a particular transaction should be recast in accordance with its substance. Thus, internal law principles of the source State may be applied to identify the beneficial owner of an item of income, and Article 22 then will be applied to the beneficial owner to determine if that person is entitled to the benefits of the Convention with respect to such income.

The above statement should be seen against the background of the viewpoint in the United States that, based on Article 3(2) of the OECD Model, domestic law can be referred to in order to determine beneficial ownership. As is apparent from the discussion of Article 3(2) later in this study (see 6.3.1.), the United States do not have a lot of support from other OECD member states regarding this view.

Following from the above quotation, it is necessary to further consider the relationship between the notion of beneficial ownership and that of limitation on benefits. Many United States treaties contain a specific article on limitation on benefits.

In particular, the question to be answered is whether the limitation on benefits article should be regarded as a more detailed definition of beneficial ownership. In the opinion of this study the answer is no. The two notions are obviously related because they both deal with the restriction of treaty benefits. But, instead of being regarded a more detailed definition of beneficial ownership, the purpose of the limitation on benefits article should rather be seen as further narrowing down the type of residents and also, in the case of royalties, the types of beneficial owners, entitled to treaty relief. In respect of the United States-Netherlands treaty, for example, a Dutch resident company first has to show that it is the beneficial owner of a royalty in order to be considered for treaty benefits. In addition it then also has to pass any one of a number of objective tests in terms of the limitation on benefits article. These objective tests include stock

exchange listed company, ownership, base erosion and activity tests. If none of the objective tests is passed, the United States revenue authority may nevertheless agree to allow such benefits.

A last point is that the limitation on benefits article in the above treaty only limits the benefits in respect of companies and that it does not apply to individuals. For individuals the sole question, therefore, is whether they qualify as beneficial owners.

6.2.4. Canada

*MacMillan Bloedel Limited v. The Minister of National Revenue*[^347] dealt with beneficial ownership. Appellant, a public company in Canada, funded debt in the form of debentures. Some of the registered holders of the debentures were nominees with addresses in the United States. The appellant made no inquiry as to the beneficial ownership of the debentures and deducted withholding tax of 15% from the interest in terms of the Canada-United States bilateral tax treaty which, at the time, did not have a beneficial owner rule. In 1976 a press release was issued by the Department of National Revenue stating that appellant (and others) were expected to find out who the beneficial owners of its securities were. Tax at the non-treaty rate of 25% was to be deducted if the payee was a nominee or agent unless the payee or nominee indicated that the beneficial owner of the interest being paid was a resident of a country which had a tax treaty with Canada. The appellant disputed that, in the absence of statutory authority, he had any such obligation.

The court found for the appellant, holding as follows:

As I view this assessment, one can say that it can be upheld only if words are added to the Act and the *Canada-US Tax Convention* or section 10(4) of the *Income Tax Application Rules* so that it is clearly indicated that the reduced rate of tax is not given to the registered owner, but only to the registered owner if he establishes that the beneficial

What rules can be extracted from this case? The only requirement in terms of the relevant Canadian legislation and the treaty was that the payee must be a resident of the United States in order to qualify for the lower withholding rate. The court took a very literal approach to the interpretation of this wording and was not willing to read a beneficial ownership requirement into the treaty.

The decision also provides some support to those who argue that the only effect of incorporating beneficial ownership into the OECD Model is to exclude formal agents and nominees from claiming treaty benefits (see 6.3.2.9.1. for further discussion). The decision negates one of the counter arguments, namely that if the only reason was to exclude formal agents and nominees it would not have been necessary to bring in the beneficial ownership rule, because the residency status of agents and nominees, even without a beneficial ownership rule, cannot be taken into account when determining treaty benefits.

6.2.5. Switzerland

Although it does not deal with the meaning of beneficial ownership, it is relevant to refer to decisions by the Federal Tax Administration and the Federal Court in Switzerland. Both these decisions deal with Article 9(2) of the Switzerland-Netherlands treaty which provides that a full relief of the withholding tax on dividends shall only be granted if the relationship between the companies has not been arranged or is not maintained primarily with the intention of securing such full relief.

In both instances, Dutch intermediary companies were interposed between Swiss companies and foreign companies in order to make use of the treaty benefits on the payments of dividends. In both cases these refund benefits were denied because it was found that

348. Id. at 304.
350. Decision 9 November 1984, reported in European Taxation 1986/2, at 57.
the main reason for establishing the group structure was to make use of the treaty benefits.

The relevance of dealing with the above decisions is to show that treaty partners who want to focus on the reasons why entities are interposed as a basis for denying treaty benefits, can do so by incorporating explicit wording to that effect in the treaty. The Switzerland-Netherlands treaty does not contain a beneficial ownership requirement. Although the beneficial ownership requirement certainly has an anti-treaty abuse purpose (see 6.3.2.8.3.), an investigation into beneficial ownership should not be confused with an investigation as to the reasons why a certain entity was interposed.\footnote{351}

### 6.2.6. Germany

According to Killius, there is no case law in Germany on beneficial ownership, the concept of beneficial ownership is not backed-up by German domestic law, and it is doubtful how beneficial ownership will be interpreted in Germany because it does not appear to be a uniform concept.\footnote{352}

Germany is an example of a state that does provide a definition of beneficial ownership for some of its treaties. For example, paragraph 9 of the Protocol of the Germany-Italy treaty provides as follows:

The recipient of the dividends, interest and royalties is the beneficial owner within the meaning of Articles 10, 11 and 12 if he is entitled to the right upon which the payments are based and the income derived therefrom is attributable to him under the tax laws of both States.

There are also definitions for the treaties with the United States, Norway and Sweden, although the wording and effect of the definitions are not always the same. This last mentioned fact makes it difficult to apply one of these definitions to treaties which do not define the term.

\footnote{351. See also the comments on \textit{Frank Lyon}, \textit{supra} note 134, and the comments on the \textit{Royal Dutch Oil} dividends case, in 6.2.2.}

\footnote{352. Jürgen Killius, “The concept of ‘beneficial ownership’ of items of income under German tax treaties”, \textit{Intertax} 1989/8-9, at 343-344.}
6.2.7. Belgium

Hinnekens, after referring to Belgian authors who concluded that the notion of beneficial ownership generally excludes conduit companies from treaty benefits, comments as follows:

We disagree with such economic interpretation of the concept and believe that it is rightfully also not shared by the Belgian Administration. The OECD commentaries on this concept only refer to the case of a nominee or agent, i.e. a person who is not the beneficiary of the income in a true legal sense. And why then would recent treaties (e.g. the Protocol with the US) using the beneficial ownership term still introduce an anti-treaty abuse clause? The concept is a clarification of the treaty terms “interest received by” or “paid to a resident of the other State” and should be read to mean the “true beneficiary” as distinct from this nominee or other person who is not the recipient in a legal sense.

A CC [co-ordination centre], like any other Belgian resident receiving interest income in respect of its loans and deposits, satisfies the legal test in its own right, irrespective of whether such income is soon thereafter onward distributed as a dividend to a third country resident.353

Docclo agrees with the view that beneficial owner is interpreted as a legal concept, as opposed to an economic concept. She also refers to a case,354 not related to treaty interpretation, where a taxpayer involved in a back-to-back loan has alleged that it was not the beneficial owner of interest but a mere conduit, to avoid the Belgian withholding tax on interest. The Court of Appeals of Antwerp dismissed the argument.355

Questions such as the position of conduit entities with respect to beneficial ownership (see 6.3.2.10.), and whether the reference to agents and nominees in the MC Commentary can be seen as a conclusive definition of beneficial ownership (see 6.3.2.9.1.), are discussed later in this study.

The extent of the rights held in respect of the payments received by the co-ordination centre and the parties in the back-to-back loan agreement above, is not clear. It is not clear whether they were under a legal obligation to pay on the income received, and whether they carried any risk in respect of the receipts. If, however, it is suggested that mere legal title without any further ownership attributes can constitute beneficial ownership, it has to be noted that such a (formalistic) view is not in line with the discussion in Chapter 5. From the domestic law of all the states discussed it is clear that mere legal title without any other ownership attributes does not constitute beneficial ownership (see also 6.3.2.8.1.).

6.2.8. France

Hinnekens above, finds some good support on his views from neighbouring France. At the 1998 IFA Congress in London, the French member on the discussion panel concerning the meaning of beneficial ownership, said the following:

It is true that the Model Convention does not give an explicit definition of who is a beneficial owner. Nevertheless, the Commentaries annexed to the Convention do give a precise definition and only refer to the notion of commissionnaire, or of agent. ... French Courts will try to find a definition within the OECD Commentaries. This definition does not appear in the Model, but inside the Commentaries and I believe that it would be regarded as a valid definition for the interpretation of the Convention by our Courts. ... I believe that in reality we could consider this term as defined. ... I think that the concept of beneficial owner is a strict legal one and must be strictly interpreted, without any broader analysis in terms of abuse of law.

Le Gall, writing a few years earlier, calls the beneficial owner concept the pivot of the French plan of defence against treaty shopping. He continues that it is, however, far from being easily operative – no definition is provided in the treaties, the beneficial owner concept has not been interpreted under French law, tax authorities
have never construed it officially and no case law exists in that respect.\footnote{Jean-Pierre Le Gall and Sonia Reeb, “Treaty shopping: the French policy”, Interfax 1989/8-9, at 367.}

6.2.9. India

Tillinghast reports on a ruling made in December 1995 by the Advance Ruling Authority of India which, although binding only on the particular transaction and is not judicial precedent, creates uncertainty for investors in India. Because of the favourable India-Mauritius tax treaty, a large number of investments in India have been routed through Mauritius by United States and other investors. In this instance, the parent company in the United States (a major bank) formed two wholly owned subsidiaries resident in Mauritius. These companies, in turn, each acquired a 10% interest in an Indian company. In terms of the ruling it was held that the Mauritian companies were not entitled to claim the reduced treaty rate of withholding tax on dividends received from India, on the ground that the companies were not the beneficial owners of the dividends received. The essence of the reasoning by the Ruling Authority is that, since each Mauritian company was wholly owned and wholly funded by the parent company in the United States, it was the parent company rather than the Mauritian subsidiaries that was the beneficial owner of any dividend income.\footnote{David R. Tillinghast, “Ruling on Beneficial Ownership and Tax Residence Threatens U.S. Investments in India”, Tax Notes International 1996/8 July, at 79.}

Tillinghast concludes that although the meaning of beneficial ownership is the subject of some debate, he is not aware of any authority supporting the view that a company otherwise entitled to a reduced withholding rate on income under an applicable treaty article is not the beneficial owner of such income \textit{ipsi facto} because it is the subsidiary of a company resident in a third country.
6.2.10. Russia

Fort comments on the uncertainty as to the meaning of beneficial ownership in Russia’s bilateral tax treaties as well as the inconsistency in the way the notion is employed in different treaties. There is no explicit reference to the phrase “beneficial ownership” in Russian domestic tax law. The Russian wording commonly translated as “beneficial ownership of income” may more literally be translated as “the actual right to receive income”. The question therefore, Fort continues, is if the phrase “actual right to receive income” under Russian law is the same as is understood in English law by “beneficial ownership”?

He further points out that, bearing in mind the predominantly form-based approach of the Russian tax authorities, the primary contract documentation likely to be of value is that between lender and borrower without regard to any matching structures which may be put in place offshore.

In support of his conclusion that each treaty does need to be looked at separately, and different degrees of ownership of income may apply to different treaties, Fort provides the following examples. Under the treaty with Cyprus there is no explicit requirement that interest should be any more than “received” by the claimant. Under the treaty with the United States there is no explicit beneficial ownership test in the Russian text of the interest article, whereas the English version of the treaty includes a “beneficially owned” requirement. The treaty with Germany goes further than others in requiring the claimant to have “actual possession of the right of ownership of the income” or, in German, Nutzungsberechtigte. In the treaty with the United Kingdom the Russian equivalent of beneficial owner is that the claimant must have the “factual right” to the income.

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6.2.11. New Zealand

The only reference to beneficial ownership in any of the observations and reservations of the full text of the MC Commentary, comes from New Zealand. In an observation to Article 3 ("General Definitions") of the OECD Model, the following is stated:

For 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. 360

Provisions along the lines of the above observation have been incorporated in several of the bilateral tax treaties to which New Zealand is a partner. 361

As is rightly commented by Avery Jones, the above observation is not so much an explanation of the meaning of the term, but an extension of the treaty specifically to cover such a person because use of the words "treated as" indicate that he would not otherwise be the beneficial owner. 362

It is observed, though, that the way the issue is dealt with by New Zealand is some indication of the recognition that the tax treaty meaning of beneficial ownership is the same as the meaning thereof in the common law states. As is discussed in 5.2.7., a trustee is not a beneficial owner in terms of the domestic meaning of beneficial ownership – which explains why New Zealand has deemed it necessary to specifically extend the meaning of beneficial owner to include a trustee.

6.2.12. Translation into other languages

An investigation of the translation of beneficial ownership into other languages reveals one of the major reasons for the difference

360. MC Commentary on Article 3, at paragraph 14.
361. For example, the treaties with Belgium, Canada, Denmark, Fiji and the Republic of Korea.
In opinion amongst states. For various reasons beneficial ownership is often not translated literally into the language of the non English-speaking treaty partners. It is just natural that residents of the non English-speaking state will give preference to the term in their own language. Such meaning may not be the same as that of beneficial owner in the English language.

In the table below, twenty states were selected at random. The term used as equivalent for beneficial owner in treaties of each state is listed, and next to it, a literal translation of the term back to English.

<table>
<thead>
<tr>
<th>State</th>
<th>Equivalent of beneficial owner in foreign language</th>
<th>Direct English translation of foreign language term</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>Nutzungs berechtigter</td>
<td>Entitled to use</td>
</tr>
<tr>
<td>Austria</td>
<td>Nutzungs berechtigter</td>
<td>Entitled to use</td>
</tr>
<tr>
<td>Switzerland</td>
<td>Uiteindelijk gerechtigde</td>
<td>Ultimately entitled</td>
</tr>
<tr>
<td>Netherlands</td>
<td>Uiteindelijk gerechtigde</td>
<td>Ultimately entitled</td>
</tr>
<tr>
<td>Belgium (Dutch)</td>
<td>Vir eie voordeel besit</td>
<td>Possess for own benefit</td>
</tr>
<tr>
<td>South Africa</td>
<td>Beneficiario efectivo</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>France</td>
<td>L'effettivo beneficiario</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>Italy</td>
<td>Beneficiario efectivo</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>Spain</td>
<td>Beneficiario efectivo</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>Brazil</td>
<td>Beneficiario efectivo</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>Argentina</td>
<td>Beneficiario efectivo</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>Romania</td>
<td>Beneficiario efectif</td>
<td>Real beneficiary</td>
</tr>
<tr>
<td>Hungary</td>
<td>Haszonhuzoja</td>
<td>Benefit-drawing party</td>
</tr>
<tr>
<td>Sweden</td>
<td>Har rätt till</td>
<td>Has the right to</td>
</tr>
<tr>
<td>Norway</td>
<td>Rettaessige ejer</td>
<td>Rightfully/legally entitled</td>
</tr>
<tr>
<td>Denmark</td>
<td>Rettaessige ejer</td>
<td>Beneficial owner</td>
</tr>
<tr>
<td>India (Hindi)</td>
<td>*</td>
<td>Owner</td>
</tr>
<tr>
<td>Poland</td>
<td>Wlaściciel</td>
<td>Beneficial owner</td>
</tr>
<tr>
<td>Israel</td>
<td>Bealim She'Bayoshier</td>
<td>Beneficial owner</td>
</tr>
<tr>
<td>Japan</td>
<td>*</td>
<td>Beneficiary</td>
</tr>
</tbody>
</table>

* The terms are not reproduced in the original language.

363. The translation was done with the help of the multilingual tax staff at the IBFD.
A first observation is that, apart from Denmark, Poland, Israel and India, none of the terms refer to “owner”. One possible explanation is that most of the states listed belong to the civil law legal family and therefore probably do not have a notion similar to beneficial ownership and, in addition, may not recognize a division in ownership rights.\textsuperscript{364}

Killius explains that in the common Austria/Swiss/German translation of the OECD Model of 1977 the term “beneficial owner” was translated as *Nutzungsberechtigter* and not as *wirtschaftlicher Eigentümer* (economic owner) and that this was apparently done intentionally as Switzerland did know the term “economic owner” in its domestic tax law and as Germany did not want to use such term either in order to avoid the implication that the term “beneficial owner” should be interpreted in accordance with the attribution rules of German domestic law which use an “economic ownership” concept.\textsuperscript{365}

In spite of the wide range of different terminology evidenced by the above table, it can be observed that the general meaning expressed is fairly similar: most of them pointing in the direction of the real beneficiary or the person ultimately entitled. The difference in meanings may, however, show more clearly when the different terms have to be applied to a specific factual situation, such as a conduit company, for example.

In fact, the table is an illustration of the difficulties faced by those advocating a universal tax language meaning for a term such as beneficial ownership (see also 6.3.1. and 6.3.2.3.). It is very difficult to arrive at a common meaning if the term to be interpreted is different, depending on the language of the treaty partner.\textsuperscript{366} Commentators often mention that the existence of Article 3(2) of the

\textsuperscript{364} Of all the states in the table only India can be regarded as a common law state, whilst the legal systems in Israel, Japan and South Africa were also influenced by the common law to a more or lesser extent. See K. Zweigert and H. Kötz, *An Introduction to Comparative Law*, 1992, at 233-245 and 324; René David and John E.C. Brierley, *Major Legal Systems in the World Today*, 1985, at 25, 78 and 508-515.

\textsuperscript{365} Killius, *supra* note 352, at 340.

\textsuperscript{366} Article 33 of the Vienna Convention deals with the interpretation of treaties authenticated in two or more languages.
OECD Model is an obstacle to the development of an international tax language.\footnote{367 See, for example, Michael Edwardes-Ker, Tax Treaty Interpretation, loose-leaf, at 10.01.} This study submits that the problems caused by translation is another factor prohibiting the development of an international tax language. In fact, it is probably going just a bit too far to suggest that, in order to promote the development of an international tax language, it should be considered that terms falling into this category should not be translated at all but instead be used in all treaties in the original language from which the term was borrowed.

Importantly, also, is to note that the OECD Model is officially published in both English and French. In the French text the equivalent for beneficial owner is bénéficiaire effectif. Which language should be given preference when searching for a universal meaning?

The discussion in this section underlines the importance of establishing what the drafters had in mind (or the source that they took the notion from) when incorporating beneficial ownership and bénéficiaire effectif into the OECD Model, an issue that is investigated in Part two of this chapter.

6.2.13. Revenue forms

Often the procedures for claiming treaty relief in the form of lower withholding taxes, include the completion of forms issued by the revenue authorities of the source state. It is relevant to study these forms in order to see how the revenue authorities deal with beneficial ownership and whether they provide any definitions in this regard.

In the United States the procedure is that the person purporting to be the beneficial owner reports to a withholding agent both the ownership of the royalties and the reduced rate of tax or exemption from tax, by filing Form 1001 with the withholding agent. The withholding agent then acts in terms of this information when paying over the royalties. Form 1001 requests surprisingly little information. Among a few other things, the name and address of the person claiming to be the beneficial owner has to be provided. The form
also states the following: “The term ‘beneficial owner’ means the person ultimately entitled to control the income. A nominee or any other person acting in a similar capacity is not the beneficial owner.”

The fact that Form 1001 requires limited information becomes clear when it is realized that, apart from passing the beneficial ownership test, many United States treaties also require the taxpayer to pass a limitation on benefits test. In respect of the United States-Netherlands treaty, for example, a copy of Form IB 93 USA has to be filed with each of the Dutch and United States revenue authorities, as well as with the withholding agent, to demonstrate that the beneficial owner of the royalties in the Netherlands also satisfies the limitation on benefits test.

The royalties article in the tax treaties of the United Kingdom with Belgium, Italy, the United States, Australia and Norway, for example, all contain a beneficial ownership requirement. Resident companies in all these states (in the United States: domestic corporations) have to render forms to their local revenue authorities in respect of claiming relief from United Kingdom income tax on royalties. One copy of the forms has to be forwarded to the United Kingdom revenue authorities. The information requested by the forms differs slightly among different states. In general, however, information has to be provided on the place where the company is managed and controlled, whether it conducts any trade or business in the United Kingdom and information on the person by whom the royalties are paid. None of the forms make any reference to beneficial ownership. A responsible officer of the company must, however, declare that the company is beneficially entitled to the income. For Belgium, in the Dutch language version of the form, “beneficially entitled” is substituted by the Dutch equivalent of the term beneficial owner in the bilateral treaty, that is uiteindelijk gerechtigde.

368. The Supreme Court of Canada, in Jodrey, supra note 298, at paragraph 40, confirmed a finding by the lower court that “beneficially entitled” has a slightly different meaning than “beneficial owner”: “The person beneficially entitled to property may be further removed from the exercise of ultimate ownership of the property than the beneficial owner.”
The Netherlands do not levy withholding taxes on royalties. An investigation of the forms in respect of dividends, however, may provide insight into the Dutch view on beneficial ownership. The dividends article in the tax treaties of the Netherlands with the United Kingdom, United States and Sweden, for example, all contain a beneficial ownership requirement. Residents from these states have to prove their rights to treaty relief by filing Form IB 92. Full details have to be provided, not only of the dividends but also of the underlying securities. The applicant then has to certify that “by virtue of his title to the ownership of the securities ... he is beneficially entitled to the income”. The words “beneficial owner” are not used on the form, although the Dutch equivalent thereof, *uiteindelijk gerechtigd*, is used in the place of beneficially entitled in the Dutch version of the aforementioned quotation. In the form with Sweden, however, *uiteindelijk gerechtigd* is not used but only *gerechtigd*. In the Swedish version of the form, the Swedish equivalent of beneficial owner, that is *att ha rätt till*, is used. These words are more literally translated as “have a right to” or “are entitled to”. In respect of all the states the applicant further has to certify that he has not obtained the securities by virtue of any contract, option or arrangement under which he has agreed to resell or transfer the securities or similar securities. The forms lastly state that if the applicant cannot confirm all the statements (for example, if the applicant does not hold legal title to the shares) but nevertheless is of the opinion that he is entitled to a reduction of tax under the treaty, he should motivate his case.

In summary, based on the examples above, the forms are not very helpful in determining the meaning of beneficial ownership. Apart from the United States, no explanation of the meaning of the term is provided. It is also not clear why the United Kingdom and the Netherlands use beneficially entitled on the forms, when the treaties refer to beneficially owned. There is also inconsistency in the use of terminology on the forms with different states. Lastly, in spite of the decision in the *Royal Dutch Oil* dividends case (see 6.2.2.), the Netherlands still put a strong emphasis on legal title to the underlying securities, as opposed to beneficial ownership of the dividends only.
6.2.14. Conclusion

The discussion in Part one has confirmed the variety of different opinions on the meaning of beneficial ownership, ranging from commentators in the United States advocating an economic approach to those in Belgium and France supporting a legal approach. About the only point of consensus is that formal agents and nominees are not beneficial owners. There is, however, no consensus on who else, if anyone, is excluded.

It is regrettable that there are so few court decisions on the international meaning of the term. Decisions by courts in the common law states discussed in Chapter 5 would have been particularly helpful in order to see whether those states distinguish between an international and domestic meaning of beneficial ownership.

In Chapter 5 it was concluded that, in terms of the domestic meaning thereof, the identification of the beneficial owner involves an investigation into the ownership rights held by different persons. It is submitted that the decision in the Royal Dutch Oil dividends case in the Netherlands, and the views expressed in the OECD Conduit Companies Report support a similar approach regarding the international meaning of the term. Also, Vogel’s focus on “powers” relates to ownership rights.

A further comment is that the investigation above has revealed little evidence of commentators following the steps for treaty interpretation as prescribed by the Vienna Convention. To be more specific: in terms of the Vienna Convention the starting point of interpretation is the meaning of the wording. There is no evidence of a thorough analysis of the textual meaning of beneficial ownership.

Also notable are elements of domestic interpretation methodology and thinking in the views expressed by the commentators from certain states. This should be avoided when dealing with international tax language. As it was put by Sundgren: “When embarking on the process of interpretation, ... it is necessary to break loose intellectually from domestic law and the legal tradition of one’s own country.”

Part two of this chapter is therefore dedicated to deriving an international tax meaning of beneficial ownership by closely following the rules of the Vienna Convention.

Part two

6.3. Interpretation of beneficial ownership with reference to international law

After analysing the commentaries on beneficial ownership from the various international sources in Part one of this chapter, Part two is dedicated to an own interpretation of the international tax meaning of beneficial ownership by closely following the steps prescribed by the Vienna Convention.

At a discussion on beneficial ownership at the 1998 IFA Congress in London, the chairman of the seminar, professor Klaus Vogel, identified the question whether beneficial ownership is a term to which Article 3(2) of the OECD Model applies as the first main issue for consideration. The second main issue, on the assumption that the first one is answered in the negative, was: what is the international tax language meaning of beneficial ownership?

This study agrees that these are the two main issues at stake. Even though it would seem that the second issue only arises if the first one is answered in a certain manner, the approach is rather that both issues are so controversial that each of them can be regarded as a separate issue. In fact, even if some states can make out a valid case for applying Article 3(2), there has to be an international meaning of the term. The reason for this is the fact that the term is used in treaties of so many states which do not have a similar notion in their domestic law to revert to.

Although the focus of this study is on the second issue, it would be incomplete if the first one is not addressed as well. The first sec-

370. See supra note 8. None of the two issues were conclusively answered at the IFA Congress.
tion below therefore takes a brief look at the issues surrounding Article 3(2) of the OECD Model.

6.3.1. Article 3(2) of the OECD Model

The above-mentioned Article reads as follows:

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

The role and priority to be given to Article 3(2) in the interpretation of treaties is, unfortunately, another item on the list of international tax issues on which there is no clarity. From the numerous commentaries on the subject it appears that the list of controversies includes whether the article applies to all undefined treaty terms, the meaning to be given to “unless the context otherwise requires”, whether the ambulatory or static approach should govern, the relationship between this article and the Vienna Convention, the correct sequence of applying domestic and contextual interpretation (in other words, which one should come first), and whether the article should simply be understood to mean what the plain meaning of the wording used therein suggests.371

This study does not deal comprehensively with all these issues, but concentrates only on the arguments for and against interpreting beneficial ownership with reference to Article 3(2).

There is strong support for the view that terms falling in the category of international tax language, should be interpreted in the context of the treaty and not with reference to domestic law.\textsuperscript{372}

According to Edwardes-Ker, international tax language in tax treaties should normally be interpreted by adopting an autonomous approach – which recognizes that tax treaty terms must be interpreted (consistently by both states) in their tax treaty context. Indeed, he continues, there is no alternative to an autonomous interpretation of those tax treaty terms which have their genesis in tax treaties and which have no analogues in many states’ domestic laws.\textsuperscript{373}

Vogel comments as follows:

The first and foremost reason why the term cannot be interpreted by reference to the domestic law of the State applying the treaty is that none of the national tax systems in question offer a precise definition of the terms “beneficial owner”, “bénéficiaire effectif” or “Nutzungs­berechtiger”. The terms must, therefore, be interpreted with reference to the context of the treaty, and in particular with a view to the purpose pursued by the restriction.\textsuperscript{374}

Although the above statement is true in respect of the majority of states, it should be observed, as was concluded in Chapter 5, that “beneficial owner” does have a meaning in at least some common law states. Also, Article 3(2) – at least the English language version thereof – does not require a “precise definition”. It merely requires the term to have a meaning under the law of the state for the purposes of the taxes to which the treaty applies. For these reasons, there is at least some room for arguments in the common law states that Article 3(2) should apply.\textsuperscript{375}

\textsuperscript{372} It is concluded in 6.3.2.3, that “beneficial owner” also falls into the category of international tax language.

\textsuperscript{373} Edwardes-Ker, supra note 367, at 7.02. For further support of the autonomous approach, see Vogel, supra note 329, at 58-59.

\textsuperscript{374} Vogel, supra note 329, at 562.

\textsuperscript{375} For an example of the opposite viewpoint (under different circumstances), see John F. Avery Jones, et al., “The Non-discrimination Article in Tax Treaties”, European Taxation 1991/10, at 330, arguing that the context of the OECD Model prohibits the use of the domestic meaning of “enterprise” by states in respect of which it forms part of domestic law.
Prokisch argues that to the extent that an international tax language exists, the relevance of Article 3(2) disappears. He explains the relationship, and apparent contradiction, between Article 3(2) and an international tax language as follows:

Article 3(2) is a rule of interpretation, as such it presupposes an unclear and doubtful situation which calls for interpretation. Such an undefined term, however, is not existent if the ordinary meaning of a term is clear, especially in those cases where we can find an established common international meaning of a term. The greater the consensus is regarding an international common understanding, the smaller the scope of the previously mentioned rule.376

At the 1998 IFA Congress in London, the Swiss member on the discussion panel commented as follows regarding the question whether Article 3(2) can be applied to interpret the meaning of beneficial ownership:

[M]y view is ... that beneficial ownership should be a treaty concept. The application of Article 3(2), in other words, the application of given rules in this field of domestic law could in my view undermine treaty solutions and could also lead to some kind of treaty override. I think that since one grants benefits by way of a treaty one should also say under what circumstances such benefits will be denied. And this should not be done based on domestic law but on treaty provisions.377

But, there are also those holding the view that domestic law may be applied to identify the beneficial owner. This is, for example, explicitly stated in the Technical Explanation of the 1996 United States Model Convention (see 6.2.3.).

At the 1998 IFA Congress in London, a United States member of the discussion panel, provided the following argument for applying Article 3(2):

377. See supra note 8. The panel members from Sweden, France and the Netherlands all supported the view that beneficial owner should be regarded as a treaty concept, and only a member from the United States gave some support for the application of Article 3(2).
In favour of applying a domestic definition of the term, that is the term as it is used under the law of the source state, is the plain language of Article 3(2). Article 3(2) provides that where the Model Convention uses a term that it does not explicitly define in the text, the source state’s internal law supplies the definition, unless the context otherwise requires.

It is probably true that many a user of a tax treaty, confronted with a situation where there is no treaty definition will, without hesitation, on the grounds of the plain language of Article 3(2), revert to the domestic meaning of the term.

It is also necessary to refer to the United States final conduit financing regulations,\(^{378}\) which are effective with respect to payments made after 10 September 1995, and, \textit{inter alia}, affect withholding taxes on royalties. Apart from the importance of these regulations, the discussion thereof serves as an example of an extreme case of a domestic and ambulatory approach to the application of Article 3(2).

These lengthy and rather complicated regulations provide the IRS district director with discretion and authority to disregard, for purposes of Section 881 of the IRC,\(^{379}\) the participation of one or more intermediate entities in a financing arrangement where such entities are acting as conduit entities. For these purposes (all terms with special meanings for purposes of the regulations are shown in italics) a \textit{financing arrangement} is generally defined as a series of \textit{financing transactions} (which include a licence) involving a \textit{financing entity} (for example the ultimate licensor) and the \textit{financed entity} (for example the ultimate licensee), when the arrangement is effected through one or more \textit{intermediate entities}. In order for the district director to \textit{recharacterize} a transaction, he must determine that the \textit{intermediate entity} is a \textit{conduit entity}. The requirements for such determination depend on whether the \textit{intermediate entity} is \textit{related} to either the \textit{financing entity} or the \textit{financed entity}. If such relationship does exist, the district director may determine that the \textit{intermediate entity} is a \textit{conduit entity} if, because of the participation

\(^{378}\) Treasury Regulations, Section 1.881-3.
\(^{379}\) Dealing with tax on income of foreign corporations not connected with United States business.
of the intermediate entity, United States withholding taxes are reduced, and the use of the intermediate entity is pursuant to a tax avoidance plan. If no such relationship exists, the district director must, in addition to the two requirements mentioned above, also establish that the intermediate entity would not have entered into the transaction on substantially the same terms but for the participation of the financing entity. If a financing arrangement is found to be a conduit financing arrangement, the payments made by the financed entity pursuant to the financing arrangement will be recharacterized as flowing directly from the financed entity to the financing entity.

Nowhere in the regulations is there any reference to beneficial ownership. In the preamble to the final regulations, however, under the heading “General Approach”, and in response to suggestions by commentators that the regulations constitute an override of treaty obligations and might therefore be invalid, the IRS responded as follows:

[T]he IRS and Treasury believe that these regulations supplement, but do not conflict with, the limitation on benefits articles in tax treaties. They do so by determining which person is the beneficial owner of income with respect to a particular financing arrangement. Because the financing entity is the beneficial owner of the income, it is entitled to claim the benefits of any income tax treaty to which it is entitled to reduce the amount of tax imposed by section 881 on that income. The conduit entity, as an agent of the financing entity, cannot claim the benefits of a treaty to reduce the amount of tax due under section 881 with respect to payments made pursuant to the financing arrangement.380

North and French comment as follows on the above:

It is true that most US tax treaty withholding articles contain an express requirement that the person claiming the benefits of lower withholding rates be the “beneficial owner” of the item of income in question. The term “beneficial owner” is generally not expressly defined in these treaties. Therefore, under most US tax treaties, an undefined term such as “beneficial owner” shall, unless the context otherwise requires or the competent authorities agree to a common meaning, have the meaning that it has under the law of the state concerning the taxes to which

the treaty applies (in the case of US withholding tax, the United States). Therefore the application of the regulations, as a reflection of the law of the United States, would normally not constitute a treaty override if used to define an otherwise undefined term of a tax treaty [references omitted].

The fact that Article 3(2) can be applied in the way as described above to justify the provisions of the final conduit financing regulations to represent the meaning of beneficial ownership will probably come as a big surprise to those who advocate a more restricted application of Article 3(2),\(^\text{382}\) as well as to the supporters of the goal of a common international interpretation and, one guess, as an even bigger surprise to those states who entered into treaties with the United States prior to September 1995, when the regulations came into force.

In conclusion: The view that beneficial ownership is not a term to which Article 3(2) should be applied is based on arguments such as that the term has no meaning in domestic law, or does not have a meaning in domestic law that is relevant for treaty purposes,\(^\text{383}\) or that the context of the treaty requires otherwise. The main argument that Article 3(2) can be applied, appears to be the plain language of the article.

In the opinion of this study, in those instances where beneficial ownership does not form part of the domestic law of both the treaty partners it almost speaks for itself that Article 3(2) cannot be applied. This provides sufficient justification for research into the international tax meaning of the term. In those states where the term forms part of domestic tax law, there is room for argument that Article 3(2) can be applied. This may be valid especially for those treaties into which beneficial ownership was incorporated before its

382. See, for example, Vogel, supra note 329, at 209, maintaining that Article 3(2) governs no more than the interpretation of words used in the treaty and that it provides no justification for reliance on general legal principles of domestic law in interpreting treaty law, or for closing loopholes within the treaties by reference to domestic law.
383. See Australia: Thiel v. Federal Commissioner of Taxation (1990) 21 ATR 531, at 532-533, for such a finding in respect of “enterprise”. 

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It should be noted, though, that 1977 was not the first introduction of beneficial ownership to the world of international tax. It was used much earlier in some treaties on inheritance tax. For example, Article III of the 1945 United Kingdom-United States treaty on the estates of deceased persons refers to “shares or stock held by a nominee where the beneficial ownership is evidenced by scrip certificates or otherwise”.

“Beneficial ownership” was also used in bilateral income tax treaties before 1977. For example, it was incorporated by a supplementary protocol in 1966 into the United States-United Kingdom treaty. In an explanatory note which is attached to one copy of the protocol, the following is stated:

Relief from tax on dividends, interest and royalties ... in the country of origin will no longer depend on whether the recipient is subject to tax in the other country, but will depend on the income being beneficially owned by a resident of the other country.

The explanatory note provides no further information on the meaning of beneficial ownership. One conclusion from the quoted passage is that the meaning of beneficial ownership is not the same as “subject to tax”. This is even more clear from the October 1987 Protocol which replaced the “subject to tax” requirement in the 1968 United Kingdom-France treaty with a beneficial owner requirement. An explanatory note attached to one of the copies of the Protocol states:

The Protocol generally adopts the criterion of beneficial ownership for obtaining relief under the Convention although, ... subject to tax also remains a condition for the purposes of Article 9 (dividends) of the Convention.

The United Kingdom-France treaty (after the above amendment) also provides support for the view that the beneficial owner test should not focus on the reasons why a transaction was done in the chosen manner. Paragraph 1 of the royalties article (Article 12)

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385. “Beneficial owner” is also used in paragraph 21 of the 1966 Commentary on the Draft OECD Model Estates and Inheritance Tax Treaty.
386. Other examples include the 1969 Australia-Japan, the 1975 United Kingdom-Spain and the 1968 Ireland-France treaties, and the 1968 protocol amending the 1947 United Kingdom-Antigua treaty.
contains the beneficial ownership requirement. In addition paragraph 5 of Article 12 provides that:

The provisions of this Article shall not apply if the right or property giving rise to the royalties was created or assigned mainly for the purposes of taking advantage of this Article and not for bona fide commercial reasons.

If the investigation into beneficial ownership included a "reasons for the transaction" test, it would not have been necessary to include the last mentioned paragraph.

In conclusion: Very little information is available on the history and reasons why it was decided to incorporate beneficial ownership, as opposed to some other notion, into the OECD Model. Although there is no explicit evidence on the source that the term was taken from or the exact meaning it was supposed to have, there is at least no evidence negating the view that it was taken from the common law states. The fact that the notion was used in some treaties of common law states before 1977, and that it is a term that is only known in those states, and that representatives from the common law states were part of the OECD committee incorporating the term into the OECD Model, are some of the factors supporting the argument that the term was taken from that source. The question may indeed be asked that, if not from the common law states, where else could the term have been taken from?

Other questions arise: Should the term be interpreted differently in those treaties in which it was incorporated before 1977, in other words, before the OECD Model conferred it with the status of international tax language? What was the meaning of the term in the United States-United Kingdom treaty, following the 1966 Protocol, or the meaning in the 1975 United Kingdom-Spain treaty? Can it be argued that Article 3(2) of the OECD Model should be applied to pre-1977 treaties, or maybe that a special meaning, as envisaged by Article 31(4) of the Vienna Convention, was intended in those treaties?

On the whole it appears that there is no available documentation as to the intended meaning of beneficial ownership other than official OECD documentation such as the OECD Model, the MC Commentary and the OECD Conduit Companies Report.
6.3.2.3. International tax language

It is necessary to have a closer look at the meaning of “international tax language”, a term that is used throughout this study.

Prokisch strongly supports the existence and importance of an international tax language on the basis that, to avoid misinterpretation, a common international understanding of treaty terms is necessary. He provides the following definition:

International tax language is the common international understanding of terms which are used within the formulation of tax treaties. If two states use such a term in a bilateral tax treaty, then they use it in this international sense, unless they prefer to give the term a special meaning, either by formulating a special definition of the term or by using a term which has a clear relation to domestic law.387

The House of Lords, in Ostimr v. Australian Mutual Provident Society,388 identified treaty terms such as “enterprise”, “industrial or commercial profits”, and “permanent establishment” as international tax language which have no exact counterpart in the taxing code of the United Kingdom. In South Africa in Secretary for Inland Revenue v. Downing,389 the term “contracting state” was added to this list. Other states where the courts approved of an international tax language, include Australia390 and Rhodesia.391 Edwardes-Ker adds several more terms to the list of international tax language, including “profits from the operation of ships or aircraft”, “associated enterprises”, “special relationships”, “entertainers” and “sportsmen”, and “student or business apprentice”. He also includes “beneficial owner”, which, he comments, is a term not recognized in many (civil law) OECD states.392

In summary: The question of whether beneficial ownership forms part of an international tax language is closely related to the

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387. Prokisch, supra note 376, at 103-110. Prokisch also comments (at 103), however, that although the idea of an international tax language is not new, it has not found general recognition.
388. (1959) 38 TC 492, HL, at 517.
390. Thiel, supra note 383.
392. Edwardes-Ker, supra note 367, at 7.02.
question, discussed in 6.3.1., of whether beneficial ownership is a term to which Article 3(2) of the OECD Model should be applied. For the majority of states whose tax treaties are based on the OECD Model, “beneficial owner” can properly be described as international tax language, that is, a term that has no exact counterpart in domestic tax law. In those common law states where “beneficial owner” does have a meaning in domestic tax law there is, however, room for arguing against placing the term in the international tax language category.

The fact that “beneficial ownership” is not the only term falling in the category of international tax language makes it relevant to investigate how the OECD Model and MC Commentary deal with the other terms in this category. Is it possible to detect a consistent manner of defining or explaining the meaning of international tax language terms in the OECD Model and MC Commentary, which can then be applied to beneficial ownership? Unfortunately the aforementioned question has to be answered in the negative. In some instances a definition is provided in the OECD Model, for example “permanent establishment” (Article 5) and “associated enterprises” (Article 9). In other instances there are no definitions or explanations either in the OECD Model or MC Commentary, for example “student or business apprentice” (Article 20). Lastly, there are several instances where no full definitions are provided, but an indication is given to a more or lesser extent, either in the OECD Model or the MC Commentary, on the meaning, or how to go about finding the meaning. Examples include “enterprise” (a frequent term), “profits from the operation of ships or aircraft” (Article 8), “special relationship” (Articles 11(6) and 12(4)), and “entertainers” and “sportsmen” (Article 17).

6.3.2.4. Recourse to the OECD Model

What support is there for the hypothesis that the meaning of an undefined term used in a bilateral tax treaty should be based on the meaning of that same undefined term in the OECD Model? The following statement by Vogel provides the best answer to the question:

[W]here OECD member States conclude tax treaties following the text of the MC, it is presumed that those states want the treaty provision to
convey the meaning intended by the MC and its Commentary ... as long as no particular circumstances indicate to the contrary.393

This argument is powerful. If a treaty is based on the OECD Model there is a strong presumption that those parts of the OECD Model that has been taken over without any adaptations are intended to have the same meaning as in the OECD Model. This is even more true where terms, such as beneficial ownership, are not used in the domestic law of one or both treaty partners.

What are the circumstances that may indicate a meaning different from that of the OECD Model? One possibility may be the way in which beneficial ownership was translated into a foreign language (see 6.2.12.). There is certainly an argument that where a treaty is drafted only in, say Spanish, that the treaty partners intended the term to have the meaning as per their translation. On the other hand, the argument may lose some of its strength if the translated term itself does not have a clear meaning. For example, Vogel mentions that neither the national tax systems of the French or German speaking states offer a precise definition of the terms used as the equivalent of beneficial owner in those languages, being bénéficiaire effectif and Nutzungsberechtiger.394 Further support for the view that the meaning of the term should be sought by referring back to the language of the OECD Model, comes from Prokisch who, in discussing the problems arising from the imprecision of the translation of the OECD Model, states that if German tax treaties are based on the OECD Model, the official languages (English and French) have to be considered when such a treaty term is interpreted.395 Lastly, in those states where it is accepted that Article 3(2) cannot be applied to beneficial ownership, and that the term falls into the category of international tax language, it almost follows as the next logical step that guidance should be sought from the OECD Model as to the meaning of the term.

393. Vogel, supra note 329, at 44. Vogel’s view is based on a view by Hugh J. Ault, “The Role of the OECD Commentaries in the Interpretation of Tax Treaties”, Intertax 1994/4, at 146-147, dealing specifically with the MC Commentary.
394. Vogel, supra note 329, at 562.
395. Prokisch, supra note 376, at 106.
The fact that a tax treaty is a bilateral agreement, binding only the two treaty partners, does not mean that it cannot incorporate international tax language based on the OECD Model.

The correct place and the importance of the OECD Model in the interpretation process, for example, whether it forms part of the context, or supplementary means of interpretation in terms of the Vienna Convention, is another area of dispute. In terms of the hypothesis in this study, the aforementioned issues do not arise. For purposes of bilateral tax treaties, the OECD Model is the source from which beneficial ownership was taken. The Vienna Convention places no restrictions on what can be used as the source for the investigation into the ordinary meaning of treaty terms. As far as beneficial ownership is concerned, it is not only legitimate to refer to the OECD Model (and from the OECD Model to the common law states) as the source of the term but also unavoidable.

6.3.2.5. The Vienna Convention

There appears to be a great level of consensus that the rules of the Vienna Convention codify already valid customary law and hence all international treaties would be governed by these rules of interpretation. The United States, though, have some reservations as to the rules of the Vienna Convention. The discussion of such reservations falls outside the scope of this study. Also, it is submit-
ted that the United States Supreme Court decision in *Eastern Airlines, Inc. v. Floyd*, 401 discussed below and on which a lot of weight is placed for supporting the hypothesis as stated in 6.3.2.1., closely follows the rules of the Vienna Convention.

The meaning of beneficial ownership is therefore interpreted with reference to the Vienna Convention, Articles 31 and 32 of which are reproduced below:

**Section 3. Interpretation of Treaties**

**Article 31**

**General rule of interpretation**

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to terms of the treaty in their context and in the light of its object and purpose.

2. The context for the purpose of the interpretation of the treaty shall comprise, in addition to the text, including its preamble and annexes:
   a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
   b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

3. There shall be taken into account, together with the context:
   a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
   b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding the interpretation;
   c) any relevant rules of international law applicable in the relations between the parties.

4. A special meaning shall be given to a term if it is established that the parties so intended.

Article 32

Supplementary means of interpretation

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of Article 31, or to determine the meaning when the interpretation according to Article 31:

a) leaves the meaning ambiguous or obscure; or
b) leads to a result which is manifestly absurd or unreasonable.

6.3.2.6. Multilateral treaties

Some of the key cases on treaty interpretation are in respect of multilateral treaties, as opposed to bilateral treaties. The question arises whether it is correct to take principles from cases on multilateral treaties and apply it to bilateral treaties? There is a difference between a multilateral treaty agreed upon and signed by various participating states on the one hand and, on the other hand, a bilateral treaty based on the OECD Model which, although the result of a drafting process to which many states contributed, has no legal binding power.

Since the Vienna Convention applies to both bilateral and multilateral treaties, there will be many instances, such as the interpretation methodology applied, where it will be correct not to make a distinction between the two types of treaties.

In the case of beneficial ownership, the relevance of the issue of multilateral versus bilateral treaties concerns the source that treaty terms are taken from. For example, in *Eastern Airlines*, discussed more fully in 6.3.2.7., dealing with the multilateral Warsaw Convention, the United States Supreme Court interpreted treaty terms by referring to the source of the treaty terms, being France and the French language. Can this same approach be adopted in determining the meaning of beneficial ownership in a bilateral treaty?

402. See, for example, *Eastern Airlines* and *Fothergill* discussed in 6.3.2.7.
403. For arguments that the OECD Model has no binding power, see Hans Pijl, “The Theory of the Interpretation of Tax Treaties, With Reference to Dutch Practice”, *Bulletin* 1997/12, at 545.
Say that it is accepted that the OECD Working Party took the term from the common law states when incorporating it into the OECD Model. Can the meaning of beneficial ownership in the bilateral treaty of any other state then be established by reference to the meaning of the term in the common law states?

From a pure legal binding power point of view, the OECD Model can obviously not be compared with that of a multilateral treaty. If, however, the argument in 6.3.2.4. is accepted, namely that recourse to the OECD Model is legitimate in respect of undefined treaty terms taken over from the OECD Model, it is submitted that it is not inappropriate to follow the Eastern Airlines approach in respect of a bilateral treaty.

6.3.2.7. International case law

Beneficial ownership is, of course, not the first treaty term that needed to be interpreted. There are in fact various court cases worldwide dealing not only with the interpretation of specific treaty terms but also more generally with the methodology of treaty interpretation. Therefore, before proceeding with finding the international tax meaning of beneficial ownership, it is necessary to consider some of these cases, firstly to find support for the hypothesis stated in 6.3.2.1. and, secondly, to extract further guidelines to be used in the interpretation of beneficial ownership.

None of the cases discussed deals with beneficial ownership, but that is not the issue here. The issue is to look at the approach of the courts: What was their interpretation methodology? How did they deal with international language? From which source did they take the meaning of treaty terms? How did they deal with treaty terms which had their source in a foreign state and language? How did they deal with the context, purpose and object of the treaty and how did this influence the meaning ascribed to the treaty terms? How did they deal with extrinsic evidence on the meaning of the terms?
It is appropriate to start the discussion with decisions by two courts of the highest jurisdiction, namely *Fothergill v. Monarch Airlines*\(^{405}\) by the House of Lords in the United Kingdom and *Eastern Airlines*\(^{406}\) by the United States Supreme Court.\(^{407}\) Both the cases deal with the multilateral treaty concerning carriage by air, the Warsaw Convention.

In *Fothergill* the facts were that the plaintiff, on arrival at Luton airport, found that a suitcase that was part of his luggage was badly torn. When he arrived home, the plaintiff found that some of his personal effects were missing from the suitcase. The relevant section of the Warsaw Convention states that in the case of “damage” a complaint must be lodged within seven days. The question the court had to decide on was whether “damage” include partial loss of the contents of baggage.

The case is relevant for at least two reasons. The first is the often quoted speech by Lord Diplock on the approach to treaty interpretation:

> The language of an international convention has not been chosen by an English parliamentary draftsman. It is neither couched in the conventional English legislative idiom nor designed to be construed exclusively by English judges. It is addressed to a much wider and more varied judicial audience than is an Act of Parliament that deals with purely domestic law. It should be interpreted as Lord Wilberforce put it in *James Buchanan & Co Ltd* ... “unconstrained by technical rules of English law, or by English legal precedent, but on broad principles of general acceptation.”\(^{408}\)

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405. [1981] AC 251, HL.
407. Vogel, *supra* note 329, at 40, refers to these two cases as models concerning the interpretation of an international agreement on the standardization of private law provisions. It is unfortunate that this study could not find similar cases from civil law states in order to study their approach. As Vogel (at 34) points out: “For the effective interpretation of international treaties ... it is necessary to reconcile the various national methods of interpretation. On the [one] hand, the text of the treaty must be binding to a greater extent than is recognized in European (continental) practice ... On the other hand, treaties must be interpreted more liberally than are statutes in Anglo-American law.”
408. *Fothergill, supra* note 405, at 281.
The second reason is the way in which the court dealt with the meaning of the words used. Lord Wilberforce found that whether the word “damage” in the English language can include “partial loss” is, textually, open to argument. He then considered the meaning of “damage” (*avarie*) in the French version of the Warsaw Convention. It was shown that *avarie* has both an ordinary meaning and a special meaning as a term of maritime law, with the last mentioned meaning allowing at least some scope for including partial loss. Because the linguistic argument was inconclusive, Lord Wilberforce then turned to a purposive construction of the section to conclude that the word “damage” includes partial loss. In doing so he admitted that some strain, if not distortion, of the language seems inevitable, but of the governing French text it could at least be said that it does not exclude partial loss.

Whereas *Fothergill* is an example of a wide interpretation of the meaning of the wording used, *Eastern Airlines* is an example of a narrow interpretation. *Eastern Airlines* is, however, also important because it is an example where the court, as the starting point of interpretation, investigated the meaning of the words in the source (France and the French language) that it was taken from. This meaning was then tested in the light of the context and purpose of the Warsaw Convention.

After petitioner’s plane narrowly avoided crashing during a flight, respondent passengers filed separate complaints seeking damages solely for mental distress arising out of the incident. The Supreme Court found that because the only authentic text of the Warsaw Convention is in French, the French text must guide the analysis. The question therefore was whether the relevant Article 17 of the Warsaw Convention phrase, *lesion corporelle*, should be translated as to include only bodily injury or whether it also includes mental injuries.

The Supreme Court started by looking at the meanings in French dictionaries, which confirmed a proper translation of “bodily injury”. The court then referred to the principal sources of French civil law, being legislation, judicial decisions and scholarly writing, neither of which provided proof that the term includes psychic injuries. As a next step, the court analysed the structure of Article
17, the negotiating history of the Convention, the purpose of the Convention, documentary record of the Warsaw Conference and subsequent agreements and protocols, all of which supported the view that mental injuries were not intended to be included.

_Inland Revenue Commissioners v. Commerzbank AG_ is another case that has received praise for its approach to treaty interpretation. The case is an example of interpretation where the natural and plain meaning of the wording is clear. It also provides information on the relative importance of textual interpretation as opposed to other aids to interpretation.

In terms of the relevant United Kingdom-United States treaty, interest received by a recipient in the United Kingdom was exempt from tax in the United Kingdom, provided that the recipient was not a United Kingdom citizen, resident or corporation. On behalf of the taxpayer banks, it was argued that the natural and ordinary meaning of the words are plain and that they qualify for the exemption because they fall within the terms of the treaty. On behalf of Inland Revenue, it was argued that despite the clear words of the article, relief was not available to the banks as the interpretation of a bilateral tax treaty is subject to the implied presumption that benefits are not to be conferred on persons who are not citizens, residents or corporations of either contracting state unless explicitly so conferred.

Mummery J. held that the words, both on their own and in the context of the treaty as a whole, are clear. The banks were neither citizens, residents or corporations of the United Kingdom and therefore qualified for the treaty relief. In addition, the judge continued, such construction of the treaty provision does not give rise to manifestly absurd or unreasonable consequences, neither could he find sufficient indication in the purpose of the treaty or its surrounding circumstances or in other treaty provisions to qualify the clear words. Lastly, he said, even if he did regard the wording unclear or ambiguous or as giving rise to manifestly absurd and unreasonable results and was driven to look at _travaux préparatoires_, he would

409. [1990] STC 285, Ch D.
410. See Edwardes-Ker, supra note 367, at 3.14. See, however, Katz, supra note 400, at 626-629, for a different decision in the United States on substantially identical provisions.
find that there is no such material before the court to give it guidance.

On aids to the interpretation of a treaty such as travaux préparatoires, international case law and the writings of jurists, Mummery J. held that they are not a substitute for study of the terms of the treaty, and that their use is discretionary, not mandatory.

A last comment on this case relates to the speech by Lord Diplock in Fothergill (quoted above) that the language of an international convention should be interpreted on broad principles of general acceptation ..., etc. Inland Revenue relied on this passage as support for their view of an implied presumption that benefits are only available to residents of either contracting state. The court, however, by implication, was not willing to apply this principle of broad interpretation in circumstances where the meaning of the words in the context of the treaty was clear.

There are several other examples of the court starting the interpretation process with the text, the letter, the wording. In most instances the court referred to dictionary meanings as the starting point. In some instances, however, the court also referred to other meanings, such as terminology used in the industry.

The following are some examples of the approach described in the paragraph above:

- In Rhodesia in Commissioner of Taxes v. Aktiebolaget Tetra Pak to interpret “industrial or commercial profit”;
- In Canada in Specht v. R. to interpret “retire” and “pension” and in MCA Television Ltd. v. R. to interpret “motion picture films”; 
- In New Zealand in Case J41 to interpret “a permanent home available to him” and in Wise v. CIR to interpret “branch”.

Henry H. Kimball v. Commissioner is an example of the court, realizing that a treaty is based on a model treaty (that of the League

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411. See also United States Revenue Rulings 76-19 and 74-541, and Letter Rulings 80-36-081, 81-47-148 and 81-41-069.
412. Commissioner of Taxes v. Aktiebolaget Tetra Pak, supra note 391.
417. 6 T.C. 535 (1946).
of Nations), referred back to the model treaty, the commentary thereon and the circumstances surrounding the drafting of the model treaty in order to interpret terms used in the United States-France bilateral tax treaty.

The question to be decided was whether payments from the United States to beneficiaries in France under a trust fund established by will were respectively “life annuities” and “private pensions” in terms of the treaty.

The United States Tax Court stated that its task was to discover, if possible, the sense in which the contracting parties used the terms, neither of which had a well recognized single significance, either in law or as a matter of general language. The court referred to the history of the League of Nations Model Treaty and the fact that uniform definitions were being formulated, the predominant kinds of income were being classified, and an international tax language was being developed. Because the United-States-France treaty was based on the Model Treaty and embodied the language and principles thereof, the court then investigated the official commentaries and the minutes of the meetings concerning the drafting of the Model Treaty to conclude that the relevant payments did not fall within the treaty provisions.

6.3.2.8. Ordinary meaning, context, object and purpose

Article 31(1) of the Vienna Convention provides that a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to terms of the treaty in their context and in the light of its object and purpose.

It is not necessary to have a long discussion on the principle of good faith. As Edwardes-Ker points out, it means that each signatory state must observe its obligations to perform a treaty.418

Commentators differ as to the correct interrelationship and order of precedence to be given to the different elements, being the literal

418. Edwardes-Ker, supra note 367, at 5.01
It is submitted that, what has been described as the holistic approach to the application of the different elements, is the correct approach and should be applied to the interpretation of beneficial ownership. The High Court of Australia, in support of the holistic approach, refers to the International Law Commission, who commented that: “All the various elements, as they were present in any given case, would be thrown into the crucible, and their interaction would give the legally relevant interpretation.” But, the court continues, the text is taken as the starting point.

6.3.2.8.1. Meaning of the words

The ordinary meaning is not necessarily the meaning of everyday use. The ordinary meaning is the meaning arrived at after taking into account the context, object and purpose. For example, for those terms which have acquired an international tax language meaning, that meaning is to be regarded as the ordinary meaning.

The process of interpretation therefore starts with the text, the letter, the wording: “The starting point of interpretation is the elucidation of the meaning of the text, not an investigation ab initio into the intentions of the parties.” And, as was concluded in 6.2.14., this aspect is a major criticism of this study against commentaries to date on the meaning of beneficial ownership. In spite of the clear rule from the Vienna Convention in this respect, there is little evidence in the commentaries of starting the process of interpretation with the meaning of the wording.

419. For a discussion of the different opinions, see the High Court of Australia in Applicant A v. Minister for Immigration and Ethnic Affairs (1997) 71 ALJR 381, at 396-397.
420. Id. See also Commissioner of Taxation v. Lamesa Holdings BV [1997] 785 FCA (20 August 1997).
421. In support of this view, see Vogel, supra note 329, at 37 and 44; Prokisch, supra note 376, at 106; Edwardes-Ker, supra note 367, at 4.02.
422. Supporting this view: Pijl, supra note 403, at 539; Vogel and Prokisch, supra note 371, at 68 and 73-74; Katz, supra note 400, at 616; Edwardes-Ker, supra note 367, at 4.01.
There may, of course, be doubt on what the meaning of the words is, and whether it should be the dictionary, “man in the street”, term of legal art, or some other meaning. But, if there is more than one possible meaning, then all possibilities should be listed as a starting point. It is the object of the rest of the process of interpretation to determine which one of the different meanings is the most appropriate. It may be that the meaning taken as the starting point is found to be ambiguous. In such a case guidance must be sought from the context, purpose and object to arrive at an answer. Whatever may be the difficulties surrounding the meaning(s) to be taken as a starting point, such meaning(s) cannot simply be ignored. Neither can the text be ignored because the term is not known in the domestic law of many OECD member states. On the contrary, the fact that it is not known in all states is an indication of its international tax language status and that its meaning should be determined with reference to the OECD Model. What is more, the final answer reached must still relate to the wording used. The meaning that is taken as a starting point may be interpreted very narrow, or very wide, but the final answer cannot be something that bears no relation to the wording used. Vogel puts it as follows:

Excluded, therefore, is only an interpretation which, though corresponding to the intent of the parties, is in no way supported by the wording of the treaty. It is even less acceptable for a court to use as a basis of interpretation that which it presumes the parties must have intended.

The fact that the meaning of the words must be thoroughly considered cannot be stressed strongly enough as far as beneficial ownership is concerned. It should be borne in mind that the drafters of the OECD Model had several options available to them when they had to decide on a method to restrict treaty benefits. It is known, for example, that they considered making treaty benefits dependent on the payments being liable to tax in the state of residence, or to use

424. See, however, Katz, supra note 400, at 624-633 and John F. Avery Jones, “National Reporter United Kingdom: Interpretation of double taxation conventions”, Cahiers de droit fiscal international, Volume LXXVIIIa, 1993, at 598-601, for discussions of cases and circumstances where the court looked beyond the literal language.

425. Vogel, supra note 329, at 37.
the wording “final recipient” (see 6.2.1.). There were several other options available to them. For example, they could simply have said that the treaty benefits are not available to (formal) agents and nominees, or to conduit entities, or to an entity that has been incorporated for the sole purpose of making use of the treaty benefits, or that an entity should be ignored in terms of the substance over form principle. They may have used known treaty notions such as “special relationship” or “associated enterprises”. They could have used “owner” or “economic owner”. They could have opted for wording, such as beneficially entitled, which is more neutral as far as the different member states of the OECD is concerned. Also, the OECD was aware that beneficial ownership is a notion not known in the domestic law of many of its member states. From the evidence of minutes showing that the incorporation of beneficial ownership was already discussed in 1970, it can be assumed that the matter was considered over a long period before its introduction to the OECD Model in 1977. There was thus sufficient time for any member state to object against the wording.

Instead, the choice of the OECD fell on beneficial owner, maybe because of the unique and subtle characteristics of that term. The investigation into the international tax language meaning of beneficial ownership must therefore start with an investigation of the meaning of the plain wording.

What are the meaning or meanings that should be taken as the starting point in search of the ordinary meaning of beneficial owner? Based on the strong indications that the OECD borrowed the notion from the common law states it is clear that the meaning in the common law states should be on the list of meanings to be considered. But are there any other meanings to consider? It is submitted that it is not appropriate to refer to ordinary non-legal dictionaries. Normal dictionaries usually do not define such two worded terms and it is further submitted that in order to find the meaning of the two words put together, they have to be considered as a unity. Also, the English courts have thoroughly discussed the issue as to whether beneficial

426. See also paragraphs 7 to 26 of the MC Commentary on article 1, discussing different methods of dealing with improper use of treaties.
427. See supra note 384.
owner has, in addition to a legal meaning, also a “man in the street” meaning (see 5.2.1.). This question was answered in the negative, with Jenkins J. holding that it seems difficult to ascribe any different meaning to those words from their legal meaning, and that little assistance can be derived from speculation as to what an ordinary person would take them to mean in their popular sense.

Neither does any of the statutory definitions (as distinguished from the undefined meaning in the common law states) given to beneficial ownership, for example, for purposes of conveyancing and other domestic purposes in England and Australia, or for treaty purposes in Germany,\textsuperscript{428} seem appropriate for purposes of a general meaning of the term for international tax purposes. Those definitions are arbitrary and relevant only for the specific circumstances covered by it. In addition, some of them may only have been formulated after 1977, the date when beneficial ownership was incorporated into the OECD Model. The conflicting definitions in the United States provided respectively by the Technical Explanation of the 1996 United States Model Convention (see 6.2.3.) and Form 1001 which has to be filed with the withholding agent (see 6.2.13.), are equally unhelpful.

Apart from the few definitions referred to above, the research done for this study did not reveal any meaning of beneficial ownership other than the legal sense in which the term is used in the common law states.\textsuperscript{429} The analyses of cases in the common law states in Chapter 5 have identified the most important characteristics of beneficial ownership. Listed below is a selection which is regarded as representative of the statements on the meaning of beneficial owner as expressed in those cases. The object is to see whether a single meaning can be formulated from the statements listed:

\textit{England}

– It means ownership for your own benefit as opposed to ownership as trustee for another. It exists either where there is no division of legal and beneficial ownership or where legal ownership

\textsuperscript{428} See \textit{supra} notes 233 and 286, and 6.2.6.

\textsuperscript{429} As is described in Chapter 5, the search term “beneficial owner” was entered into various data bases in order to determine the meaning thereof.
is vested in one person and the beneficial ownership ... in another (Nourse L.J. in Sainsbury\textsuperscript{430}).

- We must look into the nature and extent of the rights retained by Sainsburys in relation to the 5%. If Sainsburys was bereft of all rights which normally attach to that parcel of shares, so that its ownership was, in the words of Judge Harman, nothing more than a legal shell, then we would be bound to hold that Sainsburys was not the beneficial owner of the shares (LLoyd L.J. in Sainsbury\textsuperscript{431}).

- That means, I think, an ownership which is not merely the legal ownership by the mere fact of being on the register, but the right at least to some extent to deal with the property as your own (Harman L.J. in Wood Preservation\textsuperscript{432}).

- But if one finds, as here, that the company ... though still the legal owner of the shares, is bereft of the rights of selling or disposing or enjoying the fruits of these shares, then, I have in the end concluded that it would be a misuse of language to say that it still remained the beneficial owner of these shares (Lord Donovan in Wood Preservation\textsuperscript{433}).

- But I have been persuaded that ... one must examine the situation of the vendor and ask whether the legal ownership, which unquestionably remained in him, retained the attributes of beneficial ownership (Widgery L.J. in Wood Preservation\textsuperscript{434}).

- It seems to me that from the moment of acquisition these shares were subject to equitable obligations in favour of others (Roxburgh J. in Leigh Spinners, in holding that the appellant company was not the beneficial owner of the shares in the new company because, from the moment the new company was formed, the appellant was under an obligation to transfer the shares in it to someone else\textsuperscript{435}).

\textsuperscript{431} Id. at 328.
\textsuperscript{432} Wood Preservation Ltd v. Prior (Inspector of Taxes) (1968) 45 TC 112, CA, at 133.
\textsuperscript{433} Id. at 132.
\textsuperscript{434} Id. at 133.
\textsuperscript{435} Leigh Spinners Ltd v. Commissioners of Inland Revenue (1956) 46 TC 425, Ch D, at 427-432.
Beneficial ownership ... in property ... means, in this connection, such a right to its enjoyment as exists where the legal title is in one person and the right to such beneficial ... interest is in another, and where such right is recognized by law, and can be enforced by the courts, at the suit of the owner (Mr Justice Peckham in Montana Catholic Missions\(^\text{436}\)).

Beneficial ownership is marked by command over property or enjoyment of its economic benefits. ... The retention by a seller of formal attributes of ownership does not preclude finding a sale (Yelencsics\(^\text{437}\)).

Beneficial ownership passes when sufficient benefits and burdens of ownership pass. In the context of the instant case, NCO’s equitable ownership would have passed to Northshore Ltd when Northshore Ltd’s ownership attributes in the Complex outweighed NCO’s ownership attributes (Jones C.J. in H. Calvin Walter\(^\text{438}\)).

Rupe’s naked title and risk assumed, such as it was, must be balanced against these indicia of beneficial ownership in another ... The Tax Court could not escape the conclusion that the taxpayer had no control over the dividends or over the stock; beneficial ownership was in Texas National. This Court cannot reach any other conclusion, either. Rupe was a broker, a middleman, the conduit between the former owners ... and the new owner. (Wisdom C.J. in Rupe\(^\text{439}\))

For the sake of completeness the following definition of beneficial owner from a legal dictionary,\(^\text{440}\) which is in line with the above, can be added:

Term applied most commonly to cestui que trust who enjoys ownership of the trust or estate in equity, but not legal title which remains in

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\(^{436}\) Montana Catholic Missions v. Missoula County, 200 U.S. 118 (1906), at 128.


\(^{439}\) Rupe Investment Corporation v. Commissioner 3 AFTR 2d 1276 (5th Cir. 1959), at 1280-1281.

trustee or personal representative. Equitable as contrasted with legal owner.

One who does not have title to property but has rights in the property which are the normal incidents of owning the property. The persons for whom a trustee holds title to the property are the beneficial owners of the property, and the trustee has a fiduciary responsibility to them.

In order to formulate a single condensed meaning of beneficial ownership from the above it is necessary to extract the different elements contained therein. First, beneficial ownership can either be with legal ownership or divided therefrom, but mere legal title without the right to deal with the thing to some extent as your own, does not constitute beneficial ownership. Second, the right of beneficial ownership must be recognized by law and able to be enforced by the courts. Third, because the use of beneficial ownership in tax treaties mainly relates to conduit situations, the statements from Leigh Spinners and Rupe were specifically included above. According thereto, where something is acquired subject to the obligation to transfer it to others, such acquisition is not regarded as beneficial ownership. Fourth, the courts and dictionary variously refer to ownership rights, attributes, incidents, or to command and economic benefits, or the benefits and burdens of ownership. For international purposes it seems appropriate to give preference to “attributes”, which has a wide meaning and includes not only rights but also other attributes such as depreciation.\(^\text{441}\) Lastly, there is some uncertainty as to the number or level of ownership attributes to be held in order to constitute beneficial ownership. If it is accepted, however, that there can only be one beneficial owner in respect of a specific thing (see conclusion in 5.8.), it follows that the beneficial owner must be the person whose ownership attributes are more than that of any other person.

It is submitted that the following meaning of beneficial owner, which includes all the elements as identified above, and which should be taken as the starting point for the investigation of the meaning of beneficial owner in terms of Article 31 of the Vienna Convention, can be formulated:

\(^{441}\) For a discussion on how the different views on depreciation in England and the United States can be reconciled, see 4.2.4. and 5.8.
The beneficial owner is the person whose ownership attributes outweigh that of any other person.

Before proceeding with the evaluation of this meaning in the context, object and purpose of bilateral tax treaties, it is necessary to reflect on this meaning. What are the ownership attributes? What is meant by “outweigh”?

The importance of these questions is the fact that the meaning as formulated may be understood differently by persons from different legal backgrounds. From the perspective of the common law states, it is correct to refer to the incidents of ownership as analysed by Honoré in 4.2.4., which include the right to: possess, use, manage, the income, the capital (including the power to alienate and the liberty to consume, waste or destroy), etc. To this list can be added other ownership attributes, more prominent in the United States, such as the risk of depreciation and the hope of appreciation (see 4.3. and 5.3.4.). The Dutch Supreme Court’s (see 6.2.2.) phrase of “could freely avail of the distribution”, together with the fact that the taxpayer in that case also carried the risks in connection with the dividend distribution, aptly summarizes the ownership attributes in respect of the receipt of a payment. As far as the meaning of “outweigh” is concerned, based on the case law above it seems fair to conclude that it is not so much a case of holding the biggest number of attributes but more a case of holding the biggest weight. Both the issues of the identification of the ownership attributes and determining who holds the biggest weight, depends on the specific circumstances (see also the discussion in 5.3.5.). It is submitted that in many instances (formal agency, for example) the identification of the person holding the biggest weight of ownership attributes will be clear and there will therefore be no need for performing a knife edge balancing exercise of the attributes held by the different parties.

Persons from the civil law states may, however, take a different view on the identification and importance of the different ownership attributes. For example, because of the importance of legal title in civil law states, the person to whom a royalty payment is made in terms of an agreement may be viewed as the person holding the most important (if not only) ownership attribute. To the foregoing argument may be added the fact that the recipient of a royalty payment,
also has physical control\textsuperscript{442} thereof, which can be regarded as another strong indication of ownership.

The difference in views between the common law and civil law states is caused mainly by the different ways in which ownership is regarded by the two legal families. Whereas the distinction between legal and beneficial ownership in the common law states amounts to a splitting in ownership (see 5.2.6.), the civil law, generally speaking, does not recognize similar divided ownership. In 5.6. it was explained that the relationship between a legal and economic owner in the Netherlands, at least in the circumstances discussed in that section, is contractual. It does not amount to a splitting in ownership. Maisto explains that, in Italy, the position is traditionally taken that the real rights (which include ownership and usufruct) of enjoyment of an asset are expressly defined and limited by the Civil Code. These are the sole rights of enjoyment which can be enforced against anyone (as opposed to contractual arrangements such as lease agreements which can be enforced only between the contracting parties). Any right of enjoyment other than the ones defined and governed by the Civil Code cannot exist and consequently, could be deemed to be contrary to public policy.\textsuperscript{443} The fact that the majority of civil law states carefully avoided the inclusion of the word “owner” in the translation of beneficial owner into their local languages (see 6.2.12.) is another indication of their strict view that ownership cannot be split.

\textsuperscript{442} The wording “physical control”, instead of “possession”, is used on purpose. The exact legal meaning of “possession” is a difficult question on its own, and include issues such as whether possession is a matter of fact or of law, and whether possession is \textit{prima facie} evidence of ownership. The discussion of these issues fall outside the scope of this study. For a discussion of the topic in England and the Netherlands, see R.W.M. Dias, \textit{Jurisprudence}, 1985, at 272-291 and C. Asser, \textit{Handelideid tot de Beoefening van het Nederlands Burgerlijk Recht: Zakenrecht: Algemeen goederenrecht}, revised by F.H.J. Mijnssen and P. de Haan, 1992, at 92-152.

The word "ownership" therefore appears to be a major stumbling block for the civil law states, making it difficult for them to accept the common law states notion of beneficial ownership.

On the basis of the hypothesis in this study, however, namely that the notion of beneficial owner was taken from the common law states and that the meaning thereof in all states which afford to it the meaning as per the OECD Model should therefore be the same as the meaning in the common law states, it follows that, for international tax purposes, the civil law states must somehow accommodate the approach of the common law states to ownership attributes. The mere fact that civil law states incorporate the notion of beneficial ownership, which is not known in their domestic law, into their treaties, suggest a divergence from their strict domestic view on ownership.\textsuperscript{444} In order to overcome the difficulties caused by the different ways in which ownership is regarded for purposes of domestic law, it is suggested that, rather than looking for (and not finding) a notion similar to beneficial ownership in their domestic law, the civil law states should rather look within their domestic law for rules which achieve the same effect as beneficial ownership, even though the legal basis of those rules may be different from those in the common law states.

Instead of viewing the division between the legal owner and beneficial owner as a split in ownership, the issue should be viewed in the civil law states as a person holding legal title in accordance with the Civil Code, but subject to rights and obligations in respect of another person. The rights of the third party against the person holding legal title are personal and enforceable only against that person, as opposed to rights which can be enforced against the whole world.\textsuperscript{445}

\textsuperscript{444} This statement is made on the assumption that civil law states intend to adopt the notion of beneficial ownership, as opposed to the translated term in their own language. See also 6.2.12. and 6.3.2.4.

\textsuperscript{445} In Dutch legal terminology this falls into the category of an \textit{obligatoire overeenkomst} (an agreement giving rise to obligations to one or both contracting parties), as opposed to a \textit{goederenrechtelijke of zakelijke overeenkomst} (an agreement in connection with the creation, transfer or destruction of an absolute right). See A. Pitlo, \textit{Het systeem van het Nederlandse privaatrecht}, revised by P.H.M. Gerver, et al., 1995, at 310-311.
The approach advocated here is not foreign at all. It is, for example, in line with a decision by the Dutch Supreme Court,\textsuperscript{446} where it was held that “shareholder” should be interpreted to include not only the owner of the shares but also those persons whose legal relationship with the owner is such that the full interest in the shares accrues to them and not the owner. In 5.6, several examples of a distinction between legal ownership and economic “ownership”, which amounts to a contractual relationship, were discussed. Van IJlzinga Veenstra discusses a situation in respect of Dutch domestic dividends tax, which closely relates to the situation of royalties in conduit situations: Where a foreign investor holds shares in the Netherlands via his foreign global custodian and last mentioned’s Dutch sub-custodian, the relationship between the investor and the global custodian is that of agency (lastgeving). Therefore, he continues, the investor is not \textit{zakenrechtelijk} \textsuperscript{447} entitled to the dividend itself, but he has a personal entitlement against the global custodian to pay the dividend on to him.\textsuperscript{448}

In summary: It is submitted that the notion of beneficial ownership in the common law states can be accommodated in the civil law states by taking into account the personal or contractual rights held against the person holding legal title. It is further submitted that the fact that the rights enforced against the person holding legal title are personal, as opposed to rights that can be asserted against the whole world,\textsuperscript{449} makes no real difference for the purpose of determining the

\textsuperscript{446} Hoge Raad, 16 October 1985, No. 23 033, BNB 1986/118. See discussion in 5.6.

\textsuperscript{447} It is difficult to decide on the correct legal translation of \textit{zakenrechtelijk}. It is submitted that the author could also have used the term \textit{goederenrechtelijk}. Both these terms, however, represent absolute rights – rights that can be enforced against the whole world. See Pitlo, \textit{supra} note 445, at 110 and Asser, \textit{supra} note 442, at 1.


\textsuperscript{449} Because terms such as real, absolute, or property rights can have different meanings in different legal jurisdictions, such terminology is not used here. See also \textit{supra} note 147. When dealing with international law it is often better to explain the legal effect of certain rights, instead of giving them names. For a distinction between different types of rights in England and the Netherlands, see 4.2.1. and 4.4.2.
beneficial owner for treaty purposes. This is not a case where the competing interests of vendors, purchasers, possessors or others to a thing are at issue. From a tax treaty perspective the object is to identify the person whose rights (whether they are personal, or rights that can be asserted against the whole world) are greater than that of any other person. In addition, as discussed in 5.2.6.1., the right of beneficial ownership is, in any event, somewhat less than a right that can be asserted against the whole world and is, therefore, a bit nearer to a personal right. Lastly, the fact that beneficial ownership of a royalty means beneficial ownership of a payment (see 4.7.), in other words, a claim to something that is fungible, further diminishes the importance of whether the right is personal or can be asserted against the whole world.

Because of the problems that are caused in the civil law states by the word “owner”, it was thoroughly considered, for purposes of this study, to formulate a meaning of beneficial owner that does not include the word “owner”. The following may be one such possible formulation: The person whose interests, which are regarded as the combination of personal and real/absolute rights, together with and including the benefit of appreciation and the risk of depreciation, outweigh that of any other person. In the end, however, because of the close relationship with the case law explaining the notion of beneficial ownership, it was decided to retain the wording “ownership attributes” in the formulated meaning. Persons from the civil law states may feel uncomfortable with such wording, but, once it is realized that it is derived from the common law states, its meaning should be clear.

It should be noted that there are other examples where a notion incorporated into the OECD Model is intended to have the meaning that it has in the legal family that it was taken from. One such example is the reference to agents in Article 5, dealing with permanent establishments. Paragraph 5 of Article 5 refers to a person having authority to conclude contracts “in the name of” the enterprise. In a detailed article450 on the matter Avery Jones explains that the word-

ing “in the name of” refers to the civil law notion of direct representation (as opposed to indirect representation). No distinctions are made in common law between direct and indirect representation. He then comments as follows:

By using a term of art derived from civil law in the Model there can be no doubt that it was intended to have the civil law meaning. ... The common law reader may be unfamiliar with the terminology “in the name of”, but, once it is understood that it is derived from civil law, the meaning is clear.451

The article continues to discuss the conflict caused by the different meanings of wording used in the English (broker, general commission agent) and French (courtier, d’un commissionnaire général) texts of paragraph 6 of Article 5. By considering the context, particularly the wording of paragraph 5, the historical evolution of paragraph 6 – which is the direct descendant of the 1927 League of Nations draft convention provision which, in turn derived from United Kingdom law, and the difference in meaning between the English and French versions of the OECD Model, it was concluded that, as far as paragraph 6 is concerned, the common law meaning is to be preferred:

We therefore consider that the references to courtier and commissionnaire in the French text should not be interpreted in accordance with internal law in those countries that use the expression in their internal tax law. Something on the lines of the meaning of those expressions in English law should be used to interpret a treaty on the lines of the Model.452

6.3.2.8.2. Context

In terms of Article 31 of the Vienna Convention it is next necessary to consider the meaning of beneficial owner, as formulated above, in the context of the treaty. To begin with, context is defined in Article 31(2) as the text of the treaty, including its preamble and annexes. It is generally accepted that the entire text of the treaty is to be considered – the meaning of a specific provision is understood as soon as it is seen in the light of the entire text.453

451. Id. at 161-162
452. Id. at 178.
453. Vogel and Prokisch, supra note 371, at 68.
Various commentators have commented on the scarcity of light that is thrown on the meaning of beneficial ownership by the context of bilateral treaties which adopted the OECD Model wording. Unlike, for example the Thiel\textsuperscript{455} case in Australia, which investigated the international tax meaning of “enterprise”, and where the court was able to consider the various ways in which the term was used in the treaty, no such help is derived from the treaties in respect of beneficial owner. In treaties, based on the OECD Model, the term is used in a very similar manner in the articles on dividends, interest and royalties. An investigation of the articles on dividends and interest provides no help as to the meaning of the term in the royalties article.

There are, however, at least two observations in respect of the context. The first is that the way the term is used in the royalty article (as indeed, in the dividends and interest articles), obviously suggest a restriction of treaty benefits. Second, in those states where beneficial ownership is not known in domestic law, the fact that such wording is used in the treaty confirm its status as international tax language. With regard to these two observations, the context supports the meaning of beneficial owner as formulated above.

In terms of the Vienna Convention, context further comprises (see the full text of Article 31 above) any agreement and any instrument made in connection with the conclusion of the treaty. Also to be considered together with the context, are any subsequent agreements or practice regarding the interpretation of the treaty and any rules of international law applicable.

The above matters can also be dealt with swiftly and be discarded for purposes of this study. If such information is available, it has not surfaced yet. Neither the commentaries discussed in Part one of this chapter nor the investigation in this study could reveal any such information, at least not for those states (excluding therefore the United States) where beneficial ownership is not seen as a term to which Article 3(2) of the OECD Model should apply.

\textsuperscript{454} For example, Van Weeghel, \textit{supra} note 334, at 70, comments: “A journey undertaken through the treaty landscape to find clues regarding the meaning of the term ‘beneficial owner’ derived from the context leaves the traveller confused.”

\textsuperscript{455} Thiel, \textit{supra} note 383.
As far as subsequent practice is concerned, the forms used (see 6.2.13.) by the different states for taxpayers to prove that they are beneficial owners can maybe be regarded as subsequent practice. On the other hand, bearing in mind the conclusion in 6.2.13. on the lack of clarity of these forms, and the fact that the practice should be clear and agreed upon by all the parties, it is unlikely that the forms meet this requirement. As Sinclair comments: “The value and significance of subsequent practice will naturally depend on the extent to which it is concordant, common and consistent. A practice is a sequence of facts or acts and cannot in general be established by one isolated fact or act or even by several individual applications.”

6.3.2.8.3. Object and purpose

The avoidance of double taxation is often seen as the most important object and purpose of tax treaties. Such object and purpose do not, however, provide any help as to the meaning of beneficial ownership.

Tax treaties also have other objects and purposes, though. One such other object and purpose, which appears in the title of a number of bilateral tax treaties, is that of the prevention of fiscal evasion. At first glance it appears that such purpose of the treaty as a whole could be relevant to beneficial ownership. If one realizes, however, that the reason why it was necessary to incorporate beneficial ownership as a measure to restrict treaty benefits was because the existence of treaties could lead to treaty abuse, it is clear that such a purpose of the treaty as a whole does not, strictly speaking, relate to beneficial ownership. To put it differently: the best way to combat the type of treaty abuse which beneficial ownership is supposed to address, is not to have a treaty at all.

In addition to the purpose of the treaty as a whole, specific provisions may, however, have specific purposes. Vogel states that the purpose of introducing ‘beneficial ownership’ into the OECD Model in 1977 was to help prevent tax avoidance, in that persons not

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456. Quoted by Edwardes-Ker, supra note 367, at 17.01.
457. Edwardes-Ker, supra note 367, at 11.01.
entitled to protection by a particular treaty were to be prevented from obtaining its benefits with the help of interposed persons.459

Even though the purpose as stated by Vogel may not be stated explicitly in treaties, it is hard to dispute the validity of the statement. As was the case with the context, discussed above, such purpose supports the meaning of beneficial ownership as formulated above.

It is important to note, though, that although the incorporation of the beneficial ownership requirement has an anti-avoidance purpose, it does not always result in countering avoidance. The reason for this is the fact that an inquiry into the reasons why a transaction is done in a specific manner, does not form part of the beneficial ownership test.460 Even in a case where a person was interposed in a transaction solely to make use of treaty benefits, those treaty benefits cannot be denied in terms of the beneficial owner requirement if the interposed person holds the majority of the ownership attributes. Although the application of the beneficial ownership test should prevent treaty abuse in the majority of cases, there is no guarantee that this will always be the case. On the other hand, the beneficial ownership test may also prevent treaty benefits in cases where there are no treaty abuse purposes.461 Vogel agrees:

Treaty benefits are thus denied to a third party standing between the obligor and the beneficial owner. This measure has been adopted considering that the go-between may have been inserted into the transaction merely as a “strawman” to cause the artificial application of the treaty. Whether such abuse is actually present in a particular case is irrelevant.462

The fact that there is not always a direct relationship between the results of the beneficial ownership test and the purpose of anti-avoidance, is the result of the OECD (knowingly) opting for the beneficial ownership requirement as a treaty abuse measure, and does not invalidate the ordinary meaning of the term.

459. Vogel, supra note 329, at 561.
460. See also supra note 134, and 6.2.2., 6.2.5., and 6.3.2.2.
461. For further discussion, see 6.3.2.10.
462. Vogel, supra note 329, at 127.
It is, however, necessary to ask the question of whether the purpose of anti-avoidance does not require a wide and purposive approach, in terms of which beneficial ownership is interpreted to also exclude entities interposed for the sole purpose of enjoying treaty benefits, in circumstances where such entities may pass the beneficial ownership test in terms of its meaning in the common law states.\textsuperscript{463} In the view of this study, the aforementioned question should be answered in the negative. "Beneficial owner" is a term with a very specific meaning. It has been described by various commentators as a term of art (under English law).\textsuperscript{464} The fact that the drafters of the OECD Model decided to incorporate the notion of beneficial ownership into the OECD Model, despite the fact that the notion is not known in the domestic law of many of its member states, supports the view that they wanted to incorporate the characteristics as embodied by that notion. As discussed above, there were various options available to the drafters of the OECD Model when they considered an appropriate anti-abuse measure. If they so wished, they could have stated clearly that treaty benefits are not available to entities imposed for the sole purpose of enjoying treaty benefits. Provisions along these lines are well known in the domestic law, and in tax treaties, of various states.

There is no evidence in either the OECD Model, or the MC Commentary that beneficial ownership should be interpreted to have any meaning other than its meaning in the common law states. In terms of that meaning, the reasons why it was decided to do a transaction in a certain manner does not affect the beneficial ownership of the things involved in the transaction.

Another question that arises is whether, against the background of a purposive approach, beneficial ownership should be interpreted differently for international purposes to also exclude situations where a person is under no legal obligation to pay on any royalty received, but the royalty is in fact paid on (see 6.3.2.10.1. for further discussion). The discussion in Chapter 5 clearly shows that beneficial ownership is a question of law. In order to qualify as a right of beneficial ownership, a right must be recognized by law, and able to

\textsuperscript{463} See Baker, \textit{supra} note 333, at 103 and 230, also posing this question.
\textsuperscript{464} See, for example, Baker, \textit{supra} note 333, at 229.
be enforced by the courts. Any attempt to exclude beneficial ownership in situations of mere factual on payment, is a serious divergence from the meaning of the term in the common law states. This study has found no evidence, neither in the OECD Model, nor in the MC Commentary to support such a drastic departure from the meaning in the common law states.

6.3.2.8.4. Special meaning

Article 31(4) of the Vienna Convention provides that a special meaning shall be given to a term if it is established that the parties so intended.465

Edwardes-Ker comments that Article 31(4) should rarely be applied to tax treaties. He points out that a special meaning is the converse of the ordinary meaning to which Article 31(1) refers, and that international tax language is not “special” at all – because it is the ordinary technical language applicable in a tax treaty context.466 It is submitted that this observation applies to beneficial ownership as well.

In 6.3.2.2. it was suggested that beneficial ownership may have a special meaning in certain of the treaties that it was incorporated into before its incorporation into the OECD Model in 1977. Such special meaning, if applicable, would, however, almost certainly also have been based on the meaning in the common law states, and therefore similar to the ordinary meaning advanced in this study. There is therefore no reason for further pursuing a possible special meaning.

6.3.2.8.5. Conclusion

From the above discussion on the different elements of Article 31 of the Vienna Convention it is concluded that the meaning formulated above, as the starting point for the investigation in terms of

465. See, for example, the debate by J.F. Avery Jones and J.D.B. Oliver, “How Others See Us”, British Tax Review 1988/11, at 437, and Peter Sundgren, “Interpretation of Tax Treaties-A Case Study”, British Tax Review 1990/9, at 286, on whether a special meaning should be given to the term “income from a source” (in the United Kingdom-Sweden treaty), which has a particular meaning in English.

466. Edwardes-Ker, supra note 367, at 4.02.
Article 31, can be regarded as the ordinary meaning of beneficial owner, considered in the context of the treaty and in the light of its object and purpose. It is worthwhile repeating that meaning:

The beneficial owner is the person whose ownership attributes outweigh that of any other person.

6.3.2.9. Supplementary means of interpretation

In terms of Article 32 of the Vienna Convention (see full text above) recourse to supplementary means of interpretation is allowed under certain circumstances. On the question of what types of materials are allowed in this category, Edwardes-Ker comments as follow:

Article 32 does not define supplementary means of interpretation – beyond confirming that the preparatory work of a treaty and the circumstances of its conclusions are, in any event, included. The absence of such a definition matters little – because any material which elucidates the meaning of a treaty term will, by definition, be a means of interpretation. It is difficult to avoid the conclusion that, in practice, material must simply aid interpretation in order to rank as a (supplementary) means of interpretation.467

As far as beneficial ownership is concerned there is, apart from the OECD materials, very little information available that could be considered for inclusion as supplementary means of interpretation. For example, neither the commentaries discussed in Part one of this chapter nor the investigation in this study could reveal any preparatory work on the conclusion of any treaty in respect of beneficial ownership. As far as the Netherlands is concerned, for example, Pijl explains that preparatory work is inaccessible – the documents are in the offices of the Ministry and not published.468

In addition to the scarcity of supplementary materials, there is also a debate on whether material such as the MC Commentary, for example, should be regarded as supplementary means of interpreta-

467. Edwardes-Ker, supra note 367, at 21.01.
468. Pijl, supra note 403, at 542.
tion,\textsuperscript{469} whether it forms part of the context or should be taken into account together with the context of the treaty,\textsuperscript{470} or neither.\textsuperscript{471}

It is submitted, however, that if, as is the case with beneficial ownership, the materials available confirm the ordinary meaning as determined in accordance with Article 31 of the Vienna Convention, the argument on the exact status and place of those materials in the interpretation process becomes less relevant.

In terms of Article 32 of the Vienna Convention recourse to supplementary means of interpretation is allowable under two sets of circumstances: first, to confirm the meaning resulting from the application of Article 31 of the Vienna Convention, or second, to determine the meaning if the interpretation according to Article 31 is ambiguous or obscure or leads to manifestly absurd or unreasonable results.

In 6.3.2.10. the ordinary meaning of beneficial ownership as determined in 6.3.2.8.5. is tested by applying it to practical situations where entities are interposed in intermediary states. That discussion shows that, although the determination of the beneficial owner is certainly not always an easy matter, and that the notion of beneficial ownership does not provide an answer to treaty abuse under all circumstances, the ordinary meaning of beneficial owner as determined in this study cannot be regarded as ambiguous or obscure. Neither can it be regarded as leading to manifestly absurd or unreasonable results.

The purpose of discussing any supplementary materials is therefore merely to confirm the ordinary meaning as determined. As mentioned above, the question of whether the OECD materials discussed below can properly be regarded as falling within the ambit of Article 32 of the Vienna Convention is less relevant in the light of the fact that the materials in any event confirm the meaning as determined in accordance with Article 31.

\textsuperscript{469} In support: Edwardes-Ker, \textit{supra} note 367, at 15.04; Avery Jones, \textit{supra} note 371, at 93; McHugh J. in \textit{Thiel}, \textit{supra} note 383, at 542.

\textsuperscript{470} In support: C. van Raad, "Interpretatie van belastingverdragen", \textit{M.B.B.} 1978/2/3, at 55; Pijl, \textit{supra} note 403, at 546; Dawson J. in \textit{Thiel}, \textit{supra} note 383, at 537.

\textsuperscript{471} In support: Prokisch, \textit{supra} note 376, at 105.
6.3.2.9.1. MC Commentary

The MC Commentary on Chapter 1 of the OECD Model, dealing with the scope of the convention, says the following, under the heading: “Improper use of the Convention”:

7. The purpose of double taxation conventions is to promote, by eliminating international double taxation, exchanges of goods and services, and the movement of capital and persons; they should not, however, help tax avoidance or evasion ...

8. ...

9. This [using artificial legal constructions] would be the case, for example, if a person ..., acts through a legal entity created in a State essentially to obtain treaty benefits that would not be available directly ...

10. Some of these situations are dealt with in the Convention, e.g. by the introduction of the concept of “beneficial owner” (in Articles 10, 11 and 12) ...

The quoted passage, which has been unchanged from the 1977 OECD Model, clearly classifies “beneficial owner” as a measure to combat the improper use of bilateral tax treaties. This is in line with the ordinary meaning of beneficial ownership as determined above – any conduit entity holding no (or very few) ownership attributes will not be a beneficial owner and will not qualify for treaty benefits. The fact that (as was explained in 6.3.2.8.3.) there is not always a direct relationship between the results of the beneficial ownership test and the purpose of anti-avoidance, does not invalidate the aforementioned statement. In a majority of cases, the ownership attributes test should effectively counter tax avoidance.

It is next necessary to consider the MC Commentary on Article 12 of the OECD Model, and specifically the often-quoted paragraph 4 thereof, which is considered by many commentators to be the sole indication by the OECD as to the meaning of beneficial ownership:

Under paragraph 1, the exemption from tax in the State of source is not available when an intermediary, such as an agent or nominee, is

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472. The French version of the OECD Model uses the wording intermédiaire, tel qu’un agent ou autre mandataire, which is translated by The Pocket Oxford Hachette French Dictionary, 1996, as “go-between/middleman such as an agent or other representative”.

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interposed between the beneficiary and the payer, unless the beneficial owner is a resident of the other Contracting State.

The first observation is that this passage also supports the ordinary meaning of beneficial ownership as determined above. Agents and nominees are maybe the prime examples of persons holding no (or very little) ownership attributes and who therefore do not qualify as beneficial owners.

But, in order to refute the claims by those maintaining that this passage can be regarded as a full definition of beneficial ownership, and that the only persons excluded from beneficial ownership are (formal) agents or nominees, it is necessary to comment more extensively on the passage.

One argument why the reference to agents or nominees cannot be regarded as a full definition of beneficial ownership, is the fact that, where the meaning derived in accordance with Article 31 of the Vienna Convention is not ambiguous, the MC Commentary, as supplementary material, cannot be used to determine a meaning, but only to confirm it. As indicated in 6.3.2.9. above there is, however, no agreement on the role of the MC Commentary. Especially in the light of the classification of beneficial ownership as international tax language, there may therefore be arguments that the MC Commentary can be used earlier in the interpretation process.

A more compelling argument, though, is the use of the words “such as” in front of “agent” and “nominee”. Webster’s New Dictionary and Thesaurus defines “such as” as “of the same kind as”. In a Canadian case it was held that “the words ‘such as’ are merely

473. It is possible for agents to hold some ownership attributes, such as risk. For example, Clive M. Schmitthoff, Schmitthoff’s Exports Trade: The Law and Practice of International Trade, 1990, at 287, states that under del credere terms, the agent, usually on payment of an additional commission, undertakes to indemnify the principal for any loss sustained through an insolvency of customers introduced by him. On risk, see also H.L.E. Verhagen, Agency in Private International Law: The Hague Convention on the Law Applicable to Agency, 1995, at 6 and 34-35. In addition an agent may hold legal title and may have physical control.

474. See, for example, Romyn, supra note 342; Hinnekens, supra note 353; The French member at the IFA Congress, supra note 356.
illustrative and not excluding".\textsuperscript{475} The reference to "agent" and "nominee" are therefore only illustrative and not excluding.

Further proof of this is obtained from the rest of the 1977 OECD MC Commentary. The words "such as" are used twenty-two times in that Commentary. An investigation into the use of "such as" in other parts of the Commentary reveals that the Commentary uses these words in an illustrative and not exclusive sense. For example, the Commentary on Article 8, dealing with shipping and air transport, mentions that activities auxiliary to shipping and air transport also fall within the provisions of Article 8. The Commentary then continues, in paragraph 11 by saying: "On the other hand, the provision does not cover a clearly separate activity, such as the keeping of a hotel as a separate business" [emphasis added]. It is clear that the reference to a hotel is just an example and that there are many other situations that fall into this category.

What is mentioned after the words "such as" are merely examples of intermediaries that are excluded. "Intermediary" is defined as "a go-between".\textsuperscript{476} As a general way of speaking, the kind of words which intermediary or go-between brings to mind include agent, nominee, representative, administrator, trustee, middleman, broker, employee, proxy, conduit, fiduciary. Depending on the circumstances, any of the aforementioned persons could fall in the category of intermediaries which are excluded from beneficial ownership.

Not only agents and nominees are therefore excluded from beneficial ownership, but all other intermediaries of the same kind, in other words, those not holding the biggest weight of ownership attributes. The reference to agents and nominees should therefore not be used as the starting point of interpretation. The fact that agents and nominees are not beneficial owners is the result of applying the beneficial ownership test. It is an end result and not a starting point.


In summary: This study could find no basis, neither in the text of the MC Commentary nor with reference to the ordinary meaning of beneficial ownership, for the arguments that only (formal) agents and nominees are excluded from beneficial ownership. On the contrary, the investigation has shown that also other persons not holding the biggest weight of ownership attributes are excluded.\textsuperscript{477} This may be the reason why the OECD decided to adopt the notion of beneficial ownership. The focus of the beneficial ownership test is on the extent of ownership attributes held, in other words a test that goes wider than merely investigating whether a formal agency or nominee relationship exists. As mentioned before, if the idea was to exclude only agents and nominees it would have been easy to state so clearly in the wording of the OECD Model and actual bilateral treaties.

The above discussion does not mean that the question of agency is not important for purposes of beneficial ownership. As is discussed in 6.3.2.10.2., in practice, an investigation as to whether an agency or similar relationship exists, may be very relevant as to the question of beneficial ownership.

6.3.2.9.2. OECD Conduit Companies Report

The above report was adopted by the OECD in 1986, in other words, almost ten years after the introduction of beneficial ownership in the OECD Model in 1977. From that point of view, there may be objections to its inclusion under “supplementary means of interpretation”. It is submitted, however, that it is appropriate to discuss it here, because the part quoted below in fact merely explains certain aspects surrounding beneficial ownership. It does not provide any information that did not already apply to beneficial ownership in 1977. Once again, this report confirms the ordinary meaning of beneficial ownership as determined in this study. In part II B of the report, under the heading “Anti-avoidance provisions”, it states as follows:

\textsuperscript{477} See the discussion of court decisions in Chapter 5 of various circumstances where persons were found not to be beneficial owners.
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”.

   a) ...
   b) 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 its “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 ... The Commentaries mention the case of a nominee or agent. The provisions would, 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).

   Apart from the confirmation of beneficial ownership as an anti-avoidance measure, the passage confirms that the notion goes further than just excluding nominees and agents. In addition, the statement that formal owners, holding only narrow powers, are excluded is fully in line with the ordinary meaning of beneficial ownership determined in this study, namely that persons not holding the biggest weight of ownership attributes are excluded. 478

6.3.2.10. Entities interposed in intermediary states

Although the discussion in Chapter 5 has shown that the question of beneficial ownership is also important in other situations, for example between a seller and purchaser when an agreement has been concluded but legal transfer has not taken place yet, it is clear that in bilateral tax treaties it mostly arises in situations where entities are interposed in intermediary states (“conduit entities”). It is therefore relevant to apply the ordinary meaning of beneficial ownership as determined in this study to such situations.

478. See also Vogel, supra note 329, at 563.
As a starting point it is necessary to make a few observations: The ordinary meaning of beneficial ownership as determined in this study, is based on the domestic meaning in the common law states. Based on the cases discussed in Chapter 5, however, the practical situations to which the meaning was applied in those domestic cases, differ from the situation in bilateral tax treaties. It is important to be aware of these differences, because it may play a role in applying the beneficial owner test in tax treaties.

To begin with, the domestic cases on beneficial ownership discussed all dealt with single identifiable assets such as shares, fixed property, machinery, cattle, copyright, etc. In such cases, the question then was which of the different parties should be regarded as the beneficial owner of the specific asset. There could be only one beneficial owner at any given point in time. In bilateral tax treaties, though, the question concerns the beneficial ownership of a royalty payment. It is possible in respect of the same intellectual property, for example, where a licence is granted to one person who, in turn, grants a sub-licence to another, to have more than one royalty payment in respect of the same underlying property. Provided that the sub-licensor does not act in some sort of representative capacity, the royalty received by him is not the same as the royalty paid by him to the intellectual property owner. It is therefore quite possible that the two royalty payments can have separate beneficial owners. In addition, a payment, as least as far as it is in cash, is fungible. This means that, as opposed to the assets named above (which are all identifiable), the cash received (and paid into a bank account) is not necessarily the same as the cash paid out, a factor which may blur the link between what is received and paid out. These aspects, namely that the beneficial ownership test is not applied in bilateral tax treaties to an asset which is always easy to identify, and that there can be more

479. The importance placed by this study of determining whether the payment received is the same as the payment paid on, must not be confused with the method of payment. “Royalty” is defined as “payment” (see 4.7.). From this point of view it is necessary to investigate the extent of ownership attributes held in respect of the payment received. On the other hand, the questions of whether the same money received is paid on, or whether it is paid on by the same method of payment, do not, in themselves, determine beneficial ownership – it is merely a matter of the method of payment and does not determine the question of whether a person can freely avail of the payment received.
than one beneficial owner of royalty payments in respect of the same underlying property, makes it more difficult to apply the test in bilateral tax treaties. Put differently, the fact that the thing which is the object of the beneficial ownership test is a “payment” makes it more difficult to apply the beneficial ownership test.

Another difference is that most of the assets named above, for example fixed property and shares, are officially registered in the name of some person. It is therefore appropriate to refer to a nominee, for example, as the legal owner and some other person as the beneficial owner. Payments or money, on the other hand, are not registered in the name of any person. It may be paid into his bank account, or he may have physical control or possession of it, but whether it is correct to call an agent, who is legally entitled to receive and hold money on behalf of someone else, the legal owner of the money, is uncertain. This issue may not be very important—the importance may be mainly with respect to the correct manner of speaking. On the other hand, the fact that a payment is not legally registered in the name of the person receiving it may make it easier for civil law states to accept that it is beneficially owned by someone else.

An appropriate way of testing the ordinary meaning of beneficial ownership, is by way of case studies. The two cases below highlight some of the aspects of the beneficial ownership test.480

Case A: A resident of state X, beneficial owner of a patent, licenses it out to an independent person, a resident of state Y, for a period of five years. The royalty is determined as a fixed percentage of sales, but with a minimum royalty payable per year. The resident in state Y, after exploiting the patent for two years, decides to terminate his manufacturing activities. Because he is contractually obliged to pay a minimum royalty for the remaining three years, he sub-licenses the patent rights to a resident in state Z. He does not want to make a profit on the deal. He merely wants to cover his own obligations. He therefore determines the royalty in terms of the sub-licence to be equal to his minimum royalty obligation and pays over

480. In the examples throughout this section, X is used for the state of the intellectual property owner, Y for the intermediary state, and Z for the state of the person exploiting the intellectual property right.
the exact amount that he receives from the resident in state Z to the resident in state X.

Case B: The same three states are involved and all the parties are independent. The person in state Z will commercially exploit the patent in that state. The person in state Y has specifically been involved to make use of the tax benefits in the bilateral treaties between states X and Y, and states Y and Z. There is a written agreement among the three parties, involving a licence from X to Y, and a sub-licence from Y to Z. The royalties payable by the person in state Z are calculated as a fixed percentage of turnover, subject to a minimum payment per year. The conduit entity in state Y is not subject to the minimum payment. It merely has to pay over to the patent owner in state X whatever it receives from state Z. The conduit entity is entitled to an amount calculated as 2% of the value of the royalties received from the person in state Z. The person in state Z will quarterly issue a cheque for the full amount of the royalties to the conduit entity, who will endorse it in favour of the patent owner in state X. The amount owed to the conduit entity will be paid to him by direct bank transfer from the patent owner.

In order to determine whether the parties in state Y in Case A and Case B are the beneficial owners of the royalties received from state Z, it is relevant to restate the ordinary meaning of the term:

The beneficial owner is the person whose ownership attributes outweigh that of any other person.

Case A: It is submitted that the person in state Y is the beneficial owner of the royalty payment from state Z because he holds all the ownership attributes in respect of that payment. The fact that he pays an equal amount to the patent owner in state X does not change the fact that he is the beneficial owner. The point is that he is under no legal obligation to pay on the specific payment received to someone else. This illustrates an important factor in respect of beneficial ownership in bilateral tax treaties: the focus is on whether a person holds the biggest weight of ownership attributes in respect of the payment received, or, to use the words of the Dutch Supreme Court (see 6.2.2.), whether he could freely avail of the payment received. If this question is answered in the affirmative, then it is not relevant that he uses the money received to pay a debt directly relating to that
income. In this case the person in state Y was under no obligation to pay the patent owner with the royalty income from state Z. He could have used money from other sources to pay the patent owner. As far as the royalty payment from state Z is concerned, he could freely avail of the money received. He could have invested the money, spent it, kept it, donated it or destroyed it. He bore the full risk in respect of currency and the insolvency of the party in state Z. In practice just about every business has to use the biggest part of its income to defray its expenses. Often (if not mostly) the income received is directly related to the expenses paid – the car dealer has to use his income from car sales to pay for car purchases, the sub-licensor uses his income from sub-licensing to pay his licensor, etc. This direct relationship, in itself, does not mean that the car dealer, sub-licensor, etc. is not the beneficial owner of the money received. It is only when he does not hold the biggest weight of ownership attributes in respect of the payment received – where it is acquired subject to the legal obligation to transfer it to others481 (as is the situation in Case B below), that he is not the beneficial owner.

It is submitted that the above analysis is the basis on which the decision in the Royal Dutch Oil dividends case (see 6.2.2.) should be viewed. The comment is often made that the stockbroker in that case probably used the full dividend distribution to defray his debt in respect of the acquisition of the dividend coupons. Assuming this is correct, it does not change the fact that he was under no legal obligation to deal with the distribution in that way. He could have used any other money to defray his debt. His creditor did not have an enforceable right against him to claim the specific payment received. Had he, however, ceded the dividend coupons, and consequently the payment, to his creditor, it is submitted that he would not have been the beneficial owner.

481. Several of the cases discussed in Chapter 5 confirm that the moment there is an obligation to transfer to someone else, beneficial ownership is lost. See, for example, Lysaght v. Edwards, Parway Estates, Leigh Spinners and Holmleigh (Holdings) in 5.2.4. For further support on the importance of a direct obligation to pass the income on, to the issue of beneficial ownership, see IBFD, “Further Attacks on Treaty Shopping”, European Taxation 1981/5-6, at 150; Romyn, supra note 342 at 319 (last sentence); and Nederlandse Regelingen van Internationaal Belastingrecht, IIB, Groot-Brittannië en Noord-Ierland, loose-leaf, at paragraph 10.
Contrary to the criticism by others,\textsuperscript{482} this study therefore supports the statement by the Dutch Underminister (see 6.2.2.) that a person cannot be considered the beneficial owner if he is contractually obliged to pay the largest part of the income to third parties. This study also does not agree with the conclusion that the decision in the \textit{Royal Dutch Oil} dividends case negates the aforementioned statement.\textsuperscript{483} In the last mentioned case there was no obligation to pay the dividends on.

\textit{Case B}: It is submitted that the person in state Y is not the beneficial owner of the royalty payment from state Z because he does not hold the biggest weight of ownership attributes in respect of that payment. Although he is legally entitled to receive the cheque and to have physical control over it for awhile, he is under an obligation to endorse the cheque in favour of the patent owner. From the moment of acquisition of the cheque, he is under the obligation to transfer it. At no stage can he deal with the payment or money as his own. He cannot invest, spent, donate or destroy the money received. In the words of Harman L.J. in \textit{Wood Preservation}: he is tied hand and foot (see 5.2.2.). Importantly, he bears no risk in respect of the payment from state Z. He simply has to endorse the cheque. He receives his 2\% compensation regardless of any risk that may be attached to the cashing of the cheque.

In agreement with the discussion in 4.7., the above analyses focused only on the ownership attributes in respect of the payments, and not on those in respect of the underlying property and licences. An investigation into the right to receive payment confirms the conclusions above. In both Case A and Case B, the person in state Y had the right to receive payment. In Case A, however, the person could freely deal with that right. He could, for example, cede it to someone else. He was the beneficial owner of the right. In Case B, on the other hand, the person was in no position to freely deal with that right and was therefore not the beneficial owner thereof. It can lastly be observed that also an investigation into the ownership attributes

\textsuperscript{482} See Van Brunschot, \textit{supra} note 341.
\textsuperscript{483} See Van Brunschot, \textit{supra} note 341.
of the licences confirm the conclusion in respect of the payments. In Case A the person in state $Y$ was free to decide whether to exploit the patent rights himself or to sub-license them out, who to license them out to, for what period, and at which terms. In Case B, on the other hand, the person in state $Y$ had no say in any of these issues.

There are other observations on the above case studies. The first is that the amount of royalties paid, compared to the amount received, is not, in itself, conclusive of beneficial ownership. In Case A the two amounts were the same and still the person in state $Y$ was found to be the beneficial owner. In Case B the person in state $Y$ was entitled to a portion of the royalty received, but was found not to be the beneficial owner.

A next observation is that, as has been stressed at various places in this study, only the beneficial ownership test was applied to the cases above and no other tests, for example the reasons why the conduit entity was used, were applied. The reasons why a transaction is done in a certain manner is not part of the beneficial ownership test, even though the beneficial ownership test in Case B above did manage to exclude treaty benefits from an entity who had been used solely to make use of the treaty benefits. There is, however, no guarantee that the beneficial ownership test will always manage to exclude benefits from such entities. In addition, the opposite is also true – the beneficial ownership test can also exclude treaty benefits in circumstances where no treaty abuse was intended (see also 6.3.2.8.3.). For example, say in Case A above, the person exploiting the patent rights in state $Z$ has issued bank guaranteed promissory notes in respect of the royalty payments over the remaining three years, and those promissory notes were endorsed by the sub-licensor in state $Y$ in favour of the patent owner in state $X$. It is submitted that under these circumstances the person in state $Y$ has lost his ability to freely avail over the payment and consequently, has lost his beneficial ownership.

484. In 4.7. it was concluded that an investigation into the ownership attributes in respect of the licences may provide some help as to the beneficial ownership of the payments, but that such investigation should not be conclusive.

485. See supra note 134, and 6.2.2., 6.2.5., 6.3.2.2., and 6.3.2.8.3.
In Case B above, factors such as the three-party agreement, and that payment took place by cheques which were endorsed, made it relatively easy to apply the test of ownership attributes and to conclude that the person in state Y is not the beneficial owner. In practice, though, there are an endless variety of circumstances under which royalty payments can be made and the facts may be quite different. For example, any or all of the following circumstances may be present: there are two separate agreements (between X and Y, and Y and Z) instead of a three-party agreement; payment takes place per bank transfer or cash, in other words, the direct link or identification between the incoming and outgoing streams is broken; the obligation of the person in state Y to pay is at an earlier date than the date on which he will receive payment.

There is another problematic factor that should be mentioned. In practice, where a royalty payment takes place between two states, it is the revenue authorities in the source state who have to determine the beneficial owner in the residence state. Various commentators have commented on how difficult and burdensome this exercise may be. It speaks for itself that it may in practice be very hard for the source state to uncover all the agreements between the parties and to determine the real nature of the relationship between them.

Although the factors as described in the above two paragraphs may make it more difficult, it is submitted that, where all the parties involved are unrelated, the ownership attributes test should always be able to identify the beneficial owner, provided all the information on the relationship between them are available. Unrelated parties should always make sure that respective rights and obligations are precisely spelled out, in order to cater for a situation where things go wrong. Even in the circumstances as explained above, where the link between the incoming and outgoing streams are blurred, the question of risk provides important information as to beneficial ownership. What happens if the last person in the royalty chain does not perform? If that risk of non-performance is not carried by the

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486. See, for example, D. Lüthi, “Countering the abuse of tax treaties – A Swiss view”, Interfax 1989/8-9, at 336; OECD Conduit Companies Report, at paragraph 14(b).
next person in the chain, it would be very hard for such person to prove that he is the beneficial owner.

There are circumstances, though, where it may be difficult to decide who holds the biggest weight of ownership attributes, even between unrelated parties. One such example may be where a person is legally bound to pay on a royalty received (and consequently loses his ability to freely avail over that payment), but still carries the risk of non-performance by his sub-licensee.

6.3.2.10.1. Group situations

Probably the most difficult situations in which to identify the beneficial owner are where all the entities in the royalty chain are from the same group. There is, in principle, no reason why the company in the middle of a group situation cannot hold the biggest weight of ownership attributes. The fact that such a company can be a beneficial owner, is acknowledged by the OECD.\(^{487}\) In paragraph 7 of the MC Commentary on Article 12, the OECD draws attention to the fact that all the shares in a company who is the beneficial owner, may be held by shareholders in another state, and requests members to consider whether it is justifiable to provide treaty benefits to the beneficial owner under these circumstances. In paragraph 14(b) of the OECD Conduit Companies Report it is stated that the fact that its main function is to hold assets or rights is not sufficient to categorize a company as a mere intermediary, although this may indicate that further examination is necessary.

The difficult question is to determine the extent of the ownership attributes held by the subsidiary. One moves into the problematic area of the nature of the relationship between a holding company and its subsidiary. The question is whether the control of a holding company over its subsidiary can be seen as a situation which places a legal obligation on the latter to pay on all royalties received, and consequently deprives the latter of the ownership attributes in respect of the receipt. The uncertainty which surrounds group situations is evident from the following statement by Vogel: “If the com-

\(^{487}\) For further support, see IBFD, \textit{supra} note 332, at 150; Vogel, \textit{supra} note 329, at 563.
pany is bound by a controlling shareholder’s decision on what should be done with certain assets and the yields they generate, its ownership may be formal, but this depends on factual situations.

The same sentiments are present in the following statement by Baker, which is described in 6.2.1. as an apt summary of the main issue surrounding the international tax meaning of beneficial ownership: “It remains open whether a company under the control of a resident of another Contracting State – and therefore likely (though not legally obliged) to pay to its ultimate owner any sums received – could be regarded as beneficial owner of the dividends it receives.”

The problem is that factors such as the extent to which the company in the middle can freely avail over payments received, or which party carries the risk, are often not stated clearly in agreements between group companies. From a group point of view, these factors are probably not very important. Even where these factors are clearly spelled out, it can be changed at any later stage by the group. The fact is that the type of legal stipulations that any unrelated party would insist on being incorporated in the agreements between the parties, are not needed in group situations. There is no need for a holding company to legally bind its subsidiary by means of an agreement to pay on all royalties received. The holding company can achieve the same effect by means of its control over the subsidiary. The question then arises as to how this control affects beneficial ownership.

Based on the analysis of cases in Chapter 5, this study supports the view that beneficial ownership is a question of law. Beneficial ownership, in terms of its meaning in the common law states, represents a form of ownership. The right of beneficial ownership is a right that can be asserted against (almost) the whole world (see 5.2.6.1.). The case law discussed has shown that in order to qualify as a right of beneficial ownership, a right must be recognized by law, and be able to be enforced by the courts. This study has found no

488. Vogel, supra note 329, at 563.
490. See discussion 6.3.2.8.1. on how to reconcile the common law and civil law views on split ownership.
evidence, neither in the OECD Model nor in the MC Commentary, to support a different meaning for international purposes, namely that beneficial ownership is excluded not only where a person is under a legal obligation to pay on a royalty but also where it is paid on in fact and in the absence of a legal obligation.\textsuperscript{491} The question is therefore not whether a royalty is in fact paid on to a next person, but whether there is a legal obligation to pay it on. If this principle is applied strictly to group situations, then, in the absence of an agreement in terms of which the company in the intermediary state is obliged to pay on the royalty received, (and if it can also be argued that the company bears the risk of non-payment by its sub-licensee), that company is the beneficial owner even though it may have very little substance. Such a result may come as a surprise, and may even be considered an unreasonable result. On the other hand, if the total control of the holding company over its subsidiary is seen as a situation which places the holding company in the legal position to compel the subsidiary to deal with its assets as dictated by the holding company, then the subsidiary is not the beneficial owner.\textsuperscript{492} One also enters the difficult area of whether it is a case of lifting the corporate veil. Pennycuick J., in \textit{Rodwell Securities} (see 5.2.4.), held that a holding company may well have a controlling interest right down the line, but does not own any of the assets of its subsidiaries. Dickson J., delivering the dissenting judgement in \textit{Jodrey} (see 5.5.), strongly emphasized that the concepts of control and ownership should not be confused. He also stated that the creation of power over property does not in any way vest the property in the person holding the power, though the exercise of the power may do so. As far as tax treaties are concerned, the question that arises is whether the fact that the holding company has used its control to compel the subsidiary to pay the royalties on to it can be seen as an exercise of power that vested the beneficial ownership in the holding company?

\textsuperscript{491} Vogel, on the other hand, states that the fetters that exclude beneficial ownership may be legal or merely factual – see \textit{supra} note 330.

\textsuperscript{492} This was the decision of the Supreme Court of Canada in \textit{Jodrey} – see \textit{supra} note 301.
6.3.2.10.2. Agency

In order to provide answers in group and other problematic situations, it is appropriate to turn to the question of agency or other representation. In 6.3.2.9.1. it was concluded that a formal agency agreement is not a prerequisite for exclusion from beneficial ownership. All other persons, who may be called by many different names, who act in a similar representative capacity, and whose weight of ownership attributes held is less than that of another person (the beneficial owner) are excluded. Even though the application of the ownership attributes test does not, in the first place, involve an investigation as to whether an agency or other representative relationship is present, it follows that if it can be proven that such relationship does exist, it is conclusive evidence that such person is not a beneficial owner. It is submitted that in the majority of cases the question of whether a person is a beneficial owner is the converse of the question whether that person acts in an agency or other representative capacity. Support for the aforementioned statement comes from the Dutch Supreme Court who, in the Royal Dutch Oil dividends case (see 6.2.2.) supported its finding that the stockbroker was the beneficial owner by pointing out that he did not act as voluntary agent or for the account of the principal.

Therefore, in cases where it is problematic to identify the beneficial owner by means of the ownership attributes test, it may be appropriate to investigate the case from the opposite direction, i.e. to see whether an agency or other representative relationship exist. As is seen from the discussion below, there are many similarities between the two tests, at least as far as group situations are concerned.

A closer investigation into the characteristics of agency or other representation is therefore necessary, although a full discussion of this difficult topic is beyond the scope of this study. The rules and characteristics of agency may differ among the legal jurisdictions of different states. Special caution should be exercised when translating terms used for certain types of representation in other states.
Some of these terms, such as the French *commissionnaire*\(^493\) or the Dutch *lasthebber*\(^494\) may not have the same meaning as the English (common law) agent. Judging by the results of a comparative survey of agency by Verhagen,\(^495\) however, there are important similarities on the general notion of agency and representation internationally:

**At 1:**
The essential characteristic of agency agreements is that pursuant to such agreements one person acts *on behalf of* another person.

**At 6:**
The normal legal consequences triggered by the mechanisms of agency and representation are that the rights and obligations arising under the transaction concluded by the agent are automatically attributed to the principal. The agent, on the other hand, usually (though by no means always) incurs neither rights nor liabilities.

**At 10:**
The essential legal characteristic of agency/representation found in both civil law and common law jurisdictions could therefore be said to be that the agent has the power to create direct legal relationships between his principal and third parties.

It is noteworthy that agency or other representative relationships are not uncommon to dealings with intellectual property. The existence of collecting societies for copyright, acting as a link between music “producers” and music “consumers” is an example of this. As explained by Bainbridge, in England a proprietor of a hairdressing salon can obtain a licence from the Performing Right Society (PRS) to be able to play music to the shop’s clients. The PRS operates by taking an assignment of the copyright in the performance and broadcasting of musical works, administering that copyright, collecting

\(^{493}\) Schmitthoff, *supra* note 473, at 293, describes a *commissionnaire* as a person who internally, i.e. in his relationship to his principal, is an agent but externally, i.e. in his relationship to the third party, is a seller in his own name.

\(^{494}\) Van Weeghel, *supra* note 334, translates *lasthebber* as “acting for the account of the principal”. The *Van Dale* dictionary, 1992, describes *lastgeving* as order, agency, mandate. Article 7.414 of the BW defines *lastgeving* as the agreement of authority whereby one party, the *lasthebber*, binds himself to perform one or more legal actions for the account of the other party, the *lastgever*.

\(^{495}\) Verhagen, *supra* note 473.

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fees and distributing them amongst its members. WIPO states that the legal position of the collective administration organization is that of the trustee of authors and publishers.

As far as the issue of beneficial ownership, especially in group situations, is concerned, the important questions regarding agency or other representative relationships include the following: Do such relationships only exist where there is a formal agreement to that effect or can it also be inferred from the circumstances, for example, where the control of one person over another is so big that the latter is not in a position to make any decisions of its own? Does there have to be an intent to act as an agent or representative? Is a formal agreement which indicates the parties respectively as licensor and licensee conclusive as to the question of whether subsequent income received by the licensee from sub-licensing is received for his own account or as agent or representative of the licensor? Is the relationship between a holding company and its subsidiaries one of agency or other representation?

It appears that, at least in the common law states, it is possible to infer an agency relationship from the circumstances. The Rupe case in the United States, discussed more fully above (see 5.3.5.), is such an example. In terms of the headnote to this case, the findings significant to hold the taxpayer an agent rather than a principal were first, that the taxpayer’s buyer supplied it with funds for original purchase without requiring interest until maturity date, and second, that the taxpayer’s purchase terms were set by its buyer. The Canadian Revenue Department has stated that: “Although an agency relationship is usually supported by a written agreement to that effect, such a contract may be implied. An implied agency relation-

497. WIPO, supra note 496, at 530.
498. For more examples of cases, see United States Tax Reporter, Volume 3, 1997, at 13,387.
ship may be found to exist where the conduct of the parties shows an intention to create an agency."

In 5.5. the Canadian cases\textsuperscript{500} of \textit{Cowan} and \textit{Jodrey}, concerning the question of whether a holding company can be regarded as the beneficial owner of the assets of its subsidiary, were discussed in detail. It was concluded in 5.5. that, although it was not explicitly stated as such, based on the reasoning in those cases it seems fair to conclude that the reason for finding that the assets of the subsidiary were beneficially owned by the holding company, was because the former acted in some form of representative capacity for the latter. In \textit{Jodrey}, Martland J. said the following on the relationship between the companies:

Both of them had the same directors. Both had the same officers. This is eminently a case in which the Court should examine the realities of the situation and conclude that the subsidiary company was bound hand and foot to the parent company and had to do whatever its parent said. It was a mere conduit pipe linking the parent company to the estate.\textsuperscript{501}

Regarding England, Gower mentions that there is no presumption of any agency relationship between a holding company and its subsidiary and in the absence of an express agreement between the parties it is difficult to establish one. While it may be possible to establish that in particular transactions a subsidiary has acted as the authorized agent of its parent (or vice versa), any prospect of establishing that it has general authority to carry on the latter’s business is remote.\textsuperscript{502} Sealy states that agency must be shown on the evidence to


\textsuperscript{500} See Van Weeghel, \textit{supra} note 334, at 71-72 for a discussion of the agency relationship between corporations and their shareholders in the United States.

\textsuperscript{501} \textit{Jodrey, supra} note 298, at paragraph 53-54.


\textsuperscript{503} L.S. Sealy, \textit{Cases and materials in company law}, 1985, at 51.
exist and may not be inferred merely from control of a company or ownership of its shares.\textsuperscript{503}

It is important to note that the suggestion that a relationship of agency or other representation may under certain circumstances exist between a holding company and its subsidiary, does not amount to the lifting of the corporate veil.\textsuperscript{504} Gower comments that a case of establishing that a company is an authorized agent of its controllers or members is not a true example of lifting the veil. The separate personality of the company is not denied, but the practical effect on the parties’ rights and liabilities is the same as if it had been.\textsuperscript{515} Schreurs, also discussing the position in England, points out that if the corporate veil is lifted there is in effect a unification (\textit{vereenzelving}) between the subsidiary and the holding company, whereas the separate legal personality of the subsidiary is preserved by applying the agency construction. The existence of an agency affirms that the subsidiary, being capable of acting as an agent, is a separate person.\textsuperscript{506} Where a holding company has, in terms of a formal agreement, appointed its subsidiary as its agent, this contractual relationship between the parties does not amount to lifting of the corporate veil. Similarly, when an agency or other representative relationship is implied between the parties it is in the nature of a contractual relationship and does not amount to the lifting of the corporate veil.

The issue of whether the nature of the relationship between a holding company and its subsidiary is that of agency, is also the topic of an ongoing debate in the Netherlands. Struycken, in support of the view that such a relationship does exist, concedes that the relationship between the holding company and subsidiary is not the result of an agency agreement (\textit{lastgevingsovereenkomst}), but sub-

\textsuperscript{504} In support: Martland J. in Jodrey, supra note 298, at paragraph 46, discussed in 5.5.

\textsuperscript{505} Gower, supra note 502, at 133. According to Gower, a true example of lifting the veil is when the court is satisfied that a company is a “mere façade” concealing the true facts.

\textsuperscript{506} J.A.W. Schreurs, “Agency”, in L.G.H.J. Houwen, A.P. Schoonbrood-Wessels and J.A.W. Schreurs, \textit{Aansprakelijkheid in Concernverhoudingen}, 1993, at 661-662. Scheurs mentions, however, that not everyone is making this distinction between the two situations.
mits that the legal relationship between the two companies is by its nature that of agency \textit{(lastgevingsverhouding)}. He calls the subsidiary the manager \textit{(zetbaas)} of the holding company.\textsuperscript{507} The aforementioned view by Struycken is, however, disputed by Kortmann and Struycken, Jr.\textsuperscript{508} Kortmann comments that Schreurs’s view is neither in agreement with the notion of agency \textit{(lastgevingsbegrip)}, nor with the legal conception of the company as legal entity. A company acts for its own account and risk.\textsuperscript{509}

As was stated in the beginning of this section, a full investigation into agency is beyond the scope of this study. There are, however, at least two conclusions from the above discussion. The first is that, at least in the legal jurisdictions of some states, it may be possible to regard a subsidiary as an agent or other representative of the holding company with respect to specific transactions. Secondly, however, it is very difficult to determine clear rules for the exact cut-off point when the control of a holding company over its subsidiary changes to an agency relationship. It is hard to determine the circumstances under which it can be said that the subsidiary is receiving a royalty payment on behalf of its holding company.

As was the conclusion above in applying the ownership attributes test, the conclusion is similar when applying the agency construction, namely that neither test is easy to apply in group situations and subsequently neither test can be regarded as a certain and effective way of determining the beneficial owner in group situations.


Although the above conclusion, that the beneficial ownership test is not an easy and effective test to apply in group situations, is somewhat disappointing, it does not come as a complete surprise. The OECD is actually quite open about the fact that the notion of beneficial ownership does not provide a solution for all conduit situations. The use of phrases such as “Model provisions precluding in certain cases persons not entitled ... from obtaining its benefits [emphasis added]” (paragraph 14) and “whether the absence of an overall solution to the conduit problem was at the time a serious flaw in the 1977 OECD Model” (paragraph 16) in the OECD Conduit Companies Report, is acknowledgement of this. The fact that the aforementioned report then deals with specific clauses which treaty negotiators might consider when searching for a solution to specific cases, further confirms acceptance of the fact that the beneficial ownership test, either because of the legal nature of the test or the practical difficulties to apply it across borders, does not solve all the conduit problems. The specific clauses discussed in part III of the OECD Conduit Companies Report are:

- the look-through approach, in terms of which treaty benefits are allowed to a company only insofar as the company is owned by residents of the state of which the company is a resident;
- the exclusion approach, in terms of which tax-exempt companies are excluded from the scope of the treaty;
- the subject-to-tax approach, in terms of which treaty benefits in the state of source are granted only if the respective income is subject to tax in the state of residence;
- the channel approach, in terms of which treaty benefits are denied to a company which is controlled by persons not resident in the company’s state of residence if more than a stipulated percentage of the income of the company is channelled to the persons controlling.

6.4. CONCLUSION

As conclusion to this chapter it is necessary to reflect on the hypothesis as stated in 6.3.2.1.
In the absence of a detailed multilateral tax treaty covering all the nations of the world, there is little chance that any view on treaty matters which purports to be the answer that should be applied to all individual bilateral tax treaties will go unchallenged. This is also true as far as the meaning of beneficial ownership is concerned. Because of factors such as the lack of guidance in the OECD Model and MC Commentary as to its meaning, the fact that it is not known in the domestic law of many states, the different opinions on the application of Article 3(2) of the OECD Model, the way the term is translated into different languages, and the different views on ownership in the common law and civil law states, there is a lot of scope for different opinions.

The conclusion reached in this chapter is, however, the result of closely following the steps for interpretation as prescribed by the Vienna Convention, which is widely accepted as a codification of already valid customary law which governs all international treaties. It is further submitted that the answer reached is reasonable and makes sense against the background of the purpose of the introduction of beneficial ownership into the OECD Model. The problem that revenue authorities are faced with as far as conduit entities are concerned, is that the formal or legal recipient of a payment may not be the beneficial owner of the payment. Against this background the adoption of the notion of beneficial ownership makes sense, because it represents a method of identifying someone other than the formal or legal owner as the beneficial owner. The meaning as established in this study can be applied in both common law and civil law states. The fact that the beneficial ownership test is not easy to apply and effective in respect of all treaty abuse conduit situations does not take away from the meaning as determined in this study. Treaty abuse, and the role of conduit entities in such abuse, is a complicated area and, as acknowledged by the OECD by its discussion of various other anti-abuse measures, there is little chance that any one test will solve all the problems.

As far as the hypothesis is concerned, it is submitted that there is sufficient evidence that the notion of beneficial ownership in the OECD Model was taken from the common law states. There are also strong arguments that the meaning of the term in bilateral treaties of those states who have taken over the wording of the OECD Model
without adaptation or reservation, should be the same as the meaning in the common law states. By applying the rules of interpretation as prescribed by the Vienna Convention this study emphasized the importance of giving effect to the textual meaning of the wording. The context, purpose and object of the treaty as a whole, as well as supplementary means of interpretation, has confirmed the international tax meaning:

The beneficial owner is the person whose ownership attributes outweigh that of any other person.
The conclusion reached in this chapter is, however, the result of closely following the steps for interpretation as prescribed by the Vienna Convention, which is widely accepted as a codification of already valid customary law which governs all international treaties. It is further submitted that the answer reached is reasonable and makes sense against the background of the purpose of the introduction of beneficial ownership into the OECD Model. The problem that revenue authorities are faced with as far as conduit entities are concerned, i.e., that the formal or legal recipient of a payment may not be the beneficial owner of the payment. Against this background the adoption of the notion of beneficial ownership makes sense because it represents a method of identifying someone other than the formal or legal owner as the beneficial owner. The meaning as established in this study can be applied in both common law and civil law states.

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