Chapter 6

The Meaning of "Beneficial Ownership" as Applied to Dividends under the OECD Model Tax Convention

by Philip Baker[1]

6.1. Introduction

Much has already been written about the meaning of "beneficial ownership", so there is a limited amount that this chapter can add to the existing literature.[2] However, this chapter focuses on the current understanding of the meaning of beneficial ownership as it applies to dividends and, in particular, discusses recent proposals from the OECD to amend the Commentary relating to beneficial ownership.

An initial question is whether there is anything special about the meaning of beneficial ownership as it applies to dividends (as opposed to the application to interest, royalties or other income). Dividends may differ from interest and royalties, for example, in that they are less predictable and rely upon a decision of the board of directors or the shareholders of a company before payment. It may also be that the dividend flow can be more easily separated from the ownership of the underlying shares (though, of course, it is always possible in the case of interest to separate the interest coupons from the underlying debt). None of these potential differences suggest that beneficial ownership in the case of dividends should have in any sense a different meaning from beneficial ownership as it applies to interest, royalties and other income. To that extent, therefore, the comments made in this chapter relate to the terms wherever they are used in the OECD Model.

1. Queen's Counsel, Gray's Inn Tax Chambers, London; Senior Visiting Fellow, Institute of Advanced Legal Studies, University of London.
2. See Charl du Toit, *Beneficial Ownership of Royalties in Bilateral Tax Treaties* (IBFD, 1999); *Klaus Vogel on Double Taxation Conventions* (3rd English ed., Kluwer Law International, 1997), Preface to Arts. 10-12, Para. 5 et seq.; Richard Collier, "Clarity, opacity and beneficial ownership", [2011] BTR 684-704, and other works cited in these works.

6.2. History of the beneficial ownership limitation

A great deal is now known about the early history of the introduction of the beneficial ownership limitation into the OECD Model. It first began to appear in double taxation conventions entered into by the United Kingdom in the mid 1960s. The first public appearance was in the 1966 protocol to the UK–US double taxation convention of 1945.[3] In fact, the beneficial ownership wording had first been suggested by the United Kingdom in a draft of what subsequently became the Double Taxation Convention between the United Kingdom and the Netherlands of 1967.[4] Documents at the UK National Archive[5] show that the term was proposed by the United Kingdom negotiators and explained as an alternative to the previous "subject to tax" wording which had proved problematic in the case of tax-exempt entities such as charities and pension funds.[6] This proposal was accepted by the Netherlands.

The beneficial ownership wording first came into the OECD Model in 1977. At that time the Commentary to the provisions that used the beneficial ownership terminology was very short and provided only as follows:

> 12. Under paragraph 2, the limitation of tax in the State of source is not available when an intermediary, such as an agent or nominee, is interposed between the beneficiary and the payer, unless the beneficial owner is a resident of the other Contracting State. States which wish to make this more explicit are free to do so during bilateral negotiations.

This remained the essence of the Commentary until 2003 when, following the Conduit Companies Report,[7] the Commentary was amended so that it read as follows:

> 12. The requirement of beneficial ownership was introduced in paragraph 2 of Article 10 to clarify the meaning of the words "paid … to a resident" as they are used in paragraph 1 of the Article. It makes plain that the State of source is not obliged to give up taxing rights over dividend income merely because that

3. Supplementary Protocol of 17 March 1966 to the Double Taxation Convention between the United Kingdom and United States of 16 April 1945. Some of the background to the beneficial ownership limitations in the United Kingdom is discussed in R. Collier, "Clarity, opacity and beneficial ownership", id.
4. UK–Netherlands double taxation convention of 31 October 1967.
5. See reference IR 40/17128.
6. I have spoken about this material in the National Archive during the Klaus Vogel lecture in Vienna in 2010.
7. *Double Taxation Conventions and the Use of Conduit Companies*, adopted by the OECD Council on 27 November 1986. The report can be found in Vol. II of the looseleaf version of the OECD Model.

> income was immediately received by a resident of a State with which the State of source had concluded a convention. The term "beneficial owner" is not used in a narrow technical sense, rather, it should be understood in its context and in light of the object and purposes of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance.
>
> 12.1 Where an item of income is received by a resident of a Contracting State acting in the capacity of agent or nominee it would be inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption merely on account of the status of the immediate recipient of the income as a resident of the other Contracting State. The immediate recipient of the income in this situation qualifies as a resident but no potential double taxation arises as a consequence of that status since the recipient is not treated as the owner of the income for tax purposes in the State of residence. It would be equally inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption where a resident of a Contracting State, otherwise than through an agency or nominee relationship, simply acts as a conduit for another person who in fact receives the benefit of the income concerned. For these reasons, the report from the Committee on Fiscal Affairs entitled "Double Taxation Conventions and the Use of Conduit Companies" concludes that a conduit company cannot normally be regarded as the beneficial owner if, though the formal owner, it has, as a practical matter, very narrow powers which render it, in relation to the income concerned, a mere fiduciary or administrator acting on account of the interested parties.

This is the current version of the Commentary as at the time of writing (January 2012). It excludes from beneficial ownership a recipient of the dividends who is an agent or nominee or a conduit who has, as a practical matter, very narrow powers which render it a mere fiduciary or administrator acting on account of the real beneficial owner. This is relatively easy to understand and is quite narrow in its scope as to who are not beneficial owners of the income.

6.3. The proposed changes to the Commentary

In April 2011, the OECD released a discussion draft on suggested changes to the Commentary relating to the meaning of the term "beneficial owner".[8] If adopted, the key elements of the change would be as follows:

8. OECD, *Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention*, Discussion draft, 29 April 2011 to 15 July 2011.

12. The requirement of beneficial owner was introduced in paragraph 1 of Article 10 to clarify the meaning of the words "paid ... to a resident" as they are used in paragraph 1 of the Article. It makes plain that the State of source is not obliged to give up taxing rights over dividend income merely because that income was paid direct to a resident of a State with which the State of source had concluded a convention.

12.1 Since the term "beneficial owner" was added to address potential difficulties arising from the use of the words "paid to ... a resident" in paragraph 1, it was intended to be interpreted in this context and not to refer to any technical meaning that it could have had under the domestic law of a specific country (in fact, when it was added to the paragraph, the term did not have a precise meaning in the law of many countries). The term "beneficial owner" is therefore not used in a narrow technical sense (such as the meaning that it has under the trust law of many common law countries[1]), rather, it should be understood in its context, in particular in relation to the words "paid ... to a resident", and in light of the object and purposes of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance. This does not mean, however, that the domestic law meaning of "beneficial owner" is automatically irrelevant for the interpretation of that term in the context of the Article: that domestic law meaning is applicable to the extent that it is consistent with the general guidance included in this Commentary.

[Footnote to paragraph 12.1]
1. For example, where the trustees of a discretionary trust do not distribute dividends earned during a given period, these trustees, acting in their capacity as such (or the trust, if recognised as a separate taxpayer), could constitute the beneficial owners of such income for the purposes of Article 10 notwithstanding that the relevant trust law might distinguish between legal and beneficial ownership.

12.2 Where an item of income is paid to a resident of a Contracting State acting in the capacity of agent or nominee it would be inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption merely on account of the status of the direct recipient of the income as a resident of the other Contracting State. The direct recipient of the income in this situation qualifies as a resident but no potential double taxation arises as a consequence of that status since the recipient is not treated as the owner of the income for tax purposes in the State of residence.

12.3 It would be equally inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption where a resident of a Contracting State, otherwise than through an agency or nominee relationship, simply acts as a conduit for another person who in fact receives the benefit of the income concerned. For these reasons, the report from the Committee on Fiscal Affairs entitled "Double Taxation Conventions and the Use of Conduit Companies" concludes that a conduit company cannot normally be regarded as the beneficial owner if, though the formal owner, it has, as a practical matter, very narrow powers which render it, in relation to the income concerned, a mere fiduciary or administrator acting on account of the interested parties.

12.4 In these various examples (agent, nominee, conduit company acting as a fiduciary or administrator), the recipient of the dividend is not the "beneficial owner" because that recipient does not have the full right to use and enjoy the dividend that it receives and this dividend is not its own; the powers of that recipient over that dividend are indeed constrained in that the recipient is obliged (because of a contractual, fiduciary or other duty) to pass the payment received to another person. The recipient of a dividend is the "beneficial owner" of that dividend where he has the full right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass the payment received to another person. Such an obligation will normally derive from relevant legal documents but may also be found to exist on the basis of facts and circumstances showing that, in substance, the recipient clearly does not have the full right to use and enjoy the dividend; also, the use and enjoyment of a dividend must be distinguished from the legal ownership, as well as the use and enjoyment, of the shares on which the dividend is paid.

12.5 The fact that the recipient of a dividend is considered to be the beneficial owner of that dividend does not mean, however, that the limitation of tax provided for by paragraph 2 must automatically be granted. This limitation of tax should not be granted in cases of abuse of this provision (see also paragraphs 17 and 22 below). As explained in the section on "Improper use of the Convention" in the Commentary on Article 1, there are many ways of addressing conduit company and, more generally, treaty shopping situations. These include specific treaty anti-abuse provisions, general anti-abuse rules and substance-over-form or economic substance approaches. Whilst the concept of "beneficial owner" deals with some forms of tax avoidance (i.e. those involving the interposition of a recipient who is obliged to pass the dividend to someone else), it does not deal with other cases of treaty shopping and must not, therefore, be considered as restricting in any way the application of other approaches to addressing such cases.

12.6 The above explanations concerning the meaning of "beneficial owner" make it clear that the meaning given to this term in the context of the Article must be distinguished from the different meaning that has been given to that term in the context of other instruments[1] that concern the determination of the persons (typically the individuals) that exercise ultimate control over entities or assets. That different meaning of "beneficial owner" cannot be applied in the context of the Article. Indeed, that meaning, which refers to natural persons (i.e. individuals), cannot be reconciled with the express wording of subparagraph 2 a), which refers to the situation where a company is the beneficial owner of a dividend. Since, in the context of Article 10, the term beneficial owner is intended to address difficulties arising from the use of the word "paid" in relation to dividends, it would be inappropriate to consider a meaning developed in order to refer to the individuals who exercise "ultimate effective control over a legal person or arrangement".[2]

[Notes to Para. 12.6]
1. See, for example, the Glossary to the Financial Action Task Force's Forty Recommendations (http://www.fatf-gafi.org/glossary/0,3414,en_32250379_32236930_35433764_1_1_1_1,00.html#34276864) 5 which sets forth in detail the international anti-money laundering standard and which includes the following definition of beneficial owner: "the natural person(s) who ultimately owns or controls a customer and/or the person on whose behalf a transaction is being conducted. It also incorporates those persons who exercise ultimate effective control over a legal person or arrangement." Similarly, the 2001 report of the OECD Steering Group on Corporate Governance, "Behind the Corporate Veil: Using Corporate Entities for Illicit Purposes", http://publications.oecd.org/acrobatebook/2101131E.PDF, at page 14, defines beneficial owner as follows:
In this Report, "beneficial owner" refers to ultimate beneficial owner or interest by a natural person. In some situations, uncovering the beneficial owner may involve piercing through various intermediary entities and/or individuals until the true owner who is a natural person is found. With respect to corporations, ownership is held by shareholders or members. In partnerships, interests are held by general and limited partners. In trusts and foundations, beneficial owner refers to beneficiaries, which may also include the settlor or founder.
2. Glossary to the Financial Action Task Force's Forty Recommendations (http://www.fatf-gafi.org/glossary/0,3414,en_32250379_32236930_35433764_1_1_1_1,00.html#34276864).

At the time of writing (January 2012) it is not yet clear what, if any, of these changes will be adopted by the OECD Committee on Fiscal Affairs. The proposed changes contain a number of helpful clarifications:

- Para. 12.1 makes it clear that the term is not used in a narrow technical sense (e.g. as it is used under the trust law of common law countries).
- Para. 12.4 is perhaps the most significant attempt to clarify the meaning of beneficial owner and is discussed below.
- Para. 12.5 makes it clear that the beneficial ownership limitation is not the only possible provision in a convention that might deal with the improper use or abuse of the convention. The other side to this point is that the beneficial ownership limitation should be regarded as relatively narrow and should not be expanded as a general anti-abuse provision.
- Finally, Para. 12.6 distinguishes between beneficial ownership as used in the OECD Model and the use of the term "ultimate beneficial own-

er" in the context of other regulatory legislation and money-laundering legislation. This is particularly important because there has been an increasing danger recently of a confusion between the beneficial ownership of dividends etc. for double taxation convention purposes and the ultimate beneficial ownership of assets for money-laundering purposes, for example.

Perhaps the most significant of the proposed changes is new Para. 12.4 clarifying that the recipient of the dividend is not the beneficial owner if the recipient does not have the full right to use and enjoy the dividend and "this dividend is not its own". This has close similarities with some of the recent statements in court decisions discussed below. The proposed new paragraph then goes to say "the powers of that recipient ... are indeed constrained in that the recipient is obliged (by a contractual, fiduciary or other duty) to pass the payment received to another person". It then goes on to talk about the right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass the payment received to another person. This identifies the essence of the beneficial ownership limitation as explained by the Commentary. If the recipient of the dividend has a binding contractual, legal or fiduciary duty to pass the actual payment received to another person, then the recipient does not have the full right to use and enjoy the dividend and the dividend is not its own: that recipient is not the beneficial owner. However, anything less than a binding obligation to pay the actual payment to another person does not deprive the recipient of beneficial ownership.

This is fundamentally important. Any person receiving a payment might/may/should/would/will pay the sum received ultimately to another person. An individual receiving his salary may be surrounded by debts that require him to use the money to pay the butcher/the baker/the candle-stick maker/his ex-wife/and his mortgage lender. However, he is still the beneficial owner of his salary. Equally, a company may/will use dividends received to: pay interest on its debts; pay its suppliers; pay its staff; pay on a dividend to its shareholders, etc. If the beneficial ownership is tested by asking whether the recipient of a dividend will, in practice, pay it on to another person, then we are virtually none of us the beneficial owners of the income we receive. If, however, it is tested by asking whether there is a binding legal, contractual or fiduciary obligation to pay the actual dividend received to another person, then that properly identifies the essence of the beneficial ownership limitation.[9]

9. Even then, it might be argued that a lender who has agreed, for example, to have interest paid into a blocked account that can only be used to pay interest on sums bor-

Even if the 2001 proposals of the OECD are accepted (and there is no doubt that they could be improved upon to a certain extent) there still remain issues to be resolved about the meaning of beneficial ownership in the context of dividends, interest, royalties and other income.

First, there is the ongoing question as to whether "beneficial ownership" has a meaning to be determined from the domestic law of the contracting state applying the double taxation convention (in accordance with the equivalent of Art. 3(2) of the OECD Model). Alternatively, it has been suggested[10] that the phrase should have an "international fiscal meaning" not dependent upon the domestic law of any particular country. This international fiscal meaning should be derived from the OECD Commentary. Para. 12.1 of the proposed amendments would seem to support this approach that does not relate the meaning of beneficial ownership to a technical meaning in the law of a particular country (though, frankly, the last sentence of proposed 12.1 is confusing and unhelpful in this respect).

Secondly, if beneficial ownership has an international fiscal meaning based upon the OECD Model Commentary, then the question arises as to how far it is appropriate to delve into the historical origins of the beneficial ownership limitation and how far it is appropriate to look at later versions of the Commentary.

So far as the history is concerned, the documents to date do not suggest that those who proposed the inclusion of the beneficial ownership limitation in the OECD Model in 1977 had a particularly clear idea as to what the limitation meant. Archive research, while interesting, has therefore yielded little so far that clarifies the meaning of the concept.

The issue of changes to the OECD Commentary is a general one relating to the interpretation of double taxation conventions. Different views on this have been expressed by academic writers and in judgments of courts in different countries. A distinction which may be relevant is between changes to the Commentary that simply elaborate previous understandings as to the meaning of the Model and those changes which go further and approach a fundamental change of meaning as expressed through the Commentary.

rowed by the lender, is still the beneficial owner. This would suggest that a binding obligation to pay on the dividend etc. is not, by itself, sufficient to deprive the recipient of beneficial ownership. It seems that there must be some abuse of the treaty protection for the treaty benefits to be denied.

10. See Philip Baker, *Double Taxation Conventions*, 3rd ed., loose-leaf, Para. 10B – 14, London: Sweet & Maxwell, 2011.

Looking at the proposed changes to the Commentary published in April 2011, it is possible to see those as they stand as a clarification and elaboration of the existing Commentary, at least as it stood since 2003. To that extent, and provided that the proposed changes to the Commentary do not go further than the proposals, it may well be that there is quite a good argument that existing treaties should be interpreted in the light of the change to the Commentary that result from these proposals.[11] However, this is no doubt going to be an issue which will have to be addressed in future years.

6.4. Existing case law

Turning from the OECD Commentary and its history to the existing jurisprudence and guidance on the meaning of beneficial ownership as applied to dividends, many of the country reports published in this volume contain some discussion of the beneficial ownership concept. These reports confirm that there has been relatively little case law on the meaning of beneficial ownership, most of it only within the last 5 years and that there is little official guidance or clarification in specific tax treaties.

So far as the case law is concerned, for many years the only reported decision was the "Royal Dutch" case (sometimes referred to as the "Market Maker" case) from the Netherlands.[12] The case concerned a usufruct of the dividends of shares in the Royal Dutch company and the essential question was whether it was possible to be the beneficial owner of the dividends where the recipient did not own the shares themselves. The *Hoge Raad* confirmed that it is possible to be the beneficial owner of dividends in those circumstances. That must be correct since the issue of beneficial ownership in the articles of tax treaties is concerned with the right to the income flow, not the rights over the shares, debt etc.

In 2000, an Austrian case[13] touched on the beneficial ownership limitation when the issue arose whether a reduced withholding tax could be refused where insufficient information had been provided to determine the beneficial owner of payments. This was followed by a Swiss Federal Court case,[14] which is interesting as it discusses the application of the abuse of law concept to tax treaties. In that case, a claim was made to the reduced with-

11. On this issue generally, see the Introduction to the OECD Model (2010 version), Paras. 33-36.1.
12. BNB 1994/217, discussed in the Netherlands country report at 20.8.4.
13. *N AG v. Regional Tax Office Upper Austria* (2000) 2 ITLR 884.
14. *A Holding ApS v. Federal Tax Administration* (2006) 8 ITLR 536.

holding tax on a payment to a Danish company that appeared to have been interposed and which paid on the dividend to the ultimate owner in a third state. It seems to have been accepted that the Danish company, even though it paid the dividend on to the ultimate owner, was the beneficial owner of the dividend; the case proceeded on issues concerning abuse of law.

A great deal of heat, but relatively little light, was generated by the *Indofood* case in the United Kingdom.[15] It was somewhat unfortunate that the issue arose there in the context of a commercial case, argued by lawyers none of whom was a tax expert, before judges who were not tax experts, and without any representation from any revenue authority. The case is clear authority for the "international fiscal meaning" to be given to the term "beneficial owner", but with rather less helpful guidance as to what that term actually means.

The decision of the French *Conseil d'Etat* in the *Bank of Scotland* case[16] is again perhaps an illustration of the extreme application of the abuse of law doctrine to tax treaties. In that case, the specific treaty provision at issue did not even contain the beneficial ownership limitation; nevertheless, the French Supreme Administrative Court read the limitation into the treaty and denied treaty benefits where a payment had been made to acquire the right to receive future payments.

At the time of writing, undoubtedly the most complete discussion of the meaning of beneficial ownership by a court in a tax context is the decision of the Canadian courts in *Prévost Car*.[17] In that case, a joint venture had been formed between a UK company and a Swedish company to acquire all the shares in a Canadian car company. To implement the joint venture, a Dutch holding company was established that held the shares in the Canadian company. Dividends were paid by the Canadian company to the Dutch company and paid on to the UK and Swedish corporate shareholders. There was a shareholders' agreement that profits of the Canadian company should be distributed and those distributions should pass through the Dutch holding company to the two shareholders: in practice, dividends were demanded by the shareholders and were paid up through the Dutch holding company and on to the ultimate shareholders. It is somewhat surprising that the payment of the dividends from the Canadian company to the Dutch company was challenged under the beneficial ownership provision of the treaty, though perhaps the existence of the shareholders' agreement and the

15. *Indofood International Finance Limited v. JP Morgan* (2006) 8 ITLR 653.
16. *Société Bank of Scotland* (2007) 9 ITLR 683.
17. *Prévost Car Inc v. R* (2009) 11 ITLR 757.

onward payment of the dividends in practice explain the challenge by the Canadian revenue authorities. Both the Tax Court of Canada and the Court of Appeal confirmed that the Dutch company was the beneficial owner of the dividends it received. Although in practice it paid those dividends on to its shareholders and there was a shareholders' agreement to that effect, nevertheless the intermediate holding company was the real owner of the dividends and could take a decision whether or not to pay them on to its shareholders. This decision seems to be consistent with Para. 12.4 of the proposed amendments to the OECD Commentary.

There is a further Canadian case involving a company called Velcro that is understood to have been heard before the Canadian courts but in respect of which at the time of writing (January 2012) no judgment has appeared. Hopefully, that judgment will not disturb the position reached in the *Prévost Car* case.

Most recently, the Danish High Court has decided on the application of the beneficial ownership limitation in the Denmark–Luxembourg treaty.[18] Following the acquisition of a Danish group of companies by two equity funds, via Luxembourg subsidiaries, a dividend of EUR 745 million was paid up from the Danish company, FS Equity A/S, to its immediate Luxembourg parent, FS Invest II Sarl. The amount was immediately then lent back by the Luxembourg company to the Danish company. The Danish company was obliged to withhold taxes on the dividend distribution unless the Denmark–Luxembourg Treaty or the Parent-Subsidiary Directive[19] applied. The Danish Tax Authorities argued that the Luxembourg company was not the beneficial owner of the dividend. In a long judgment, the Danish High Court considered that the concept of beneficial ownership had an international fiscal meaning, referred to the OECD Commentary and concluded that the Luxembourg company was the beneficial owner of the dividend it received.

It is surprising that the Danish authorities challenged this payment, given that the Luxembourg company did not pay the dividend received up to its parent company or its ultimate owners but rather re-subscribed the dividend to the Danish group via a loan.

The country reports in this volume refer to a few, less well-known cases. The Belgian report refers to a decision of the Court of First Instance of

18. The *FS Equity A/S Case*, Decision of 20th December 2011. This will be published in (2011) 13 ITLR.
19. Council Directive 90/435/EEC.

Ghent of 12 May 2008 and a subsequent Court of Appeal of Ghent decision of 15 December 2009 involving a Luxembourg holding company.[20] Similarly, the Spanish report refers to three cases involving various forms of structured transactions involving interest or dividends.[21] Those cases appear to have been decided on the basis of the Spanish "simulation" doctrine rather than to involve a discussion of the meaning of the beneficial ownership limitation.

6.5. Administrative guidance and specific treaty provisions

So far as administrative guidance is concerned, the country reports refer to a small amount of guidance, not all of it entirely consistent between the different countries.

The Belgian report refers to the Administrative Commentary to Belgium's tax treaties, which takes a line consistent with the Ghent decisions that the question of beneficial ownership is fundamentally a legal issue. The Dutch report refers to the early memorandum from 1987 relating to the Dutch standard tax treaty, which takes a somewhat different approach. The current commentary to the US Model takes the line that beneficial ownership has a meaning according to the domestic law in the state of payment. The United States appears to be one of the few countries that takes this view (and this may explain the last sentence to Para. 12.4 of the proposed amendments to the Commentary). Frankly, this is unhelpful when there is a head of steam building up behind the idea that beneficial ownership should take an international fiscal meaning. Finally, following the *Indofood* case, HM Revenue and Customs issued guidance on the decision.[22] That guidance distinguishes between circumstances where there is no tax avoidance (in which case the international fiscal meaning is unnecessary) and those where there is avoidance and where the international fiscal meaning is to be applied. This HMRC guidance has been useful in practice and has confirmed a practice that is acceptable to the City law firms. However, it is very hard to see the justification for the distinction made by the guidance. At the

20. See the Belgian National Report at 14.7. (text to note 240).
21. A decision of the Supreme Administrative Court of 23 November 2006 (involving a sale and repurchase to a Spanish permanent establishment: decision of 14 March 2008 (involving a stock loan to a Spanish subsidiary); decision of 25 July 2007 (involving a fixed/floating swap).
22. Which is now contained in the International Tax Manual at INTM332040 to 080.

time of writing, it is understood that HMRC is working on some further guidance which, hopefully, may reflect more the OECD position.

A few of the country reports refer to specific treaties that contain some clarification of the beneficial ownership concept. Thus, for example, the final protocol to the Belgium–Turkey convention of 2 June 1987 contains the following:

> 5. With reference to Articles 10, 11 and 12
>
> It is understood that the "beneficial owner" clause would be interpreted in the meaning that a third country resident will not be allowed to get benefits from the Agreement with regard to dividends, interest and royalties derived from Turkey or Belgium but this restriction shall in no case be applied to residents of a Contracting State.

Similarly, the treaties concluded by Germany contain the following provisions. First, the Germany–Italy Convention of 18 October 1989 in its protocol states as follows:

> 9. With reference to Articles 10, 11 and 12 The recipient of the dividends, interest and royalties is the beneficial owner within the meaning of Articles 10, 11 and 12 if he is entitled to the right upon which the payments are based and the income derived therefrom is attributable to him under the tax laws of both States.

The Germany–Norway treaty of 4 October 1999 in its protocol contains the following:

> 4. Ad Articles 10 through 12
>
> The recipient of dividends, interest, and royalties shall be deemed the beneficial owner within the meaning of Articles 10, 11, and 12 if he is entitled to the rights underlying such payments and if the income derived therefrom can be allocated to him in accordance with the tax laws of both States.

Finally, the Germany–Sweden treaty of 14 November 1992 contains a specific article, Art. 43 on the "Application of the Convention in Special Cases". Art. 43(3) states as follows:

> (3) For the purposes of Article 10 through 12, a resident of a Contracting State shall be considered the beneficiary owner of dividends, interest and royalties, if they are to be attributed for purposes of taxation to this person in accordance with the legislation of that State. This person, however, is not the beneficiary owner if according to the law of the other State, this income is to be attributed for purposes of taxation to other persons who are entitled to the use of this income and who are not residents of the first-mentioned State.

[German text]:

(3) *Sinne der Artikel 10 bis 12 gilt eine in einem Vertragsstaat ansässige Person als Nutzungsberechtigter von Dividenden, Zinsen und Lizenzgebühren, wenn sie nach der Gesetzgebung dieses Staates dieser Person steuerlich zuzurechnen sind. Diese Person ist jedoch nicht Nutzungsberechtigter, wenn nach dem Recht des anderen Staates diese Einkünfte steuerlich anderen Personen zuzurechnen sind, denen die Nutzung für diese Einkünfte zusteht und die nicht in dem erstgenannten Staat ansässig sind.*

These few examples of specific provisions hardly establish a consistent treaty practice.

The country reports also refer to some of the relatively copious, academic writing on the meaning of beneficial ownership. It is perhaps appropriate to single out here that *Klaus Vogel on Double Taxation Conventions* identifies the beneficial owner as having two attributes: the beneficial owner must either have the right to decide how capital is invested or the right to decide about the use of the return of the capital invested.[23]

6.6. Concluding comments and a problem

In the light of the material discussed above, it is now possible to present some conclusions on the meaning of beneficial ownership as applied to dividends under the OECD Model.

The meaning of "beneficial ownership" for dividends is no different from the meaning that applies to interest or royalties or other income. This meaning is an international fiscal meaning, not one dependent upon the domestic law in either of the contracting states. Though the term "beneficial owner" is not defined in the convention, this is a situation where the "circumstances otherwise require" that the domestic law meaning is not applied in accordance with Art. 3(2) of the Model. There are several reasons for this: in many countries there is no domestic meaning of the term; where there is such a meaning, it is now clear from the OECD Commentary that a technical meaning is not to be applied; the term is essentially one that has come into tax treaty usage from international tax practice and not from the domestic tax systems of the countries concerned. This is particularly so for treaties where there is a foreign language text (i.e. a text other than in English) which uses another term. For example, the French version of the OECD

23. See Preface to Arts. 10-12, Para. 5 et seq.

Model uses the term *bénéficiare éffectif.* This clearly has a different connotation from the idea of beneficial ownership: it makes no reference to ownership and emphasizes the question of the real beneficiary of the income.

The international fiscal meaning should be found from the OECD Commentary. Under that Commentary, persons who receive income as nominees, agents, mere fiduciaries or other administrators are not the beneficial owners. The proposed amendments to the OECD Commentary focus on the receipt of income subject to a binding obligation (contractual, legal or fiduciary) to pay on the income to another person: in those circumstances, the recipient is not the real owner. This is an appropriate focus of the enquiry; and in circumstances where there is no such binding obligation to pay on the specific income received, the recipient is the beneficial owner.

It follows from this that the beneficial ownership limitation is a relatively narrow provision, largely concerned with potential abuse of treaty claims, but more broadly intended to ensure that the treaty benefit accrues to a real owner and not to someone who is subject to a binding obligation to pay on the specific dividends received to another person.

It should be emphasized in this context that the degree of substance of the beneficial owner is of very limited relevance. It is perfectly possible for a holding company to have real ownership of dividends, and not to be under a binding obligation to pay on the dividends received to another person, even though the holding company has no premises, staff or assets other than the shares that are held. Those countries that have begun to examine the question of beneficial ownership by examining the substance of the recipient are, fundamentally, misinterpreting the international fiscal meaning.

If the beneficial ownership limitation is a narrow limitation, there is nothing to stop pairs of states from putting more specific anti-abuse measures into their conventions if they wish to do so. In fact, arguing *a contrario,* the fact that many states place anti-conduit and other limitation-on-benefit provisions into their treaties is a clear indication that they do not consider that the beneficial ownership limitation is a broad measure which would catch the type of abuse for which these anti-conduit rules are applicable.

One might end by posing a specific factual scenario which raises, in a very practical sense, the meaning of beneficial ownership. Suppose that company A is the owner of the shares in company B and anticipates receiving a dividend from company B in relation to those shares. Suppose then that company A transfers to company C the right to receive that dividend. This could be by way of a sale of the shares with a right to repurchase them (a repo), it could be by way of a stock loan, it could be by way of a sale of a usufruct over the income from the shares, or it could be by a form of swap arrangement under which the dividends are paid to company C and company C makes swap payments to company A. Suppose now that, had the dividends been paid from company B to company A, there would have been a 25% withholding tax, but under the double taxation convention with the state of company C, that withholding tax is reduced to zero. One can now see one of the main reasons why the right to receive the dividends may have been transferred to company C: this reduces the withholding tax on dividends to zero, provided that company C is the beneficial owner of the dividends. To put figures to this, let us assume that the dividend to be paid is 1 million, which, minus the normal withholding tax of 25%, would have left company A with 750,000. Company A sells the right to the dividend to company C for 875,000, so that company C receives the dividend of 1 million, pays 875,000 to company A, and retains 125,000 itself. In effect, in this scenario company A and company C are sharing between themselves on a 50:50 basis the saving in the withholding tax by the shares being held by company C at the time of the dividend payment, as opposed to the situation if company A had retained those shares.

In those circumstances, is company C the beneficial owner of (a) the entire dividend of 1 million; (b) only 125,000 of the dividend (this being the amount that it retains); (c) none of the dividend?

If one tests this by asking whether company C is under a binding obligation to pay on the dividend to company A, then in most circumstances, it would not be under such obligation. It may be that it has already paid the 875,000 to acquire the right to the dividend, or the arrangement may require it to pay a manufactured payment of 875,000 after it has received the 1 million.

Answering this question is somewhat critical since such arrangements, whether they relate to dividends or interest or other income, are a key part of structured financial arrangements.

It is only appropriate to emphasize here that the question of whether or not company C is the beneficial owner is not the only factor to consider when deciding whether this is an abusive transaction and whether or not company C should be entitled to the benefit of the convention. If the states in which company B and company C are resident consider that this type of transaction is abusive, then there are other ways that they can tackle this issue other than by denying the beneficial ownership of company C.