



Tales and details on dividend definition in double taxation conventions

Historias y detalles sobre la definición de dividendo en los convenios de doble imposición

Contos e detalhes sobre a definição de dividendos em convenções de dupla tributação

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Abstract

The term “dividends” is used in many law areas with specific purposes. Particularly, the dividend concept in tax treaties is used to distribute the taxing power among the contracting states. Art. 10.3 of the OECD Model is commonly adopted by actual treaties. This paper describes the issues arising from the interaction of the dividend definition in tax treaties and the dividend definition provided by the private and fiscal law of the contracting states. Moreover, this paper sustains that three essential elements of the dividend concept in tax treaties should be present in order to qualify the income as dividends: a dividend-distributing entity, a corporate right and the link between the previous elements and the income. However, an analysis of the case law and the international doctrine allows the author to conclude that article 10 of the OECD Model allows the application of the definitions provided by domestic law of the source State of the dividends, in a wider scope than the one supported by major authors. Consequently, the research demonstrates that the three-elements of the concept should be interpreted given preference to the meaning provided by the source law.

Keywords: double taxation conventions, hybrid instruments, hybrid entities, hidden and constructive dividends.

Resumen

El término *dividendos*, se utiliza en muchas áreas del derecho con fines específicos. En particular, en los tratados fiscales, *dividendo* se emplea para distribuir el poder tributario entre los Estados contratantes. El artículo 10.3 del Modelo de la OCDE es comúnmente adoptado por los tratados actuales. Este artículo describe los problemas que surgen de la interacción de la definición de dividendo en los tratados fiscales y la definición de dividendo proporcionada por el derecho privado y fiscal de los Estados contratantes. Además, este trabajo sostiene que tres elementos esenciales del concepto de dividendo en los tratados fiscales deben estar presentes para calificar las rentas como dividendos: una entidad distribuidora de dividendos, un derecho corporativo y el vínculo entre los elementos anteriores y la renta. Sin embargo, un análisis de la jurisprudencia y la doctrina internacional permite al autor concluir que el artículo 10 del Modelo OCDE permite la aplicación de las definiciones previstas por el derecho interno del Estado fuente de los dividendos, en un ámbito más amplio que el sustentado por los principales autores. En consecuencia, la investigación demuestra que los tres elementos del concepto deben interpretarse con preferencia al sentido que le otorga la ley fuente.

Palabras clave: convenios de doble imposición, instrumentos híbridos, entidades híbridas, dividendos ocultos y ficticios.

Resumo

O termo “dividendos” é usado em muitas áreas do direito para fins específicos. Em particular, o conceito de dividendo em tratados fiscais é usado para distribuir o poder tributário entre os estados contratantes. Arte. 10.3 do Modelo OCDE é comumente adotado pelos tratados atuais. Este artigo descreve os problemas que surgem da interação da definição de dividendo em tratados fiscais e a definição de dividendo fornecida pelo direito privado e tributário dos estados contratantes. Além disso, este trabalho argumenta que três elementos essenciais do conceito de dividendo em tratados tributários devem estar presentes para classificar a renda como dividendos: uma entidade distribuidora de dividendos, um direito societário e a ligação entre os elementos acima e a renda. No entanto, uma análise da jurisprudência e da doutrina internacional permite ao autor concluir que o artigo 10.º do Modelo OCDE permite a aplicação das definições previstas na legislação interna do Estado de origem dos dividendos, num âmbito mais amplo do que aquele suportado pelo principais autores. Consequentemente, a investigação mostra que os três elementos do conceito devem ser interpretados preferencialmente ao significado dado pela lei de origem.

Palavras chave: Acordos de dupla tributação, instrumentos híbridos, entidades híbridas, dividendos ocultos e construtivos.

Introduction

Since the Corporate tax exists around the world, dividend taxation has been a topic of special interest by authors from diverse perspectives. Several economic and juridical reasons support the allowance of multiple economic taxation. Countries adopt several systems which deal with the relationship between personal income tax and corporate tax. Under those rules, dividend definition plays a key role in the structure of direct taxation for domestic tax systems.

The meaning of dividends in international tax law is the vortex of several mismatches and conflicts of qualification, since it relays on domestic definitions included with specific purposes in each tax system. In this line, tax treaties distribute taxing powers between countries and rely on the definition of dividends included in article 10.3 of the OECD Model, which is arguable an autonomous definition.

Some international tax law authors have created theories about an intrinsic and autonomous meaning of dividends, which contrasts with de details provided by actual tax treaties. In this paper we will go back to the scope of article 10 of the OECD Model, its history and the most common conflicts of qualification in order to demonstrate that the dividend definition in tax treaties relay on the source State definition.

This article contains the conclusion of the research on the application and interpretation of art. 10.3 of the OECD Model made by the author on his doctoral thesis in 2015,

and goes into the most common conflicts of qualification of the aforementioned thesis and recommend solutions from a *lege lata* and *lege ferenda* perspective.

I. Scope of Article 10.3 Mcoode

A. Definition of Dividend under Domestic Law

The dividend concept has always been important to income tax law (Lang, 2005, p. 18)¹. This relevance is evidenced by the fact that impersonal taxes, common tax liabilities two centuries ago and predecessors of source tax rules (Avery Jones, 2012, p. 67), dealt with the problem of deciding if the shareholder of the company produced the original sourced and qualified income or, if the fiction of the personality implied a (another) fiction, that the shareholders derived income from the corporate rights². Nowadays it is worldwide extended that dividends are sourced in the State of residence of the company (Harris, 2014, aptdo. 3.3). Moreover, global income taxes gradually adopted by countries in the 20th century (Lang, 2005, p. 18)³ prohibited the dividend deduction in the taxable base of the payer companies. Therefore, dividends must be defined for rules attempting to eliminate economic double taxation (Vid. Harris, 2014, aptdo. 3.3).

The importance of the dividend concept is closely connected with the admission of legal entities as taxpayers of income tax. Once those subjects obtain income, the shareholders will not receive the same source earnings (Schön, 2012, p. 502). This fiction is important to specify the income tax regime of two different taxable objects: outbound dividends and inbound dividends. Outbound dividends are not deductible from the taxable base of the payer and sometimes the beneficiary or the direct recipient can eliminate or alleviate economic double taxation (v. gr., art. 15 LIS; art. 25 LIRPF). Inbound dividends are those that accrue to recipients resident in one State (by means of subjective connecting factors), whose legislation usually alleviate the economic double taxation.

Non deductibility of dividends is based in the private law idea of capital impairment. However, tax law extends the meaning of dividends because the corporate law concept is not wide enough to describe other distributions of profits that may affect the ability to pay principle. The limitation of dividend deduction is one of the most recurrent debates in tax law: the taxation of entities and its members. The revision of the economic and

1 Vid. League of Nations (1925) *Double Taxation and Tax Evasion*, Report and Resolutions submitted by the Technical Experts to the Financial Committee. Ginebra: League of Nations official number C.115.M.55.1925. II; Avery Jones (2012): p. 67;

2 Vid. League Of Nations (1923) Report on Double Taxation, submitted to the Financial Committee by Professors Bruins, Einaudi, Seligman and Sir Josiah Stamp (Committee of Four), (Official No E.F.S.73.F.19.) Ginebra: League of Nations.

3 Vid. Global income taxes have not achieved the theoretical purity level proposed by Von Schanz, Haig and Simons.

juridical doctrine (Harris, 1996, pp. 60 ss.); reveals that the dividend concept is required in classic and integration systems, rather than the unity one. But the extension of the concept depends on the degree of neutrality achieved by those systems in relation with: i) the way the undertaking is carried by: the individual as itself or as the corporate entity; ii) the debt-equity choice; and, iii) the different methods of compensating shareholders. Each of the three types of asymmetries is related with the three elements of the dividend concept: i) dividend distributing entity; ii) corporate rights, and; iii) the relationship between income and participation. It also worth mentioning that integration systems can vary the quantification of income tax at the level of the entity or at the level of shareholder, and even create different tax regimes of dividends. For example, dividends derived from profits taxed at the general rate, at the reduced rate or exempted; or dividends received by individuals, companies, companies with a substantial participation, active shareholders or passive shareholders.

In the shareholder's residence State, dividends are part of the global income of the shareholder. However, the concept of dividends is again relevant to distinguish a taxable object that, for economic reasons (capital export or import neutrality), should be treated in a special manner. The shareholder's residence State legislation usually grants an exemption or an indirect tax credit for inbound dividends (Avery Jones, 2012, pp. 67-76). The use of those methods to eliminate economic double taxation can create asymmetries in the taxation of other elements of income that, from an economic point of view, are substitutional of dividends, such as interests, business profits with permanent establishment (PE) and capital gains for the alienation of corporate rights (Schön, 2010, pp. 65 ss.; Brown, 2012, pp. 28-29; Avery Jones, 2012, p. 76). Also, the distinction between dividends from substantial participation and from portfolio investments is arbitrary and incoherent, insofar both lead equally to (undesirable) economic double taxation. Furthermore, substitution problems (Vogel, 1997, Introduction párr. 91 a) can arise due to the fact that the three elements of the general concept of dividends are defined according with two different legal orders. To be precise, each legal order has at least one definition for tax law purposes and other for private law purposes. Consequently, each element of the general concept of dividends can be defined, at least, in four different ways. Therefore, the classical problem of concepts from private law used in tax law rules is aggravated in international tax law, and conflicts in the qualification of entities, debt-equity instruments and income are not only hypothetically possible, but usual. In addition, we cannot deny the principle of uniformity of the law, but cases and legislations reviewed in this research show us that autonomous definitions in tax law are emerging. For example, BEPS (OECD, 2014, parr. 53 ss.)⁴ project (and legislations inspired by) is looking at the relevant characteristics of entities and financial instruments (Helminem, 2010, pp. 169-170; Bärsch, 2012, p. 323; Brown, 2012, pp. 34-39) in tax law. This characterization entails the existence of an independent

4 Vid. Código de Conducta, ECOFIN Council, 8 June 2010, n.º 1033/10.

taxpayer and the non-deductibility of dividend, rather than the condition of being a legal person or the granted rights of the instrument. However, if the deductibility criterion is accepted, one could argue that it should also be the solution for those interests and other income not deductible in the company's tax base (i.e. interest barriers). Likewise, if the goal of the inclusion of those characteristics in double-taxation-method rules (in particular exemption) is to avoid double non-taxation, what is the difference between deducting the income from the taxable base of the company and mitigating double taxation at the level of the shareholder (credit in source)?

B. Allocation of Taxing Rights under DTC

In tax treaties, dividends are elements of income defined and ruled by Art. 10 (of the OECD Model and similar articles in actual tax treaties). The dividend category attempts to distribute the taxing rights of States and mitigate double taxation. Consequently, the definition of art. 10.3 applies only when a secondary qualification is required. Second qualification prevails over the first qualification made under domestic rules (Vogel, 1997, Introduction, párr. 56; Lang, 2010, n.º 58) on inbound and outbound dividends. This result makes sense because treaties restrict domestic law. Source tax rules are limited to the provided percentage in art. 10.2, unless the corporate rights are effectively connected with a PE in that country (art. 10.4). Art. 10 does not restrict the taxing rights of the residence state of the shareholder, but as a “*distributive rules with incomplete or open legal consequences*” (Vogel, 1997, p. 30; Calderón, 2012b, aptdo. 4.1; párrs. 4-7, comment on art. 10), the residence State should eliminate double taxation through tax credit method (art. 23 A and 23 B OECD Model) (Chapter I, section 2).

The model admits taxation of the same taxable object twice in the residence State of the company: when income is derived by the dividend-distributing entity and when the profits are distributed to shareholders. Therefore, article 10 presumes the conventional entity's residence State (art. 4 OECD Model) (Harris, 2014, aptdo. 3.3, párr. 9, Art. 10, CMOCDE) is the source country (objective connecting factor) for dividends. This presumption is confirmed by the prohibition of some types of extraterritoriality in article 10.5 of the Model, in particular, the place where underlined benefits originate (Vogel, 1997, p. 692 ss., n.º 251, May 2011: p. 418, párr. 34, art. 10, CMOCDE) (origin principle), the “loser” country as a result of the application of art. 4.3 tie break rules when the company is a dual resident⁵. Conversely, extraterritoriality prohibition does not preclude the application of alternative connecting factors as the place of payment of dividends, the taxation of undistributed profits in the residence State (párr. 37, Art. 10 CMOCDE; Rust, 2004, p. 269) (i.e. Controlled Foreign Corporation rules), nor branch taxes or second layer of taxation of PE.

5 i.e. Dividends of a Company with double residence which is tax under the criteria of source according to the domestic law, but not according to the DTC.

Article 10.2 limits the applicable rate in the source tax law insofar the beneficial owner of the dividends is resident in the other contracting State. The taxation of the distributing-company is not affected by the restriction. The second paragraph of art. 10 qualifies the person receiving dividends through the beneficial owner clause and, under subparagraph a), the substantial participation (i.e. the “holder” of the required capital-percentage) and partnerships exclusion. Under actual treaties, special rules include or exclude specific dividend recipients from the benefits of the paragraph or subparagraphs. Of all the aforementioned delimitations we have found the beneficial owner clause is the main one, however a deeper reflection about it, escapes the scope of this thesis. Beneficial owner is the person with a legal ownership right on the income and, in principle, the beneficial owner clause (párrs. 12.4 al 12.7, art. 10, CMOCDE) is just a requirement of the subjective scope of the treaty which the author has assumed. On the other hand, dividend definition does not mention the personal requirement of the income recipient and it does not presume the attribution of the income to the legal owner of the corporate rights. In short, dividends could be the income paid to the direct recipient or to the beneficial owner.

The OECD Model has been conceived in accordance with the classical system of corporate/shareholder income taxation (párr. 1.63, art. 10, CMOCDE). Since this conception inspired the wording of art. 10, there is only a formal reciprocity in the statutory tax rate on dividend taxation. However, integration systems, common during the second half of the last century, consider one taxable object taxed in two different subjects. As a result, when the integration systems reduce the taxation of the entity and pursue to tax the shareholder by increasing its taxation, tax treaties could be incoherent from a fiscal policy perspective and could not guarantee the effective reciprocity (párrs. 40-67, art. 10, MCOCDE). Moreover, the simple increasing of the corporate tax rate can break the effective reciprocity of art. 10.

Art. 10.1 respects the taxing rights of the Residence State of the beneficial owner or direct recipient. However, that State is obliged to eliminate double taxation with the specific method provided for dividends. Dividend definition is required in art. 23 A and 23 B of the Model (párrs. 24, 47 and 48, art. 23, CMOCDE). Both articles create asymmetries between dividends and business profits due to the fact that the applicable method for each one is different in the first article, and because the extent of the credit in the second article is also different. When this research started, we assumed the scope of the dividend definition was clear, and probably out of the scope of the thesis. Nevertheless, important confusions were found in literature and jurisprudence in relation with the application of methods for the elimination of double taxation (Vid. Avery Jones et al., 1999, pp. 103 ss.). After having described and analyzed the problems in Chapter one, it is important to conclude that treaty methods only apply if domestic law does not eliminate double taxation. In those circumstances, art. 10.3 is required to defined the character of income, even if the wording of the treaty method contains a reference to the residence State domestic law. Most treaties, with and without references to domestic tax law, require that income should be taxed “in accordance with the provisions of” the Convention. Only, through the

qualification of the element of income is possible to know if the taxation is in accordance with the DTC. Thus, art. 10.3 is necessary to define that the source taxation has been in accordance with the Treaty.

Contrary to the opinion of some relevant authors, it is stated in this contribution that art. 10.3 is relevant no matter if the wording of the method refers to the element of income by number (i.e. art. 10), by number and description (i.e. dividend in art. 10) or by a mere description (i.e. dividends) (Avery Jones et al., 1996, pp. 136 ss.; Avery Jones et al., 1999, pp. 106-107). Finally, despite the fact that the credit method in art. 23 applies to the element of income characterized in the aforementioned three ways, it is absolutely important to say that the method provided for *business profits* applies to dividends derived from corporate rights effectively connected with a PE.

Conflicts could emerge in cases where double taxation is not relieved by domestic methods due to application of a narrower definition of dividends than the one provided by the treaty. *Memec* case (Reino Unido, Memec vs. IRC, 1998, STC. 754) in UK is an example of this kind of conflicts. It is also possible that the treaty provides for a narrower meaning than the domestic definition. Under these circumstances, it could be wrongly understood that the treaty method should not apply. The qualification of Brazilian *juros sobre o capital proprio* by the Spanish Supreme Court is an example of this kind of mistakes in the resolution of international tax law conflicts⁶. Both errors are caused by the absence of distinction in the scope of each method and the purpose of each measure. Finally, if treaties contain a reference to domestic methods and that reference includes the dividend definition, conflicts of qualification could increase and would not be possible to solve them under the wording of art. 3.2 and 23 of the treaty.

Conversely, if art. 10.3 is the rule governing the distribution of taxing rights, conflicts of qualification are resolved through the limitation of the residence State arguments to deny the method for the elimination of double taxation. The residence State is prevented to use its own definition to qualify the terms of art. 10.3. This conclusion is similar, but not identical to the solutions argued by the *Partnership Report* in 1999 and the *International Tax Group* (Avery Jones et al. 1996, pp. 126-145) in 1996. In our opinion the former authors fail to explain the reasons why the State of Residence have to follow the result of the source State's qualification of income (Vid. Lang, 2010, párr. 128). Indeed, the real problem in qualification conflicts is the applicable rule to define the terms not defined in the treaty, therefore, the final result of the categorization of the element of income in the source State should not be binding to residence State. To a great extent, the lack of clarity in the applicable dividend definition (art. 10.3, source or residence definition) causes inconsistencies in the taxation of international profit distributions.

6 Vid. Spain, Resolution of the TEAC of april 13th 2011, Vocalía Tercera, RG. 1202/10; 1202/10 y 1884/10, reaffirmed in Resolution of april 26th 2012, Vocalía Segunda, n.º 00/4085/2010; SAN 712/2014, of february 27th, Recurso 232/2011. vid. Calderón 2012b.

C. Absence of Neutrality

Dividend taxation under treaties and domestic law is not neutral if compared with business profits, interest and capital gains. The absence of neutrality encourages tax arbitrage, as a result of the similarity in the economic effects of each type of income and the possibilities of substitution. Provided that taxation is considered as a cost on the economic transactions, there are, at least, three aspects of each element of income that can be treated differently: the deductibility of the payment in the payer taxable base, the withholding tax on the investor and the personal liability in the residence State (including methods of relief). The corporate finance literature shows that there is a systematic preference for debt and for alternative ways of shareholder remuneration.

II. Definition of Dividend under DTC

A. Interpretation and application of the definition of dividends

Once the scope of art. 10.3 has been explained, it is possible to study the application of the rule. The application of the dividend definition is complex due to the dual nature of tax treaties (Helminen, 2010, p. 32). Tax treaties are domestic law and international law simultaneously. In consequence, art. 10.3 can cause conflicts with rules of those legal orders (Vogel & Prokisch, 1993, p. 62). This thesis presumes the dividend definition should prevail in case of conflict, but in practice it can be problematic. Secondly, the authorities of each state interpret the treaty and they are not bound by each other. International tax law does not have a Supreme Court to resolve conflicts on the application of treaties. Thirdly, there is no an homogeneous social and juridical context in both contracting States, so the framework that permits to establish the right answer (as suggested by Dworkin) can be arguable. In spite of these profound problems, it is possible to provide some reasonable results applying the Vienna Convention on the Law of Treaties (VCLT). According to the VCLT, treaties must be applied in good faith, searching for the ordinary meaning through the grammatical, systematic and teleological methods for interpretation (art. 31 and 32 VCLT) (Vogel & Prokisch, 1993, pp. 66 ss.). As a result of the former articles and art. 3.2 of the Model (Lang, 2010, p. 40), the interpretation requires to analyze the possible meanings of the wording, giving prevalence to the autonomous meaning over those used in domestic law, and the tax meaning over the general law meaning. However, it is difficult to interpret the terms out of their definition in private law, when treaties and tax legislation use private law concepts without giving a special tax meaning. For instance, art. 10.3 is defined in tax treaties, and, in principle, has an autonomous meaning. However, since the terms used in the definition have neither a special meaning in international tax or in domestic tax law, it is quite hard to argue that these terms do not refer to the private law meaning. A systematic interpretation is not helpful in most cases, because the existence of context is difficult to demonstrate, and many of the means of interpretation are arguably

valid for tax law purpose when the rule of law is mandatory. For this reason, OECD Model Commentaries cannot be accepted as context (Lang, 2000, p. 18). Still, Commentaries are probably one of the most important doctrines but, to a great extent, OECD Model Commentaries do not offer the right answer. Instead, they usually offer several interpretations and the preferred one. The latter is usually the one defended by tax authorities since it fits better with their intended tax policy. Moreover, OECD Commentaries vary according to time, so their value for the interpretation of tax treaties is equal of the best doctrine when it comes to the interpretation of tax treaties. Above all, the use of principles and values for the interpretation of dividend definition is of little help, on account of the difficulty that lays in arguing that art. 10.3 has a different purpose than the one of distributing the taxing powers of States. The abuse of law principle has different contents (Lang, 2010, párr. 74) in each legal system and it can arguably be used to extend the meaning of dividends (Vogel, 1997). Since it is difficult to find a different meaning than the one provided by private law, history could provide insights of the relevance of the inclusion of this category in tax treaties and the principles to resolve the questions arise by the application of art. 10.3⁷.

B. Evolution of dividend definition under DTC

This research sought for the purpose of the dividend clause in tax treaties, and the possible solutions to the main interpretation issues concerning art. 10.3. As a result, the history of the dividend definition in the 2014 OCDE Model is deeply linked with the extraterritoriality rule (art. 10.5) and the idea that the same taxable object could be taxed in the hands of two different taxpayers, which in turn justifies art. 10.2. lit. a). The latter comes from the first period of evolution of tax treaties, and before the consolidation of the contemporary dividend article. The first tax treaties and federal harmonizing rules, in particular, the imperial law for the elimination of double taxation in Germany (*Reichsgesetz wegen Beseitigung der Doppelbesteuerung*) of the 3rd may 1870, did not contain an specific rule for dividends (Harris, 1999, p. 8). Notwithstanding, the Administrative Court of the Grand Duke of Baden admitted the fiction that shareholders do not produce the business profits of the entity⁸. That is probably the reason for the inclusion of dividends into the category of income from movable capital in tax treaties. Many of the first tax conventions allowed source taxation for Income from movable capital. Thus, in absence of this rule, dividends must be exempted in the source State. As the result of the inclusion of dividends in the movable capital article, classical system of taxation was admitted in tax treaties (Harris, 1999, pp. 7 ss.).

7 See Friedlander and Wilkie (2006, pp. 907 ss.); Vann (2011, p. 11).

8 Germany, Criminal Division, Judgment of 26 February 1883. R. No 3084/82.

The Draft model convention of 1927⁹ and the Draft 1 A of 1928 (Harris, 1996, p. 305) of the League of Nations were the first models including a specific article for dividends. “Income from shares and similar interest” in “undertakings” were considered dividends. Nonetheless, the mentioned League of Nations models are not the direct precedent of the contemporary dividend definition. The most important and direct precedents of Art. 10.3 are the London Model¹⁰ and the discussions of Working Party 12 of the OEEC¹¹. The latter, ended up in art. 10.3 of the 1963 OECD Model and Commentaries. The WP12 documents and the London Model laid down the basic configuration of the dividend article since the 1950’s until now. Both works understood dividends as an element of income which was previously considered taxable business profits of the dividend-distributing entity. Consequently, the residence State of the company is presumed to be the source country of dividends and, the mitigation of economic double taxation is taken into account in art. 10.2., paragraph b¹² and in the commentaries related with relief methods in the source (integration) and residence State (participation exemption). Art. 10 allows and protects the taxing rights of the residence State of the entity on the business profits of the company and on the dividends. That is reason why art. 10 allows the taxation of hidden distributions. The philosophy of the type of income dealt under the name of dividends has its inception in the United States and United Kingdom in 1945. Under the negotiation of the aforementioned treaty, the US Congress asked for the effective reciprocity and considered as a benchmark the sum of the tax rate at the level of the entity and the level of the shareholder in both countries¹³. To put it in other words, it is accepted the object of distribution in the dividend article is an element of income composed by a single taxable object taxed twice. US Government and Congress even included a rule attempting to maintain the effective reciprocity in time, permitting the interruption of the validity of the rule if the benchmark’s rates changed. Unlike the 1946 US-UK Treaty, the OECD Model gave precedence to the legal certainty principle over the justice on the distribution of taxing rights. Therefore, a fixed rule was included in art. 10 of OECD Model implying that changes in domestic law would not affect the force of States’ obligations, but the general understanding of the taxable object distributed in art. 10 is kept in the OECD Model.

9 Vid. League of Nations (1927). *Double Taxation and Tax Evasion*, Report presented by the Committee of Technical Experts on Double Taxation and Tax Evasion (Official n.º G.216.M.85.1927.II.) Geneva: League of Nations, pp. 10-18.

10 Vid. League of Nations (1946). *London and México Model Tax Conventions: Commentary and Text*, Fiscal Committee, (Official number C.88.M.88.1946.II.A.), Ginebra: League of Nations: pp. 63-65.

11 Vid. www.taxtreatieshistory.org

12 For Harris (1996, p. 307), the London Model is a step forward to the acceptance of a classic system entity-partner and the allocation of taxing rights base on the type of taxpayer.

13 Vid. Koch (1947, pp. 70-71); League of Nations. (1946b). Fiscal Committee, *Report on the work of the Tenth Session of the Committee held in London from March 20th to 26th, 1946*. (Official n.º C. 37.M.37.1946.II.A.) Ginebra: League of Nations.

Art. 10.3 contains three parts. Each part's history can be traced from the OEEC WP 12 works. OEEC and OECD's documents from 1958 to 1963¹⁴ reflects several confusions in the translation of company types and other legal entities, and the interest or shares in them. Taking into account that the official languages used by the Organization were English and French, the issues faced were not only those susceptible of being lost in translation, but also the use of private law terms belonging to the two extremes of legal traditions¹⁵.

Dividend definition should include income from the ownership rights in companies. Unfortunately, neither the kind of rights nor the types of legal entities were harmonized or even resembles in countries. The first part of the definition is the result of the common rights found in the majority of the member countries. The second part was included with the intention of including securities with a contingent remuneration. In spite of the fact that securities was a wide term, WP 12 First Report Commentaries required the essential condition of the dividend definition, namely that income should derive from a contract of association in an independent tax entity¹⁶. The amplitude of the essential condition, and the ambiguity of the wording of the First Report, caused the progressive characterization of the second part, beginning with the English word "share", then replaced by "rights", and the French word "parts". It is not clear the reason, but later on, the rights or *parts* were negatively defined as "not being debt claim"¹⁷. The doctrine offers two explanations for that inclusion: the wideness of the English terms and the necessity of clarifying the borders between interest and dividends. The 2014 OECD Model maintains the difference in the translation of the second part of the definition. The revision of the current tax treaties analyzed by the WP 12 shows that the second part pretends to include interests not mentioned in the first part that represents a right to participate in profits. It was assumed that all rights included in the first part gave rights to participate in profits and were treated as ordinary dividends¹⁸. The third part comes from the necessity of describing certain rights

14 OEEC, FC/WP12 (58)1 Part I. (28/11/1958); FC/WP12 (58)1 Part II. (28/11/1958). FC/M(59)1. TDF/FC/57 (1st revision) (19/03/1959). FC/M(59)2 (15/05/1959). FC/WP12(60)1 (08/01/1960). TDF/FC/88. FC/M(59)5 (30/12/1959). FC/WP12(60)1 (08/01/1960). FC/WP12(60)2 (30/4/1960). WP12(60)3 (01/08/1960). FC/WP12(60)4 (24/09/1960). FC/M(60)5 (12/10/1960). FC/WP12(61)1 (06/01/1961). FC/WP12(61)2 (09/02/1961).FC/WP12(61)3 (20/02/1961). OEEC, FC/WP12(58)1 Part I. (28/11/1958); FC/WP12(58)1 Part II. (28/11/1958)

15 Avery Jones et al. (2009).

16 Vid. Hattingh (2009, p. 510). Pijl (2011, p. 498), considers that the requisite was wide because it could be a contract different from a society and the term of association is undetermined.

17 OEEC, FC(61)1 Annexes. Avery Jones et al 2009, Nota al pie 68; "The exclusion for debt-claims is first found in a version of 23 May 1961 (FC(61)1ann) without any explanation for the change, but it is assumed that the drafting group made it because the general words "other rights participating in profits" were more general in English than parts in French and could have included creditor rights, which were not intended to be included on the change from the inappropriate reference to shares to other rights. In the same report, the definition of interest included "income from... bonds or debentures... whether or not participating in profits".

18 FC/WP12(58)1 Part II, p. 18 y ss. Switzerland-Germany 1931; Germany-Sweden 1928; Germany-Austria 1954. Switzerland- Sweden 1948; Italy- Switzerland 1946.

in legal entities that were neither shares in companies nor any of the corporate rights listed by the first and second part. Indeed, the third part was included when the Fiscal Committee eliminated the description of the “shares in co-operative societies and limited liability partnerships.” In conclusion, the reference to the domestic law pretends to include rights representing the share capital in all the taxpayers of corporate income tax. Although the First Report included in the Commentaries a sort of reference to domestic law as an attempt¹⁹ to include non-formal dividends, constructive dividends and hidden distributions, the third part reference to domestic law gave more support to the Commentaries, as expressly mentioned in 1977 Commentaries²⁰.

The wording of the dividend definition in the 2014 OECD Model has remained practically untouched since the 1963 Model. However, in 1977, the third part of the definition was modified. Commentaries on art. 10 have also been maintained until today, although some updates were introduced in the 1977 and 1992 Model. In 1977 the Committee of Fiscal Affairs concluded that treaty negotiation on dividend definition requires a special study of the context in both contracting States and should not be copied in tax treaties without further considerations²¹. In 1992, the risk criterion to differentiate interests from dividends was included as a result of the Thin Capitalization Report of 1987. Furthermore, OECD Model Commentaries mentioned that CFC regimes and tax treaties are compatible, as concluded by the Base Company Report.

The analysis of the treaties according with the methodology adopted by this thesis reveals that the OECD Model dividend definition is not commonly altered in actual treaties. Similarly, the UN Model copied the OECD Model definition. In spite of that, the following modifications on the dividend definition were found:

First part: few treaties vary the rights included. For instance, some treaties only include “shares”, or eliminate *jouissance* shares or *jouissance* rights²². Some treaties wrongly eliminate the word “shares” repeated twice in the first part. The aforementioned modification causes the problem of defining if only *jouissance* shares²³ are included and not mere shares. The Ecuador-Spain treaty listed the remuneration of “contributions”²⁴, while the Switzerland-Spain treaty refers to the Parent-Subsidiary Directive. The latter Convention uses the dividend definition in the treaty and the reference to the Directive could also cover the definition of profit distributions. Due to the fact that art. 10.3 of the OECD Model

19 Maybe that was already the interpretation of the projects WP12 de Comité Fiscal en la Sesión 20. FC/M(60)5. Vid against: Hattingh (2009, p. 514).

20 Against Avery Jones et al. (2009, p. 19-21).

21 Par. 35 art. 10 MOCDE. See changes in the third part of the definition. Vogel (1997, par. 199, p. 656). And the projects of the WP23 which conclusions were approved by the WP 1 in its 7th meeting which took place from February 13th to 15 th of 1973. OECD, CFA/WP1(73)2 (31/01/1973); DAF/CFA/WP1/73.5 (11/04/1973).

22 Spain- Norway 2001.

23 Spain-Korea 1994; Spain-Cuba 2001; Spain-Ireland 1994; Spain-Luxemburg 2007.

24 Spain- Ecuador; Germany- Ecuador. Vid. Vogel (1997, Párr. 203, art. 10).

and the definition of profit distributions in the Directive do not resemble, conflicts of interpretation can arise.

Second part: few treaties eliminate the second part or even combine the first and the second parts. For instance, some Spanish tax treaties use a translation closer to the French Model read as "...otras partes beneficiarias/otros derechos que permitan participar en beneficios, excepto los de crédito"²⁵. This wording increases doubts on the supposed requirement which sets that all the assets mentioned in the first part should not be debt-claims. However, unlike the Spanish translation, official English versions of the majority of those treaties have the same wording of the English OECD Model and the IEF's Spanish version of the Model. Consequently, it could be inferred that the different wording in those treaties were not necessarily the product of a conscious deliberation. As a result, the conclusions under the OECD Model should not be different in the mentioned treaties. Second part is also modified in Dutch tax treaties and other few countries. They delete the debt-claim exclusion. Moreover, dividend definition in some of them includes benefits from silent partnerships and debentures and bonds participating in profits²⁶. That inclusion is closely connected with the policy in those countries because the income from that kind of debt-claims is taxed as income from shares. In spite of that, most probably it could cause asymmetrical results in the other contracting States if the latter jurisdiction tax as interest income from the aforementioned debt-claims.

Third part: like the OECD Model, most treaties contain a reference to the domestic legislation in the third part of the dividend definition. The reference is under the condition that the income derives from "corporate rights". Some treaties' wording have a wide reference to the domestic law through the replacement of "...corporate rights..." by "...other rights..."²⁷. Other conventions establish an even broader reference²⁸ to the domestic law, which do not mention the income-generating asset, and are worded as "other income...". The US Model follows

25 Spain-Tunisia 1987; Even new DTC like Spain-Cyprus 2013 have the same mistake, although de MCOECD 2010 translation of the IEF does not have it. DTC as old as Spain. Canada 1981 or Spain-Finland 1968 do not have that mistake. Spain – Saudi Arabia 2008; Spain-Armenia 2012; Spain-Croatia 2006; España-Egypt 2006; Spain-United Arab Emirates 2007; Spain-Slovenia 2002; Spain-Georgia 2011; Spain-Greece 2002; Spain-Island 2002; Spain-Japan 1974; Spain-Moldavia 2009; Spain-Nigeria 2009; Spain-New Zealand 2006; Spain-Serbia 2010; Spain-South Africa 2008; Spain-Albania 2011; Spain-Barbados 2011; Spain-Bosnia Herzegovina 2010; Spain-United States 2013; Spain-Estonia 2005; Spain-Jamaica 2009; Spain – United Kingdom 2013 (Ratification process); Spain-Singapore 2012.

26 PIJL (2011, p. 496).

27 p. ej. Colombia-Korea 2013; Colombia-Mexico 2013; Spain-Chile 2004. That last one with the following wording: "otras participaciones sociales o derechos sujetos..."

28 With wording similar to: "...otros rendimientos sujetos al mismo régimen fiscal que los rendimientos de las acciones por la legislación del Estado del que la sociedad que realiza la distribución sea residente." Spain-Germany 2012; Spain-Albania 2011; Spain-Barbados 2011; Spain-Belgium 2003 with the difference "... así como las rentas -incluso las satisfechas en forma de intereses-..."; Spain-United States 2013; Spain-Hong Kong 2012; Spain-United Kingdom 2014, with the difference "... así como cualquier otro elemento sujeto al mismo régimen fiscal..."; Spain-Singapore 2012; Spain-Uruguay 2011; Colombia-Czech Republic 2013. Spain-Australia 1992 "otros rendimientos que la legislación fiscal del Estado contratante del que sea residente la sociedad que los

the latter locution and, as the technical explanations defend, the widest reference solves most conflicts of qualification connected with the dividend article²⁹. The third part has other elements, to some extent forgotten by the doctrine, such as the mode in which the remittance is made. Differences can be drawn between the wording of the 1963 or 1977 models. The former includes the income "...assimilated to..." income from shares, while the latter mentions the income "...subjected to the same taxation treatment...".

C. Antiabuse legislation and doctrine on dividends

Dividend domestic tax regime may be abused through avoidance or through capture. Reactions from States usually entail reclassification of elements of income that raise questions from the perspective of the dividend definition provided in the art. 10.3 of treaties. Different types of requalification should be mentioned.

First of all, source tax law requalification's must be qualified as dividends for tax treaties if the third part of the definition is fulfilled; namely, if the reclassified income got the same taxation treatment than income from shares, and the source of the income is a corporate right (under the OECD Model). This conclusion can be drawn from the history of the definition and, from a literal and teleological interpretation³⁰. Although, only company's assets or equity decreases can qualify as dividends in tax treaties.

By contrast, the third part of art. 10.3 neither include the requalification of dividends in other types of income by the source State, nor the requalification made by the residence State. Compatibility of the aforementioned types of requalification depends on the solution chosen to answer the question of the compatibility of domestic anti-abuse rules with tax treaties. There is too much debate between doctrine, international organization and jurisprudence on this problem and the OECD. Commentaries³¹ to the OECD Model are not coherent on the arguments supporting the application of GAAR'S and SAAR'S in treaty situations. The 2003's Commentaries³² adopted the guiding principle and the factual approach as arguments to support the compatibility between treaties and anti-avoidance rules under the idea of a common standard of abuse. However, as stated by ZORNOZA & BAEZ, the former is an ambiguous test of purposes, on account of the fact that it could be the main, one of the principal or the sole purpose. Moreover, the guiding principle is based on the idea that the object and purpose of treaties is the prevention of tax avoidance and evasion. It is a circular way to describe what is the conventional standard of avoidance

distribuye asimile a los rendimientos de las acciones." Spain-Finland 1968; Spain-Morocco 1985; Spain-Sweden 1977.

29 Vid. Helminen (2010, p. 176).

30 Párr. 28 art. 10 CMOCDE.

31 Par. 7, 23 art. 1 CMOCDE 1997. Pars. 22-26 art. 1 CMOCDE 1992.

32 Párrs. 9,2 art. 1 CMOCDE; Párr. 22.1 art. 1 CMOCDE.

and could clash with other clearer purposes of tax treaties, as the elimination of double taxation and the promotion of economic transactions between countries.

In fact, the object and purpose of the art. 10 OECD Model is the distribution of taxing rights on dividends. This purpose only can be defined within the framework of the definition of dividends provided by treaties³³. Thus, it is hard to assert that art. 10.3 has been object of rule shopping as consequence of the application of a domestic GAAR. In conclusion, all kind of requalification of dividends in other elements of income o vice versa, need to comply with art. 10.3 of treaties, unless there is an express rules on the contrary or the scheme was a sham transaction³⁴. The latter is just a discovery of the real facts and it can be accepted as long as those facts qualify on the wording of the dividend definitions. As noted before, this conclusion if only valid in relation with the secondary qualification and the effects derived therefrom. That is, consequences of the reclassification of income under domestic rules are valid if they complain with treaty's limitations. For instance, in a reclassification of a hybrid instrument that does not comply with the art. 10.3, non-deductibility will be valid under tax treaties, but maximum tax rate for interests should be respected. As result, it is reasonable to conclude that problems on hybrid entities and hybrid financial instruments can hardly be solved by GAAR's and SAAR's, taking into account that reclassifications can only affect definitions and the tax regime in one contracting State, but they not always can sway the tax treatment of the income in tax treaties nor in the other contracting states.

III. Elements of the definition of dividends under DTC

Three elements of the dividend definition are present in Art. 10.3 of the Model: a) dividend-distributing entity; b) the corporate rights in that entity which give the rights to participate in profits; and, c) the relationship between the income paid by the company and the corporate right in the entity. Those three elements are also elements of the domestic dividend definition, but specifications vary.

A. Dividend-distributing entities

The dividend-distributing entity is a crucial element to define dividends, but its meaning faces challenges. For instance, the lack of harmonization of private law, namely, the concept of legal entity and its attributes (Couzin, 2002, p. 11); Avery Jones *et al.*

33 The solution proposed in 2003 that aims to justify the anti-abuse purpose of the DTC has been strongly criticize. Vid. Zornoza & Báez (2010, par. 51 y ss.); Martín Jiménez (2004, p. 321). The same critics apply to del MCONU 2011, although they decrease due to par. 27 of the commentary on article 1 which tends to minimize the uncertainty, using ash requisite that the guiding principle is apply under the facts and not only under the intention of the parties. par. 25 of the Comentario on art. 1 MCONU.

34 Differences between scheme and sham: Zornoza & Báez (2010, párr. 13); Arnold & Van Weeghel (2006, aptdo. 5.4.6).

(2009, pp. 9 y 10) creates conflicts of classification of entities which become conflicts of qualification of income. Most of the domestic tax laws define the taxpayer of corporate taxes by referring to corporate law³⁵. However, tax law considers legal persons as transparent, and non-legal persons as opaque entities. In other words, the absence of harmonization is also a fact in tax law. Thus, although theoretically it could be argued that dividends should only come from profits that have been liable to tax at the entity level, in practice this cannot happen. Divergences on the classification entity or in the attribution of income to the entity or its owners are possible under two or more laws (Lang & Staringer, 2014, pp. 19 y 27). As a consequence, conflicts of classification or attribution, double taxation or double non-taxation can emerge. For instance, if a State considers that the entity exists and therefore yields partners are dividends, the other State could understand that the benefits are obtained by the participants (by all of them proportionally or by some of them), and keep the same source, nature and original qualification (OECD, 1999, párrs. 5-22; Lang & Staringer, 2014, p. 30).

Tax treaties define the dividend-distributing entity by the terms company and corporate rights (art. 3.1 and 10 OECD Model). However, the entity must comply with the subjective scope of the treaty, that is to say, the entity must be a resident person. Graphically it could be explained by four concentric circles: starting by the larger one, the first circle represents “persons”. The second one deals with the subjective scope of the Treaty and is restricted to “resident persons”. The third circle is described by the locution “company” and is connected with the subjective scope of art. 10.1, and the fourth and smallest circumference is the dividend-distributing entity which allows the qualification of the income as dividends. The subjective scope of tax treaties includes individuals, companies and other body persons being residents in one State. Residence requires, among other conditions, being liable to tax. *Lato sensu*, the liable to tax requirement is understood as a simple link with a State that allows the taxation of the entity, even if there is not actual liability. The prevailing interpretation in the Commentaries of the OECD Model suggests a narrower interpretation, because it is required to have, at least, the legal nature of taxpayer of taxes covered by the treaty. Furthermore, some countries argue that subject to tax means effective taxation in the State, or even so, that liable to tax condition excludes shell companies³⁶.

In conclusion, subject to tax criterion is rather ambiguous. From 2000’s OECD Model Commentaries, liable to tax phrase is interpreted as being opaque i.e. the income should not be attributed to its members according to the law of the residence State of the entity³⁷. This creates the difficulty of knowing when there is opacity or transparency. It is to be noted that the subjective scope of the OECD Model also includes body of persons (*agrupación de personas, groupment de personnes* or *associazione di persone*) and that actual

35 Vid. Lang & Staringer (2014, pp. 24-28).

36 Vid. Couzin (2002); Vogel (1997); Art. 4 Párr. 24 y ss.

37 Vid. OECD (1999, par. 40). Critics: Lang (2000, p. 37); Couzin (2002, p. 109).

tax treaties often treats as “persons” or as “residents” transparent and non-liable to tax entities (Pars. 3 and 8 art. 4 CMOCDE). The existence of transparent entities entitled to the application of conventional benefits can lead to cases of double non-taxation, to the extent that a kind of fiction is created, similar to what is happening with the dividend-distributing entity, but with the exception that art. 10 is not applicable since there is not a dividend-distributing entity. In fact, art. 10 of the Model entitles the State of residence of the owners of the entity (shareholders, partners, etc.) to tax them. Thus, even if under domestic law of that State transparency regime applies, the treaty could prevent the taxation of profits obtained through the body of persons in the other contracting State. Actually, this happened in the case *Padmore UK* (United Kingdom, *Padmore vs. Inland Revenue Commissioners*, 1989, STC 493).

Collective Investment Vehicles (CIV's) can be transparent, and in such cases, they might not be a dividend distribution entity. This result does not seem contrary to the fiscal policy that the OECD pretends to justify for these entities, provided that States offer expeditious mechanisms to ensure that investors can access to conventional benefits. Conversely, if the CIV is the taxpayer of the corporate tax and the legal system allows it to: a) deduct payments to investors; b) have a reduced or zero tax rate; or, c) eliminate double taxation at the investor level through a system of integration; according to the OECD, the entity arguably should be considered as a resident or as a dividend-distributing entity (Par. 6.12 art. 1 CMOCDE). OECD's doubts on the consideration as resident of entities subjected to tax under those systems seem illogical, since, at least in the case c), this is what usually happens in integration systems. Nevertheless, Real Estates Investment Trust (REIT's) have similar problems and the OECD justifies the need to consider these entities as residents and as dividend-distributing entities, although they are transparent and/or non-taxable. Given the restrictions imposed by the wording of the Model, the organization expressly suggests to include them in the fourth circumference (OECD (2007, par. 18-19). The review of the tax treaties shows examples of these clarifications, and left as observation, that in all these cases is relevant to review if the remaining circles remain concentric. Whenever the circumferences become polycentric, conflicts of interpretation could arise.

The definition of company under the literal b) of article 3.1 of the model is part of the third concentric circle which allows the determination of the subjective scope of article 10 of the Model. At the same time, art. 3.1 and art. 10.3 characterize the element of the dividend-distributing entity, the fourth circle. Art. 3.1 defines companies as “legal persons” (first part) or “any entity that is treated as body corporate for tax purposes” (second part). It has been discussed if the first part is a reference to the private law. In the author's opinion, only legal entities for tax purposes are “companies” for the OCDE Model, because there is evidence that the drafters of the WP14 of the OEEC³⁸ did not intend to give the

38 OEEC, FC/WP14(59)1. The first definition stated: “The term ‘company’ means anybody corporate and any entity which is treated as a body corporate for tax purposes”; FC/WP14(61)1 in par. 3 explains two parts of the definition: FC/WP14(61)2 this report replaces “means” for “includes FC/M(61)5 This report approaches the

precise meaning of civil and commercial law. In addition, using the private law meaning contradicts the rules for the interpretation in tax treaties. Besides, it does not lead to a clear answer and contradicts the purposes clearly described in historical documents of the WP 14 and WP12³⁹. The latter Working Party pointed out that the dividend-distributing entity must be opaque, this is, to be considered as a legal entity for tax purposes. Anyway, *lege ferenda*, and for the sake of legal certainty, the Elimination of the first part of the definition of dividends is recommended. With regard to the second part, it has been questioned what does legal entity for tax purposes mean and in accordance with which state the entity must be treated as such. In our view, being a legal entity for tax purposes requires being opaque. To be more precise, history and wording of the OECD model articles' do not support para. 27 of the Commentaries to article 10, which seems to require that the entity should be liable to tax as "companies limited by shares" (*sociedades anónimas*)⁴⁰. In addition, the same paragraph requires to have a substantial similar treatment as legal companies, according to the State of the place of effective management. The latter is also an imprecise reference. It seems more reasonable to argue that art. 3.1 refers to the conventional residence status. Surprisingly, para. 3 of the articles 3 2010' OECD Commentaries refers to the State where the entity is 'organized', an equally equivocal statement, unless the express wording supports it, as the US Model⁴¹. In fact, in 2014 the Model Commentaries were amended to refer to the residence State of the entity. Doctrine supports other interpretations⁴² and some tax treaties expressly refer to the State of organization⁴³. That could lead to a situation where while the first two circles and the latter contain referrals to the domestic law of the State of residence, the circumference of the third acquires another Center to refer to the State of incorporation. It would give rise to conflicts of qualification highly discussed in the literature (Helminen, 2010, p. 82). But the author believes that those conflicts can

problem from a partnership perspective. vid. Avery Jones et al. (2009, p. 7). En contra: Avery Jones et al. (2000, pp. 8 y 9); Helminen (2010, p. 81).

39 Currently par. 2, 3 y 27 of the CMOCDE on art. 10, background, first report WP12 (FC/WP12 (60)4); CMOCDE 1977 art. 10 par. 26.

40 This can be seen at: OEEC, WP14(61)1; FC/WP14(61)2 this report is discussed in the Fiscal Comité FC/M(61)5. For entities not treated as independent tax payer by any contracting state. Also, entities treated as independent tax payers different from societies, would be excluded from the subjective scope of art. 10. FC/WP14(61)2; FC/WP14(61)4. Par. 5. Avery Jones et al 2009: p. 11.

41 Avery Jones et al 2009: p. 12 Organized and incorporated are synonyms. IEF's proposal adequate to the French version of the Model. English version the doubt is in the use of the word incorporated, however taking into account that the Word means creating companies and considering that other type of legal entities different from companies exists, we can conclude that the word organized is correct and its translation to Spanish should be "constituido" under the understanding that laws that regulate the contract "domicilio contractual" or "domicilio social", according the case.

42 CMOCDE previous to 2014. Also, Avery Jones et al. (2009, pp. 11, 12 y 44). Even though he suggests to modify the comentary, he admits that interpretation. Same does Helminen (2010, pp. 80 y ss).

43 Background: OECD (2013, par. 4).

be solved by disregarding the referral to the State of organization, as none other solution derives from a historical, systematic and teleological interpretation of DTC's.

DTC's do not contain rules on the allocation of income to a person, unless arguments from the Partnerships Report are accepted and the allocation made by the residence State is considered decisive (FC/WP14(62)1: párr. 11. FC/WP14(62)1: párr. 11). However, arguments used by the Partnership Report are not consistent (Lang, 2000, pp. 59-63), are not supported by the text of the OECD Model, and hardly would be applicable outside the subjective scope of DTC's. Consequently, internal rules which attribute the taxable transactions to a subject are not restricted by the treaties. However, for purposes of the income qualification, there is an implicit rule of attribution whenever the legal facts for the fiction of dividends are present in the actual situation. Thus, when there is a dividends-distributing entity in accordance with art. 3.1 and 10 of the OECD, the State of residence of the partners can tax the profits of the entity in the hands of the resident shareholders, even if no actual distribution takes place. However, partners Residence State should provide the method for the elimination of double taxation set by the Convention for dividends. (Chapter III, section 1.4)

As a result of the aforementioned conclusion, the legal fiction of dividends is not triggered if the entity is qualified as transparent by the State of the organization, even if somehow the entity is considered as resident by the applicable tax treaty (e.g. by the specific inclusion of pension funds, CIV's and REIT's). It can be gleaned from the fact that the definition of the transparency or opacity of the entity is referred by the tax treaties to the law of the State where the entity is organized. Only if the entity is opaque, the facts of the fictions are complete. Consequently, if the State of incorporation considers as transparent the entity, and the income is sourced in the same jurisdiction⁴⁴, the facts of the fiction are not fulfilled and the State of residence of the shareholders will not have to grant the method for the elimination of double taxation for dividends⁴⁵. Tax regimes of hybrid systems of transparency, such as the French *translucence*, may cause many problems and even legal double taxation due to conflict of qualification. In the author's opinion, the main conclusion that could be drawn for these issues is that treaty negotiations require a deep study of transparent regimes in the contracting States, provided that Governments really pretend to eliminate double taxation and share taxing powers with fairness and reciprocity. For example, partner's income from a French SCI under the Belgian jurisprudence was understood as immovable property, and Belgium had to grant the elimination of double taxation for the full taxes of the SCI that were allocated by the French law to the partners⁴⁶.

44 Similar requisite in example 6 of the Partnerships Report.

45 Lang & Staringer (2014, pp. 49-52). Although this is the solution they proposed, the *General Report* proposes different ones.

46 Belgium, Court of Appeals of Brussels, Case law from June 4th 1974, JDF, 1975, p. 83; Belgium, Courte of Appeals of Brussels, Case law from November 7th 2002, FJF2003/128. A similar critic in De Broe & De La Serna 2005: p. 15 et seq. Different perspective: Avery Jones et al 2009: p. 8; OECD (1999): párr. 124-139;

On the other hand, the fiction becomes mandatory when one of the contracting States considers the entity as its resident opaque company, regardless of the partner's residence State legislation⁴⁷. Consequently, if the income is sourced in the partner's residence State, such jurisdiction may tax the share of the partner, but it does not mean that the State of residence/organization of the entity could tax at the entity. That conclusion is clear from the Partnerships Report⁴⁸ and by the best doctrine (Lang, 2000, p. 92), because otherwise the functioning of treaties will tear. Connected with the aforementioned idea, the elimination of double taxation on the shareholders is arguable under the OECD Model Commentaries, because art. 23 A and 23 B (Par. 69.2 of the Commentary on art. 23 MCOCD) do not support an indirect credit is available to the shareholders for the proportional part of taxes paid by the dividend distributing-entity, as the Commentaries states. The result of the Commentaries generates a lack of neutrality if compared with entities in which there is not a conflict of attribution, insofar only a direct tax credit for the dividends is granted in non-conflict situations⁴⁹. Therefore, the author concludes that in this case only the method provided for dividends (under the OECD Model i.e. direct credit) should be granted to the shareholders. A remaining economic double taxation is possible, but only legal double taxation is relieved by art. 10 and 23 of the OECD Model. In any case, the Residence State must grant a direct credit, even if there is a timing mismatch.

CFC rules⁵⁰ are quite similar to conflicts of attribution referred in the latter paragraph and, in the author's opinion, both conflicts should receive the same solution. This conclusion is drawn due to DTC's are obliged to eliminate double taxation by admitting the fiction of dividends⁵¹. Even if the residence State of the partners ask for the *lex fori*

47 This are the exceptions content in examples 16 to 18 of the partnerships report.

48 Incorporated in par. 6.1 art. 1 MCOCD.

49 Same critic in Lang (2000, p. 98).

50 "Un análisis de la historia y el derecho comparado en la doctrina española": Almuñí (2005, pp. 29-106); par. 23 art. 1 MCOCD.

51 The MCOCD refers to the CFC rules since the modification to the Commentary in 1992, were they included arguments on favor (par. 22 art. 1 MCOCD 1992) and against (par. 23 art. 1 MCOCD) of compatibility. In 2003 Commentary establishes that such regimens are compatible with DTC, and reduces the contradictions. Supporting a dynamic approach: Almuñí (2010, p. 1110). In favor of in application of DTC rules for application of CFC rules: Supreme Administrative Court of Sweden. Case RA 2008 ref. 28; indicating that it constitutes a *treaty override* y that the CFC rule prevails. Supreme Administrative Court of Sweden (*Regeringsrätten*) SE: SAC, april 5th 2008, X AB v. Swedish Tax Agency 12 ITLR 311. Available at *Tax Research Platform* IBFD, Case Law. www.ibfd.org Furthermore, Canada and the United States establish that treaties do not apply to income from CFC. De Broe et al (2011): p. 378-379). Several Spanish DTC explicitly state that CFC rules must be applied according to the specific wording. Spain–Argentina 2013; Spain–Germany 2008; Spain–Armenia 2012; Spain–Barbados 2011; Spain–Bosnia Herzegovina 2010; Spain–Indonesia 2000; Spain–Jamaica 2009; Spain–Luxemburg 1987; Spain–Moldavia 2009; Spain–Dominican Republic 2013; Spain–Serbia 2010; Spain–Singapore 2012; Spain–Trinidad y Tobago 2009; Colombia–Mexico 2013. Spain–Australia DTC 1992 has a particular rule in art. 10.4 "4. En el caso de España, el apartado 2 de este artículo no será aplicable a las rentas que, con arreglo a las disposiciones de la legislación fiscal española, relativa a las sociedades en régimen de transparencia fiscal, sean imputables a los accionistas de dichas sociedades, se distribuyan o no a los

to interpret the term “income” used in article 10.1 of the Model, and consequently, the residence State find competence to tax CFC income of its resident persons, the treaty requires to qualify that fictive income as dividends. Thus, the treaty requires granting the tax treatment provided for dividends. In most cases CFC rules eliminate economic double taxation, through an underlying tax credit rule for taxes paid abroad (which will usually be zero or very low). Also, domestic CFC rules exempt actual distribution (Harris, 2010, p. 587). However, CFC rules will be restricted by the international law if the treaty sets a participation exemption rule, an indirect credit method or a tax sparing for dividends (Rust, 2004, pp. 264 ss; Almudí, 2005, pp. 356-359). In conclusion, CFC rules do not contradict article 7⁵², since it is well known that this is a general rule that must give in to special rules like art. 10⁵³. Fictitious income does not qualify as “other income” according to article 21 of the Model, since it is clear that there is a dividend distribution entity and there are corporate rights. The fact that a State autonomously defines the term “income” as fictive earnings does not prevent the application of article 10.3.

Actual treaties assimilate certain situations or contracts to a dividend-distributing entity. For instance, silent partnership yields under the OECD Model qualify as interest or business profits, but some actual treaties include that income in art. 10.3⁵⁴. However, the inclusion of silent partner’s income in the dividend definition modifies the center of the fourth circumference (the dividend-distributing entity) and almost always, the modification does not simultaneously amend the third circle’s center (the company)⁵⁵. As a result, it would be possible that income qualifies as dividends according to the definition,

mismos. Dichas rentas pueden someterse a imposición en España con arreglo a su legislación interna en tanto no estén sometidas al Impuesto sobre Sociedades español; Finland’s DTC states that participation exemption does not apply in those cases. In a similar way DTC Spain- Philippines 1994 states that paragraph 2 del art. 10 will not apply, but it additions that “no se concederá crédito alguno en Filipinas por impuestos pagados sobre tales rentas.” DTC Spain–Bulgaria, China de 1992, Philippines 1992, India de 1995 state that “el caso de España, el apartado 2 del artículo 10 (equivalente al MCOCDE) no se aplicará a la renta imputable, distribuida o no, a los accionistas de las Sociedades y Entidades a que se refiere el artículo 12.2 de la Ley 44/1978, de 8 de septiembre, y el artículo 19 de la Ley 61/1978, de 27 de diciembre, en tanto dicha renta no esté sometida al Impuesto sobre Sociedades español. Dicha renta puede someterse a imposición en España con arreglo a su legislación interna.”

- 52 Almudí (2010, p. 1109). Wassermeyer: en Debatin/Wassermeyer, Doppelbesteuerungsabkommen, art. 1 OECD-MC, marg. Note 76 seq.; idem, Pref. to art. 6-22 OECD-MC marg. Note 15. Cited by Rust (2004, p. 265).
- 53 Income attributed to the owner of a non-resident controlled company under the CFC rule, are dividends according to art. 10 MCOCDE because they are “yields of shares” in a “company” of the other contracting state. The word “company” defined by art. 3.1.b) supposes that the State that applies the CFC rule has to follow the meaning of “Company” that results from the application of the legislation of the other contracting state. Hence, income must be qualified as dividend.
- 54 As the expression income is not defined in the DTC it must be defined according to the *lex fori*. The doctrine states that the domestic definition of the State that applies the treaty is the one that applies. In CFC rule cases it would be the residence State the one applying article 10.1 MCOCDE. In this sense Helminen (2010): p. 136-137. Against, case law from June 28th 2002 of the French *Conseil D’Etat* in *Schneider* case.
- 55 Protocol of the DTC Spain–Portugal 1995. The ruling of the DGT in February 19th 1992 stated that the DTC Spain-Portugal dividends are the retribution obtained by a non-resident individual for the contributions to a silent partnership.

but the payer does not qualify as a company. The aforementioned situation is quite possible because the general partner can perfectly be an individual or a body of persons not treated as body corporate for tax purposes. Anyway, from a tax policy perspective the definition pretends to cover income similar to company-shareholder distribution of profits, and if potential double taxation is the main characteristic of this type of income, most probably income obtained by silent partners should not be treated as dividends whenever the payment could be deducted in the general partner taxable base. (Chapter III, section 1.5.1) Furthermore, conflicts of qualification can arise in relation to yields received by the trust's beneficiaries, since such contracts have different typologies and usually trusts are not considered as dividend-distributing entities and the beneficiaries' rights in the estate do not meet the conditions of being corporate rights.

Thirdly, CIV's could have problems qualifying as a dividend-distributing entity. For example, Finnish jurisprudence qualified as "other income" payments made to investors, in spite of the fact that the fund was a "resident" "company" in Finland. The Finnish Court argued that the taxation of dividends is not equal to the yields of investors because funds are exempt, forgetting that the third part of art. 10.3 refers to the tax treatment of partners or investors and not to the regime of the dividend-distributing entity (Helminen, 1999, pp. 1155 y ss.; Helminen, 2000, pp. 135 ss.; Helminen, 2013, pp. 211 ss.)⁵⁶. In addition, the rights of investors could be subsumed in the second part of article 10.3 of the model. Actual treaties sometimes exclude funds of the resident definition⁵⁷, but other treaties expressly include funds in the subjective scope of the treaty (the second circle)⁵⁸. Few treaties include fund's returns in the dividend definition, which could be also problematic with article 10.1 (the third circle) and 1 (the first and second circles) of the Model if funds as such are not considered companies or resident persons. Finally, it is highly recommended to evaluate if the objective of neutrality is achieved, because when CIV's are opaque and the domestic tax law pretends to tax the investors, art. 10.2 of the Model could limit the taxing powers. Therefore, the treaty must allow the tax policy desired taxation at the level of the investors. United States' recent treaties are examples of best practices in this regard.

Fourthly, fiscal policy suggests to promote investments through REIT's. In order to achieve this policy, several States eliminate the taxation at level of the entity. Under those regimes, the investors do not obtain income from the same source or original qualification, since it would imply an unlimited taxation in the source States due to the fact that REIT's mainly receive income from immovable property. The OECD Commentaries suggested to treat REIT's as dividend-distributing entities, even if they were not considered as "residents" under the Model wording and Commentaries. The approach proposed by the Model

56 Vid. Finland, *Korkein Hallinto-oikeus*, Caselaw of June 14th 1999, n.º 1600; KHO: 1999:34. Available at *Tax Research Platform*, IBFD.

57 Spain-Chile 2004; Spain-Jamaica 2009; Spain-Uruguay 2011; The application of a DTC is allowed with the condition that authorities establish the requisites in de DTC: Spain-Germany 2012; Spain-France 1997.

58 Spain- Korea 1994; Spain-Germany 2012; Russian Model.

is the direct amendment of art. 10, that is, the Model suggest to include income from REITS in the dividend article⁵⁹. This proposal also arises problems with respect to article 10.1 (the third circle). In short, it can be gleaned from the OECD REIT's Commentaries that article 10 of the Model is used to trigger the fiction that investors are not receiving the underlying income. To put it in a different way, whenever art. 10 includes REIT's distributions, the dividend article does not to characterize an item of income that potentially entail economic double taxation, which is clearly in absent therein. In brief, the traditional *ratio* of art. 10 is lost.

Finally, PE's are taxable units which can be assimilated to the dividend-distributing entities⁶⁰. However, PEs are not "companies" "resident in the other State Contracting", nor the headquarters have a corporate right on the PE. As a result, the OECD Model hardly could offer fiscal neutrality for repatriation of PE's profits and the dividends paid to subsidiaries, unless the subjective scope of the DTC's and the dividend definition were opened to cover the PEs. Moreover, discrimination issues can emerge as far as a branch tax is a tax on the same taxable person liable for business profit tax: the non-resident company. It means that while the single same non-resident is taxed twice, resident entities are taxed only once. The person liable for the second level of taxation is the shareholder. Thus, branch taxes could transgress articles 24, 10.5, 10.1 and 3.1. b) of the Model Convention. Under the current structure of the Model, better results are achieved through the inclusion of specific safeguard clauses and the allocation of a neutral tax treatment for dividends from a substantial participation and branch taxes. In conclusion, some actual tax treaties do not qualify PE's profit repatriations as dividends, but align their tax regime under tax treaties⁶¹.

The dividend-distributing entity as the first element of the dividend definition requires to differentiate between dividends paid to the shareholders and profits of the entity. Restrictions from article 10.2 of the Model refer only to dividends. Courts and doctrine have established that the criteria for distinguishing must be strictly formal, i.e., dependent on who is the taxpayer⁶². Consequently, if the dividend-distributing entity pay the tax for the distributions, but the entity is not the taxpayer, DTC's limits would apply because the taxpayer is the shareholder and the company in only liable for collecting the revenue. Therefore, differentiation must be taken into account by the negotiators of the CDI clarify cases where it can be difficult to determine who is the taxable person for the distribution of

59 Par. 67.1 ss. art. 10 CMOCDE. DTC Spain-Singapore 2012.

60 France, *Cour administrative d'appel de Lyon*, Caselaw September 22nd 2009, *Caso Sté Médecine Beauty*, n.º 06-1048. Available at www.ibfd.org

61 Chilean DTC are an example of a reasonable solution to the question. Vid. Reservation to par. 74 al art. 10 of the CMOCDE made by Chile. Consequently, United States are a good example, because the second level of taxation applies to immovable income taxed on net basis. United States has a regimen that regulates a presumptive value called *equivalent amount*. Vid. MCEUA, *Technical Explanations*, art. 10, paragraph 8, p. 38. Based in the *Internal Revenue Code* § 884(a). Finally, DTC Canada-Spain 1981.

62 Australia, Case L23 (1979) 79 A.T.C. 110 (Board of Review).

benefits. Reciprocity⁶³ in DTC`s depends on the aforementioned distinction. For example, Colombian domestic law eliminates economic double taxation exempting dividends from profits which has been taxed at the company level. Dividends from untaxed profits are liable to tax. Colombian system has required the addition of exceptions to article 10 of the MCOEDE in order to allow Colombian taxing right above the limits of 5-15 %. However, the wording of some CDI protocols has not accomplished this purpose.

B. Corporate rights

Article 10.3 points out that the source of the income described therein are the corporate rights defined formally in the first part, described in a broad way in the second one, and referenced to the source State in the third one. The relationship between the three parts of the definition is far from clear. Yet most of the scholars (following VOGEL's position⁶⁴) hold that there is an intrinsic meaning in all three parts of the definition. However, they seemed to assume as intrinsic meaning the debt-equity distinction under the German domestic legislation. And the use of domestic dividing-lines between both categories is not a proper way to describe the treaty's (autonomous) meaning, because those lines are not the same in accountancy, corporate and tax law, neither they are similar in meaning in the different domestic legal orders. Drawing-line rules can use formal or substantial criteria. Even so, substantial criteria can give more or less weight to political rights, the participation in profits or the participation on liquidation proceeds⁶⁵. As a result, the author concludes there are three distinct parts of the definition, which use three different approaches to describe the source of the income. That is the reason why this thesis plea to the treaty negotiators to evaluate the meaning that each right mentioned in the three parts of art. 10.3 could acquire under the domestic (private or tax) law definition. If those interests in companies derive income which is not taxed as income from ordinary shares, tax policy results must be considered. This is quite important, because the two conditions mentioned in the second part of the definition, i.e. to participate in profits and not being debt-claims, do not restrict the rights included in the first part⁶⁶. Certainly, the aforementioned two conditions seek to characterize the "other rights". WP12 documents support this conclusion.

63 South Africa, High Court Volkswagen of South Africa (Pty) Ltd v. The Commissioner for the South African Revenue Service, 70 SATC 195, 21 April 2008. Analysis of the case in Hattingh (2009, pp. 442 y ss).

64 Vogel (1997, art. 10, par. 185, 188, 189); adopted with some differences by: Eberhartinger & Six (2009, p. 9); Helminen (2010, p. 175); Bärsch (2014, p. 435).

65 Conclusion of an important analysis of Australia's, Germany's, Italy's and the Netherland's systems Bärsch (2012, p. 322). On the other side, a study made by the Insitute *Max Planck* directed by SCHÖN studied the tax systems of Austria, Germany, France, Switzerland, United Kingdom and United States. The study concluded that corporate qualification of the Company's equity or rankings in bankruptcy process, should not be relevant for tax purpose from a theoretical point of view, but in reality they are. SCHÖN et al. (2009, pp. 95-99). Financial and accounting rules have a minore role.

66 Pijl (2011, pp. 493 ss). In the same sense Bärsch (2014, pp. 434-435).

The first part of the definition lists a number of rights. The list could be interpreted in two different ways. Firstly, it could be stated that those rights have the specific meaning under the private law in the residence State of the entity or, secondly, that common characteristics of the listed rights under private and tax law should define the category. However, it is difficult to establish which features are common, since:

(i) In English language, the word shares mean interests in companies (*sociedades de capital*), while in Spanish and French language the locution *actions* and *acciones* represents the participation in *sociedades anónimas* and *sociedades en comandita por acciones*⁶⁷. Indeed, the Spanish and French meaning is narrower than the English one. Besides that, given that there are different dividing lines between debt and equity, the types and classes of shares may be subject to different classifications under corporate, accounting or tax rules. For example, redeemable shares, preferred shares and non-voting shares may be classified as debt for accounting or fiscal purposes, but those shares keep the classification of capital under corporate law.

Most of scholars state that the participation in losses or the participation in the liquidation proceeds is the main feature of dividend-generating assets (Vogel, 1997: art. 10, par. 192, p. 653; Helminen, 2010, p. 204). However, these features seem arbitrary, insofar there are preference shares subjected to caps and floors on the liquidation proceeding. Those cap and floor clauses do not necessarily imply that the income received by the shareholder have ceased of having an underlying taxation nor is possible to argue that the preference shares are not shares. In addition, shares with such caps and floor privileges would not qualify as interest-generating asset nor as dividends-generating assets under the criterion of the participation in the liquidation proceedings. Most probably, income from those preference shares qualifies as business profits (art. 7 OECD Model) or other income (art. 21 OECD Model), thus the source State must restrain its taxing powers. Consequently, the outcome of the participation-on-liquidation-proceedings requirement is questionable from the perspective of neutrality and the fair share of taxing rights. Furthermore, it is not clear what would happen if the shareholder participates in the increases of value in the liquidation share, but not in the losses, or vice versa. Neither is it clear if the participation-on-liquidation-proceedings requirement excludes shares which do not have a right in the contingent repayment amount or even if it excludes contingent rights to participate on the liquidation proceedings. For instance, redeemable shares participate in the risk of the company until the redemption date. Conversely, redeemable shares do not participate in the risk of the entity after the conversion date or if the shareholder has a put option. Finally, some authors set as intrinsic characteristics of corporate rights the participation in the liquidation proceedings and the participation in the current profits. This thesis has defended that both criteria allows two different qualification results in cases of hybrid financial

67 There are several differences in the English, French and Spanish versions of the Commentary on article 10. The first, refers to capital of a *corporation*, or *joint stock Company*. While the French version refers to *societe anonym* and explains it like a capital society.

instruments. Moreover, participation in profits could be interpreted as the contingency on the right to receive the yields, or a contingency on the amount of the yields. Doctrine is not always clear in front of this disjunctive, and for instance, it would lead to different answers with respect to the shares with a fixed-dividend (cumulative and non-cumulative) amount. In conclusion, an (subjective) intrinsic meaning in art. 10.3 of the Model leads to legal uncertainty.

(ii) “Jouissance shares” and “jouissance rights” have different meanings in private and tax law across the world, as this thesis has probed. In the French and Spanish versions of the Model only “bonos de disfrute” are included. However, English version includes jouissance “rights”. Consequently, English version seems to be broader than the Spanish/French version, insofar the latter only cover what could be translated as “bonds”. “Jouissance shares” and “jouissance rights” do not pretend to describe the same type of rights, because in the Spanish version the word “bonos” and “acciones” are securities, but only the latter represents the shared capital. So, it is hard to argue that these words seek to designate the same kind of property. The inclusion of “jouissance shares” and “jouissance rights” in DTC’s is arguable when the domestic law does not rule these assets in the corporate law. Moreover, the author has found the following interpretations of “jouissance shares” and “jouissance rights”: (a) an usufruct right⁶⁸; (b) an asset that gives the right to participate in profits, but with restricted political rights (e.g. non-voting shares)⁶⁹; (c) a participation right without voting-rights issued after a capital reduction. This meaning has an important historical support⁷⁰; (d) any right to participate in the corporate profits that cannot be classified as other income. Without doubts, the aforementioned four meanings probe that “jouissance shares” and “jouissance rights” have not a single common or intrinsic meaning (Lucas, 2000, p. 217). Actually, those words are an open door in the intended boundaries between dividends and interest. Finally, VOGEL’s intrinsic meaning

68 The *International Tax Group* admits that in France exist jouissance rights, but not jouissance shares. Jouissance rights are conceived as real rights of shares, for instance, usufruct or Contractual rights. The owner of the usufruct generally has the right to vote”. Avery Jones *et al.* (2009, footnote 82, p. 17). It refers to art. L225-110 *Code de Commerce*.

69 Vogel (1997, art. 10. par. 193, p. 652). Avery Jones (2009, p. 17 ss). Belgium legislations have *Winstbewijzen* or “parts bénéficiaires” see art. 483 of the *Code des Societes*. This provision refers to securities that societies can emit, but do not represent capital. (art. 460). Belgium, art. 483 *Code des Societes*. Italy article 2351 of the *Código Civile*. Refers to the right to vote that shares have. According to which the holder of the privileged shares can vote if the society statutes approve it. This same provision establishes that shareholders of shares with limited voting rights cannot surpass half of the capital. Scholars agree that bonds or jouissance shares are social interest with no voting rights. In Switzerland, *jouissance rights or shares* are the same as *bons de jouissance/ Genusscheinen*. Netherlands legislation establishes that they are comparable to *winstbewijzen* that are certificates of participation in profits.

70 The Belgium *Code des Societes* (art. 615) and the French *Code de Commerce* (art. 1225-198) uses “actions de jouissance”, that is similar to “jouissance bonds” used by the Spanish LSC (art. 260 y 341), previously regulated in art. 48.3 LSA. El TEAC, Resolution June 11th 2004 (n.º 00/4008/2001) established that yields on jouissance bonds are considered interest in mutual funds and must be differentiated from the distribution of bonds that could be tax as capital gains. See OECD, CFA/WP1(73)2.

could restrict the wide meaning of “jouissance shares” and “jouissance rights”, but it only would make sense from a German law perspective (although there are judgments contrary to such a conclusion in that country). Outside Germany, VOGEL’s⁷¹ intrinsic meaning is arguable⁷².

(iii) The Spanish locution “participaciones mineras” are described in English as “mining shares”. Probably “shares” in English is a word used in a broader sense than the French term “actions” or the Spanish locution “acciones”. If the English broader sense is accepted, the first asset set forth by article 10.3 of the model could also have a wider meaning in English than the terms “acciones/actions” in Spanish and French. Furthermore, mining shares may have a special meaning under the domestic law. Conflicts or qualification will arise if under the domestic law the mining company is a transparent entity, because from a formal perspective the yields in transparent mining companies could be classified as dividends. However, this thesis concludes that previously to the qualification of the corporate rights, it is necessary to classify the entity as a “company” under art. 3.1 and 10.3 of the Model. Nevertheless, in order to avoid discussions, it is important to exclude mining shares when mining companies are transparent⁷³. Founders’ shares are also dividend-generating rights in the OECD Model, but some actual treaties do not include them in the dividend definition. The exclusion of founders’ shares make sense whenever they could be qualified as “shares” or even as “other corporate rights” subjected to the same taxation treatment as income from shares. But the exclusion also makes sense when that taxation treatment is not similar to the one for income from shares. For instance, Spain includes founders’ shares in most DTC’s dividend definition, although that earnings are taxed as employment income under the domestic law (Art. 16.2 lit. g) LIRPF). As a result, income from founders’ shares sourced in Spain could have an asymmetrical tax regime in treaty situations. Documents from the WP 1 of the OECD in 1973 explain that the words “founders’ shares” attempted to include rights “allotted to persons who have rendered services in connection with the promotion” of the company. Those documents contradict VOGEL’s interpretation of the intrinsic meaning of corporate rights, insofar WP1 admits that founder shares usually do not give rights on the liquidation proceeds (OECD, CFA/WP1(73)2; vid. Pijl (2011, p. 492).

The third part of the definition contains a dynamic reference to the domestic law of the source State. The reference must be applied in good faith, as the provided by the VCLT. Under the OCDE Model the income should: a) arise from a corporate right; and

71 VOGEL (1997, art. 10. parr. 193, p. 652); in the same line Helminen (2010, pp. 187-190).

72 Germany, FG KÖLN – Finance Court Cologne (*Finanzgericht Köln*), December 11th 2003, 2 K 7201/00, EFG 2005, p. 541. Avery Jones (2009, footnote 86, p. 17). Against Vogel (1997) Germany, Federal Fiscal Court (*Bundesfinanzhof*), Case I R 53/09, 26 August 2010 Available at: *Tax Research Platform*, IBFD. Germany, *Finanzgericht Nordrhein-Westfalen* (Köln), Case law from April 29th 999, case 2 K 3998/95. Available at: *Tax Research Platform*, IBFD.

73 Similarly, Vogel (1997, p. 654, par. 196).

(b) be subject to the same taxation treatment as income from shares. The wide and the widest reference used by actual treaties amend the first requirement because corporate rights can be understood: i) *stricto sensu*, as rights which have the common characteristics of the assets mentioned in art. 10.3 of the treaty. For example, VOGEL's intrinsic meaning or the OECD Model Commentaries' risk criterion can be considered the common characteristics; (ii) *lato sensu*, corporate rights are any financial relationship treated by the law as such, or even by any relationship in which the counterpart is the company, as PIJL states⁷⁴.

The reference to the domestic law contains a second condition: the comparability test. It is clear that the OECD and the OEEC pretended to ensure the tax regime under the DTC for those elements of income that have been taxed as income from ordinary shares. Income from shares' regime is characterized as one single taxable object that is liable to two taxable events in two subjects. Therefore, that kind of income would be the intended meaning, and the words and expressions of article 10.3 would be the signs. The primacy of the treaty (autonomous) interpretation of "corporate rights" and the first and second part of definition only can dissociate the meaning and the signs used to describe dividends. The aforementioned dissociation increases the debt-equity conundrum⁷⁵.

Under the 1963's OECD Draft Model wording of the third part of article 10.3 it is possible to directly refer to the definition rules for income from the participation in companies' equity, and also it is possible to check other rules that assimilate income to the dividends category. By contrast, the wording of art. 10 in the 1977's OECD Model refers to the tax regime of income from shares. That wording requires assessing a very large number of factors (the subject, the tax rate, the tax base, the timing issues and the territorial scope) that are difficult to compare. For instance, there are different tax regimes for domestic income from shares, for outbound income from shares, for income from shares earned by individual or companies, for income from shares that represent a portfolio holding or a substantial participation, etc. Furthermore, some domestic systems do not differentiate the tax treatment of some interests and capital gains, like DUAL systems. Conflicts of qualification could arise in those cases, especially if the deductibility criterion is not taken into account. The deduction of the payment from the taxable base of the payer company seems to deviate from the wording of the reference to the domestic law, because it mentions the tax regime of the shares, but not the taxation of the profits of the company. Consequently, the *ratio* behind the definition suggests considering the income as one single taxable object.

The relationship between dividends and interests in tax treaties is defined by the idea that debt-claims cannot qualify for the second part of the definition of dividends⁷⁶. However, debt-claims can be considered "corporate rights" under the third part of the definition, if a *lato sensu* interpretation is accepted (Pijl, 2011, p. 484). However, the OECD Model

74 Pijl (2011, p. 494). See Brown (2012, p. 34).

75 Chez Republic, Case: AAA v. Financial Directorate, 8 ITLR, 178 *et seq.*

76 Vogel (1997, n.º 229, art. 10 y n.º 61, art. 11). Against: Bundgaard & Dyppel (2010, p. 662).

Commentaries lack of clarity due to the fact that they pretend to justify the existence of a treaty (autonomous) meaning based on the criteria of the effective assumption of the risk run by the company (OECD, 1987a, par. 56). The Commentaries do not explain if that criterion applies as an intrinsic meaning (Vogel, 1997, par. 188, art. 10) for all the rights mentioned in the definition, or if it only applies to the third part. The author concludes that risk criterion could only be based on the third part wording, but anyway the risk criterion could not be supported because is far from clear. What should be kept in mind is that the risk criterion or the *lato sensu* interpretation of “corporate rights” would cause an overlapping between art. 10 and 11, since “debt-claims” are always interest-generating assets, but when they participate in the risk run by the company⁷⁷, article 10.3 would also apply. This overlapping should be solved by giving preference to art. 10 of the Model, although some actual treaties rightly include a tiebreaker rule that expressly addresses that issue.

The author’s conclusion on the *lato sensu* meaning of “corporate rights” is not supported by the OECD. The OECD Commentaries, instead of accepting the broad reference to the domestic source tax law (as a result of the wide meaning of corporate right), assume the risk run the company criterion to distinguish between yields dealt in articles 10 and 11. The risk is measured by a multi-factorial analysis that may produce inconsistent results. Some factors give prevalence to the criterion of remuneration, while others give prevalence to the legal repayment criterion. In the meanwhile, other factors analyze the economic risk of the repayment, which analyze possible thin capitalization situations⁷⁸. Scholars have attempted to justify a single factor for distinction, but the authors vary on which factor would be considered as “The Factor”. The first group of scholars argues that shares should give rights to participate from the eventual increases in the value of the company’s assets⁷⁹. The second group of authors partially agrees with the former because they accept a positive perspective of the risk-sharing, but at the same time they ask to see beg for seen the other side of the story: the participation in the possible losses, which is mainly the repayment subordination to claims from other creditors (Lang, 1991, p. 124 ss., Cited by Bärsch, 2014, p. 436; Rotondaro, 2000, p. 265; Eberhartinger & Six, 2009, p. 9; Helminen, 2010, pp. 183-184; 197-198; 193-195). These criteria are also blurry to delimit the categories in structured hybrid instruments, and in some way these criteria lacks of any fiscal policy sense⁸⁰. Finally, it is worth to mention that treaties with interest definitions containing references to the domestic tax law can create conflicts of qualification⁸¹. For instance,

77 Vid. par. 19 art. 11 and par. 25 art. 10 CMOCDE.

78 Vid. par. 25 art. 10 CMOCDE.

79 Distinctive criterion of the social interest Lang (1991, p. 125) (cited by Bundgaard & Dyppel (2010, p. 658).

80 Scholars agree that MOCODE definition generates qualification conflicts. Eberhartinger & Six (2009, p. 10); Helminen (2010, pp. 183-184; 197-198; 193-195); Bärsch (2014, p. 444).

81 Chez Republic case n.º 2 Afs 42/2008-62, *LACRUM Velke Mezirici s.r.o. vs. Finanční reditelství v Bme* the Supreme Administrative Court analyses the DTC subscribed with Germany in 1980 and concludes that the “interest requalified as dividends under domestic law do not fall under the scope of article 10 od the DTC and

the Brazilian *juros sobre o capital proprio* (JSCP) can be considered dividends for treaty purposes under the risk run the company criterion⁸². However, under the Spain-Brazil tax treaty, interest definition has a reference to the domestic tax law in the residence State. Due to the fact that Brazilian domestic law treats JSCP as income from debt-claims, for treaty purposes the income must be qualified as interest rather than dividends⁸³. Nevertheless, interest and dividend definition in tax treaties are not applicable to the Spanish domestic participation exemption rule. Consequently, income from JSCP could be exempted by art. 21 of TRLIS (in force until the 31st December 2014). In conclusion, hybrid instruments mismatches should be tackled through a comprehensive approach⁸⁴

Measures adopted by the States to combat thin capitalization situations have strained the definition of dividends and the reason for the existence of art. 10 of the Model. Three types of rules prohibit the interest deduction in the payer taxable base. The first type of rule re-qualifies the financial instrument in equity; the second one reclassifies the yields in dividends; and the third one, only prohibits the deductibility. Tax treaty classification of non-deductible income under these three types of rules is questionable under the third part of the dividend definition. On one hand, the right should be considered as a corporate right at least under the OECD Model. If the criterion of the risk run by the company is accepted, the instrument in the three types of rules could be considered as a corporate right for treaty purposes, provided that the investor actually shares that risk and regardless of the private and tax law classification. The same interpretation could be gleaned from the wide meaning of corporate right i.e. all kind of financial or associative relationships. However, some authors and some case law admit that only reclassifications of the first type qualify as dividends, because only in such cases the financial instrument has been re-characterized as a corporate right in accordance of the treaty. On the other hand, the tax treatment comparison should be evaluated with all the factors that have been mentioned before and, in principle, the non-deductibility should not be part of the taxation treatment of income from shares.

In practice, the discussion about the meaning of corporate rights as the source of the income leads to the determination of the reasonable capitalization of a company. Therefore, the problem relies in the determination of the non-deductible interest amount and/

the definition of dividend included in the treaty". Available at www.ibfd.org Tax Research Platform. In the same sense Czech Republic—Case 2Afs 108/2004–106, 10 February 2005. Available at www.ibfd.org Tax Research Platform. vid. Van Weeghel (2010): p. 33. However, a recent case in Russia analyses the DTC subscribed with United States and concludes that the re-qualification due to thin capitalization rules cannot be affected by the Treaty's articles 10 and 11. It should be referenced to the domestic legislation of the State of Source. Russia, Cassation Court of Arbitration of Moscow Region N A40-1164/11-99-7, 28 February 2012. Available at: www.ibfd.org Tax Research Platform. MCOECD 2010 of Russia has a explicit reference to a requalification in dividends to the excesses of interest, according to thin capitalization in the definition of dividends.

82 Against: Calderón (2012b) y España, SAN 712/2014, del 27 de febrero, Recurso 232/2011.

83 Vid. bibliography cited: Castro (2014), pp. 120-122).

84 OECD 1987a: par. 56; par. 25 art. 10 del CMOCDE 2010; Calderón 2012b: aptdo. 4.

or the amount of income subject to the taxation treatment as income from shares. The OECD Commentaries propose that the aforementioned amount has to be assessed through the risk run by the company criterion and also through the principle of arm's length. In the author's opinion each of the methods can reach different results and create legal uncertainty⁸⁵. Under the wide meaning of corporate rights theory, the quantification of the aforementioned amount is not relevant.

Finally, paragraph 68 of the OECD Commentaries on article 23 sets the conditions for the cases in which the residence State is obliged to grant the method for elimination of double taxation for dividends of income from debt-claims, that have been qualified under the art. 10 by the source State. It is worth to mention that the 1987 OECD Report on thin capitalization included those conditions for domestic methods or treaty methods that refer to the category of income without indication of the article 10 of the Treaty. Consequently, restrictions set in par. 68 of the OECD Commentaries on art. 20 neither apply under the wording of art. 23 of the Model, nor under treaties with methods containing a reference to article 10.

Solutions for the lack of neutrality in the tax treatment of debt and equity can be found in theoretical proposals and in some few countries' law. The reason for the existence (*ratio*) of the dividend definition in the OECD Model is questionable when differences between dividends and interests are relieved through those proposals. The solutions can be classified into two broad groups according to their impact on the international taxation: (a) proposals that reinforce the taxing powers of the source State, in particular. i) limiting the interest deduction⁸⁶; and, ii) imposing a dividend equivalent withholding tax at the source State for interest from debt-claims with an economic meaning similar to equity. Both solutions may cause inconsistencies in tax treaty situations. For example, yields that are non-deductible could be understood as "corporate rights" in a broad sense and subject to a similar tax treatment to income from shares (Schön, 2012, p. 501). Moreover, the second solution requires defining which instruments are similar in economic terms and, consequently, renegotiate the tax treaties should in order to allow the dividend equivalent withholding tax for interest for that kind of debt-claim⁸⁷; (b) Proposals that reinforce the

85 In this sense Helminen (2010, pp. 220-221); Castro (2014, p. 123). Vid. par. 25, art. 10 CMOCDE. OECD (1987a) Committee of Fiscal Affairs. *Issues in International Taxation n.º 2 –Thin Capitalization and Taxation of Entertainers, Artistes and Sportmen*. París: OECD: par. 48 y 49. In the same sense par. 3 of the Commentary on art. 9 of the MCOCDE. Makhmudova (2007), p. 258. Art. 9.1 of the MCOCDE authorizes States to correct the taxable base to adjust the operations vintulated as long as they are in accordance with the Independent principle OECD (1987a) Committee of Fiscal Affairs. *Issues in International Taxation n.º 2 –Thin Capitalization and Taxation of Entertainers, Artistes and Sportmen*. París: OECD: par. 48 y 49. In the same sense commentary 3 al art. 9 del MCOCDE. vid. Makhmudova (2007, p. 258).

86 The proposition supposes increasing the taxable base of corporate income tax. Vid. Schön (2012, p. 490).

87 Schön (2012, pp. 499 ss). Vid. MCEUA 2006 article 11.2 lit. Similarly, protocol n.º 1 del German Model 2013. Bärsch (2014, p. 441).

taxation in the Residence State⁸⁸. For instance, allowance for corporate equity and dividend deduction reduce the taxation in the source State and increases the liability in the Residence State if the former jurisdiction does not grant the indirect tax credit nor the exemption. Dividend deduction systems could cause conflicts of qualification under tax treaties⁸⁹.

C. Relationship between source and yields

Art. 10.3 requires a link between the income and the source — the corporate rights —. The required relationship is described with the word “de” in the dividend definition, and no more requirements can be derived from the treaties. Thus, domestic tax law link between the income and the source is not restricted by treaties. Therefore, there is no legal support for statements made by most of the doctrine⁹⁰ in the sense that it requires a shareholder relationship as the source of the income. As discussed above, domestic tax law can assume wide and narrow perspectives on the *societatis causa* which could result in conflicts of attribution (Helminen, 2010, p. 57). However, conflicts of attribution are not solved by tax treaties, and art. 10.3 requires a link between the income and the corporate right that can be determined by the domestic laws of the Contracting States within a very wide framework. In the author’s opinion and according to article 10.3 and 3 (section 1 and 2) of the Model, if domestic laws define the nexus in a way that produce a conflict of qualification of the income, the Source State nexus prevails over the residence State nexus. The OECD Model Commentaries recognize that dividends could be considered income from corporate rights or profit distributions⁹¹ depending on the tax policy decision adopted by the States regarding the higher or lower weight attributed to the entity’s ability to pay conditions or the partners’ ability to pay conditions. Hence, tax treaties do not restrict the measures seeking to prevent hidden profits distributions that reduce the assets of the dividend-distributing entity when a corporate right is the source of the income, even if the dividend is attributed to a person that is not the shareholder.

The word Income is part of the nexus required by the dividends concept in tax law. Tax treaties do not define income. Domestic tax laws define income in different ways, and several times domestic laws have different tax treatments for income from corporate rights and capital gains arising from the alienation of corporate rights⁹². Different tax treatment

88 Including the deduction of dividends of the distribut entity. *ACE* systems include *notional interest* that allows the deductibility of distributed dividends to shareholders to a maximum or fictional limit of the taxable base from the distributing entity. For instance, admitting the deduction of the rate of interest from a bond with no risk. Schön (2012, pp. 501-502).

89 SAN 712/2014, February 27th, *Recurso* 232/2011; Calderón (2012b, aptdo. 1 ss).

90 Vogel (1997, párr. 188). Similarly, Helminen (2010, p. 9 ss.) and Hattingh (2009, p. 518).

91 Par. 1 and 24 art. 10 CMOCDE. Vid. Hattingh (2009, p. 518).

92 OECD (1988, p. 121); par. 1-4 art. 13 CMOCDE.

of income and capital gains from shares in domestic legislation creates opportunities for tax arbitrage. Thus, it is common that domestic laws' biases toward capital gains encourage the avoidance of the dividends tax regime. DTCs emphasize those differences, insofar as taxing powers of capital gains on the alienation of corporate rights are allocated to the residence State (art. 13.5 OECD Model). By contrast, taxing powers on income from corporate rights may be taxed in the source State under the limits or art. 10.2 of the Model. As a result, the principle of symmetry is broken between the tax-treaty treatment of assets income, gain and capital⁹³. However, the author concludes that the source State can attempt to tackle the bias through the application of the same tax treatment of dividends to capital gains on the alienation of shares. DTCs do not prevent the dividend qualification in the source State of capital gains from shares in the third part of article 10.3 of the model. Therefore, the residence State should not oppose its domestic law in order to deny the method for the elimination of double taxation granted for dividends in tax treaties, despite the fact that the concept of income under its tax legislation does not include capital gains from shares. To put it in other words, capital gains in the alienation of corporate rights that would qualify in article 13.5 of the Model can be considered as dividends if the source State decides to tax them as income from shares⁹⁴. Therefore, a priority rule can be gleaned from arts. 10 and 13.5. it is worth to mention that the term income used in the tax treaties cannot be the basis for claiming the theory of the fruit and the tree, and under this reason it is not valid the argument that states the dividend article in tax treaties should include income that does not consume its source (Vogel, 1997, art. 10, par. 9a). *Lex fori* interpretation and application of the word "income" becomes mandatory under tax treaties. Each State law should make the distinction between capital gains and ordinary income and art. 10.3 could not limit it. Under this conclusion fictitious income, payments in kind and hidden distribution of benefits could be considered "income" for the art. 10.3 purposes. However, few tax treaties avoid possible restrictive interpretations, and have replaced the word "income" with "earnings", "receipts", "items" or "amounts" (Vogel, 1997, par. 186 art. 10; DTC Spain–United Kingdom, 2014; Hattingh, 2009, 518). In conclusion, the word income must be interpreted in accordance with the taxes covered by the Commission (art. 2 MCODE) and therefore in accordance with the *lex fori*. For instance, the State of residence can understand as "income" one that has not even been qualified as "income" in the other State.

In view of the *lex loci* interpretation of "income", article 10 should be studied with respect to the restrictions that may be imposed by the words "from" and "corporate rights". In the author's opinion, the nexus could only be derived from those two words but as mentioned before, the allocation of income is not restricted by the dividend definition

93 Vid. Van Weeguel (1998, pp. 141-142).

94 Par. 28 art. 10 and par. 31 art. 13 CMOCDE.

in tax treaties. Art. 10.3 includes payments made by the dividend-distributing entity to the owner of the corporate rights or to a third party, provided that the source State considers that the income has a *societatis causa*. Under this hypothesis the following problems should be analyzed:

Tax planning schemes could transfer the dividend-distributing entity's profits to the shareholders without generating dividends from a strictly private law point of view. Non-arm's length (Combarros Villanueva, 1988, p. 30; Davies, 1997, pp. 281-295) commercial and financial transactions between associated companies are probably the most known schemes used to divert company's profits. Whenever the taxable base of one of the associated companies is adjusted, the excess of income or expenses must be qualified for tax purposes. Set offs, compensatory adjustments (OECD, 2010b, p. 4.72), and second adjustments implying a payment made by the dividend-distributing entity to its shareholders, may qualify as dividends if the source State treat that income as income from shares (Helminen, 2010, p. 152). In other words, the third part of article 10.3 should allow the dividends treaty qualification⁹⁵ for income from secondary adjustments if the source State creates an indirect or direct nexus with the income and the corporate rights based on the *societatis causa*. For instance, it would not matter if the income is attributed to the grandparent company or to a sister company, or even if it is allocated to individuals specially related with the partner⁹⁶. Conversely, the domestic laws (like the French) should be limited by article 21 of the OECD Model when they tax as dividends any amount exceeding the quantification rules, regardless of whether the excess amount has its source in the corporate right or not. It seems reasonable that art. 10 of the OECD Model requires at least some relationship between the share and the subject who holds the corporate right and the one who receives the excess of the market price⁹⁷. The result is different if the secondary adjustment is made by the residence State of the parent company or the State of the other associated company, because the reference of article 10.3 does not apply⁹⁸. In the author's opinion, the first and second parts of the dividend definition in tax treaties cannot support the prevalence of the nexus created under the residence State law over the nexus developed under the source State law. In this case, a conflict of qualification emerges and, in accordance with the solution defended before, the source State legislation should prevail in order to qualify the income in accordance with the treaty.

A second scheme to transfer benefits from the company to the shareholders consist on dividend payments on shares. In those schemes there is a nexus between the income and

95 Par. 28 of the Commentary on art. 10 MCOCDE; Helminen (2010, p. 160).

96 Vid. OECD (2010b, párr. 4.66).

97 Case law seems to be consistent in this issue vid. Hattingh (2009, pp. 525 ss.).

98 Germany, *Finanzgericht Baden-Württemberg*, Case law of October 6th 2005, 13 V 50/04. Available at: www.ibfd.org Cfr. Hattingh (2009, p. 527).

the corporate rights, and it is undeniable that the payment has a *societatis causa*. Though in this case, the problem relies on the fact the dividend payments on shares do not decrease the assets or the equity of the company when the shares become from a capital raising (Helminen, 2010, pp. 141-142).

Corporate rights market value in a perfect market represents the undistributed profits and hidden reserves. Consequently, the alienation of corporate rights allows the partner to earn the implicit value of dividends. Given the lack of neutrality in the tax treatment of income and capital gains from corporate rights, there are several tax planning schemes that generate questions with regard to the definition of dividends. Two kinds of schemes are relevant to this thesis, dividend stripping and liquidations.

There are several schemes of dividend stripping which exploit the differences between the tax treatment of income and capital gains, and between the dividend tax regimes applicable to each kind of recipients⁹⁹ (residents, residents in a contracting State, individuals, companies, etc.). If the receiver meets the personal conditions set forth the more favorable domestic dividend regime or if the receiver is included in the personal scope of a treaty, taxpayers would be interested in altering the person that receives the income. In the author's opinion, the dividend definition in the OECD Model neither rule the allocation of dividends, nor restrict the configuration of the subjective element of the taxable event provided for in domestic legislation. Thus, art. 10.3 of the OECD Model does not prevent the dividend qualification of the income paid by the dividend-distributing entity to the holder of the dividend coupon or to the usufructuary, or even to the legal owner of the corporate rights. Conversely, the income qualification of earnings obtained by the alienation of the dividend coupon may be questionable (Helminen, 2010, pp. 91 ss.; Against, Vogel, 1997, art. 10, párr. 192). The owner of the corporate rights does not obtain income from a direct source in the corporate rights, but from another contractual right. Moreover, equity loans, swaps, repos and other contracts involving substitutive payments of dividends paid by the current shareholder to the initial holder of the participation cause several questions in the relation to the dividend definition (Vogel, 1997, art. 10, par. 9a; Helminen, 2010, p. 103). In the author's opinion, domestic tax law could qualify as dividends under art. 10 of the Model the payments made by the dividend-distributing entity to the current or to the former shareholder. The aforementioned statement is consequence of the hypothesis that domestic law is not restricted by tax treaties to define the nexus between the income and the corporate rights. Part of that nexus is the definition of the subjective elements of the taxable event. Therefore, the definition of the tax liability on the bases of the subjective characteristics of the direct receipt (the current shareholder) or the beneficial owner (the former shareholder) of the income is not restricted by tax treaties. The conclusion

99 Vid. Van Weeguel (1998, pp. 141-149); Helminen (2010, pp. 91 ss.).

adopted by this thesis avoids to rely in weak arguments, as the acceptance of the 2003's OECD Model Commentaries about the abuse, the justification that the lender was at some point a shareholder, or even admit that the lender is who actually supports the risk of run the company. However, it is worth to mention that dividend-substitute payments hardly qualify as dividends under the art. 10.3 of the OECD Model. Finally, re-qualification of capital gains on sale of shares into dividends based on GAARs could be accepted by the OECD Model dividend-definition if the dividend-distributing entity reduced its assets or equity in favor of the corporate rights seller, as happened in the case *RMM Canadian Enterprises v. The Queen*¹⁰⁰.

Accumulated profits can be distributed to the shareholders via full or partial liquidation of the company's equity. Income from the liquidation proceeds or the redemption value of the share, less the historical cost of the corporate rights results in an amount equivalent to the accumulated profits. These yields arise for the partners at least in three situations, when: a) the company is liquidated; b) the company acquires its own shares in order to keep them as treasury stock or to make a capital reduction; c) the company reduces the capital with the return of contributions. In those three situations there is a reduction of assets or equity in the company, condition that has been stated in this thesis as a requirement to the source State to qualify as dividends the capital gains on the alienation of shares¹⁰¹. However, there are different arguments against that position, and in order to avoid conflicts of qualification it seems advisable the adoption of the widest reference to the domestic law in the dividend definition, as suggested by the US Model.

Finally, there are cases where the dividend source is doubtful and consequently the conclusions set forth before should be refined. For instance, alienation of corporate rights on real estate companies ruled by art. 13.4 of the OECD Model and similar articles in Spanish actual treaties are *lex specialis* and prevails on arts. 10.3 and 13.5 of the Model Convention. Similarly, tax refunds in integration systems like the ACT in UK or the *avoir fiscal* in France are payments made by the tax administration, but not by the dividend-distributing entity. Moreover, those payments do not have their direct source in corporate rights. For that reason, it is recommended to include expressly those payments in the dividend article if the tax policy result of taxing that income as income from shares is coherent and systematic.

100 Canada, Tax Court, Case law from April 10th 1997, case no: 94-1732(IT)G and 94-1753(IT)G entre *RMM Enterprises Inc. and Equilease Corporation vs. Her Majesty the Queen*. Available at: www.ibfd.org See Hattingh (2009, p. 520); Arnold & Van Weeguel (2006, aptdo. 5.4.3).

101 Qualifying as dividends earnings from the alienation of interest for treaty purpose: Rust (2013): 5.3. Modifications on par. 28 and 31 of the Commentary on art. 10 and 13 of MCOCDE 2014, respectively support a conclusion stating that the benefits of liquidation and the alienation of interest to the same entity that issues it can be qualified as dividends for treaty purposes if the State of Source taxes it as shares.

Conclusion

As a general conclusion from a *lege ferenda* perspective, it is recommended to: i) delete the reference to the domestic law in the interest article; ii) adopt the widest definition of dividends; iii) exclude those rights included in the first part of the definition that, understood from the private law meaning, are not subject to the same taxation treatment as income from ordinary shares; iv) provide specific solutions for the most common conflicts of qualification described throughout this article.

According to LARENZ's statements on the "internal system", in the authors opinion in international tax law there is not that internal system. The international legal order does not have principles allowing the coordination of the domestic legal systems in the contracting States. Domestic laws of contracting States can be considered "internal systems" and DTCs, at least concerning with the distributive rules (art. 6-22 MCOCDE), just aim to distribute the taxation power of contracting States and to promote the economic exchange. Given, on one hand, that the ability to pay principle is not defined at the international level and, on the other hand, that different economic policy purposes lead the tax treaties structure, the definition of dividends in DTC's is an "abstract concept" attempted to be subsumed, which, using LARENZ's words, is useful only to the "internal system" of the source State, as its degree of abstraction in the treaty level makes vacuum the content for the international system and for the residence State system (Larenz, 2010, pp. 465-482).

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