Exam in Int'l Tax Treaties (Fall 1998)
McIntyre Notes on the Answers (revised Fall 2001)

1a. GCo is taxable only if it has a p.e. in the U.S. and then only on the profits attributable to that p.e. It does not have a p.e. in New York or Cincinnati, but the fair grounds in Philadelphia is a p.e. The agent, ACo, appears to be a independent agent and does not appear to have the authority to bind GCo. Thus it is not a p.e. of Gco. Gco is taxable on the net profits attributable to the operation of the circus in Philadelphia (that is, on the income generated on the business conducted at that location, not just on the fair rental value of the fair grounds).

1b. C may be a sportsman or artiste within the meaning of Article 17 of the Model Treaty. If so, she is not exempt from tax with respect to the income earned in the United States. Otherwise she would be an employee within the meaning of Article 15. Under that article, she is exempt. The line between artiste and regular employee is not real clear, but she does appear to me to be a performer and not part of the support caste.

1c. T is governed by the U.S./France treaty, as he is a resident of France. T is an artiste within the meaning of Article 17, so he is not exempt from tax in the United States.

1d. L is an employee governed by Article 15. He is exempt only if he meets the three tests of Article 15(2). He is present for less than 184 days, and his remuneration is paid by a foreign corporation, so he means the first two tests. I think that his employer has a p.e. in the U.S., however, so we have to know whether the p.e. deducted his compensation. The facts are not clear. We might expect that the employer would deduct the wages with respect to L's work at the Philadelphia location in order to reduce its U.S. tax.. In that event, L's compensation relating to Philadelphia would not be exempt and the rest would be exempt. Note: The treaty does not make clear that L would be exempt on the non-Philadelphia income — the argument for taxation would be that once the conditions of Article 15(2) are not met, the general rule of Article 15(1) applies. The contrary argument is that only the income borne by the PE is taxable. This latter result is more in tune with general OECD policy (see, e.g., the PE rule under which only income attributable to the PE is taxed).

1e. In fact, D is not protected, due to the Saving Clause in U.S. tax treaties. The question asked you to assume, however, that the U.S./German treaty was based on the OECD Model in ALL RELEVANT RESPECTS. Under that model, there is no Saving Clause. D is performing independent personal services within the meaning of Article 14. She has no fixed base in the United States. Thus she is exempt from the U.S. tax, assuming (counterfactually) that the U.S. treaty is based on the OECD model and has no Saving Clause.

2a. The U.S./Switzerland treaty provides for significantly less exchange of information that the U.S. Model. First, only information "necessary" for carrying out the treaty is to be exchanged, except in the case of fraud. In the case of fraud, exchange with respect to taxes covered by the treaty is required. The U.S. Model allows exchange if exchange is "relevant" for carrying out provisions of the treaty or enforcing domestic laws. Second, the "trade secret" limitation in the U.S./Switzerland treaty prevents exchange if it would disclose a trade secret, etc., whereas the

U.S. Model simply says that disclosure is not required.

2b. The U.S. always wants as much exchange of information as possible to discourage tax avoidance and evasion and to help it determine the income of the many foreign activities of U.S.-based multinationals. It also is not too concerned about the possible burden on the tax administration from foreign requests for information.

2c. Under international law, a protocol is a type of treaty. It has the same status as a treaty. A later in time protocol would take priority over a prior treaty, but here the treaty and protocol were adopted at the same time. Thus neither takes priority over the other.

3. The anti-treaty shopping rules of Article 22 (Limitation on Benefits) would come into play to deny treaty benefits to UCo. UCo is not described in any of the provisions of Art. 22(2). Its stock is owned by a non-resident company and is not traded on a stock exchange, etc., and most of its income is reduced by deductions paid to nonresidents. Its best chance for qualifying is under the active-business test of Art. 22(3). It is engaged in an active business in the United States, and that business is "connected with or incidental to" the active business conducted in Country S. The business in the United States, however, is not "substantial" in relation to the business conducted in Country S within the meaning of Art. 22(3)(a)(iii).

Note: The original question did not state clearly that Country S as well as Country V have treaties with the United States. Apparently everyone taking the exam correctly assumed that Country S had a treaty with the United States. I have corrected the question to avoid confusion.