NEW ARTICLE 28 (SUBSEQUENT CHANGES IN LAW:

Article 28

SUBSEQUENT CHANGES IN LAW

1. If at any time after the signing of this Convention, the general rate of company tax applicable in either Contracting State falls below 15 percent with respect to substantially all of the income of resident companies, or either Contracting State provides an exemption from taxation to resident companies for substantially all foreign source income (including interest and royalties), the provisions of Articles 10 (Dividends), 11 (Interest), 12 (Royalties) and 21 (Other Income) may cease to have effect pursuant to paragraph 4 of this Article for payments to companies resident in both Contracting States.

2. If at any time after the signing of this Convention, the highest marginal rate of individual tax applicable in either Contracting State falls below 15 percent with respect to substantially all income of resident individuals, or either Contracting State provides an exemption from taxation to resident individuals for substantially all foreign source income (including interest and royalties), the provisions of Articles 10, 11, 12 and 21 may cease to have effect pursuant to paragraph 4 of this Article for payments to individuals resident in either Contracting State.

3. For purposes of this Article:

   a) the allowance of generally available deductions based on a percentage of what otherwise would be taxable income, or other similar mechanisms to achieve a reduction in the overall rate of tax, shall be taken into account for purposes of determining the general rate of company tax or the highest marginal rate of individual tax, as appropriate; and

   b) a tax that applies to a company only upon a distribution by such company, or that applies to shareholders, shall not be taken into account in determining the general rate of company tax.

4. If the provisions of either paragraph 1 or paragraph 2 of this Article are satisfied by changes in law in one of the Contracting States, the other Contracting State may notify the first-mentioned Contracting State through diplomatic channels that it will cease to apply the provisions of Articles 10, 11, 12 and 21. In such case, the provisions of such Articles shall cease to have effect in both Contracting States with respect to payments to resident individuals or companies, as appropriate, six months after the date of such written notification, and the Contracting States shall consult with a view to concluding amendments to this Convention to restore an appropriate allocation of taxing rights.

TECHNICAL EXPLANTATION:

The negotiation of the Convention took into account the desire of the two Contracting States to allocate taxing rights between them in a manner that would alleviate double taxation that could otherwise result if cross-border income, profit or gain were taxed under the domestic laws of the two Contracting States. The Contracting States recognize that certain subsequent changes to the domestic laws of one or both of the Contracting States that lower taxation could reduce the risk of double taxation but in addition increase the risk that the Convention would give rise to unwanted instances of low or no taxation. In addition, such subsequent changes in law could draw into question the continued appropriateness of the allocation of taxing rights that was originally negotiated in the Convention.

Article 28 addresses this possibility by providing that if, at any time after the signing of the Convention, either Contracting State enacts certain changes to domestic law that could implicate the terms of the Convention, certain benefits of the Convention may cease to have effect, and if so the Contracting States shall consult with a view to amending the Convention in a way that would restore an appropriate allocation of taxing rights.

Article 28 is consistent with the tax policy considerations that are relevant to the decision to enter into a tax treaty, or to amend an existing tax treaty, as articulated by the Commentary to the OECD Model, as amended by the Base Erosion and Profits Shifting initiative. In particular, paragraph 15.2 of the introduction of the OECD Model now provides:

> Since a main objective of tax treaties is the avoidance of double taxation in order to reduce tax obstacles to cross-border services, trade and investment, the existence of risks of double taxation resulting from the interaction of the tax systems of the two States involved will be the primary tax policy concern. Such risks of double taxation will generally be more important where there is a significant level of existing or projected cross-border trade and investment between two States. Most of the provisions of tax treaties seek to alleviate double taxation by allocating taxing rights between two States and it is assumed that where a State accepts treaty provisions that restrict its right to tax elements of income, it generally does so on the understanding that these elements of income are taxable in the other State. Where a State levies no or low income taxes, other States should consider whether there are risks of double taxation that would justify, by themselves, a tax treaty. States should also consider whether there are elements of another State's tax system that could increase the risk of non-taxation, which may include tax advantages that are ring-fenced from the domestic economy.

Paragraph 1

Paragraph 1 addresses certain subsequent changes in the domestic taxation law of resident companies. First, if the general rate of company tax applicable in either Contracting State falls below 15 percent for substantially all income of resident companies, the provisions of Articles 10 (Dividends), 11 (Interest), 12 (Royalties) and 21 (Other Income) may cease to have effect for payments made to a resident company of either Contracting State. A general rate of company tax that is applicable to business profits generally, or to so-called "trading income" that is broadly defined to include income from manufacturing, services or dealing in goods or commodities, shall be treated as applying to substantially all income, even if narrow categories of income (such as income from portfolio investments or other passive activities) were excluded.

A reduced rate of tax that applies only with respect to capital gains would not be within the scope of this Article.

According to subparagraph 3(a), this provision applies equally to reductions in a statutory company tax rate, as well as to other changes in domestic law that would have the same effect using a different mechanism. For example, if the statutory company tax rate in a Contracting State was 20 percent, but after the signing of the Convention, companies resident in the Contracting State are permitted to claim deductions representing 50 percent of what otherwise would be their taxable income, the general rate of company tax would be 10 percent. Similarly, if the statutory company tax rate in a Contracting State is 20 percent, but after the signing of the Convention, companies resident in the Contracting State are allowed to deduct an amount equal to a percentage of their equity up to 50 percent of what otherwise would be their taxable income, and in general, most companies are able to utilize the maximum available deduction, the general rate of company tax would be 10 percent

Subparagraph 3(b) states that neither taxes that are imposed at the company level only when the company distributes earnings nor taxes that are imposed at the shareholder level shall be taken into account when determining the general rate of company tax. For example, if after the signing of the Convention a Contracting State were to provide that resident companies are not subject to any taxation at the company level until a distribution is made, such tax would not be considered part of the general rate of company tax. This would be the result regardless of whether the tax in question was classified as a company tax under the domestic laws of the other Contracting State. Furthermore, a tax imposed on shareholders (including withholding taxes) would not be considered part of the general rate of company tax.

Second, in addition to rules based on changes to the general rate of company tax, paragraph 1 also provides that, if at any time after the signing of the Convention, either Contracting State provides for taxation of companies on a territorial basis through an exemption from taxation for substantially all foreign source income (including interest and royalties) earned by a resident company, the benefits of Articles 10, 11, 12 and 21 may cease to have effect. The reference to an exemption for substantially all foreign source income earned by a resident company is intended to describe a taxation system under which income (including income from portfolio investments) from sources outside a Contracting State is exempt from tax solely by reason of its source being outside that Contracting State. This would include a regime under which, for example, 95 percent of income from foreign sources was exempt from tax by reason of its foreign source, but five percent remains taxable as a proxy for the disallowance of allocable deductions. The reference does not include taxation systems under which only foreign source dividends or business profits from foreign permanent establishments are exempt from tax by a Contracting State.

Paragraph 2

Paragraph 2 sets forth rules that are equivalent to those of paragraph 1, but which are with respect to domestic law changes and treaty benefits affecting individuals. First, if the highest marginal rate of taxation applicable to individuals in either Contracting State falls below 15 percent with respect to substantially all income of resident individuals, the provisions of

Article 10 (Dividends), 11 (Interest), 12 (Royalties), and 21 (Other Income) may cease to have effect for payments made to a resident individual of either Contracting State. A reduced rate of tax that applies only with respect to capital gains would not be within the scope of this Article.

As is the case for paragraph 1, paragraph 3(a) provides that this provision applies equally to reductions in the highest marginal tax rate, as well as to other changes in domestic law that would have the same effect using a different mechanism. For example, if the highest marginal tax rate for individuals resident in a Contracting State is 20 percent, but after the signing of the Convention, the law was amended to provide such individuals with a standard deduction representing 50 percent of what otherwise would be their taxable income, the highest marginal tax rate for individuals resident in that Contracting State would be 10 percent.

Second, paragraph 2 also provides that, if at any time after the signing of the Convention, either Contracting State provides for the taxation of individuals on a territorial basis through an exemption for substantially all foreign source income (including interest and royalties), the benefits of Articles 10, 11, 12 and 21 may cease to have effect pursuant to paragraph 4. As in the case of paragraph 1, the reference to an exemption for substantially all foreign source income is intended to describe a taxation system under which income (including income from portfolio investments) from sources outside a Contracting State is exempt from tax solely by reason of its source being outside that Contracting State. The reference does not include taxation systems under which only foreign source dividends or business profits from foreign permanent establishments are exempt from tax by a Contracting State.

Paragraph 3

Paragraph 3 provides additional rules for determining the general rate of company tax or the highest marginal rate of individual tax. These additional rules are discussed above in the context in which they are used.

Paragraph 4

Paragraph 4 provides that if the provisions of either paragraph 1 or paragraph 2 of this Article are triggered by changes in domestic law in one of the Contracting States, the other Contracting State may notify the first-mentioned Contracting State through diplomatic channels that it will cease to apply the provisions of Articles 10, 11, 12 and 21. In such case, the provisions of such Articles shall cease to have effect in both Contracting States with respect to payments made to resident individuals or companies, as appropriate, six months after the date of such written notification, and the Contracting States shall consult with a view to concluding amendments to this Convention to restore an appropriate allocation of taxing rights.

Relationship with other Articles

Neither a gap nor an overlap is intended between the application of Article 28 and the definition of “special tax regime” in subparagraph 1(l) of Article 3 (General Definitions) with respect to interest, royalties and other income. In the event that a Contracting State were to exempt only certain categories of income, and such categories included, for example, foreign source interest or foreign source royalties, and it was determined that the exemption did not rise to the level of an exemption of substantially all foreign source income so as to trigger the application of this Article, the regime would be considered to disproportionately benefit the exempted categories of income such that the definition of "special tax regime" provided in subparagraph 1(l) of Article 3 (General Definitions) would apply for purposes of the Convention with respect to the exempted categories of income. If, on the other hand, a Contracting State provided a broad exemption for foreign source income, the provisions of this Article would apply.

Similarly, if a Contracting State maintained a general rate of company tax at or above 15 percent, but provided a reduced rate below 15 percent with respect to certain categories of income that included interest, royalties or other income (or some combination thereof), the reduced rate would be considered to disproportionately benefit interest, royalties or other income, as appropriate, and would be considered a special tax regime with respect to such categories of income. On the other hand, as described above, if a Contracting State provided a reduced tax rate with respect to substantially all business income, the provisions of this Article would apply.