A CRITICAL ASSESSMENT OF THE ORIGINS AND CONTINUED VALIDITY OF VARIATIONS IN AUSTRALIAN TAX TREATIES FROM THE OECD MODEL

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ABSTRACT

Tax treaties are the main mechanism for international income tax co-ordination among countries. The thesis concerns the development of Australia’s tax treaty policy and practice in the period from 1946 when the first treaty with the United Kingdom was signed to 1969 when the treaty with Japan was signed. The 1969 Japan Treaty was the last tax treaty that Australia concluded before joining the OECD in 1971. The thesis is based on archival and related historical research in Australia, Canada, New Zealand, the United Kingdom and the United States. The thesis explains the original rationale for a number of Australian tax treaty policy idiosyncrasies and how they have persisted even when contrary to OECD norms and when the original rationale for them has disappeared. The thesis submits that the present is a propitious time for a comprehensive review of those idiosyncrasies and of Australian tax treaty policy and practice generally.

KEY WORDS

Tax treaties
Australian tax treaty policy and practice
Archival research
History
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I hereby certify that this thesis is entirely my own work and that any material written by others has been acknowledged in the text.

The thesis has not been presented for a degree or for any other purposes at The University of Sydney or at any other university or institution.

The research on which this thesis was based did not require approval by the University of Sydney Human Research Ethics Committee.

The information in this thesis was derived from archival material available on request from the National Archives of Australia in Canberra, the United Kingdom National Archives at Kew, the United States National Archives and Records Administration at College Park, Maryland, Library and Archives Canada at Ottawa, and Archives New Zealand in Wellington. Other information was derived from published sources, all of which are acknowledged in the text.

During the research phase assistance in locating archival material was provided by staff at the National Archives of Australia in Canberra, the United Kingdom National Archives at Kew, the United States National Archives and Records Administration at College Park, Maryland, Library and Archives Canada in Ottawa and Archives New Zealand in Wellington.

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SECTIONS OF THE THESIS THAT HAVE PREVIOUSLY BEEN PUBLISHED

CHAPTER TWO

Parts of this chapter were previously published in:


CHAPTER THREE

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CHAPTER FOUR
Parts of this chapter were previously presented as a conference paper at the 3rd Australasian Tax History Chapter Meeting at Griffith University, 2nd July 2015.

CHAPTER FIVE
Parts of this chapter were previously in:

CHAPTER SIX
Parts of this chapter were previously published in:
CHAPTER SEVEN

Parts of this chapter were previously published in:


All of the above publications were published after the commencement of the candidature and were based on research conducted after the commencement of the candidature. I located the relevant archival materials and relevant primary and secondary literature, analysed them and wrote the drafts of the articles and book chapters that were submitted for publication.
OECD Organisation For Economic Co-operation And Development
UN United Nations
US United States of America
UK United Kingdom of Great Britain and Northern Ireland
NZ New Zealand
ATO Australian Taxation Office
ITAA(1936) Income Tax Assessment Act (1936)
NAA National Archives of Australia
GDP Gross Domestic Product


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Appendix Seven: Analysis Of Deemed Source Rules In Currently Operative Australian Tax Treaties
CHAPTER ONE: INTRODUCTION

Background

1.1 Australia joined the Organisation for Economic Co-operation and Development (hereafter ‘the OECD’) on 7th June 1971. On 23rd October 1997, the Council of the OECD adopted Recommendation I [C(97)195/FINAL], which stated that member countries should:

- Pursue their efforts to conclude bilateral tax conventions on income and capital with those Member countries, and where appropriate with non-Member countries, with which they have not yet entered into such conventions, and revise those of the existing conventions that may no longer reflect present day needs;
- When concluding new bilateral conventions or revising existing bilateral conventions, conform to the Model Tax Convention, as interpreted by the Commentaries thereon;
- Their tax administrations follow the Commentaries on the Articles of the Model Tax Convention, as modified from time to time, when applying and interpreting the provisions of their bilateral tax convention that are based on those Articles.

By Recommendation II of 23rd October 1997, the Council of the OECD invited the governments of member countries to continue to notify the Committee on Fiscal Affairs of their reservations on articles and observations on the commentaries.

The introduction to the OECD Model recognises that member countries may enter reservations relating to particular provisions in the OECD Model, and that when they do so they and their potential treaty partner in negotiations retain their freedom of action in relation to those provisions.¹ The introduction to the OECD Model also recognises that there is no need for member countries to make reservations indicating their intent to use alternative provisions that the Commentaries allow countries to include in their tax treaties.²

1.2 Australia has made 15 reservations in relation to articles in the OECD Model,³ the eighth highest number of reservations of any OECD country⁴ and well above the

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³ Australia’s reservations to the OECD Model are set out in Appendix 2.
average for OECD countries of 8.8 reservations. Current Australian tax treaties contain 114 instances of variations from the current OECD Model in relation to the articles examined in this thesis. The origins of 22 of these variations can be directly traced to the 1946 UK Treaty. The origins of a further 22 of these variations can be traced to the 1967 UK Treaty. The origins of a further 25 of these variations can be traced to other tax treaties negotiated prior to Australia joining the OECD in 1971; 8 of these originated in the 1972 German Treaty, which was negotiated but not signed before Australia joined the OECD. If variations originating with the 1972 German Treaty are excluded, a total of 61 of 114 variations can be traced to Australian tax treaties negotiated before Australia joined the OECD. Australia’s most recent treaties still contain a large number of variations that originated in Australia’s pre 1971 tax treaties. The 2010 Turkey Treaty contains 28 variations from the OECD Model that originated in pre 1971 Australian tax treaties. The 2013 Swiss Treaty, the most recent Australian tax treaty to come into force, contains 15 variations from the OECD Model that originated in pre 1971 Australian tax treaties. The 2015 German Treaty, the most recent Australian tax treaty to be signed, contains 19 variations from the OECD Model that originated pre 1971. A further group of variations from the OECD Model, which has not been taken into account in Appendix 3 nor, comprehensively, in prior literature, are deemed source rules spread through different articles in different Australian tax treaties. This thesis will demonstrate that the origins of Australian

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5 Arginelli and Dirkis, above n 4, 139.

6 The variations are summarised in Appendix 3 and include variations contained in the 2015 German Treaty. The focus of the thesis will be on articles with direct relevance to cross border investment by multinational enterprises. For this reason, it will not contain significant discussion of articles in the current or former OECD Models dealing with: Independent Personal Services (former OECD Art 14); Income From Employment (OECD Art 15); Pensions (OECD Art 18); Government Service (OECD Art 19); Students (OECD Art 20); Members of Diplomatic Missions and Consular Posts (Art 27 then 28); Territorial Extension (OECD Art 28 then 29); Entry into Force (OECD Art 29 then 30); and Termination (OECD Art 30 then 31). Further variations from the OECD Model are contained in the 2015 German Treaty, which is not yet in force. Many of these variations can be characterised as being responses to the OECD/G20 Base Erosion and Profit Shifting Project, and as such cannot be seen as being products of Australia’s pre 1971 tax treaty policy and practice. These variations are summarised in Appendix 3. The count of variations is confined to variants on or omissions of OECD Model articles. It does not include additional articles found in Australian treaties, such as the articles dealing with fringe benefits tax in the current treaty with the UK or the current treaty with NZ.

7 The details of the articles that can be traced to the 1946 UK Treaty are set out in Appendices 3 and 4.

8 The details of the articles that can be traced to the 1967 UK Treaty are set out in Appendices 3 and 5.
deemed source rules can be traced to treaties entered into prior to 1971.\textsuperscript{9} The number of variations from the OECD Model in Australian treaty practice that originated prior to Australia joining the OECD raises questions as to why these variations arose and persisted and as to the factors that influenced Australian tax treaty policy and practice prior to 1971.

1.3 Although Australia remains an overall net importer of capital, the level of Australian offshore investment has increased significantly since Australia joined the OECD in 1971; and in many of its bilateral relationships, Australia is a net exporter of capital. In view of these changes in Australia’s trade and investment position since it joined the OECD in 1971, it is legitimate to ask whether its tax treaty practices and policies that were developed prior to 1971 continue to be appropriate.

The Central Questions Investigated In This Thesis

1.4 The background discussion at 1.1 to 1.3 gives rise to the following questions, which this thesis will investigate:

1. What explanations do available archival materials relating to the negotiation and drafting of Australian bilateral tax treaties prior to 1971 provide for variations in Australian treaties from the current OECD Model?
2. Having regard to available archival materials, what factors influenced Australian taxation treaty policy and practice between 1946 and 1971 and how, if at all, did those factors change in that period?
3. What variations in Australian taxation treaties from the OECD Model should be discontinued in future Australian treaty practice, having regard to the original reason why those variations were introduced and subsequent changes in circumstances relevant to Australian taxation treaty practice and policy?

The Structure Of This Chapter

1.5 The balance of this chapter contains: (i) a review of previous secondary academic literature, and Australian government commissioned reports directly relevant to the questions identified at 1.4; (ii) an explanation of and justification for the methodology used in this thesis; (iii) a statement of the contribution to knowledge claimed to be made by the thesis.

\textsuperscript{9} The deemed source rules in currently operative Australian tax treaties are analysed in Appendix 7. As these rules relate to different articles in different treaties, previous research which has identified Australian variations from individual OECD Model articles has not identified them comprehensively.
Prior Literature Directly Relevant To The Questions Identified At 1.4

1.6 The prior literature\(^\text{10}\) directly relevant to the questions identified at 1.4 can be divided into five main categories. The first is technical legal analyses of Australian tax treaties that interpret them using traditional legal analysis having regard to the text of the treaty, relevant case and statute law and such extrinsic material permissible under treaty interpretation principles. The second traces the history of the development of articles in Australian tax treaties by comparing published Australian, foreign and model treaties entered into or developed at different points in time. Within that category, note is sometimes taken of case law and statutory developments that are regarded as explaining the background to or the origins of the development of particular provisions in Australian tax treaties. A third category compares articles in Australian tax treaties with either the tax treaty practice of other jurisdictions or with model treaties developed by international and national organisations. A fourth category is commentary on Australian tax treaty policy and practice by individuals who had direct involvement in either the negotiation or drafting of Australian tax treaties. The fifth category is commentary on what should be Australian tax treaty policy and practice having regard to what the commentator perceives to be relevant considerations, such as: international tax policy norms; and economic, foreign policy and political considerations. Contributions to the literature in categories 1 to 5 will now be reviewed.

Prior Technical Legal Analyses Of Australian Tax Treaties

1.7 Technical legal analyses of Australian tax treaties have been published by commercial publishers since Australia’s first bilateral tax treaty was entered into in 1946.\(^\text{11}\) As might be expected, given their intended audience, these analyses have

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\(^{10}\) The review of secondary academic literature will be confined to legal scholarship on Australian tax treaties and Australian tax treaty policy. Although Chapters 2 to 7 of the thesis make frequent reference to scholarship by general historians and economic historians, that scholarship is concerned with biographical, economic and geopolitical considerations relevant to the contextual background of the narrative but is not directly relevant to the questions identified at 1.4 when approached from a perspective of legal research.

\(^{11}\) The earliest analysis of an Australian tax treaty was F E Koch, *The Double Taxation Conventions, Volume 1, Taxation of Income* (Stevens & Sons, 1947). The earliest Australian analysis appears to be in J A L Gunn, O E Berger, J M Greenwood and R E O’Neill, *Gunn’s Commonwealth Income Tax Law and Practice* (Butterworth & Co (Australia), 2nd ed, 1948), which at pp1152–74 discussed the 1946 Australia – United Kingdom Tax Treaty. Another early publication was N E Challoner and C M Collins, *Income Tax Law and Practice (Commonwealth)* (The Law Book Co. of Australasia, 1953), which at pp892–919 also discussed the 1946 Australia – United Kingdom Tax Treaty. *Gunn’s Commonwealth Income Tax Law and Practice* was the progenitor of what is now Thomson Reuters, *Australian Income Tax 1936 Commentary*, which is currently available online at <www.checkpointau.com.au>. Challoner and Collins was the progenitor of what is now the CCH *Australian Federal Tax
interpreted Australian tax treaties using traditional legal analysis. With one exception, discussed at 1.10, all technical legal analyses of Australian tax treaties examined by the author as part of this research have been based on published material and have not made reference to archival material relating to the negotiation and drafting of Australian tax treaties. As such, any conclusions that they draw as to the reason why particular provisions were included in Australian tax treaties can only be based on: (a) instances of official or unofficial statements by ministers or officials explaining why particular provisions were included in Australian treaties; and (b) inferences drawn from the texts of treaties and a comparison between them using traditional legal analysis. Dependent as these works are on inferences from published material and on the reliability of official and unofficial and statements by ministers and officials, these works cannot provide sufficiently definitive answers to questions 1 and 2 identified at 1.4. These analyses usually do not include recommendations for changes in Australian tax treaty practice or policy having regard to relevant considerations, and as such are not of assistance in answering question 3 identified at 1.4. The analyses which were produced in close temporal proximity to particular treaties can provide evidence of the understanding of the effect of the particular treaty current in the tax profession at the time of its entry into force.

1.8 A more recent example of a technical discussion of a particular treaty is the 2004 discussion of the 2003 UK Treaty by Vann and Oliver. As was the case with the works by Parsons and Magney (to be discussed at 1.9), this analysis is based on a comparison of the text of the treaty with the texts of previous Australian and United Kingdom tax treaties, on a comparison with the OECD Model and Commentary, on official explanations by governments of this treaty and previous treaties, and on unpublished statements by officials. The article notes features of the treaty that appear to be distinctive features of Australian tax treaty practice and, through a comparison with UK tax treaty practice, is able to suggest whether Australia or the United Kingdom was likely to have initiated variations from the OECD Model. The authors' intent clearly did not extend to ascertaining the origins of these features, and

Reporter (ITAA 1936 and others) currently available online at <intelliconnect.wkasiapacific.com.wwwproxy0.library>.

R J Vann and J D B Oliver, 'The New Australia–UK Tax Treaty' [2004] British Tax Review 194. It is reasonably common for journal articles on particular Australian tax treaties to be published when a treaty is entered into. An earlier example is S H Goldberg, ‘The United States–Australia Income Tax Convention’ (1984) 18 Taxation in Australia 904. Articles of this nature typically rely on an analysis of the text of the treaty and a comparison with prior treaties entered into by Australia and the treaty partner. None of the articles in this category that have been examined by the author as part of this research has referred to archival sources.
their methodology did not involve the use of archival material to explain the origin and persistence of these features. Features of Australian treaty practice were identified which were either inconsistent with a more residence based treaty policy or which (for example in the case of royalties and the substantial equipment permanent establishment provision) are varied between treaties in a way that is not consistent with a coherent underlying policy.

1.9 Other works based on traditional technical legal analysis have focused on problematic aspects of the interpretation of Australian tax treaties and, in some instances, on the historical background and geopolitical context in which treaty provisions were developed. An early example of an analysis that focused on problematic aspects of a particular tax treaty in particular business contexts was an article by R W Parsons in 1968, which provided a detailed analysis of tax problems relating to a UK business operating in Australia. In those instances where Parsons’ article points to differences between the 1967 and 1946 UK treaties, it can assist in drawing inferences that are relevant to questions 1 and 2 identified at 1.4. As a detailed interpretation of the 1967 UK Treaty in a cross border business context made shortly after that treaty was negotiated, it provides evidence of a contemporary interpretation (using the methods of traditional legal research) of that treaty by a senior Australian tax academic. A later example is a book by T W Magney, which also focuses on problematic aspects of the application of Australian tax treaties in particular situations. Magney’s book largely uses traditional legal research but also takes into account extrinsic material, in particular the OECD Commentary and the OECD Model and understandings of the intent of provisions derived from experience as a practitioner and, possibly, through informal discussions with ministers and government officials. Magney’s book did not rely on archival material; therefore, the answers it can provide to the first two questions identified at 1.4 are less definitive than if they had not had this limitation.

1.10 A further variation on this approach is articles providing a technical discussion of particular issues associated with tax treaties. There is a large group of articles written before the Federal Court decisions in Virgin Holdings SA v Commissioner of Taxation [2008] FCA 1503 and Undershift v Commissioner of Taxation [2009] FCA 41 concerning the issue of whether Australia’s tax treaties entered into before the introduction of a general capital gains tax in Australia effective from 19th September

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1985 protect non-residents, who are treaty residents for purposes of those treaties, from Australian capital gains tax. These articles use traditional legal analysis to discuss this question and examine the text of relevant treaties, the OECD Model and Commentary and official statements by government or government officials. None of these articles makes reference to archival materials. The consensus in these articles is that, for various reasons, Australia’s pre CGT treaties did protect non-residents from Australian capital gains tax at least in some circumstances. Following the Federal Court decisions, Vann wrote a comment on them which made reference to some archival material, discussed in Chapter 5, supplied by the author and by Philip Baker QC. Vann’s conclusion was that the negotiators of the 1967 Australia – United Kingdom Tax Treaty did not intend to limit Australia’s right to tax capital gains. Chapter 5 of this thesis will examine these arguments in more detail, and further archival evidence which supports the conclusion reached by Vann will be examined in Chapters 4 and 6.

Published Literature Which Traces The Development Of Australian Tax Treaties

1.11 Avery Jones et al in 2006 traced the origins of concepts and expressions used in the OECD Model and their adoption by states including Australia. The research by Avery Jones et al was confined to published material and examined treaties negotiated which represented the first treaty use of a concept, models developed by the League of Nations, statutory provisions and general law concepts and case law of the relevant countries discussed in the research. Vann was responsible for the initial research relating the first use of concepts in Australian law prior to the development of the OECD Model and of the subsequent influence of concepts in the


OECD Model on Australian domestic law. For the purposes of this thesis, this research is valuable in identifying: (a) concepts the use of which was well established prior to the negotiation of the first Australian tax treaty in 1946; (b) concepts in the OECD Model which had their origins in civil law; (c) concepts for which antecedents can be found in Australian domestic law; (d) concepts which subsequently were adopted in Australian domestic law; and (e) concepts which have been interpreted by Australian court, board of review and tribunal decisions or by ATO rulings.

1.12 The focus of Avery Jones et al’s research was on the converse of question 1 identified at 1.4; that is, examining when concepts in the OECD Model were first used in treaties rather than focusing on the origins of differences between Australian tax treaty practice and the OECD Model. The research by Avery Jones et al is relevant to question 1 identified at 1.4 in that it identifies potential factors (prior tax treaties, prior model treaties, prior domestic law and interpretations of Australian tax treaties by courts, boards of review, tribunals and the ATO) which may have influenced Australian tax treaty policy and practice, but its limitation is that it is entirely based on published material. Thus, this research can tell us whether a concept now appearing in the OECD Model would have been familiar or unfamiliar to Australian negotiators and drafters and hence the likelihood of the concept being adopted or modified or influenced by them. Its reliance on published sources, however, means that it cannot provide more direct evidence of such adoption, modification or influence. This thesis will attempt to overcome this limitation by examining archival records relevant to the negotiation and drafting of Australian tax treaties negotiated prior to Australia joining the OECD in 1971.

**Literature Comparing Australian Treaty Practice With That Of Other Jurisdictions Or With Models Developed By International Organisations**

1.13 Contributions to the literature in this area have been made by T W Magney in 1994,20 by Bain, Krever and van der Westhuysen in 2011,21 by Bain, Krever and O’Connor in 2012,22 and by Dirkis and Burch in 2014.23 All of these contributions, with varying

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degrees of comprehensiveness, identify variations between current, and in some instances former, Australian tax treaty practice and the OECD Model. In the case of the contributions by Bain, Krever and van der Westhuysen and by Bain, Krever and O’Connor, a comparison is also made with the United Nations Model. The identification appears to be the result of research based on published material and, in some cases, on public presentations by officials. Appendix 3 to this thesis was based on the 2012 book chapter by Bain, Krever and O’Connor. Appendix 3 updated the findings in that chapter for Australian treaties entered into since the chapter by Bain, Krever and O’Connor was written, and corrected some errors in that chapter which had arisen due to the failure of the authors to take account of the effect of some protocols concluded contemporaneously with particular treaties. Appendix 3 also takes into account the analysis in the 2014 book chapter by Dirkis and Burch.

1.14 While the studies discussed at 1.13 are all valuable contributions to the literature, none of them provides adequate answers to the first two questions identified at 1.4. First, they all place significant reliance on inferences drawn from a pattern of behaviour and on the reliability of published statements and public presentations as to the reason behind a variation from the OECD Model. This limits the value of the research undertaken in those studies for answering the second of the questions identified at 1.4. None of the studies attempts to identify the first instance in an Australian tax treaty of any particular variation from the OECD Model. Moreover, their approach means that none of these studies is able to identify which variations from the OECD Model in particular Australian tax treaties might have been initiated by the treaty partner rather than by Australia. Nor does the approach adequately allow a determination to be made whether the precise form of a variation from the OECD Model was the product of an interchange of drafts during the negotiation process.

1.15 Dirkis and Burch argue that the variations of Australian tax treaties from the OECD Model are broadly due to: (a) variations between versions of the OECD Model over time; and (b) compromises reached during negotiations. Although Dirkis and Burch recognise that variations may have been due to compromises in the negotiation process, they do not identify which variations were the product of such compromises.

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24 The book chapter by Dirkis and Burch and the book by Magney, while apparently the result of a comprehensive analysis of Australian treaties operative at the time they were writing, only provide examples of variations from the OECD Model. The article by Bain, Krever and O’Connor and the book chapter by Bain, Krever and van der Westhuysen attempt to provide what they state to be a comprehensive comparison.

25 Dirkis and Burch, above n 23 make some comparisons with prior Australian tax treaty practice.

26 Dirkis and Burch, above n 23, 188.
Dirkis and Burch suggest that compromises in the negotiations may have arisen from:

- The relative economic positions of the contracting states;
- The international tax policy positions adopted due to the stage of economic development;
- Changes in the tax policy of the contracting states;
- Long-held positions by contracting states on particular types of income;
- Differences in business structures used; and
- Tax competition.\(^{27}\)

While these are reasonable inferences to be drawn from published material relevant to Australian tax treaty policy and practice and from presentations by officials, they are based on inferences and on presentations for which the only publically available record is a ‘bullet point’ summary. Moreover, their research does not attempt to distinguish between policies and practices that may have arisen due to one factor but which were continued because of another or other factors. Hence, the explanation they provide of the causes of the variations is less definitive than it may have been had their research taken relevant archival material into account.

1.16 This thesis seeks to address the gaps in the literature left by the studies discussed at 1.13 to 1.15 by using archival materials relevant to the negotiation and drafting of Australian treaties prior to 1972 to identify: (a) not only the first instances of variations but also the party to the negotiations who initiated the variation; (b) the factors that influenced the introduction of the variations and their persistence or abandonment during the period between 1946 and 1971.\(^{28}\)

**Commentary On Australian Tax Treaty Policy And/Or Practice By Individuals Involved In Negotiation And/Or Drafting Of Australian Tax Treaties**

\(^{27}\) Dirkis and Burch, above n 23, 188. Dirkis and Burch provide generic examples of each of the factors they list.

\(^{28}\) General commentaries on double tax treaties also make mention of Australian practice on particular articles. For example, E Reimer and A Rust (eds), *Klaus Vogel on Double Taxation Conventions* (Kluwer Law International, 4\(^{th}\) ed, 2015) refers to Australian practice on particular articles when discussing divergent country practices in relation to those articles. Works of this nature typically compare model treaties, use traditional legal analysis, note variations by particular jurisdictions and refer to secondary literature commenting on issues relating to tax treaties.
1.17 It is uncommon for Australian individuals involved in the negotiation and/or drafting of Australian tax treaties to publish material relevant to Australian tax treaty policy and/or practice. An exception is the publication by K T Allen, former Assistant Commissioner (International Branch) Policy and Legislation Group, ATO, apparently originally published between 1988 and 1990. While not reflective of current Australian tax treaty practice and policy, on some issues it does contain the views of the then Australian lead negotiator on tax treaties which contained many of the variations between Australian treaty practice and the OECD Model that are a major concern of this thesis. After acknowledging the need to prevent international double taxation arising from conflicts of source and residence rules, Allen emphasised the importance of trade, investment, political and other ties between Australia and the potential treaty partner as a reason for concluding a tax treaty with it. Allen indicated that the allocation of taxing rights in the 1967 UK Tax Treaty had formed the model for Australian tax treaties, noting that while those treaties followed the OECD Model in many respects, in others they gave greater emphasis to the taxing rights of the source country. This Allen saw as reflecting the desire of successive Australian governments to ensure that Australia, as a net importer of capital, obtained an appropriate share of tax revenues flowing from it. Allen then discussed how this broad policy objective was implemented and reflected in particular articles in Australian tax treaties. This thesis will enable an assessment to be made of

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29 Australian officials do make seminar and conference presentations but do not usually present a formal paper that is subsequently published as part of conference proceedings.

30 K T Allen Assistant Commissioner (International Branch) Policy and Legislation Group, ATO, Canberra ‘The Relevant Considerations, Factors and Criteria Involved in Negotiating Australia’s Double Tax Agreements’, Thomson Reuters, Checkpoint, Commentary, International Agreements. The commentary is currently undated, but internal evidence (Allen, at 1870, refers to the 1988 Australia – China Tax Treaty as being signed but not yet in force) and the history of the Thomson Reuters commentary suggests that it was originally written in approximately 1990 as part of Australian Income Tax Law And Practice published by Butterworths.

The URL for the online edition of this portion of the commentary as at 8th March 2015 was <http://www.checkpointau.com.au/wwwproxy0.library.unsw.edu.au/maf/app/fulldocument?endChunk=1&parentguid=AUNZ_AU_LEGCOMM_TOC||laaf929df7ad711e38c02ad4129764cda&startChunk=1&bgcguid=AUNZ_TOC||i0896b63badf933573f545ad6234b170&docguid=I090cb152a01811e0a942f53c5c101aad&pcs=AUNZ_CA_INTLAGREE&tocDs=AUNZ_AU_LEGCOMM_TOC&epos=&predefinedRelationshipsType=fullDocRetrieval&resultType=list&isTocNav=true&tocGuid=AUNZ_AU_LEGCOMM_TOC||laaf902b27ad711e38c02ad4129764cda>.

31 Allen, above n 30, 1805.

32 Allen, above n 30, 1850.

33 The features of Australian tax treaties that Allen saw as reflecting this policy objective are set out in Appendix 6. It is extremely rare for Australian ministers to make public statements about Australian tax treaty practice. An exception occurred in 2008 when the Rudd Government commissioned a review of Australian tax treaty policy. Although the review itself was never published, key features of Australia’s tax treaty practice as at 2008 as stated by the then Assistant Treasurer and Minister for Competition Policy and Consumer Affairs (The
whether Allen’s published statements are consistent with the archival records of the
negotiation and drafting of Australian tax treaties in the period prior to 1971.

**Commentary On What Should Be Australian Tax Treaty Policy And Practice Having
Regard To Perceived Relevant Considerations**

1.18 While there were internal reviews by Australian government departments and officials
of Australian tax treaty policy and practice in the period reviewed in this thesis, none
of these was published. The first published comment in an Australian government
commissioned report was in the 1975 Taxation Review Committee: Full Report34
(hereafter referred to as the ‘Asprey Committee Report’). The Asprey Committee
made the following brief comments on the factors that influence taxation treaties:

‘Double taxation agreements reflect the revenue interests of the parties, their
economic and social policies and, of course, their respective bargaining
strength. They also reflect the concern of the parties to prevent injustice and
discouragement of trade, investment and other contact between their
residents which tend to result when the same income is subject to unrelieved
double taxation.’35

While relevant to the first question identified at 1.4, this statement by the Asprey
Committee is of limited value in answering that question as there is no indication in
the Asprey Committee Report of the basis on which it was arrived at; although the
Asprey Committee Report does note that information had been supplied by the
Secretary of the Treasury and the Commissioner of Taxation and their officers.36

1.19 The Asprey Committee thereafter confined itself to making some general
observations on the structures and techniques of treaties likely to be most effective in
preventing double taxation.37 The Asprey Committee commented that a tax treaty

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34 Australia, Taxation Review Committee: Full Report 31 January 1975 (Australian Government
35 Asprey Committee Report, para 17.97.
36 Asprey Committee Report, xvii.
37 Asprey Committee Report, para 17.98.
needed to resolve conflicts of jurisdictional claims, and discussed dual residence conflicts, residence source conflicts and conflicts of source rules.\textsuperscript{38}

1.20 In the case of conflicts of source rules, the Asprey Committee argued for the inclusion in tax treaties of definitions of source of different categories of income.\textsuperscript{39} Similarly, the Asprey Committee considered that tax treaties should contain their own definitions of terms used when referring to different categories of income.\textsuperscript{40} In both these cases, the Asprey Committee noted that some Australian tax treaties of the time either applied the law of each contracting state or gave a term a meaning by reference to its meaning in the law of one of the contracting states.\textsuperscript{41} All of these observations are relevant to technical aspects of the broad policy objective of ensuring that tax treaties prevent unrelieved double taxation and hence are relevant to the third question identified at 1.4. As officers of the Australian Treasury and ATO supplied the Asprey Committee with information, it is possible that these observations by the Asprey Committee may have been influenced by and, to some extent, reflect attitudes of those officers to tax treat policy shortly after the period examined in this thesis. Hence these observations may be relevant to the second of the questions identified at 1.4.

1.21 The 1999 report of the Review of Business Taxation\textsuperscript{42} (hereafter ‘the Ralph Review’) made brief comments and four recommendations in relation to Australian tax treaties. As globalisation had provided opportunities for Australian companies to expand offshore, the Ralph Review recommended reciprocal lowering of withholding taxes on non-portfolio dividends in Australia’s tax treaties\textsuperscript{43} to facilitate cross border direct investment by lowering the tax cost of repatriation of profits.\textsuperscript{44} The Ralph Review commended the then recent Australian policy of matching non-taxation of the franked portion of a dividend with lower rates of withholding tax on non-portfolio dividends by

\textsuperscript{38} Asprey Committee Report, paras 17.100 to 17.103.
\textsuperscript{39} Asprey Committee Report, para 17.102
\textsuperscript{40} Asprey Committee Report, para 17.104.
\textsuperscript{41} Asprey Committee Report, paras 17.102 to 17.104.
\textsuperscript{43} Ralph Review, recommendation 22.21, p677.
\textsuperscript{44} Ralph Review, p677. The comment has to be seen in the context of the then current Australian tax treatment of foreign source non-portfolio dividends. At the time, generally non-portfolio dividends funded from income which had been taxed in a country with which Australia had a tax treaty were exempt when received by an Australian resident company while other non-portfolio dividends and portfolio dividends received by an Australian received a foreign tax credit. For a brief discussion of relevant Australian rules at the time see R L Hamilton, R L Deutsch and J C Raneri, Guidebook to Australian International Taxation (Prospect Media Pty Ltd, 7th ed, 2001) paras 3.10 and 3.110.
the treaty partner.\textsuperscript{45} The Ralph Review considered that this would be of significant benefit to Australian investment offshore, particularly into the United States, where a 15\% dividend withholding tax continued to be levied under the 1982 Australia – United States Tax Treaty.\textsuperscript{46}

1.22 The Ralph Review recommended that Australia agree to the non-discrimination article in future tax treaties,\textsuperscript{47} noting that while Australia was the only OECD country which did not include a non-discrimination article in its tax treaties, a recent study had found that Australia had one of the least discriminatory tax regimes applying to non-residents.\textsuperscript{48} If Australia agreed to a non-discrimination article in tax treaties, that would mean that Australian enterprises expanding overseas would be able to rely on reciprocal rules to protect them against tax discrimination by the host country.\textsuperscript{49} The Ralph Review considered that not agreeing to the non-discrimination article had made progress in negotiating Australia’s tax treaties difficult.\textsuperscript{50}

1.23 The third of the Ralph Review’s recommendations was that priority be given to renegotiating Australia’s ageing tax treaties with its major trading partners to make them consistent with Australia’s current tax treaty policy and with decisions concerning tax reform.\textsuperscript{51} The Ralph Review observed that none of Australia’s then operative tax treaties with the United Kingdom, Japan and the United States: properly reflected modern tax treaty policy; took into account emerging tax treaty issues; nor reflected decisions yet to be taken in relation to business tax reform.\textsuperscript{52} Finally, the Ralph Review recommended a review of Australia’s overall tax treaty policy to ensure that it reflected a balanced taxation of international investment and changed investment patterns.\textsuperscript{53}

1.24 The background to the third recommendation, and one of the major themes of the Ralph Review, was that while Australia remained a net capital importer, the percentage of Australian investment abroad as a share of foreign investment in Australia had grown from 10–20\% in the 1980s to about 60\% at the time of the Ralph Review. Hence, the Ralph Review saw a need for Australian treaty policy to move from its historic emphasis on source basis taxation to ‘an appropriate balance of

\textsuperscript{45} Ralph Review, pp677–8.
\textsuperscript{46} Ralph Review, p678.
\textsuperscript{47} Ralph Review, recommendation 22.22, p678.
\textsuperscript{48} Ralph Review, p678.
\textsuperscript{49} Ralph Review, p678.
\textsuperscript{50} Ralph Review, p679.
\textsuperscript{51} Ralph Review, recommendation 22.23, p679.
\textsuperscript{52} Ralph Review, p679.
\textsuperscript{53} Ralph Review, recommendation 22.24, p679.
source and residence based taxing rights that will encourage both inbound and outbound investment'. The observations concerning the need to balance source and residence taxation, given the changes in the balance of Australian inbound and outbound investment, is the most significant aspect of the Ralph Review relevant to the third question identified at 1.4.

1.25 The Board of Taxation's 2003 *International Taxation: A Report to the Treasurer* (hereafter ‘the 2003 Review’) contained a discussion of tax treaty policy in the context of a chapter titled ‘Promoting Australia as a location for internationally focussed companies’. The 2003 Review saw the balance between residence and source taxation and whether the balance struck in the Protocol to the US Tax Treaty should be the basis for future policy as major policy questions. The 2003 Review noted Australia’s historic emphasis on source basis taxation, and identified the wide definition of ‘permanent establishment’ and the relatively high withholding tax ceilings in Australian tax treaties as examples of this emphasis. The 2003 Review also noted that Australian tax treaties negotiated since the introduction of capital gains tax in 1985 had preserved Australian domestic law source taxing rights over capital gains including the then domestic law rule relating to capital gains on shares. The 2001 Protocol to the Australia – US Tax Treaty was characterised as moving further away from source taxation by reducing withholding tax rates and qualifying Australia’s levy of capital gains tax on US residents.

1.26 Problems with Australia’s historic emphasis on source taxation were noted by the 2003 Review. The source based tax treaty policy was regarded as having detrimental impacts on Australian firms investing offshore by exposing them to high taxes in treaty partner countries in a context where Australia had unilaterally given up significant areas of source taxation. The 2003 Review noted that the treatment of capital gains in Australia’s pre 1985 tax treaties was a vexed issue with the private sector and that this and Australia’s broad claim to capital gains tax jurisdiction adversely affected investment decisions by non-residents. Moreover, the 2003 Review considered, Australia’s emphasis on source basis taxation had made

56 2003 Review, para 3.49.
60 2003 Review, para 3.55.
updating some of Australia’s tax treaties problematical.\textsuperscript{62} The 2003 Review pointed out that, as Australian offshore investment was concentrated in a few countries, priority should be given to revising and updating treaties with those countries.\textsuperscript{63}

1.27 Again, the major policy conclusion was based on the change in investment inflows and outflows. The 2003 Review noted that as Australia moved towards a balance of inflows and outflows, the need for source taxation receded, and considered that the efficiency gains from moving to a residence based tax treaty policy might exceed the revenue foregone.\textsuperscript{64}

1.28 The 2003 Review made four recommendations in relation to tax treaty policy. The first was to move to a more residence based treaty policy.\textsuperscript{65} The second was against a Ralph Review recommendation to apply Australian capital gains tax to the sale by non-residents of non-resident interposed entities with underlying Australian assets.\textsuperscript{66} The third was to review and keep the ‘key country treaties’ up to date and aligned with the first recommendation, and to give priority to the most important partners for Australia in tax treaty negotiations.\textsuperscript{67} The fourth related to consultation with the 2003 Review, recommending similar processes to those that the government had adopted for domestic tax legislation.\textsuperscript{68} As was the case with the Ralph Review, the most significant aspect of the discussion of tax treaty policy by the 2003 Review for the third question identified at 1.4 was its observations concerning the need for a balance between source and residence taxation given changes in the balance of Australian inbound and outbound investment.

1.29 Several commentators reported on the implementation and/or practical application of recommendations by either the Ralph Review or the 2003 Review, or both.

1.30 In 2003, Norman,\textsuperscript{69} in surveying Australia’s recent tax treaties and protocols up to the 2002 Mexico Treaty, noted the extent to which these treaties and protocols implemented recommendations made in those reviews, the policy background behind them and their practical effects.

\begin{itemize}
\item \textsuperscript{62} 2003 Review, para 3.58.
\item \textsuperscript{63} 2003 Review, para 359.
\item \textsuperscript{64} 2003 Review, para 3.61.
\item \textsuperscript{65} 2003 Review, recommendation 3.5 and discussion, para 3.70 to 3.73.
\item \textsuperscript{66} 2003 Review, recommendation 3.6 and discussion, para 3.74 to 3.76.
\item \textsuperscript{67} 2003 Review, recommendation 3.7 and discussion, para 3.77 to 3.80.
\item \textsuperscript{68} 2003 Review, recommendation 3.8 and discussion, para 3.81 to 3.83.
\end{itemize}
1.31 In 2008, Dirkis\textsuperscript{70} reviewed changes in Australian double tax treaty practice following on from recommendations made by the Ralph Review and the 2003 Review. He found evidence of implementation of the first recommendation in the use of an exemption (rather than a foreign tax credit) method and the use of lower rates of withholding tax in Australia’s then recent bilateral tax treaties and protocols. Dirkis discussed the various attempts that Australia has made to override treaties through domestic legislation and the relevant case law that gave rise to these attempts. In particular, Dirkis discussed s3A of the *Income Tax (International Agreements) Act 1953* (enacted in response to the decision in *FTC v Lamesa Holdings BV* 97 ATC 4752). Other modernisation developments that Dirkis noted were changes to the exchange of information article and the assistance in collection provisions (based on Article 27 of the OECD Model) contained in the 2006 treaties with Norway, France and Finland and the 2005 changes to the treaty with New Zealand.

1.32 Vann,\textsuperscript{71} in 2009, in an analytical and critical discussion, reviewed Australian current and previous reviews of Australian tax treaty policy. Vann summarised the discussions of treaty policy in the Asprey Report, the Ralph Review and the 2003 Review and made observations on the review of Australia’s Tax Treaty Negotiation Policy commissioned by the Rudd government.

1.33 Vann considered that the general theme of a more residence, as distinct from source, based treaty policy which came out of these reviews was ‘the most important substantive policy change in Australian tax treaty policy since its inception’.\textsuperscript{72} Vann noted that a major driver for the change was the trend that the ratio of inward and outward investment was shifting closer to 1:1, a point by then already reached for equity investment.\textsuperscript{73} Vann then argued that when investment flows are in balance or are trending towards balance, a country does not give up revenue by treaty decreases in source taxation because these were counterbalanced by increased revenue from residence taxation.\textsuperscript{74} Vann then observed that Australia’s shift to a residence based policy was still not being pursued consistently and needed to be


\textsuperscript{72}Vann, above n 71, 407.

\textsuperscript{73}Vann, above n 71, 407–08.

\textsuperscript{74}Vann, above n 71, 408–09.
thought through across tax treaties, with Treasury and the ATO needing to think about Australian outbound investment as much as inbound investment.\(^75\)

1.34 Vann then argued in favour of the signalling effect of tax treaties, seeing them as ‘one of several instruments of international economic law which indicate that a country has accepted the economic liberalism orthodoxy that underlies the international economic order’ and, without endorsing the international economic order, observed that the countries which ‘seem to succeed most are ones which embrace it’.\(^76\)

1.35 Vann then argued that on joining the OECD in 1971, Australia carried its previous treaty practices with it with the result that for the next three decades Australian tax treaty practice was set in stone and characterised by an extreme source position for an OECD country and language oddities being maintained even where the OECD terminology produced similar results.\(^77\) Vann asserted that these features, coupled with Australia’s low number of tax treaties and its ‘take it or leave it’ negotiating style, meant that, ‘Australia is not regarded internationally as a country which embraces tax treaties as a good thing for the country and the world.’\(^78\)

1.36 Hence, Vann argued that Australia, apart from the substantive changes in tax treaty policy resulting from the shift in investment patterns, should ‘retreat from its exceptionalism in tax treaties and align itself much more closely with the intent and wording of the OECD Model’. Vann noted that needless difficulties in negotiations were still produced because of Australian peculiarities in treaties, adopted many years ago and for which the need has since disappeared.\(^79\)

1.37 Australian exceptionalism, in Vann’s view, had adverse consequences for the interpretation of Australian tax treaties because it meant that doubt was created as to what extent the OECD Commentaries applied, with the result that giving advice or rulings to Australian or foreign investors was more difficult and increased the tax risks attached to Australian related inbound and outbound investment. For this reason, Vann argued in favour of Australia making more information public on its tax treaty

\(^{75}\) Vann, above n 71, 409. As an example of the adverse effects of Australia’s inbound mindset, Vann instanced the omission of the non-discrimination article in the current Australia–France Tax Treaty and Australia’s litigation in Deutsch Asia Pacific Finance Inc v FCT (No 2) (2008) 172 FCR 336.

\(^{76}\) Vann, above n 71, 410–11. The quotation is from p411.

\(^{77}\) Vann, above n 71, 411–12.

\(^{78}\) Vann, above n 71, 412.

\(^{79}\) Vann, above n 71, 412.
negotiating positions, noting that currently this has to be indirectly derived through
the type of research discussed at 1.13 to 1.16.\textsuperscript{80}

1.38 The element in Vann’s response to the Ralph Review and the 2003 Review that goes
beyond their recommendations is his call for a retreat from Australian exceptionalism
in tax treaties and that Australia pursue a more residence based treaty policy
consistently across treaties. That call highlights the relevance of the first two
questions identified at 1.4 to the third question. Ascertaining, with the assistance of
archival research, the reasons behind Australian exceptionalism can provide valuable
information for assessing whether those exceptional features in Australian tax
treaties should continue given the acknowledged changes in the balance of
Australian inbound and outbound investment.

The Methodology Used In This Thesis

1.39 The method of traditional legal research is concerned with: (a) identifying what the
law is; (b) analysing its conceptual coherence; (c) determining how and why it came
to be what it is; and (d) assessing how it would or should apply in the present.\textsuperscript{81}
Traditional legal research thus has a limited scope and serves limited functions. It is
nonetheless essential to the informed development and reform of the law. This thesis
utilises archival material as a means of considering, in particular, concerns (c) and
(d) of traditional legal research. As argued at 1.40 to 1.42, the methodology of
traditional legal research is distinct from other forms of empirical research. While it
refers to records of past events, the approach taken in this thesis, and in traditional
legal research in general, is distinct from the research performed by professional

\textsuperscript{80} Vann, above n 71, 412–13.

\textsuperscript{81} Legal research of this type was described as ‘doctrinal research’ in D Pearce, E Campbell
and D Harding, \textit{Australian Law Schools: A Discipline Assessment for the Commonwealth
Pearce, Campbell and Harding described ‘non-doctrinal’ research as being research ‘about
law’ as distinct from research ‘in law’. A similar characterisation of traditional legal research in
the tax context specifically was made by Judith Freedman, ‘Taxation Research as Legal
Research’ in M Lamb, A Lymer, J Freedman and S James (eds), \textit{Taxation: An
Interdisciplinary Approach to Research} (Oxford University Press, 2005) 13. For works that
focus on the process of finding the law and identifying and locating sources of law see, for
example, Enid Mona Campbell, Poh York Lee and Joycey G. Tooher, \textit{Legal Research
Materials and Methods} (LBC Information Services, 4\textsuperscript{th} ed, 1996) and more recent works
that have greater focus on electronic search techniques such as Bruce Bott, Ruth Talbot-Stokes
and Irene Nemes, \textit{Nemes & Coss’ Effective Legal Research} (LexisNexis Butterworths, 4\textsuperscript{th}
ed, 2009). For an argument that legal research should embrace and does include social science
methodologies see Terry C M Hutchinson, \textit{Researching and Writing in Law} (Thomson
Reuters/Lawbook Co., 3\textsuperscript{rd} ed, 2010) ch 5.
historians. Nor, it is submitted, is the methodology adopted in this thesis or in traditional legal research in general properly classified as social science research.

1.40 All empirical research is conducted in a present moment or in a series of present moments. As each present moment is infinitesimal, all reports of empirical research in any field are necessarily reports of past events and are themselves past events that are experienced in a present moment. What distinguishes history from empirically based research in social sciences is the object of historical enquiry. The actual events of history to which records relate, being past, cannot be returned to, nor can they be replicated in the present, although reconstructions of them can aid their historical interpretation. The object of historical enquiry may be thought to be knowledge and understanding of past events or of a past reality. By contrast, empirically based social science research is considered valid to the extent to which its observations are able to be replicated in the present in circumstances that, except for the temporal difference, are otherwise identical. This is because empirically based social science research is concerned with making claims about a present reality. The claims may be spatially or culturally qualified, but once the claim is temporally qualified to the extent that it is incapable of being replicated in the present in otherwise identical conditions, it becomes a claim about a past reality and can be considered a historical artefact. Hence, the object of social science research may be thought to be knowledge and understanding of a present reality.

1.41 Traditional legal research is concerned, at least in part, with identifying what the law is at a given point in time and how it will or should apply in given factual circumstances. It does so by referring to records of past events and by applying them, as distinct from replicating them, in a present moment. In the process of applying the historical records, legal research may interpret the record using historical methods in understanding the development of the record and may take into account the results of social science investigation in assessing the likely effect of the application of the rule in the present moment. The use of the methods and results of these other disciplines, however, is peripheral and supplementary to the key objects and concern of traditional legal research, which, as argued at 1.39, is how the record of a past event should be applied in a present moment.

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82 It is conceded that social science research can be concerned with changes in society over time. It is submitted, though, that when such research is making observations that cannot be replicated in the present, it is making observations about historical events and to that extent is engaged in history. It is submitted, though, that the use of this historical material in social science is to contrast the past event with present reality. The past event is not understood for its own sake, but rather in contrast to the different present reality.
1.42 So far as the interpretation of the past event involves a conclusion by a court of what the law was and/or is, it is an authoritative determination and remains authoritative until overturned by a subsequent court decision or by statute. Hence, when seen from this perspective legal research is at once both a study based on history and a study that draws conclusions about present reality.83

1.43 Only rarely, and then more recently, has traditional legal research paid attention to archival materials relevant to statutes and reports of court decisions. Some published works have made use of materials in foreign archives relating to tax treaties or model tax treaties;84 however, other than literature produced by the author as part of the present research and the article by Vann referred to at 1.10, none makes use of material in the National Archives of Australia. In addition, other than literature produced as part of the present research and a 2014 article by Avery Jones and Ludicke,85 none of the prior published works makes use of materials in the archives of both partners to a particular tax treaty.

1.44 In the treaty context specifically, one factor that may have led to the relative lack of research based on preparatory materials has been their lack of availability until

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83 For a discussion of the impossibility of having direct evidence of past events and distinguishing between history and social science see Murray G Murphey, Truth and History (State University of New York Press, 2009) 5–13 and 181–2 respectively. A similar argument that legal research should be distinguished from other disciplines, such as social and physical sciences, is made by Jan M Smits, The Mind and Method of the Legal Academic (Edward Elgar, 2012). Smits, at 151, submits that the other disciplines are often limited to understanding social or physical reality while the legal discipline should reflect on what ‘people or organizations legally ought to do’.


85 John F Avery Jones and Jurgen Ludicke, above n 84.
comparatively recent times. For example, many countries only make government documents relevant to treaty negotiations publically available after the expiration of a period of time, usually not less than 30 years but in some instances in some jurisdictions, 60 years. As the first Australian taxation treaty was only signed in 1946, government files relating to its negotiation only became publically available in 1976. Australia’s next four treaties were negotiated in 1953, 1957, 1960 and 1967 respectively, and hence government files relating to their negotiation only became publically available in 1983, 1987, 1990 and 1997 respectively.

1.45 The method adopted in this research seeks to reverse this lack of attention to archival materials and uses historical methods as a supplementary means of achieving objectives (c) and (d) of traditional legal research identified at 1.39. This research seeks to identify the origins of distinctive features in Australian taxation treaty practice and to assess the factors which influenced the development of those distinctive features.

1.46 Distinctive features of Australian taxation treaty practice were identified at 1.2 by comparing currently operative Australian treaties with the OECD Model Taxation Treaty. The thesis then seeks to identify the origins of those features and to assess the factors which influenced their development by examining official government files that relate to the negotiation and drafting of selected Australian taxation treaties in the period 1946 to 1971. The factors that influenced Australian taxation treaty policy and practice, and their changing degrees of importance, will become apparent through an account in the form of a narrative of the negotiation and drafting of Australian taxation treaties in the period 1946 to 1971.

1.47 The only treaties examined have been those in relation to which the author has been able to locate reasonably extensive archival evidence in either the National Archives of Australia or in foreign government archives. As a result, the negotiation and drafting of the 1960 New Zealand Treaty has not been discussed. Considerations of space have meant that discussion of the 1957 Canada Treaty has been confined to analysis in the concluding chapter of the few variations from the current OECD Model that originated in that treaty. The 1969 Singapore Treaty is not discussed because, for reasons explained more fully at 6.1, that treaty contains features that are atypical of Australian treaties in the period. The last treaty to be discussed in this thesis is the 1969 Japan Treaty, which was the last Australian tax treaty that came into force before Australia entered the OECD and which, it will be argued, in some respects represents the ‘high-water mark’ of Australian pre 1971 exceptionalism.
Although the 1972 German Treaty was negotiated but not signed before Australia entered the OECD, it did not come into force until after Australia joined the OECD, and the Australian attitude to its negotiation may have been influenced by Australia's pending OECD membership in a way that did not affect the negotiation and drafting of earlier Australian tax treaties. An examination of the negotiation and drafting of that treaty would be more relevant to a thesis concerned with the impact of Australia's OECD membership on Australian tax treaty policy and practice.

This chapter has included a review of literature relevant to Australian tax treaty practice. Taking that literature into account, the final chapter of the thesis will draw on the narrative accounts in previous chapters to identify the factors that influenced Australian tax treaty policy and practice in the period and to identify explanations for variations in Australian tax treaty practice from the OECD Model. On the basis of that identification, the final chapter will then assess what distinctive features of Australian tax treaty policy and practice should be discontinued.

The Contribution To Knowledge Made By This Thesis

The first contribution to knowledge by the thesis will be deriving information to assist in answering the first two central questions identified at 1.4 through an examination of archival materials. While identification of instances of variations in Australian tax treaty practice from the OECD Model would be possible without referring to archival materials, this is something which has, to an extent, previously been done in the research by Dirkis and Burch, by Bain et al and by Magney. As noted previously, those works do not provide a comprehensive historical account of the development of variations in Australian tax treaty practice from the OECD Model. By examining archival material, Appendices 3, 4 and 5 of this thesis identify and tabulate the history of the development of Australian tax treaty practice in the period 1946 to 1972.

While useful for analysis, adopting this approach alone would risk: isolating particular developments from each other and from policy developments; failing to take account of the interplay of argument in negotiations; and not adequately accounting for relevant personal, economic and geopolitical influences. Instead, the thesis takes a narrative approach in which the development of particular features of Australian tax treaty practice and policy are identified from the process of telling the story of the negotiation of particular treaties and the development of Australian tax treaty policy in the period under review. This will enable the development of particular features and

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86 See the discussion at 1.9 and at 1.13 to 1.15.
factors not only to be identified, but to be appreciated in the context of: the development of other features; the interplay of argument in the negotiation process; and relevant personal, economic and geopolitical influences.

1.52 A contribution to knowledge of the thesis is the narrative itself; telling this story which has not, on the basis of archival material, been completely told before. The narrative is the story of when, how and why Australian taxation treaty policy and practice came to have some of its distinctive features. That will be the thesis’ second contribution to knowledge.

1.53 The third contribution to knowledge will be the method itself. In telling the story by using archival evidence, the thesis aims to highlight the value of archival based, historical research for an understanding of the law in general and of taxation treaties in particular and for the development and reform of the law.

1.54 The final contribution to knowledge will be the assessment of those features of Australian tax treaty policy and practice that should be re-evaluated having regard to the original reason why they were introduced and subsequent relevant changes in circumstances.

The Remaining Chapters Of This Thesis

1.55 The remaining chapters in this thesis are:

Chapter Two: Australia’s First Comprehensive Tax Treaty

Chapter Three: Australia’s Tax Treaties Negotiated in the 1950s


Chapter Five: Australia’s Second Treaty With The UK, in 1967

Chapter Six: The 1969 Treaty With Japan

Chapter Seven: Conclusions

In addition the thesis contains the following appendix which have been prepared as summaries of the archival and other material relied on in this thesis:

Appendix One: Chronological Table Of Australian Comprehensive Tax Treaties, Amending Protocols, Exchanges Of Notes And Exchanges Of Letters

Appendix Two: Current Australian Reservations In Relation To The OECD Model Convention

Appendix Three: Variations In Currently Operative Australian Tax Treaties From The OECD Model Convention On Income And Capital
Appendix Four: Variations From The Current OECD Model Having Their Origins In The 1946 Australia – UK Tax Treaty And Variations From The 1945 UK – US Tax Treaty


Appendix Seven: Analysis Of Deemed Source Rules In Currently Operative Australian Tax Treaties

A bibliography of archival material and books and journal articles considered in completing this thesis follows the appendices.
CHAPTER TWO: AUSTRALIA'S FIRST COMPREHENSIVE TAX TREATY

2.1 Australia's first comprehensive tax treaty was concluded with the UK in 1946. Examination of the history of the negotiation and drafting of that treaty is important for two key questions investigated in this thesis.

2.2 First, this chapter will demonstrate that several distinctive features of Australian taxation treaty practice have their origins in that treaty. The treaty had a structure which was maintained in Australian treaties throughout the period under consideration. It is argued at subsequent points in this thesis that this structure influenced the form of particular Australian variants on articles (particularly the other income article) after the structure itself was abandoned in Australian taxation treaties. Hence some distinctive features of Australian treaty practice were indirect products of the structure established in this treaty even though articles equivalent to them were not contained in the treaty itself.

2.3 Secondly, examining the factors that influenced the negotiation (including the decision to negotiate) and drafting of this treaty is an essential step in investigating the key question of what those factors were and how they developed during the period reviewed in this thesis.

2.4 To understand the factors that influenced the negotiation and drafting and the distinctive features of the 1946 UK Treaty, it is necessary to understand why both the UK and Australia wanted to enter into a comprehensive bilateral taxation treaty by 1945. This will involve a brief description of the approaches to relieving international double taxation between Australia and the UK that preceded the treaty; namely, broad exemption for foreign source income in Australia's case and the Dominion Income Tax Relief System in the case of the United Kingdom. It will also be necessary to explain the reasons why both the UK and Australia wanted Dominion Income Tax Relief discontinued by 1945. This will involve a brief discussion of the Australian economy in 1945 and key elements of the respective income tax systems in 1945 as they affected cross border transactions.

The Australian Economy In 1945

2.5 The Second World War produced major changes in the Australian economy and society. Manufacturing as a share of GDP increased at an unprecedented rate.¹

¹ A recent discussion is I W McLean, Why Australia Prospered: The Shifting Sources of Economic Growth (Princeton University Press, 2013) ch 8 ‘The Pacific War and the Golden Age’. At p180 McLean notes that whereas between federation and the First World War the share of GDP originating in manufacturing only increased from 12.1 to 13.5% then reached
Australian xenophobia as an Anglo-Saxon-Celtic outpost at the edge of Asia was heightened by the Japanese invasion of Papua and New Guinea and by air and naval attacks on the Australian mainland. Australia embarked on a post war policy of European immigration to provide the necessary manpower for manufacturing, nation building projects and increased defence security. During the period of the Chifley government, however, the policy intent was for immigration and investment to be predominantly from, and for the trade to be predominantly with, the United Kingdom.

2.6 Despite Australia’s reliance militarily on the US in the Second World War, the UK remained Australia’s major trading partner and its major source of portfolio and non-portfolio investment. The Chifley government’s policy of UK/Commonwealth preference meant that Australia maintained long-term food contracts with the UK and participated in the ‘Sterling Area’.

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2.6 Despite Australia’s reliance militarily on the US in the Second World War, the UK remained Australia’s major trading partner and its major source of portfolio and non-portfolio investment. The Chifley government’s policy of UK/Commonwealth preference meant that Australia maintained long-term food contracts with the UK and participated in the ‘Sterling Area’.
In 1945 Australia had a nominal worldwide system of income taxation but exempted income that had been subject to tax in a foreign country. Non-residents were taxed on their Australian source income.

The Australian system of corporate-shareholder taxation, having previously been a dividend deduction system, then an imputation system and then a shareholder relief system, had been gradually converted to a classical system due to the increasing revenue demands imposed by Australia’s involvement in World War II. The intercorporate dividend rebate which had been available to all companies since 1915 ceased to be available to non-resident companies in 1939. The system effectively

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8 ITAA 1936 s17 levied income tax on the ‘taxable income’ of residents and non-residents. ITAA 1936 s6(1) defined ‘taxable income’ as ‘the amount remaining after deducting allowable deductions from assessable income’. ITAA 1936 s25(1)(a) included the gross income from all sources, whether in or out of Australia, in the assessable income of a resident. ‘Income’ was not exhaustively defined and the reference to gross income had been interpreted as including a reference to the meaning of ‘income’ under ordinary concepts and usages, an interpretation which excluded capital gains and relied heavily on UK precedents. The most comprehensive analysis of Australian case law on the ordinary concept of income remains R W Parsons, Income Taxation in Australia (Law Book Company, 1985) ch 2. ITAA 1936 s26 did not contain jurisdictional limits. Two views developed of the relationship between ITAA 1936 s26 (and other provisions deeming amounts to be included in assessable income) and ITAA 1936 s25(1). These were the ‘parallel provisions’ analysis and the ‘central provision’ or ‘single meaning’ analysis. R W Parsons, Income Taxation in Australia [4.1] to [4.11] argued strongly in favour of the ‘central provision’ analysis under which amounts deemed to be included in assessable income via ITAA 1936 s26 (or most other but not all specific provisions) were included in ‘gross income’ for purposes of ITAA 1936 s25(1).

9 The nominal worldwide system had been introduced by ITAA 1930 (Cth) Act No 50 of 1930, which amended s13 of ITAA 1922 (Cth) with the effect that subject to exceptions, residents were taxed on their income from all sources, whether in Australia or elsewhere, while ‘absentees’ (defined as persons who were not ‘residents’) were taxed on their income from Australian sources. Act No 50 of 1930 also amended s14(q) of the ITAA 1922 (Cth) to provide an exemption for foreign source income that was chargeable with income tax in any country outside Australia. By 1945, the exemption was under ITAA 1936 s23r. A definition of ‘resident’ had been inserted in ITAA 1922 (Cth) by ITAA Act No 50 of 1930. By 1945, the definition was contained in s6(1) of ITAA 1936 (Cth).

10 ITAA 1936 s25(1)(b) included the gross income from all sources in Australia in the assessable income of a non-resident. ITAA 1936 s23r exempted from Australian tax income derived by a non-resident from foreign sources.
became a classical system in November 1940 with the abolition of the dividend rebates previously given to individual shareholders.\textsuperscript{11}

2.9 Subject to certain exceptions, dividends paid by a resident or non-resident company, out of profits derived from any source, were included in the assessable income of a resident shareholder.\textsuperscript{12} Dividends\textsuperscript{13} paid out of profits derived from Australian sources were included in the assessable income of a non-resident shareholder.\textsuperscript{14} Although several of the pass-through features of the imputation system were initially retained, previous exemptions for dividends funded from foreign source income, corporate capital profits and exempt Commonwealth loan interest were repealed in 1941.\textsuperscript{15} From 1942, non-corporate shareholders were allowed a deduction for foreign tax paid on dividends.\textsuperscript{16}

2.10 Originally, the Commonwealth and the States had levied concurrent income taxes. In 1942, under the Uniform Tax Scheme, the Commonwealth government effectively excluded the Australian States from the income tax field by collecting sufficient tax at the Commonwealth level to enable the Commonwealth to reimburse the States for the income tax they would have otherwise collected.\textsuperscript{17}

2.11 By 1945, the company tax rate was 30\%. Non-private companies were subject to the higher of Super Tax or War-time (Company) Tax. Super Tax of 5\% was payable by non-private companies on the excess, if any, of its taxable income over £5000. War-time (Company) Tax was levied on the amount by which the company's taxable profit

\textsuperscript{11} ITAA (No 2) 1940 cl 4 amended ITAA 1936 by omitting the rebate provision for individual shareholders in s46(1) and by amending the inter-corporate dividend rebate provisions in s46(2).

\textsuperscript{12} ITAA 1936 s44(1)(a).

\textsuperscript{13} ‘Dividends’ were given an expansive definition by ITAA 1936 s6(1) and certain liquidator’s distributions were deemed by s47(1) to be dividends paid by the company to shareholders out of profits derived by the company.

\textsuperscript{14} ITAA 1936 s44(1)(b).

\textsuperscript{15} ITAA 1941 cls 6 and 7.

\textsuperscript{16} ITAA (No 2) 1942 inserted ITAA 1936 s72A.

exceeded 5% of its capital employed. The rate of War-time (Company) Tax was 24% on the portion of taxable profit that represented the next 7% of capital employed and 48% on the balance of taxable profit. No inter-corporate rebate was available in respect of War-time (Company) Tax, which meant 2.56 that it cascaded when the same income was distributed as a series of dividends through a chain of resident companies.

2.12 Undistributed profits tax at the rate of 10% was payable by non-private companies, with the company being allowed a deduction for Australian and foreign income tax paid on the company’s income. Private companies, including non-residents carrying on business in Australia through a principal office or a branch, were subject to additional tax (calculated as the tax shareholders would have paid if a distribution had been made) on profits not distributed within specified time periods.

2.13 As noted at 2.9, from 1942 foreign source dividends were included in the assessable income of Australian residents with a deduction being allowed for non-corporate residents for any foreign tax paid. In the case of dividends received from UK companies, tax deducted at source (representing tax paid by the company) was not included in the shareholder’s assessable income with the consequence that the shareholder was not entitled to a deduction for the tax deducted at source.\(^{18}\) Foreign source dividends received by Australian resident companies received an inter-corporate dividend rebate. The effect of the rebate was that Australian companies receiving dividends from UK companies did not incur a net Australian tax liability.\(^{19}\)

2.14 Australia taxed domestic source income of non-residents without requiring any minimum business presence in Australia. Presumptive tax regimes applied to non-residents deriving certain shipping income,\(^{20}\) film business income\(^{21}\) and insurance

\(^{18}\) This followed from the decision of Dixon J in \textit{Jolly v FCT} (1934) 50 CLR 131 affirmed on appeal by the Full High Court and discussed in J L Gunn, O E Berger, J M Greenwood and R E O’Neill, \textit{Gunn’s Commonwealth Income Tax Law and Practice} (Butterworth & Co Australia, 2nd ed, 1948) 606, para 1010.

\(^{19}\) Corporate residents were entitled to a deduction under \textit{ITAA 1936} (Cth) s72A, had tax calculated at the corporate rate, and were then entitled to an inter-corporate rebate at the corporate rate under \textit{ITAA 1936–1945} (Cth) s46. The rebate did not extend to undistributed profits tax. A further rebate allowed under s46(2A) was available where the dividend was paid out of profits which had borne super tax. The s46(2A) rebate produced anomalous results and a cascading of tax where dividends were paid through a chain of companies.

\(^{20}\) \textit{ITAA 1936} div 12 had the effect of deeming 5% of the gross receipts for carriage of passengers, livestock, mails or goods shipped in Australia to be taxable income.

\(^{21}\) \textit{ITAA 1936} div 14 had the effect of imposing a liability to pay income tax on a non-resident deriving income under a contract relating to a business carried on in Australia by the other party of distributing, exhibiting or exploiting motion picture films or from leasing or licensing others to exhibit or display them. Division 14 provided that 10% of the gross income so derived was included in the non-resident’s taxable income. Division 14 further deemed the
income. Both individual and corporate non-residents had always been assessable on a net basis on dividends paid to them by a company (whether an Australian resident or not) to the extent to which they were paid out of profits derived from sources in Australia. Where the paying company was an Australian resident, the Commissioner had some prospect of enforcing tax liabilities if the non-resident had property in the form of shares in Australia. Where the paying company was not an Australian resident and the shareholder did not have property in Australia, the Commissioner refrained from assessing the dividend.

2.15 In 1945, companies paying interest to non-residents, other than companies carrying on business in Australia, were taxed at a rate of 30% on the payment and were entitled to deduct the tax from the interest they paid. However, this provision did not apply where the paying company could establish to the satisfaction of the Commissioner that the creditor could enforce payment of the interest without deduction of tax at source.

2.16 Australian residents having the receipt, control or disposal of money belonging to a non-resident who derived income from sources in Australia were liable, when required by the Commissioner, to pay the tax due and payable by the non-resident and were authorised and required to retain, from moneys that came to the resident on behalf of the non-resident, sufficient funds to pay the tax. A company paying dividends to a non-resident had no personal liability to pay tax under these provisions in the absence of notification by the Commissioner of an assessment of the non-resident.

2.17 The requirements discussed at 2.16 interacted with ITAA 1936 (Cth) s256 in relation to royalties. Under s256 where a resident paid a royalty to a non-resident the payer was required to advise the Commissioner of the amount of the royalty and to party carrying on business in Australia to be the agent of the non-resident and prohibited that party from making payments to the non-resident until satisfactory arrangements were made with the Commissioner in relation to the income tax imposed on the non-resident.

ITAA 1936 div 13 deemed premiums paid or payable to non-resident insurers in respect of property situated in Australia or in relation to insured events which could only happen in Australia to have an Australian source. Where the actual profit derived by the non-resident insurer from these premiums could not be established to the satisfaction of the Commissioner, the non-resident was deemed to have derived taxable income equal to 10% of the total premiums paid or payable in the income year in respect of those contracts of insurance. The provisions did not apply to life insurance.

See the discussion in Gunn et al, above n 18, 341–2, para 549.

ITAA 1936–1945 (Cth) s125. See the discussion in Gunn et al, above n 18, 859–62, paras 1363–71.

ITAA 1936–1945 (Cth) s255. See the discussion in Gunn et al, above n 18, para 1849.

See the discussion in Gunn et al, above n 18, 1135–6, para 1849.

See the discussion in Gunn et al, above n 18, 1135–6, para 1849.
ascertain from the Commissioner the amount to be retained in respect of tax due by
the non-resident. Royalties were taxed on a net assessment basis and at rates
applicable to non-residents.

Relevant Features Of The UK Income Tax System In 1945

2.18 In 1945, the UK operated a system of corporate-shareholder taxation under which
the company paid income tax at the standard rate of 50% and dividends were
assumed to be paid out of taxed profits. As income tax was assumed to have been
deducted from dividends at the standard rate, only those natural person shareholders
who had a surtax liability would be liable to any further tax on the dividend. This was
ture for both resident and non-resident shareholders. The UK did not apply a
withholding tax to dividends paid to non-residents, and practical difficulties were
associated with the collection of surtax from non-residents. Various reliefs were
allowed to resident natural persons which could mean that a natural person
shareholder was entitled to some refund of tax in respect of a dividend in some
circumstances.

2.19 Annual interest and most royalties were not deductible in computing profits, but the
payer deducted tax and retained tax from the payment. This was true whether or not
the recipient was a resident or non-resident, and no separate withholding taxes
applied to interest or royalties paid to non-residents.

2.20 Companies also paid the higher of Excess Profits Tax and National Defence
Contribution. Excess Profits Tax was introduced as a war-time measure and was
abolished in 1946. Unlike income tax, neither Excess Profits Tax nor National
Defence Contribution could be passed on to shareholders by way of deduction from
dividends. For this reason, Australia viewed Excess Profits Tax and National Defence
Contribution as equivalents to Australian company tax.

2.21 As will be seen at 2.129 to 2.130, issues about the operation of the credit article in
the treaty in relation to excess profits tax were the subject of a significant amount of
discussion in the treaty negotiations. For the purposes of the Seventh Schedule of
the Finance Act (No. 2) 1945, as originally enacted, Excess Profits Tax included the
National Defence Contribution. As the Seventh Schedule stood in 1945 foreign

28 See the discussion in Gunn et al, above n 18, 1136, para 1850.
29 The description of the UK system in 1945 has been based on John F Avery Jones, ‘The
History of the United Kingdom’s First Comprehensive Double Taxation Agreement’ [2007]
British Tax Review 211 in particular 222–3.
30 NAA, ATO Tax Credits, Notes on Article XII by Belcher and Mills, p43.
31 Seventh Schedule, Clause 1(1), Finance Act (No 2) 1945.
excess profits taxes could only be credited against UK Excess Profits Tax and not against income tax. Similarly, foreign income tax could only be credited against UK income tax and not against Excess Profits Tax.\textsuperscript{32}

\textbf{The System Of Dominion Income Tax Relief\textsuperscript{33}}

\textbf{2.22} To appreciate why both Australia and the UK wanted to enter into a comprehensive double taxation treaty by 1945, it is necessary to understand how the previous system of Dominion Income Tax Relief worked.

\textbf{2.23} In 1922, the Royal Commission on the Income Tax, following a report from a Subcommittee which conferred with representatives of the Dominions, recommended the system of Dominion Income Tax Relief, which was implemented in the UK as s27 of the \textit{Finance Act} 1921.\textsuperscript{34}

\textbf{2.24} Under the system of Dominion Income Tax Relief, for income which had been taxed in a Dominion, the UK provided a credit against UK tax of the lesser of the rate of Dominion tax or one half of the relevant UK rate. The aim of the system of Dominion Income Tax Relief was that the total tax paid by a UK resident on Dominion sourced income should not exceed the greater of the UK or the Dominion rate. In other words, the total relief provided was required to equal the lesser of the relevant UK rate or the relevant Dominion rate. Where the relief provided by the UK did not produce this result, the expectation was that the relevant Dominion would provide a rebate of tax to make up the difference.

\textbf{2.25} The operation of the system can be illustrated by taking an example of a UK resident subject to UK tax at the standard rate of 50\% receiving £1000 of Australian source interest which had been subject to Australian tax of £260 at the rate of 26\%. The UK would gross up the interest for the Australian tax, would apply UK tax of £500 and

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{32} Seventh Schedule, Clause 2, \textit{Finance Act (No 2) 1945}.
\item \textsuperscript{34} Between 1803 and 1914 the United Kingdom, while taxing on a residence and source basis, had only taxed foreign source income when it was remitted to the United Kingdom. From 1914, major types of foreign source income had been taxed in the UK independently of remittance. Temporary relief from international double taxation had been provided by s43 of the \textit{Finance Act 1916}. See the discussion of the history of the jurisdictional scope of UK income tax laws in P A Harris, \textit{Corporate/Shareholder Income Taxation and Allocating Taxing Rights Between Countries} (IBFD Publications, 1996) 287 and 294.
\end{itemize}
\end{footnotesize}
would allow a credit of £250, being one half of the applicable UK rate, which was less than the applicable Dominion rate of 26%. Hence UK tax of £250 would be payable. As the total tax paid of £510, being £260 Australian tax and £250 UK tax, would have exceeded £500 (being the tax that would have been payable if £1000 had been subject to UK tax at the rate of 50%, being the greater of the relevant UK and Dominion rates), Australia would then allow a rebate of £10 so that the total tax paid was £500. In this case, the UK would have provided relief of £250 while Australia would have provided relief of £10. The UK would have collected tax of £250 while, after allowing the rebate, Australia would have collected £260 less £10 = £250.

2.26 Several Dominions decided not to participate in the scheme, and Dominions in Federal Systems (such as Australia and Canada) that provided reciprocal relief at one but not both levels of government were regarded as non-participating. Where a Dominion was not participating, in some circumstances, less UK tax was in fact assessed, but the process for calculating the relevant relief resulted in administrative complexities and depended on extra statutory concessions.35

**The United Kingdom’s And Australia’s Dissatisfaction With The System Of Dominion Income Tax Relief**

2.27 By the 1930s, the UK was dissatisfied with the system of Dominion Income Tax Relief as it meant that Dominions could increase their rates to equal one half of the UK rate without being required to provide reciprocal relief. The result was that the total burden of relief was provided by the United Kingdom. Neville Chamberlain, as Chancellor of the Exchequer, made desultory efforts to negotiate amendments to the system with the Dominions in the 1930s, but these were met with stonewalling and came to nothing.36

2.28 It seems likely that initially Australia was not entirely satisfied with Dominion Income Tax Relief.37 Nonetheless, Australia by the 1930s regarded the system as working

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35 For discussions of the operation of Dominion Income Tax Relief where a Dominion was not participating see R Staples, *Dominion Income Tax Relief and Practice* (GEE & Co., 1925) 37–9 and 65–72; W E Snelling, *Dictionary of Income Tax and Sur-Tax Practice* (Sir Isaac Pitman & Sons, 8th ed, 1931) 79 and R L Renfrew, *The Practice of Dominion Income Tax Relief* (The Solicitors’ Law Stationary Society, 1934) 14–23. The position was complicated by the interdependence of the rate of relief and the amount of the gross up for Dominion tax paid and by the source by source (country by country) approach to providing relief.

36 Chamberlain’s attempts to amend the system of Dominion Income Tax Relief in the 1930s are discussed in more detail in Taylor, above n 33, 69–70.

37 At the 1920 conference with the Sub-committee of the Royal Commission on the Income Tax, Australia had argued for the primacy of source basis taxation, had sought an unlimited foreign tax credit if mutual exemption was not possible, and had initially resisted providing additional
well. Australia’s dissatisfaction with the operation of the system corresponded with the conversion, discussed at 2.8, of Australia’s shareholder relief system to a classical system. Following these developments, as is illustrated in paragraph 2.29, the UK for purposes of calculating Dominion Income Tax Relief grossed up the Australian dividend for the shareholder tax but not, it appears, for the Australian corporate tax. Australia, in providing reciprocal relief, only took into account the Australian shareholder tax.

2.29 The effects of the procedures outlined at 2.28 can be seen once actual tax rates are taken into account, as is shown in the following table. The Australian corporate rate, including super tax, by 1945 was 35% and the shareholder tax payable on distribution to a foreign parent was 30%. The UK standard rate of tax was 50%.

<table>
<thead>
<tr>
<th>Pre Tax Income</th>
<th>Australian Corporate Tax</th>
<th>Australian Shareholder Tax</th>
<th>United Kingdom Corporate Tax</th>
<th>Relief by UK at ½ UK rate</th>
<th>Relief by Australia (excess of combined rate over standard UK rate)</th>
<th>Total Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>£1</td>
<td>7/-</td>
<td>3/-10d</td>
<td>6/-6d</td>
<td>3/-3d</td>
<td>7d</td>
<td>13/-6d</td>
</tr>
</tbody>
</table>

rebates of tax to ensure that the total tax did not exceed the higher of the two countries’ rates. See the discussion in Taylor, above n 33.

Numerous Australian government internal documents and correspondence in this period reflect this view. See for example: Earle Page (Australian Treasurer) to S M Bruce (Australian Prime Minister) 25th August 1928; S M Bruce (Australian Prime Minister) to Secretary of State for Dominion Affairs 30th August 1928; L S Jackson (Acting Australian Commissioner of Taxation) to Secretary Prime Minister’s Department, Canberra, 5th September 1934; Cable, Bruce (Australian High Commissioner, London) to Australian Treasurer and Treasury 30th April 1936. Cable, Bruce (Australian High Commissioner, London) to Australian Treasurer and Treasury 30th April 1936. NAA, PM file.

An example of the interaction of the systems is contained in L S Jackson, Income Tax and Estate Duty, Double Taxation Between Australia and the United Kingdom. Report of Mission to London. 7th January 1946, 7–8, para 20. NAA, PM file. In Jackson’s example, the UK does not appear to gross up the dividend for underlying Australian corporate tax.

In calculating UK corporate tax and relief under Dominion Income Tax Relief, the UK grossed up the dividend for the Australian shareholder tax but not for Australian corporate tax.

In calculating relief, Australia regarded the total tax as the Australian shareholder tax of 30% and 25%, being one half the UK standard rate. Hence Australia regarded the total tax as being 55% and reduced its shareholder tax by 5% to 25%.
The end effect was that UK companies deriving dividends from 100% subsidiaries in Australia were subject to an effective rate of tax approaching 66.25%.\(^{42}\)

\textbf{2.30} By the mid 1940s, the perception of both UK business\(^{43}\) and the UK and Australian governments was that the economic double taxation being produced under the Dominion Income Tax Relief system would inhibit direct UK investment in Australia after World War II. Hence consideration had been given, both in the UK and in Australia, to reform of the system.

\textit{The Consequences Of The UK – US Double Taxation Treaty Of 1945}

\textbf{2.31} The key development that led to the 1946 UK Treaty was the United Kingdom’s Double Taxation Treaty with the US, negotiated in 1944–1945. As part of that treaty, the UK agreed to introduce a foreign tax credit into its domestic law. In one respect, credit would be more generous than the credit provided under the Dominion Income Tax Relief system as it would be up to the full amount of UK tax paid on the relevant income. On the other hand the credit would be less generous as it would only be available to UK residents. As the credit would not involve any additional credit being given by the treaty partner in relation to income of UK residents sourced in the treaty partner country, it was expected to be simpler in its operation than the Dominion Income Tax Relief system had proved to be.

\textbf{2.32} Previously, the UK Internal Revenue had considered that at least some modification of the Dominion Income Tax Relief system would be both desirable and necessary if and when the UK actually concluded a comprehensive Double Tax Treaty with the US.\(^{44}\) By January 1945, Inland Revenue officers stated that the credit provisions in the still proposed US treaty would eventually be extended to the world on a unilateral basis without a reciprocity condition. Relief provided under Dominion Income Tax Relief would be withdrawn, with credits thereafter only being available to UK residents. It was proposed to implement the US treaty in the Finance Bill and in the

\footnotesize{\textsuperscript{42} Based on the example in Jackson, above n 39, 7–8, para 20.\textsuperscript{43} The Australian Secondary Industry Commissioner, following representations by UK industrialists, raised the issue with the Australian Treasurer in April 1945, urging that the Dominion Income Tax Relief provisions should be modified. An account of these discussions and submissions is contained in L S Jackson, above n 39, 1, para 2.\textsuperscript{44} John F Avery Jones, above n 29, 237 points out that the Inland Revenue had recognised as early as April 1944 that it would be necessary to offer a similarly favourable credit to the Dominions. The Chancellor of the Exchequer (Sir John Anderson), in a letter to Andrew Duncan (Minister of Supply) dated 15\textsuperscript{th} June 1944, had previously indicated that it was intended to review the system of Dominion Income Tax Relief in conjunction with the negotiation of a double tax treaty with the US. The Chancellor indicated that it was likely that the arrangements with the US would take a simpler form and be more beneficial than the existing system of Dominion Income Tax Relief.}
same Bill grant power to extend the credit provisions to the Dominions and Colonies.\textsuperscript{45}

\textbf{The Negotiation And Drafting Of The 1946 UK Treaty}

\textit{The Initial UK Proposals}

2.33 Following preliminary correspondence and meetings, Sir Cornelius Gregg (Chairman of the UK Board of Inland Revenue) met formally with S G McFarlane (Secretary of the Australian Treasury, who was in London) on 29\textsuperscript{th} May 1945 and outlined the UK proposals for a taxation treaty with Australia.\textsuperscript{46} These proposals were subsequently confirmed in writing on 1\textsuperscript{st} June 1945.\textsuperscript{47}

2.34 Gregg’s covering letter stressed the importance of the treatment proposed for taxation of direct cross border investment. The UK proposed that the source country tax trading profits of investors of the other country at the same rate it applied to its own traders, that no further tax be levied by the source country on interest or dividends paid out of such profits; but that, the residence country would give credit for source country tax on the profits. Part of the logic in the United Kingdom’s position was that the UK did not allow a deduction for interest payments, but the payer deducted tax from the payment.\textsuperscript{48} Significantly, Gregg’s letter contains the following comment on these proposals:

> 'In the field of trade the consideration of taxing all businesses whether home or foreign at the same rate lends great weight to the “origin” theory and I imagine that our proposal will accord with Australian policy. It is the further taxation of the dividend and interest or other distribution of the profit that goes to the investing country which acts as a deterrent on investment and we pressed the US to accept the general proposal that we make to you to abandon any such taxation. They accepted it for interest and royalties but for political reasons could not go the whole way on dividends and only met us to the point of limiting their charge to a withholding rate of 15 per cent on

\textsuperscript{45} Minutes of the meeting of officers of Inland Revenue, Treasury, Dominions Office and Colonial Office, 15\textsuperscript{th} January 1945. HM Treasury file 1403.


\textsuperscript{47} Inland Revenue file, p54, Gregg to McFarlane.

\textsuperscript{48} See the discussion of the UK’s treatment of interest payments at the time at 2.19.
dividends. We did not accept this at Washington but our Government decided to accept it on our return in view of the political considerations involved. I do hope that Australia and the other Dominions will find themselves able to go the whole way, for any system of taxation which seeks to obtain in addition to the ordinary tax on profits something additional by way of a personal tax from an outside investor is not calculated to promote the flow of investment from one country to the other which is for the good of both countries.  

2.35 McFarlane had previously pointed out to Gregg that under the Australian classical system of corporate-shareholder taxation, dividends paid to residents were treated as if they had borne no previous tax. The question of the appropriate treatment of dividends paid to non-residents was to prove to be possibly the major issue in the treaty negotiations.

2.36 The UK position was surely weakened by its previous treaty with the US, which merely limited US withholding tax to 15% on portfolio dividends and 5% on non-portfolio dividends, and by the fact that it had not been able to get the US to agree to the position on dividends that it was now putting to the Dominions.

2.37 The full set of proposals put by Gregg to McFarlane at the meeting on 29th May was as follows:

- Each country to have the right to tax income from trading profits sourced within its borders of residents of the other country. The residence country to retain the right to tax and would give full credit for source country tax.

- Trading profits of residents of the other country not made through a permanent establishment to be exempt from tax in the source country. Both branch profits and parent and subsidiary profits to be computed on an arm’s length basis.

- Shipping and Air Transport profits to be taxed only on a residence basis but, if Australia would not agree to this, then Australia should at least end its arbitrary method for calculating Australian profits.

- That Australian tax on dividends paid to UK residents be abandoned with the UK foregoing the surtax on dividends from the UK to Australia. This would mean that Australia would also abandon attempts to tax dividends paid by British

49 Inland Revenue file, p54, Gregg to McFarlane.

50 Inland Revenue file, p39, notes by Willis, above n 46. The differing treatments in the two systems of dividends paid by resident companies to residents may have led them to different conclusions as to the appropriate treatment of dividends paid to non-resident shareholders. Under modern terminology, each was applying a policy of non-discrimination but with opposite results.

51 See the discussion in Avery Jones, above n 29, 226–9.
companies to British residents on the basis that the dividend was partly derived from Australian sources. The UK would give a full credit for underlying Australian corporate tax and that Australia, when taxing British dividends, would recognise for credit purposes the British tax deducted by the British paying company.

- Interest to be taxed only in the country of residence\(^{52}\) except in the case of interest between a parent and subsidiary company. The exemption from tax would probably not apply to any non-resident trading in the source country.
- Royalties to be taxed on the same basis as interest.
- That an exchange of information provision, similar to that agreed to in the UK – US Double Taxation Treaty, would be included.\(^{53}\)

2.38 A memorandum on 1\(^{st}\) June 1945 set out the UK proposals in more detail and included other proposals in relation to dual residence, corporate residence, the profits of inter-connected companies, film income, other types of income dealt with in the 1945 UK – US Treaty, and giving credit for source country tax on income.\(^{54}\) The formal proposals contained several references to the terms of the recently concluded UK – US Double Taxation Treaty as examples of the type of article proposed.\(^{55}\)

2.39 The UK proposal in relation to dual residence was that provisions that gave exclusive right to tax certain types of income to one of the countries would not apply to dual residents.\(^{56}\) For corporate residence, the UK proposed a management and control test.\(^{57}\) Profits of ‘inter-connected’ companies were proposed to be determined on an arm’s length basis.\(^{58}\) The proposal in relation to film income was that Australia would not tax UK film producers who did not have a permanent establishment in Australia, and that where a permanent establishment existed its profit would be determined on an arm’s length basis and not on the arbitrary basis then adopted by Australia. A UK producer distributing through an Australian subsidiary would not be taxed, but the profits of the Australian subsidiary would be determined on an arm’s length basis.\(^{59}\)

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\(^{52}\) Both the UK and Australia at the time exempted interest on government securities paid to non-residents.

\(^{53}\) Notes by Willis of meeting, above n 46.

\(^{54}\) Inland Revenue file, pp50–3. Outline of UK proposals for a double taxation agreement with Australia (hereafter ‘Outline of UK proposals’).

\(^{55}\) Outline of UK proposals. Reference to specific articles in the UK – US Double Taxation Treaty is made in paragraph 5 to Article 1(b), in paragraph 7 to Article III(3), paragraph 8 to Article IV, paragraph 10 to Article XV, paragraph 11 to Article XIII, and paragraph 15 referring to the treatment of other income generally in the US – UK Double Taxation Treaty.

\(^{56}\) Outline of UK proposals, para 2.

\(^{57}\) Outline of UK proposals, para 3.

\(^{58}\) Outline of UK proposals, para 8.

\(^{59}\) Outline of UK proposals, para 9.
The Initial Australian Response

2.40 J B (Ben) Chifley, the Australian Prime Minister and Treasurer, replied to Gregg’s proposals by telegram on 23rd July 1945. The reply stressed that, since 1915, Australia had relieved international double taxation by not taxing foreign source income that had been taxed at source. The policy had been varied during World War II by taxing Australian shareholders on dividends from UK companies. As part of a general double taxation agreement, Australia was prepared to review the taxation of dividends derived by Australian residents from UK sources and to bear the whole burden of relieving Australian residents from double taxation of income derived from UK sources. It was, Chifley commented, open to the UK to adopt the same method of relief.

2.41 Chifley stated that Australia was reluctant to consider any proposal which departed from the principle that the source country had first claim to tax and that the residence country should only tax if the source country did not. Australia would agree to taxation by the residence country provided it gave full credit for tax paid by its residents in the source country. Recognising that investment of UK capital in Australia would provide advantages to the UK and would promote the economic development of Australia, Chifley noted that an arrangement for avoiding double taxation particularly between UK parent companies and Australian incorporated subsidiaries might assist trade, commerce and the flow of capital.

2.42 The telegram pointed out that, as Australia was a debtor nation relative to the United Kingdom, the proposed reduction in source country taxing rights would mean a loss of revenue to Australia. Because of the existing reciprocal relief provisions and ties between the two countries, Australia was prepared to consider proposals which would involve a smaller portion of net revenue loss for it. It was noted that the UK proposals were based on those agreed in the UK – US Treaty and that, while that treaty achieved a fair and reasonable result as between those two countries, they

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61 Chifley had been Australian Treasurer since the swearing in of the first Curtin government on 7th October 1940. See David Day, John Curtin: A Life, above n 4, 460–2; David Day, Chifley, above n 60, 369–70; and Ross McMullan, ‘Joseph Benedict Chifley’, above n 60, 253.

would, as between Australia and the United Kingdom, be heavily loaded to the
detriment of the Australian revenue.

2.43 In relation to the specific proposals on income tax made by the UK, Chifley commented that:

- ‘Resident’ of either country should be defined suggesting, for example, that
domicile could be used in the case of individuals and place of incorporation in the
case of companies;

- UK shipping companies which entered into contracts through Australian agents
should be treated the same as other UK residents selling their goods in Australia
through permanent establishments. As their actual profits were difficult to
ascertain, Australia arbitrarily determined profit as 5% of freights and passenger
fares. Although Chifley considered this to be fair and to be a simple solution to a
difficult question, he indicated that Australia was prepared to discuss the
ascertaining of actual profit and adopting that as the basis in lieu of the present
arbitrary basis.

- The proposals in relation to other trading profits made through a permanent
establishment did not clash with principles maintained by Australia and in broad
outline appeared to be acceptable. The proposals relating to dividends, however,
appeared to be inconsistent with those relating to trading profits. Any equitable
arrangement had to have regard to the admitted basic principles of source
taxation.

- Film producers who leased their films for distribution in another country were in
partnership with the local distributor and hence their profits arose through a
permanent establishment in the other country and should be taxed on the same
basis as other trading profits. However, as the profit could not be ascertained on
an arm’s length basis, Australia would not agree to change from assessing non-
resident film producers on an arbitrary percentage of rentals for films distributed
in Australia.

- Australia would not agree to the proposals for the source country to exempt cross
border interest and royalties, because the source country should have first claim
to tax this income, and would request that the residence country should provide a
credit for the source country tax when imposing a residence country tax.

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63 The UK had also made proposals for an Estate Duty Treaty. Chifley’s reply also commented favourably on proposals relating to salaries, pensions and annuities and taxation of government employees. Discussion of the Estate Duty Treaty and these provisions is outside the scope of this thesis.
In view of the above, no specific comment was thought to be necessary in relation to tax credits.

The UK proposals on exchange of information were generally acceptable to Australia.

2.44 The consistency of the attitudes in Chifley’s telegram with those of the Australian government at the 1920 conference (as discussed in note 37) with the Subcommittee of the Royal Commission on the Income Tax is notable. The first preference was still for mutual exemption of foreign source income followed by a second preference for an unlimited foreign tax credit. Source country taxing rights continued to be seen as primary.

The Negotiations With The First Australian Delegation

2.45 An Australian delegation, comprising the then Commissioner of Taxation, L S Jackson, and three of his staff, was sent to London and met with UK Inland Revenue officers and a representative from the Dominions Office in August 1945. At that meeting both sides generally adhered to positions that they had previously put, with Australia adhering to its emphasis on source basis taxation while the UK emphasised taxation on a residence basis.

2.46 Robert Willis, Secretary of the UK Board of Inland Revenue, reported that ‘they won’t budge an inch on the main question of taxation of dividends paid by Australian companies to UK residents’, noting also that the States would never agree to concessions on dividends which would create obstacles for a uniform system if the States were to resume taxation after World War II. Willis’ statement is not entirely accurate as Australia did offer to reduce its taxation of dividends paid to UK residents by one half and regarded this reduction as being equivalent to the reductions in US withholding tax in the 1945 UK – US Double Taxation Treaty, having regard to relevant tax rates in the respective countries. Willis reported that Australia was

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64 Willis to Sir Charles Dixon (Dominations Office) 26th July 1945. UK National Archives, Inland Revenue file. Gregg had suggested that Australia send a delegation to London as he had not regarded Chifley’s reply as very accommodating.

65 Inland Revenue file, p59. Official Secretary, Australian High Commission, London to Chairman Board of Inland Revenue 23rd July 1945 indicates that the delegation left Sydney on 28th July 1945, but the actual date of arrival in London is not disclosed in archival material that the author has examined. Jackson was appointed Australian Commissioner of Taxation in May 1939 and continued in that role until May 1946. Leigh Edmonds, Working for All Australians: A Brief History of the Australian Taxation Office (Australian Taxation Office, Canberra, 2010) 57 and 76.


67 Jackson, above n 39, 6, paras 16 and 17.
tentatively prepared to overrule its *Biddle* case and to give credit to its residents for tax deducted from UK dividends.\(^{68}\)

2.47 Willis noted that Australia recognised that its taxation of dividends, funded from Australian source profits, paid by a non-resident company to a non-resident shareholder was largely unenforceable. However, Australia refused to drop it, because to do so would have been inconsistent with the principle of priority of source basis taxation,\(^{69}\) and merely undertook to convey the UK view to the Australian government. Australia also purported to apply its undistributed profits tax to non-resident companies with Australian branches to the extent that the profits were Australian sourced.\(^{70}\) Australia considered that the tax should apply because the profits had an Australian source and exempting them would produce an anomaly with the treatment of Australian companies subject to the tax.\(^{71}\)

2.48 Willis viewed the Australians’ reiteration of the views in Chifley’s telegram at 2.43 on shipping and films as highly political. As Australia had virtually no international shipping industry, obtaining some tax from the shipowner meant that Australia ‘didn’t feel so bad’.\(^{72}\) Willis considered that the Australian use of an arbitrary basis for taxing film profits was also political, noting that ‘Americans getting big money out of Australia’.\(^{73}\)

2.49 The Australians had also indicated that Australia would not exempt interest and royalties flowing to a UK resident.\(^{74}\) Australia considered that Dominion Income Tax Relief had generally produced appropriate results in these cases and that the principal need was simplification of the procedures and the elimination of a few anomalies.\(^{75}\)

2.50 Consensus was reached on exchange of information where Willis described the Australian attitude as being ‘They seem keen on it; they have great powers of

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\(^{68}\) Willis, above n 66, 74. In *Biddle v Commissioner* 302 US 573, a US resident individual was denied a foreign tax credit for tax deducted by the payer because the recipient had not paid the tax. Australia’s *Biddle* case was *Jolly v FCT* (1934) 50 CLR 131, where Dixon J held that only the net amount of a dividend received by an Australian shareholder from a UK company, which had deducted tax it had paid on the source of the dividend, was included in the assessable income of the shareholder.

\(^{69}\) Willis, above n 66, Jackson above n 39, 7, para 18.

\(^{70}\) Willis, above n 66.

\(^{71}\) Jackson, above n 39, 7, para 19.

\(^{72}\) Willis, above n 66, 73–4 and see Jackson, above n 39, 8–9, para 22.

\(^{73}\) Willis, above n 66, 74 and Jackson, above n 39, 9–10, paras 25–8.

\(^{74}\) Willis, above n 66.

\(^{75}\) Jackson, above n 39, 11, para 33.
inquisition and, one gathered, would be glad to have all sorts of information from us." 76

**The Modified UK Proposals And The Breakdown Of Negotiations**

2.51 Considering that the meeting in August 1945 had not resolved anything, Gregg sent modified proposals to Jackson on 21st September 1945. 77 Gregg submitted that the difficulties in their discussions to date had sprung from a clash between Australia’s ‘origin’ theory of taxation and the United Kingdom’s ‘residence’ theory. Gregg argued that the original proposals were a compromise between the two theories as they conceded the origin basis for taxation of trading profits but retained the residence basis for dividends, interest and royalties. From discussions to date, a treaty was not likely on this basis as the proposal in relation to dividends, interest and royalties clashed with Australia’s emphasis on source basis taxation and would have an appreciable cost to the Australian exchequer. Gregg submitted that under the modified proposal there would be a slight gain to the Australian exchequer a greater loss to the UK exchequer and a gain accruing to the benefit of traders investing in Australia.

2.52 The modified proposal was that the Double Tax Treaty only operate in relation to trading profits and that the existing system of Dominion Income Tax Relief operate in relation to investment income (including dividends paid outside a parent–subsidiary relationship) and personal taxation. The UK continued to propose that shipping and air transport be taxed on a residence basis but that, in broad terms, all other trading profits be taxed on an origin basis with credit being given by the residence country for any origin tax paid. More specifically, the UK proposed that:

(a) UK companies trading though Australian branches would be subject to tax on their branch profits at the Australian corporate rate, with the UK giving credit for the Australian tax paid;

(b) An Australian subsidiary of a UK company would be taxed at the Australian corporate rate, but Australia would not tax dividends paid by the subsidiary to the UK parent and the UK would give the parent company credit for any underlying Australian tax;

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76 Willis, above n 66, 73.
77 Gregg to Jackson, 21st September 1945, Inland Revenue file, pp101–04. The content of Gregg’s letter is discussed in paragraphs 2.51 to 2.55.
(c) Australia would not tax a UK company on dividends that it paid out of Australian source profits and would not charge undistributed profits tax on the Australian source profits of a UK company;

(d) The profits of shipping and air transport ‘concerns’ of one country would be exempt from tax in the other country.

There would also be a general provision that trading profits of a non-resident would only be taxable in the source country where they arose through a permanent establishment in that country.

2.53 In Gregg’s view, the current Australian system discriminated against UK investment through the use of a subsidiary (evidently because of the taxation of dividends paid to parent companies) rather than a branch. Australian legislation that purported to tax dividends paid by UK companies that were sourced in Australian profits was unenforceable and was unjustifiable in principle as being extra-territorial taxation. If Australia wanted to encourage British, rather than foreign, subsidiaries to be established in Australia then, as the UK would give credit for Australian underlying tax, it was not too much to expect Australia to contribute by exempting the dividends themselves.

2.54 Gregg noted that the proposal on shipping and air transport was in conflict with Australia’s source principles, but the UK regarded it as a matter of first importance and pressed it strongly. Residence basis taxation had been regarded as appropriate in agreements that the UK already had with the principal foreign countries and with Eire and Canada and by the League of Nations Fiscal Committee owing to difficulties associated with attributing this type of income to particular sources.

2.55 In relation to other income (principally interest, dividends and royalties), Gregg proposed that the existing Dominion Income Tax Relief provisions continue, but he indicated that, if Australia wished, the UK was prepared to make special provision for salaries and pensions.

2.56 Gregg had previously given a draft of his letter of 21st September 1945 to Jackson. After seeking instructions from Chifley, Jackson had advised Gregg informally of the Australian government’s response,78 which he subsequently formally confirmed by letter to Gregg on 25th September 1945.79

78 Gregg to Dixon (Dominions Office) 21st September 1945, Inland Revenue file, p106.
79 Jackson to Gregg, 25th September 1945, Inland Revenue file, pp107–09. The content of Jackson’s letter is discussed at 2.59 to 2.65.
2.57 In brief, Chifley had advised that Australia would not accept the proposals. Australia would not entertain any departure from the source principle, would not agree to taxing shipping profits on a residence basis, and continued to claim the right to tax subsidiary companies on dividends paid to UK parents. Chifley advised that, in the event of Gregg not accepting the Australian proposals, Jackson was to report to H V Evatt (the Australian Minister for External Affairs and Attorney-General who was then Acting Australian Minister in London), who was to raise the matter with the Chancellor of the Exchequer (Hugh Dalton).

2.58 Gregg advised Jackson that he could not agree to the Australian proposals and that the matter would have to be taken up at the ministerial level. Gregg suggested to Jackson that it would be unlikely that ministerial level discussions would lead to settlement as the Chancellor of the Exchequer could not give one Dominion what he denied to another.

2.59 Jackson’s 25th September letter to Gregg reiterated the Australian view that the responsibility for removing international double taxation rested entirely on the United Kingdom. The Australian view was that the source country had the primary right to tax income over the country of residence, a claim which, Jackson noted, was admitted by the US by allowing a unilateral credit for foreign tax paid.

2.60 Jackson disputed the claim that Australia would suffer no financial loss under the amended proposals, because the claim: (a) assumed that the existing Dominion Income Tax Relief arrangements were fair even though they required Australia to provide relief in respect of Australian source income; and (b) ignored the loss of revenue to Australia from foregoing the right to tax shipping and air transport. The original proposals had contemplated the total abrogation of the existing Dominion Income Tax Relief proposals, and Australia considered it desirable that the original proposals in this regard be consummated.

2.61 On the key question of Australia foregoing its tax on dividends paid by Australian subsidiaries to UK parents, Jackson commented that the UK request was not

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82 Gregg to Dixon, above n 78.
regarded as feasible because of the Australian incidence of tax upon company profits and dividends. In Jackson’s words, while the UK put the whole weight of its tax incidence on the company’s profits (apart from surtax on dividends), Australia put its incidence partly on the profits and partly on the dividends. If dividends paid to UK parent companies were exempted, then Australian tax on corporate profits would have to be increased and Australia would face claims from other countries and Australian shareholders for a similar exemption. Jackson noted that the US did not agree to exempting dividends but had agreed to reduce the rate of tax on dividends flowing to the UK. Australia had made a similar offer which would, in Jackson’s view, leave the burden of Australian tax on company profits and dividends comparable with that charged in the US.\footnote{Jackson’s report to the Australian government on the negotiations contains an explanation of the reasoning behind this assertion. Jackson above n 39, 6, para 17.}

2.62 The proposal that Australia not tax Australian source dividends paid by UK companies to UK residents was rejected as it ignored the priority of Australia to tax such dividends. Jackson admitted, however, that Australia could not enforce such taxation where the UK resident had no other Australian income.

2.63 Nor could Australia agree to the proposal to exempt UK companies from Australian undistributed profits tax on their Australian source income as this would create an anomalous discrimination compared with the treatment of Australian companies and would deprive Australia of a portion of its tax on profits derived in Australia.

2.64 Jackson indicated that political considerations and the principle of origin made it impossible for Australia to agree to taxation of shipping profits on a state of registration basis, alluding to the strong feeling of resentment by Australian exporters over exploitation of Australian freights by foreign shipping companies. Jackson indicated that no Australian government could hope to carry any exemption for any section of the shipping industry through Parliament.

2.65 Jackson considered that Australia’s differential treatment of branches and subsidiaries of foreign direct investors was a product of the absence of international provisions to enforce another country’s tax laws. The fact that Australia could not, in certain circumstances, enforce the full effect of its taxation laws was no justification for departing from the principle of source basis taxation. To do so would undermine the foundations of its taxation structure. Taxing dividends paid by UK companies out of Australian profits was not admitted to be extra-territorial taxation; rather, it was regarded as a proper imposition of tax on Australian source income. Here Jackson
appears to have conflated Gregg’s comparison of the Australian treatment of branches and subsidiaries with his criticism of Australia’s taxation of non-residents on dividends paid by non-resident companies funded from Australian source profits. The latter was unenforceable in practice, but Gregg’s criticism of the treatment of subsidiaries was more directed at the enforceable tax on non-resident shareholders on dividends paid by non-resident companies funded from Australian source profits.

**Evatt Meets With Dalton**

2.66 Prior to Evatt meeting with Dalton, he received a letter from Jackson.\(^{84}\) Stressing that the key item to be settled first was the treatment of dividends paid by an Australian subsidiary company to a UK parent company, Jackson pointed out that under Dominion Income Tax Relief the combined Australian and UK tax in this situation exceeded the UK standard rate of 50%.\(^{85}\) It was this aspect that ‘the commercial world’ and the Australian Secondary Industries Commission wanted corrected. It would be best to abrogate the whole present arrangement and to give Australia, as the country of origin, the prior right to collect taxes. If the UK wanted to tax on the basis of residence, then it should allow a foreign tax credit for the whole of the Australian tax.

2.67 Jackson noted that the UK had been unable to persuade the US to agree to exempt dividends paid by a wholly owned subsidiary from source taxation and that the Board of Inland Revenue had been overruled by the then Chancellor of the Exchequer (Sir John Anderson). Australia had offered to reduce its tax on dividends by 50% which, when the Australian corporate tax rate (35% including super tax) was taken into account, gave a mean somewhere between the 15% and 5% rates in the 1945 UK – US Tax Treaty. Jackson noted that Gregg had refused to accept this offer. In Jackson’s view, the established precedent in the UK – US Treaty made Gregg’s position on this issue untenable.

2.68 Jackson commented that the UK – US Treaty could not be adopted in toto in the UK – Australia context. He pointed out that both the UK and the US taxed on both a residence and source basis whereas Australia largely taxed only on a source basis, and that the reciprocal flow of income that existed between the UK and the US did not exist as between the UK and Australia. Even if a reciprocal flow of income did

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\(^{84}\) Jackson to Evatt, 26\(^{th}\) September 1945, Inland Revenue file, pp111 and 112. The content of Jackson’s letter is discussed in paragraphs 2.66 to 2.69.

\(^{85}\) See the table at 2.29 and accompanying footnotes.
exist, Australia would, generally, not be imposing tax on UK source income and hence any question of Australia allowing a tax rebate would not arise.

2.69 On the proposal that ‘personal items’ (portfolio dividends, interest, royalties, rents, salaries, pensions and annuities) continue to be covered under the Dominion Income Tax Relief system, Jackson admitted that it was the Australian revenue not the taxpayer that suffered under the present arrangements. In Jackson’s view, it was best to concentrate on trading profits and settle that item first rather than break down the whole negotiations.

2.70 Correspondence followed between Gregg and B F Trend (the Private Secretary to the Chancellor of the Exchequer) in which Gregg enclosed a memorandum outlining what he saw as the key points of difference between the UK and Australia.\(^{86}\) Gregg emphasised three issues: (a) the taxation of dividends paid by an Australian subsidiary to a UK parent; (b) Australia’s levying of undistributed profits tax on the Australian profits of UK companies with Australian branches; and (c) shipping and air transport profits.

2.71 Dalton met with Evatt and Jackson (but not with Gregg) somewhere between the 12\(^{th}\) and 16\(^{th}\) of October.\(^{87}\) Apparently, at that meeting Evatt handed Dalton the letter of 26\(^{th}\) September 1945 that Jackson had written to Evatt\(^{88}\) together with a short and blunt memorandum.\(^{89}\) The interesting feature of the memorandum is that, for the first time in Australian communications in the negotiations, it opens with a positive statement about what Australia requires from a treaty rather than with defensive statements about what Australia will not agree to.

2.72 The memorandum, which began with the heading ‘What Australia Asks For’, requested that the UK grant a full rebate of tax on income of Australian origin applying not only to taxes on company profits but on dividends paid out of those profits. After noting that the US conceded this principle (of granting a full credit for foreign tax) in its tax laws, the memorandum pointed out that Australia was the only

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\(^{86}\) Gregg to Trend, 12\(^{th}\) October 1945, Inland Revenue file, p125 and ‘Double Taxation And Australia: Brief Summary’, Inland Revenue file, pp123 and 124.

\(^{87}\) These conclusions can be drawn from Gregg to Trend, 16\(^{th}\) October 1945, Inland Revenue file, p131.

\(^{88}\) The original letter is in the UK National Archives. Jackson to Evatt, above n 83.

\(^{89}\) ‘What Australia Asks For’, Inland Revenue file, pp126 and 127. The content of Evatt’s memorandum is discussed in paragraphs 2.72 to 2.76.
Dominion that shared relief from double tax on income of domestic origin. Dalton marked this comment with red ink in the margin of the memorandum.

2.73 The request for a full rebate, at least on business profits, was uncontroversial. A full rebate on business profits had been offered in the amended UK proposals, and a full rebate on all Australian tax paid had been part of the original UK proposals. This request, however, did accurately state what the real gain to Australia would be under a taxation treaty with the United Kingdom. It would mean that Australia would no longer have to contribute directly to relief from international double taxation of Australian source income by providing rebates to UK residents. Rather, the UK foreign tax credit would mean that the total tax paid would not exceed the greater of the combined Australian corporate and dividend tax and the UK tax on the dividend without Australia contributing to the overall relief other than through reductions in source taxation of some categories of income.

2.74 Under the heading ‘Australia’s Minimum Position’, the memorandum noted the amended proposal that personal taxes continue to be dealt with under the Dominion Income Tax Relief provisions and commented that ‘Australia regards this as objectionable, but if we are forced, we will have to accept it.’ That Australia was prepared to accept the continuance of the Dominion Income Tax Relief system in relation to personal taxes, notwithstanding that it would rebate some tax on Australian source income, clearly indicates that Australia’s main concern was with providing more complete relief from the double taxation of business profits, corporate income and dividends.

2.75 The memorandum stated that Australia would not forgo its tax on dividends paid by an Australian subsidiary to a UK parent but would reduce its tax on dividends by 50%, pointing to the United Kingdom’s agreement to a reduction rather than an exemption in the 1945 UK – US Tax Treaty. Dalton’s handwritten notes on the memorandum suggest that he thought that a two-thirds reduction would be more appropriate given that the US had reduced its dividend withholding tax in the subsidiary–parent situation from 30% to 5%.

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90 While technically correct, this was somewhat misleading as India and the Colonies (as distinct from Dominions) all provided reciprocal relief. Australia only provided reciprocal relief at the Commonwealth level, none of the States ever having agreed to provide reciprocal relief. None of the Australian States were levying an income tax in 1945 following the introduction of the Commonwealth Uniform Tax Scheme in 1942.

91 The ink appears to be the same as is used in other handwritten comments on the memorandum. The handwriting appears to be the same as subsequent handwritten notes in the file where, from the context, it is clear that the writer is Dalton.
In response to the request that Australia exempt overseas shipping profits, the memorandum bluntly stated, ‘this Australia refuses to do’. Similarly, the memorandum indicated that Australia refused to adhere to Gregg’s request to forgo its tax on undistributed profits.

In a handwritten note on the memorandum, Dalton had written, ‘Try to settle this by Monday night.’ Evidently, Dalton told Evatt and Jackson that he would reach a decision on the matter by Monday. As it happened, no decision was forthcoming at this time. Jackson either surmised or was told that Dalton was concentrating on budgetary legislation and banking reform. Jackson and the rest of the Australian taxation delegation stayed in London for another fortnight and then returned to Australia.94

Correspondence between Dalton’s office and Gregg followed the meeting between Dalton and Evatt. Gregg reiterated points he had previously made in relation to dividends and the 1945 UK – US Double Taxation Treaty and about the prospects for negotiations with other Dominions.95

Dalton was clearly becoming annoyed at the whole process, and at Inland Revenue in particular, and wanted to take a more pragmatic approach. Dalton’s secretary, Trend, in a note to Dalton following the receipt of a lengthy draft letter for Dalton to send to Chifley, commented: ‘I doubt whether this is the sort of subject on which you will wish to write an ordinary letter, and I think it might be better for you to send a Memorandum, outlining the points at issue, with a short personal covering letter, asking Mr Chifley to come as far to meet you as you have come to meet him.’ Dalton wrote ‘Yes!’ in the margin in response to this suggestion. On the bottom of the file note Dalton wrote: ‘I suppose I must have more [indecipherable] discussion on this dreary subject. I think I.R. is being too stiff necked about the whole thing.’ Dalton went on to note that ‘we have left the Australian [tax official] hanging about in London for months’ and asked, ‘how much money is there in it anyway?’.

Trend received from Gregg a further draft note and memorandum for Chifley, which he forwarded to Dalton. He suggested to Dalton, ‘you will probably want to expand

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92 Dalton made handwritten notes on the memorandum outlining the formula by which Australia taxed shipping profits.
93 Gregg to Trend, above n 86, 131.
94 Jackson, above n 39, 3, para 9.
95 Gregg to Trend, 24th October 1945, Inland Revenue file, pp134–5.
96 ‘Chancellor of the Exchequer’, 2nd November 1945, signed ‘BT’. Handwriting in red is signed ‘HD’ and evidently is Dalton’s. Gregg to Trend, above n 82, 140. Inland Revenue file.
97 Gregg to Trend, 28th December 1945, Inland Revenue file, p148.
the draft letter yourself, as one Socialist minister writing to another’. Trend was frustrated at Dalton’s response, which was ‘settle something with some other Dominions first’. Nonetheless, it appears that Dalton’s decision at this point may have been critical in eventually producing an agreement with Australia because the treaties that the UK then agreed with Canada and South Africa involved compromises by both sides and set some precedents that appear to have been significant in resolving the deadlock in the United Kingdom’s negotiations with Australia.

The Politicians Reach A Compromise

2.81 At Australia’s initiative, Dalton then met with Jack Beasley (Australian Minister in London) on 18th April 1946, and then Dalton and Gregg met with Chifley (who arrived in London on 19th April 1946), Evatt, Beasley, H C Coombs (Director General of the Department of Post War Reconstruction) and R J Mair (Australian Second Commissioner of Taxation) on 3rd May 1946. Prior to the meeting on 3rd May 1946, Gregg had met with Coombs to discuss the issue.

2.82 Gregg’s brief to Dalton for the meeting with Beasley reiterated the points Gregg had made previously but added comments noting key points in the agreements that the UK had recently reached with South Africa and Canada. On air and shipping, Australia (contrary to international practice and the United Kingdom’s treaties with Canada, South Africa, Eire and the US) would not agree to exclusive taxation by the country of the shipowner. While there was agreement on the non-taxation at source of independent agents, Australia (uniquely in Gregg’s view) taxed independent insurance agents at source.

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98 ‘Chancellor of the Exchequer’ 1st January 1946, signed ‘BT’. Handwritten notes in red by Dalton are signed ‘HD 3/1’. Inland Revenue file, p155. See also the exasperated note from Trend to Gregg, 4th January 1946, Inland Revenue file, p154.

99 The date of Dalton’s meeting with Beasley is evident from Dalton’s letter to ‘My dear Jack’, 18th April 1946, Inland Revenue file, page number obscured. The meeting with Coombs is referred to in Board of Inland Revenue, ‘Chancellor of the Exchequer: Double Taxation – Australia’, 29th April 1946, signed ‘CG’. ‘Double Taxation – Summary of Points for Discussion’, Inland Revenue file, p167. The date and attendees at the meeting of 3rd May 1946 are set out in Board of Inland Revenue, ‘Double Taxation – Australia’, 7th May 1946, Inland Revenue file, p171. H C (Nuggett) Coombs had been an economist at the Commonwealth Bank of Australia, had joined the Australian Treasury in 1939 and had been appointed by Chifley as Director General of the Department of Post-war Reconstruction in 1943. Coombs’ career is discussed in Tim Rowse, Nuggett Coombs: A Reforming Life (Cambridge University Press, 2002).

100 Gregg to Trend, 16th April 1946, Inland Revenue file, p161 and Board of Inland Revenue, ‘Summary of differences with Australia’, 16th April 1946, signed ‘CG’. Inland Revenue file, pp159 and 160.
On dividends paid by subsidiaries to parent companies, the US had agreed to reduce source taxation to 5%, Canada and South Africa had agreed to an exemption and NZ did not tax dividends at all. Both the US and South Africa had agreed to not impose their undistributed profits tax on non-residents, and Canada did not tax undistributed profits. Australia, by contrast, had refused to budge on subsidiary–parent dividends and undistributed profits tax.

The position was different in the case of interest and royalties. There, although the US had agreed to exemption from tax at source, Canada had not and the UK was to give full credit for Canadian tax paid. The Dominion Income Tax Relief provisions were to continue to apply to interest and royalties under the treaty with South Africa. Gregg conceded that Australia would not follow the US precedent on interest and royalties and that the UK was prepared to concede Australia’s claim to tax these types of income.

In the case of film royalties, the US had agreed to exempt British film royalties but Canada had not, nor had South Africa. Gregg commented: ‘We shall certainly have to concede to Australia as good a treatment as we have conceded to Canada and South Africa.’

Gregg’s covering letter to Trend added that Australia wanted to “pick the eyes” out of the U.S. – U.K. agreement, to take what she likes and to leave out what she doesn’t like on the ground that the interflow of income between the U.K. and Australia is different from that between the U.S. and the U.K. and that Australia is not a big industrial country.’ If the treaty with the US was not seen as the standard that should apply between the mother country and a Dominion, it did not follow that the mother country should give more. This was especially so in relation to the core point of withholding tax on which the UK was unable to get the US to agree to its view.101

For his meeting with Beasley on 18th April 1946,102 Dalton forwarded a summary of the points on double taxation that were outstanding as between the UK and Australia.103 The UK was largely holding to the negotiating position set out in Gregg’s amended proposals of 21st September 1945. No modifications to that position had been made to reflect the agreements that had been reached with Canada and South Africa. However, the UK had returned to its original position, of requesting residence based taxation, in relation to interest and royalties and film royalties. Dalton indicated

101 Gregg to Trend, above n 100, 161.
that he looked forward to having discussions with Chifley very soon, stating, ‘I am sure we shall be able to settle [outstanding issues] without much difficulty.’

2.88 The United Kingdom’s assessment of the Australian negotiating position at this time was that Australia would probably: (a) continue to dispute the treatment of shipping and air transport; (b) agree on agency profits with exceptions for particular cases; (c) agree on exemption of subsidiary to parent dividends; (d) agree not to levy tax on dividends paid by U.K. companies out of Australian profits and not to impose undistributed profits tax on U.K. companies; (e) agree to exempt royalties but not interest; and (f) refuse to give way on film royalties.104

2.89 At his meeting with Coombs, referred to at 2.81, Gregg provided details of the United Kingdom’s recent treaties with Canada and South Africa. Gregg stressed that the points of greatest significance to the UK were: (a) the exemption of dividends paid by an Australian subsidiary to a UK parent, at least in the case of a wholly owned subsidiary; (b) the exemption of dividends and undistributed profits of UK companies; and (c) the exemption of shipping and air transport profits. Gregg noted that Coombs appreciated that the vital question was to relieve trade from double taxation. Gregg’s assessment was that the following solution might be able to be reached at Dalton’s proposed meeting with Chifley:

‘Australia to

Exempt shipping and air transport.

Exempt dividends paid by the wholly owned subsidiary.

Halve its rate on other dividends (as previously offered).

Exempt U.K. companies from tax on dividends and undistributed profits.

U.K. to

Concede Australia’s claim to tax interest and royalties.

Concede film royalties.

If necessary concede the point about insurance profits made through an Australian agent (they ought to be prepared to meet us on this, but it is not a point to make a stand on).

Give full credit for Australian tax in all remaining cases of double taxation of U.K. residents; “personal income” as well as trading income.’

The reference to conceding Australia’s claim to tax royalties is crossed out in a handwritten annotation to Gregg’s memorandum, and the word ‘No’ is written above ‘royalties’.105

2.90 The recent taxation treaties between the UK and Canada and South Africa made it more difficult for both Australia and the UK to hold to their previous negotiating positions. At the ministerial meeting between Dalton and Gregg (representing the United Kingdom) and Chifley, Evatt, Beasley, Coombs and Mair some further compromises were made. The agreement reached at that meeting was:

- Taxation of trading profits on a source basis with full credit being given by the residence country;
- Taxation of shipping and air transport profits on a residence basis;
- Independent agents to be exempt from source basis taxation but with Australia permitted to tax insurance agencies and certain pastoral agencies;
- Australia to retain its right to tax films, with credit being given by the United Kingdom;
- Australia to not tax dividends paid by a 100% subsidiary of a UK company holding all shares other than qualifying shares;
- UK companies trading in Australia to be exempt from Australian tax on dividends paid to Australian non-residents but to be subject to Australian undistributed profits tax.
- Australia to reduce its tax on other dividends paid by Australian companies to UK residents by one half;
- Literary and industrial royalties to be taxed on a residence basis;
- Australia to tax rents and mineral royalties, with the UK giving a full credit for the tax paid at source;
- Except in the case of government securities, interest to be taxed at full rates on a source basis, with the UK giving full credit [this was a concession made by the UK that was foreshadowed by Gregg in his meeting with Coombs];
- Taxation of pensions and purchased annuities on a residence basis.106

2.91 Both sides, in 1946, must have been satisfied with some aspects of the agreement reached at this meeting, although most of the concessions had been foreshadowed at the meeting between Gregg and Coombs. One additional concession, favouring Australia, was obtained at the meeting of ministers, namely: levying Australian undistributed profits tax on Australian source profits of UK companies. Australia retained source taxation of film and mineral royalties, in contrast to the treatment of these royalties foreshadowed at the meeting between Gregg and Coombs.

2.92 From an Australian perspective, most importantly, the system of Dominion Income Tax Relief was to be replaced by a foreign tax credit which extended to giving credit for underlying Australian corporate tax to all UK resident shareholders. Australia had successfully resisted the UK proposals to exempt dividend, interest and royalty payments entirely from tax at source. The omission of an interest article was an important difference from the 1945 UK – US Treaty. The effect was that full source country taxing rights were retained in relation to interest.

2.93 On the other hand, the compromise reached on dividends was arguably more favourable to the UK than the one achieved in the 1945 UK – US Treaty. In the 1946 UK Treaty the exemption from dividend taxation at source was confined to the 100% subsidiary situation, Australian tax on other dividends was halved and Australia retained the right to levy undistributed profits tax. By comparison, in the 1945 US – UK Treaty, US withholding tax on non-portfolio dividends paid to a company with a 95% or more voting interest was reduced to 5% and US withholding tax on all other dividends was reduced to 15%.

2.94 The UK had a victory over Australia on literary and industrial royalties. It seems clear from a comparison of the discussions between Gregg and Coombs on the one hand, with the agreement reached by the politicians at the meeting of 3rd May 1946, that this concession was made by Australia at the latter meeting, possibly in the context of Australia retaining source country taxing rights in respect of film and mineral royalties.

2.95 Australia conceded taxation on a residence basis in the politically sensitive area of shipping profits and in the nascent area of international air transport. Given the international practice that had developed in these areas, and given the terms of the

agreement that the UK had recently reached with Canada, an Australian concession on these areas was perhaps inevitable if Australia wanted to achieve significant objectives such as obtaining full foreign tax credits from the UK and preserving its source country taxing rights in other areas.

**Detailed Drafting Begins And Technical Issues Emerge**

2.96 Although the meeting of 3rd May 1946 had resolved most of the significant issues, some points were left for further negotiation as was the detail of the drafting. The UK Inland Revenue appears to have prepared a draft treaty dated 6th May 1946, which was progressively amended in consultation with Mair107 who had remained in London for the detailed drafting and was subsequently joined by the Australian Crown Solicitor H E F (Fred) Whitlam.108

2.97 Technical drafting continued until late August 1946, and in that period a total of five drafts (including the final version) were developed.109 Throughout the drafting process Mair sent regular, almost daily, cables to Patrick McGovern, the new Australian Commissioner of Taxation, who sent back less frequent replies with drafting suggestions. As the draft was progressively received in Australia, it was forwarded for comment to two ATO committees and to two Deputy Commissioners.110 The comments made on progressive stages of the draft were collated and were utilised by McGovern in making drafting suggestions to Mair and Whitlam.

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107 The draft dated 6th May 1946 is contained in NAA, ATO, Progressive draft of agreement. Mair’s initial cable of amendments to McGovern was dated 9th May 1946 and contains provisions which differ from the draft dated 6th May 1946. Mair describes the content of his cable as the ‘first instalment of the draft settled with inland revenue’, which appears to indicate that the UK produced the draft of 6th May 1946 and it was then progressively amended and settled in consultation with Mair. Mair’s initial cable is Mair to McGovern, 9th May 1946, NAA, ATO, Cables of draft agreement.

108 See Evatt to Holloway, 9th May 1946, NAA, ATO Cables of draft agreement, p20, and McGovern, 22nd May 1946, NAA, ATO Cables of draft agreement, p41.

109 The drafts are contained in NAA, ATO, Progressive draft of agreement. The first draft worked on in Australia was titled Draft II and was dated 22nd May 1946. This was followed by an untitled draft dated 19th July 1946. There were two versions of Draft III with one, apparently, being the London draft of 1st August 1946 and the other the Canberra draft of 8th August 1946. Differences between the London draft and the Canberra draft are noted in handwriting in the Canberra draft. The final version of the Treaty largely, but not entirely, followed the London version of Draft III.

110 See McGovern to Mair, 22nd May 1946, NAA, ATO, Cables of draft agreement, p41. McGovern was appointed as Australian Commissioner of Taxation in May 1946 and held that position until April 1961. Edmonds, above, note 65, 76 and 133.
2.98 The original UK offer of a double taxation treaty had made explicit reference to particular articles in the UK – US Taxation Treaty of 1945. The influence of the UK – US Treaty is apparent in this first draft prepared by the United Kingdom.

2.99 Of the 22 variations from the OECD Model in currently operative Australian tax treaties that can be traced to the 1946 UK Treaty, eleven were the result of the initial UK draft following the 1945 UK – US Tax Treaty, however, one of these was modified as a result of Australian negotiations in the drafting process. Some of these eleven variations can still be found in Australia’s most recent treaties. Two of the eleven can be found in the 2010 Turkey Treaty and in the 2013 Switzerland Treaty. A further one of these is found in the 2013 Switzerland Treaty and in the 2015 Germany Treaty. An additional three of these are found in the 2010 Turkey Treaty only.

2.100 One further variation from the OECD Model contained in the initial UK draft was modified at Australia’s request to align the final draft with the equivalent article in the 1945 UK – US Tax Treaty. As discussed in Chapter 5, the September 1966 UK draft reverted to similar language to that used in the 1946 UK draft, and this variation from the OECD Model can still be found in Australia’s most recent treaties.

2.101 The 10 remaining variations from the OECD Model were also variations from the 1945 UK – US Tax Treaty. Of these, four (which can still be found in at least one of Australia’s most recent treaties) were initiated by Australia. The remaining six

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AV1 (omission of OECD Art 2(1)); AV2 (omission of OECD Art 2(2)); AV4 (approach to defining resident of OECD Art 4(1)); AV21 (no equivalent to OECD Art 7(6)); AV29 (no equivalent to OECD Art 9(2)); AV31 (no equivalent to OECD Art 8(3)); AV41 (absence of definition of dividend); AV80 (no equivalent to OECD Art 17); AV82 (no equivalent to OECD Art 21); AV87 (no equivalent to OECD Art 22) and AV105 (no equivalent to OECD Art 25).

AV4 (approach to defining resident – basic approach in 1945 UK – US Treaty retained but details modified at Australia’s request).

AV20 (addition to OECD Article 7 allowing application of domestic law where information is inadequate to determine arm’s length – still in 2010 Turkey Treaty); AV22 (savings clause of...
variations (some of which can still be found in at least one of Australia’s most recent treaties) were initiated by the United Kingdom, but five of these were further modified at Australia’s request in the drafting process.

2.102 Some of the more significant differences between the UK draft and the 1945 UK – US Tax Treaty were: (a) the UK draft defined ‘industrial or commercial profits’ in terms that excluded specific items only, some of which were dealt with under the distributive rules; (b) the definition of ‘permanent establishment’ in the 1945 Treaty included ‘a factory’, but the UK draft did not (although it included ‘a farm’, something which the definition in the 1945 Treaty did not include); (c) the Industrial or Commercial Profits article in the 1945 Treaty adopted the ‘force of attraction’ principle, but the UK draft only permitted source taxation of profits attributable to a permanent establishment; (d) the ships and aircraft provision in the 1945 Treaty referred to the place of documentation of a ship or registration of an aircraft but the UK draft did not; (e) the credit provisions in the UK draft were considerably more detailed than those in the 1945 Treaty and became more detailed through the drafting process; (f) the 1945 Treaty contained an interest article, but the UK draft did not; (g) the 1945 Treaty contained an article exempting a UK resident (other than one engaged in a trade or business in the US) from US tax on gains from the sale or exchange of capital assets, but there was no equivalent provision in the UK draft; and (h) the 1945 Treaty contained a non-discrimination article, but the UK draft did not. Of these items (a), (b) and (e) were modified by Australia in the drafting process. Item (c) was also modified by Australia in the drafting process, to align it more closely with the equivalent article in the 1945 UK – US Tax Treaty.

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118 AV3 (definition of ‘industrial or commercial profits’ in exclusionary terms); AV6 (inclusion of ‘agricultural or pastoral property’ in definition of permanent establishment – still in 2013 Swiss Treaty and 2015 German Treaty); AV15 (modification to independent agent provision – still in 2015 German Treaty); AV36 (inclusion of beneficial ownership requirement in OECD Art 10(1) – still in 2013 Swiss Treaty, 2013 Treaty and 2015 German Treaty); AV88 (foreign tax credit provisions – still in 2010 Turkey Treaty, 2013 Swiss Treaty and 2015 German Treaty); and AV91 (omission of non-discrimination article).

119 AV3 (definition of ‘industrial or commercial profits’ in exclusionary terms); AV6 (inclusion of ‘agricultural or pastoral property’ in definition of permanent establishment); AV15 (modification of independent agent provision); AV36 (inclusion of beneficial ownership requirement in OECD Art 10(1)); and AV88 (foreign tax credit provisions).

120 The UK draft of 6th May 1946 exempted from source taxation profits of a resident of one of the territories derived from operating ships or aircraft. This was amended by Draft II dated 22nd May 1946 so that the exemption was confined to profits from operating ships whose port of registry is in that territory, or aircraft registered in that territory. A note by Willis dated 22nd May 1946 comments that he conceded the additional test of registration in the country of
Neither treaty contained an ‘other income’ article. The original United Kingdom offer of a taxation treaty had proposed to include provisions dealing with other types of income, but it is clear from the context that the intention was that what was contemplated was a series of specific provisions dealing with particular categories of income, not a general ‘other income’ article.\textsuperscript{121}

Some of the variations from the 1945 UK – US Tax Treaty appear to be the products of the ministerial agreement discussed at 2.90. This is clearly the explanation for the absence of an interest article as giving effect to the decision that full source country taxing rights would be retained in relation to interest; this was something that Australia had pressed for at the ministerial meeting and in the negotiations leading up to it. The structure of the 1946 UK Treaty that defined industrial or commercial profits did not contain articles dealing with categories of income where full source country taxing rights were to be retained and which did not contain an ‘other income’ article as one, but not the only possible, means of giving effect to the ministerial agreement to allow source country taxation of certain categories of income. The structure is found in the first UK draft of 6\textsuperscript{th} May 1946 and appears to have been initiated by the United Kingdom.

No documents that the author has examined in either the National Archives of Australia or the UK National Archives provide any indication as to why the UK draft of 6\textsuperscript{th} May 1946 did not contain a capital gains article, a non-discrimination article nor an ‘other income’ article.\textsuperscript{122} The absence of an ‘other income’ article can be explained by the overall structure of the treaty as a means of giving effect to the ministerial agreement discussed at 2.90. Full source country taxing rights in respect of income not otherwise dealt with would have been inconsistent with the presence of an ‘other income’ article which gave taxing rights to the residence country.

At the time, neither the UK nor Australia taxed capital gains as income.\textsuperscript{123} Although a gain could be income as a business profit, some gains made by a business were

\textsuperscript{121} See the discussion at 2.38.

\textsuperscript{122} As discussed at 2.38 and the accompanying note, the original UK proposals referred to the 1945 UK – US Treaty as containing examples of the types of article proposed. No express mention was made at that point of excluding the articles referred to at 2.105.

classified as capital gains and not taxed. Hence it would be understandable that
neither the UK nor Australia would see the need for an article dealing with capital
gains. This interpretation is supported by the narrow scope and non-reciprocal nature
of the capital gains article in the 1945 UK – US Tax Treaty.

2.107 The absence of a non-discrimination article could be explained by the fact that, at the
time, both countries did to some extent discriminate against non-residents. However,
it is also possible that neither the UK nor Australia saw a non-discrimination article
based on nationality as relevant to the relations between them. Prior to the British
Nationality Act 1948 and the Nationality and Citizenship Act (Cth) 1948, there was no
separate legal concept of an Australian national and Australians were British subjects
for nationality purposes.\textsuperscript{124}

2.108 In general, changes from the initial UK draft and/or the 1945 UK – US Tax Treaty that
emerged as the drafting process progressed were initiated by Australia, although the
final product of the drafting usually involved compromise between the delegations.
Some of the drafting work done from May to August 1946 was concerned with
refining the language of the initial UK draft so as to avoid ambiguity and with
technical arguments based on syntactic presumptions. Only articles which were the
subject of extensive discussion will be examined in detail here.

Undistributed Profits Tax Of Private Company Wholly Owned Subsidiaries Of UK Companies

2.109 Mair wrote to Gregg on 6\textsuperscript{th} May 1946,\textsuperscript{125} pointing out that the agreement to exempt
dividends paid by Australian 100% subsidiaries to their UK parent made problematic
the imposition of undistributed profits tax on Australian private companies that were
100% subsidiaries of a UK company. This was due to the method of calculating
Australian undistributed profits tax on private companies.\textsuperscript{126} In this situation, if the
dividend to the UK parent were exempt from Australian tax, then no Australian
undistributed profits tax would be payable either.

\textsuperscript{124} In Attorney-General (Cth) \textit{v} Ah Sheung [1906] HCA 44; (1906) 4 CLR 949 Griffith C.J., Barton
and O’Connor JJ at 949 said: ‘We are not disposed to give any countenance to the novel
doctrine that there is an Australian nationality as distinguished from a British nationality, so
that, while the term “immigration” as used in sec. 51 of the Constitution admittedly includes
the power of exclusion of British subjects in general, it would not extend to persons of
Australian nationality, whatever that may mean.’ The Nationality Act (Cth) 1920 had codified
the concept of British subject for purposes of Australian law. The concept of Australian citizen
was created by the Nationality and Citizenship Act (Cth) 1948.

\textsuperscript{125} Mair to Gregg, 6\textsuperscript{th} May 1946, Inland Revenue file, p168.

\textsuperscript{126} As discussed at 2.12, at the time Australia levied undistributed profits tax on the undistributed
profits of private companies at the same rate the tax shareholders would have paid if a
distribution had been made.
2.110 Anomalously, because undistributed profits tax on public companies was at a flat rate of 10%, where the Australian subsidiary was a public company as then defined, it would continue to be liable to 10% undistributed profits tax notwithstanding that under the proposed treaty any dividends that it paid to its UK parent would be exempt from Australian tax.

2.111 Under the definition of ‘private company’ for Australian tax purposes at the time, the key issue in the 100% subsidiary situation was whether the UK parent was a private company for Australian tax purposes. This turned on:

- Whether seven or fewer persons controlled it in the relevant sense;
- Whether the public held ordinary shares carrying 25% or more voting power; and
- Whether it was not a subsidiary of a public company, which turned on whether it was owned by one or more companies none of which was a private company.127

2.112 Mair proposed that the exemption for dividends not apply in the case of an Australian private company that was a 100% subsidiary of a UK company, but that Australia halve its rate of tax on the dividend and hence halve its rate of undistributed profits tax; a proposition which Willis appears to have found attractive. Where a UK private company was trading in Australia through a branch, Mair proposed that Australia would halve the nominal but uncollectible tax that it levied on dividends paid to its UK shareholders and consequently would halve the undistributed profits tax levied on the UK company. Willis’ conclusion was that there was not ‘very much in the dividend tax’ in both these cases and that the reduction in undistributed profits tax that would result from conceding these points was worth having.128

2.113 However, McGovern disagreed with Mair and favoured Willis’ earlier suggestion ‘that full rates of tax on undistributed profits be specifically provided for and that we (Australia) consent to exempt all dividends paid to UK parents’.129 Following a meeting with Gregg, Mair cabled a draft paragraph to McGovern which gave effect to Willis’ suggestion but which included a proviso the intent of which was evidently to ensure that the rate of undistributed profits tax on private companies would not exceed the Australian rate of tax on dividends paid to a non-resident company.130

2.114 McGovern rejected the proviso as it merely set a maximum rate but not a minimum rate for undistributed profits tax; he noted that, ‘Prime Minister advised Cabinet …

128 Memorandum ‘Australian tax on “Private Companies”’ above n 127.
129 McGovern to Mair, above n 110, 41.
130 Mair to McGovern, 30th May 1946, NAA, ATO Cables of draft agreement, p44.
that nothing in the treaty would give a UK company a trading advantage over an Australian company. This principle must be observed.\textsuperscript{131} McGovern cabled a suggested draft, which became Article VI(4) of the treaty and stated that notwithstanding the earlier provisions in the article, the undistributed profits tax assessed to a private company was to be the amount that would have been assessable if those provisions had not been included in the treaty.

\textit{Arm’s Length Computations And ITAA 1936 (Cth) s136}

\textbf{2.115} Mair also pointed out to Gregg that the meeting of ministers had left the special position of oil companies open for further discussion.\textsuperscript{132} Australian Board of Review decisions had determined the profits of oil companies on what Mair had argued was arm’s length basis. The determination, however, had been made under the then s136 of \textit{ITAA 1936 (Cth)}.\textsuperscript{133} The UK was concerned that s136 did not in terms require the use of arm’s length principles in determining taxable income.

\textbf{2.116} Australia was concerned that the draft Treaty would require the Commissioner to show that the relevant transaction was not for an arm’s length price whereas the Australian appeal provisions required the taxpayer to show that the s136 assessment was excessive. Hence Australia wanted the ‘arm’s length’ provisions in the draft treaty modified so as to leave the operation of s136 unaffected. In discussion Mair assured Willis that s136 was not invoked in normal cases if the profit ascertained was home consumption value, which Mair regarded as equivalent to arm’s length and stated that, for all practical purposes, the section was applied only in the case of oil companies.\textsuperscript{134}

\textsuperscript{131} McGovern to Mair, 7th June 1946, NAA, ATO Cables of draft agreement, pp8–50 at p49.
\textsuperscript{132} Mair to Gregg, 6th May 1946, Inland Revenue file, p168.
\textsuperscript{133} As it stood at the time, s136 empowered the Australian Commissioner to determine the taxable income of a business carried on in Australia that was either: (a) controlled principally by non-residents; (b) carried on by a company in which the majority of shareholders were non-residents; or (c) carried on by a company which (directly or through nominees) held the majority of the shares of a non-resident company. These powers could be exercised where it appeared to the Commissioner that the business either produced no taxable income or produced less taxable income than might be expected from that business. On appeal, Australian Boards of Review had power to make assessments under s136. The progenitor to \textit{ITAA 1936} s136 was s23 of \textit{ITAA 1915}, which was inserted by Act No 31 of 1921. This section became s28 in the 1922 consolidation \textit{ITAA 1922}. The provisions were based on the UK legislation of 1918. For a brief discussion of the case law on s136 and its progenitors see R J Vann, ‘Transfer Pricing Disputes in Australia’, in Eduardo Baistrocchi and Ian Roxan (eds), \textit{Resolving Transfer Pricing Disputes: A Global Analysis} (Cambridge University Press, 2012) 359–414.
\textsuperscript{134} Mair to McGovern, above note 107, p18.
2.117 Cables between Mair and McGovern followed in which McGovern argued that the formula applied by the Boards of Review was in not truly arm’s length but was an attempt to arrive at what would be an arm’s length basis if sufficient information were available. Nonetheless, McGovern instructed Mair to ‘insist upon having the protection of arbitrary provisions to cover oil companies and the like, asking the UK to rely on the fact that any arbitrary Australian basis which did not reasonably approximate to what the result might be of a true arm’s length basis would not survive the taxpayer’s appeal to the Board of Review or the Australian Courts.’\(^\text{135}\)

2.118 Following further discussions with Gregg (in which Gregg expressed concern that s136 created uncertainty on whether an arm’s length basis was being applied), Mair pointed out to McGovern that, if the operation of s136 were not preserved in the treaty, the Commissioner could still make a determination under it but would be required to apply an arm’s length principle. While Mair thought it desirable to have s136 embodied in the treaty, he did not think that the case was sufficiently strong to make ‘divergence of views an issue between us’.\(^\text{136}\)

2.119 Willis wrote to Mair on the issue on 20\(^{\text{th}}\) June 1946. Willis began by noting that it was common ground between Australia and the UK that the arm’s length basis was the right principle in computing profits of branches and subsidiaries, and pointed out that this was the League of Nations principle and that the UK regarded it as fundamental to any double taxation agreement dealing with trading profits. Although Willis understood that Australia adopted an arm’s length principle in applying s136, he noted that s136 did not actually state the principle and went to summarise the United Kingdom’s objection to a saving clause in relation to s136 as being:

‘If … the agreement were to provide that Section 136 should remain unaffected by the arm’s length provisions, it would be equivalent to saying that those provisions could be ignored by the Commissioner. Indeed it might be taken as implying that Section 136 was not founded on the arm’s length principle. We know that neither the Commissioner nor the Board of Review would ignore the principle in practice, but the point is that they would be entitled to, and might even be expected to, and that is a position which we

\[^{135}\text{McGovern to Mair, above note 108, p41. See also McGovern to Mair, 6\(^{\text{th}}\) June 1946, NAA, ATO Cables of draft agreement, pp45 and 46.}\]
\[^{136}\text{Mair to McGovern 7\(^{\text{th}}\) June 1946, NAA, ATO Cables of draft agreement, p51.}\]
could not possibly accept. The agreement would be indefensibly one-sided if we were bound to observe the principle and you were not.\footnote{137}

Willis argued that, consistently with the broad requirements of the treaty provision, the Commissioner could still continue to make assessments under s136 and that in fact the taxpayer was required to show that the assessment was not on an arm’s length basis.\footnote{138}

2.120 In a cable to McGovern dated 20\textsuperscript{th} June 1946, Mair raised a further argument to the effect that the arm’s length principle as expressed in Article III(3) appeared to be too narrow. Article III(3) would not deal appropriately with the situation where a head office purchased from a related entity at an inflated price. Here, an independent party purchasing at arm’s length from the head office would not be expected to pay any less than the head office had paid for its purchases. In computing the profits of the permanent establishment, Article III(3) would produce a purchase price at least equal to the price paid by the head office. These were the circumstances existing in the Shell case where s136 had been able to be applied. Mair noted that the UK was agreeable to Article III(3) being widened so as to deal with this perceived problem.\footnote{139}

2.121 Mair’s cable to McGovern of 20\textsuperscript{th} June 1946 also included Whitlam’s opinion on the powers of the Commissioner under s136. The conclusion of Whitlam’s advice was that Article III(3) would impose no limitation on the existing practice in relation to s136 but would prevent the Commissioner from adopting a narrower practice which, presumably, the Commissioner would not want to do. Hence, Whitlam considered that there was no justification at all for any qualification of Article III in relation to s136. If there was difficulty in accepting these views, Whitlam suggested that the matter be submitted to Dr Evatt (as Attorney-General) for his opinion.\footnote{140}

\footnote{137}{Willis to Mair 20\textsuperscript{th} June 1946, Inland Revenue file, pp197ff.}
\footnote{138}{Willis to Mair, above n 137, 197ff. Mair cabled Willis’ letter to McGovern on the day of its receipt. Mair to McGovern, 21\textsuperscript{st} June 1946, NAA, ATO Cables of draft agreement, p67.}
\footnote{139}{Mair to McGovern, above n 138. The reference to ‘the Shell case’ is likely to be to \textit{Shell Company of Australia v FCT} (1930) 44 CLR 530, a decision of the Privy Council on appeal from the decision of the Australian High Court in \textit{British Imperial Oil Co Ltd v FCT} (1925) 35 CLR 422 which concerned the validity of the appeal process and of s28 of \textit{ITAA 1922} (Cth), the predecessor section to \textit{ITAA 1936} s136. The cases on \textit{ITAA 1936} s136 are discussed in Gunn et al, above n 18, 1392–7 and in N E Challoner and C M Collins, \textit{Income Tax Law and Practice (Commonwealth)} (The Law Book Co. of Australia, 1953) 896–912. See also the discussion in Vann, above n 131, 360–1.}
\footnote{140}{Mair to McGovern, above n 138, 70.}
2.122 McGovern then sought the advice of the Australian Solicitor-General (Kenneth Bailey) on several questions in relation to the issue. Bailey’s opinion was that a covenant for ascertaining the quantum of taxable income of a taxpayer had been expressly contained in the original UK proposal of June 1945, and that Australia was bound to include the covenant in the treaty. Bailey drafted a provision which would have excluded taxpayer rights in relation to Article III(3) so that the article only had effect as an agreement between the contracting governments. In Bailey’s opinion, while the criteria applicable under Article III(3) and in s136 were broadly the same, one important difference was that the assessment of taxable income under s136 rested on the judgment or determination of the Commissioner whereas Article III(3) depended on what the Commissioner was able to establish. This appeared to shift the onus from the taxpayer to the Commissioner. Nor was Bailey confident that the considerations for the application of the arm’s length basis under Article III(3) were as flexible as those under s136, for example, in the case of inflated prices paid by an English parent organisation that supplied goods to an Australian branch. Bailey’s opinion included a draft saving clause in relation to s136 which included the following:

‘that discretion shall be exercised or that estimate shall be made with the object that the amount so liable to tax shall be determined, as nearly as the information available to the taxing authority permits, in accordance with paragraph (3) of this Article, but the application of that law and liability of any taxpayer shall not otherwise be affected by that paragraph.’

2.123 Given this advice, McGovern suggested that Mair request a re-expression of Article III(3) and Article IV as suggested by Bailey. McGovern considered that this should be acceptable to the UK officials in view of their previous comments.

2.124 The UK would not accept Bailey’s redraft of Article III(3) or his draft of the saving provision in relation to s136. The UK did not like the closing words of the saving provision as they might have prevented the taxpayer from exercising appeal rights to have profit determined in accordance with Article III. Mair indicated to McGovern that the UK would agree to extension of the original paragraph in the manner that Mair had foreshadowed in his cable of 20th June. This was achieved in the draft of 19th July 1946 by omitting the words ‘under the same or similar conditions’ from Article

141 The advice is quoted in full in McGovern to Mair 14th July 1946, NAA, ATO Cables of draft agreement, pp96–100.
142 McGovern to Mair, above n 141, 100.
143 McGovern to Mair, above n 141, 101.
144 See the discussion at 2.120.
III(3) and rephrasing the requirement for adopting the arm’s length fiction in relation to dealings. This represented a further instance of variation, initiated by Australia, from the 1945 UK – US Tax Treaty.

2.125 To meet Australia’s concerns in relation to s136, the UK suggested that the following be added to Article III(3):

> 'If the information available to the Taxation Authority concerned is inadequate to determine the profits to be attributed to the permanent establishment nothing in this paragraph shall affect the application of the law of either territory in relation to the liability of the permanent establishment to pay tax on the amount determined by the exercise of a discretion or the making of an estimate by the Taxation Authority of that territory provided that such discretion shall be exercised or such estimate shall be made so far as information available to the Taxation Authority permits in accordance with the principle stated in this paragraph.'

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2.126 Mair advised McGovern that Whitlam’s opinion was that the proposed addition fully safeguarded the powers of the Commissioner to exercise discretion or to make an estimate under s136. Mair suggested that, in order to reach finality the UK proposal be accepted.146 On 27th July 1946, McGovern advised Mair that the proposed saving provision in relation to s136 was acceptable.147 On 30th July, Mair cabled an amended Article IV, which included an equivalent saving provision in relation to s136.148 Hence both Article III(3) and Article IV(3) contained saving provisions, in the terms suggested by the UK as quoted at 2.125 The process that led to the insertion of these provisions was initiated by Australia, but the final form of the provision was a result of compromise between the negotiators.

*Foreign Tax Credits*

2.127 The treaty required that both the UK and Australia give a foreign tax credit to their residents in respect of tax paid in the other country on income sourced in the other country. However, the Australian obligation was limited to the situation where Australian tax was payable by the resident on income derived from sources in the United Kingdom.

145 Mair to McGovern, 25th July 1946, NAA, ATO Cables of draft agreement, p115.
146 Mair to McGovern, above n 145, 116.
147 McGovern to Mair, 27th July 1946, NAA, ATO Cables of draft agreement, Mair to McGovern, above n 145, 119.
148 Mair to McGovern, 30th July 1946, NAA, ATO Cables of draft agreement, p123.
2.128 At the time, only foreign source dividend income and foreign source income which was exempt from tax in the source country was included in an Australian resident’s assessable income.\textsuperscript{149} Hence, the effect of the drafting was that, while this continued to be Australian domestic law, Australia was only required to apply a foreign tax credit in relation to dividends (and other income which was exempt from tax at source). Article XII(2) had been deliberately drafted so as to be able to require Australia to provide a foreign tax credit for all forms of income if Australia subsequently changed its domestic law and taxed residents on their worldwide income.\textsuperscript{150}

2.129 In the case of an ordinary dividend\textsuperscript{151} the UK was obliged, irrespective of the level of shareholding, to give credit for underlying Australian corporate tax against UK income tax in addition to credit for any Australian tax on the dividend itself.\textsuperscript{152} Australia argued that all UK taxes on income which Australia had taxed on a source basis should be available for absorption of the tax credit. Australia was concerned that otherwise excess credits (arising, for example, from Australian undistributed profits tax liabilities) would not be able to be offset against UK excess profits tax liabilities.

2.130 Although not agreeing to this suggestion, the UK indicated that as from 1st January 1947 excess profits tax would be abolished and national defence contribution would be treated as an income tax for the purposes of the foreign tax credit provisions. As a consequence, Australia requested an exchange of letters between the High Commissioner and the Chancellor of the Exchequer on this issue.\textsuperscript{153}

2.131 In the case of a UK dividend, an Australian resident shareholder was only entitled to a credit if the shareholder elected to have the UK tax on the dividend (as reduced by

\textsuperscript{149} See the discussion at 2.7 and 2.13.
\textsuperscript{150} NAA, ATO Tax Credits, ‘Article XII’ signature illegible p39 and NAA, ATO Tax Credits, McGovern to Chifley, 3\textsuperscript{rd} October 1946, p121.
\textsuperscript{151} In the case of preference shares the same treatment was given to Australian corporate tax to the extent that the dividend exceeded the fixed share of profits to which the preference shareholder was entitled.
\textsuperscript{152} Under Article XII(1) of the Treaty, the UK was obliged to give credit for underlying Australian corporate tax to both UK companies and individuals irrespective of the level of shareholding. Although the Explanatory Memorandum to Income Tax Assessment Bill 1947, which gave the force of Australian law to the Treaty, contained examples at pp87–9 illustrating the Australian government’s understanding of the effect of Article XII(1). Example 3 at pp88–9 dealt with the situation where a dividend was paid by an Australian resident company to a UK resident individual. In Example 3, the dividend is grossed up for the nominal rates of Australian underlying corporate tax and Australian tax on the dividend itself. The UK practice, however, was to allow a gross up and credit at the lesser of the effective rate of UK tax on the dividend or the Australian effective tax rate (including underlying corporate tax) on the dividend. The UK practice is explained in Gunn et al, above n 18, 1164–6, para 1881AD.
\textsuperscript{153} NAA, ATO Tax Credits, McGovern to Chifley, 3\textsuperscript{rd} October 1946, p122.
any applicable UK reliefs) included in assessable income.\textsuperscript{154} If the election were not made, the High Court decision in \textit{Jolly v FCT} (1934) 50 CLR 131\textsuperscript{155} would have meant that the UK tax was not included in the shareholder’s assessable income.

2.132 The effect of the credit article and of its implementation in Australian law was that, irrespective of the level of shareholding, an Australian resident shareholder receiving a dividend who made the election was allowed a foreign tax credit for underlying UK tax levied on the company. Australia was obliged to give credit for UK tax deducted from the gross dividend but not for so much of the amount deducted as exceeded the net UK tax applicable to the dividend as reduced by reliefs allowed by the United Kingdom.

2.133 Australia was concerned that the effect of the gross up was that an Australian resident investing in a UK company would be in a better after tax position than if the investment had been made in an Australian company or in a UK company with Australian source profits. Australia argued that the limit of the Australian credit should therefore be the excess of the UK standard rate (at that time 9/- in the £) over the Australian corporate rate (at that time 6/- in the £). The United Kingdom, understandably, would not agree because in all existing taxation treaties the credit allowed was up to the limit of the residence country’s own tax. Australia then requested that the Chancellor of the Exchequer give an assurance, to the effect that Article XII would be amended if the advantage gained by an investment in UK companies with only UK source income was being exploited by Australian investors.\textsuperscript{156}

2.134 Australia also raised questions as to how the UK would interpret what would eventually become Article XII(1) dealing with credit being given by the UK for Australian tax on Australian source income. Mair wrote to Gregg on 5\textsuperscript{th} August 1946\textsuperscript{157} outlining the situations in which Australia wanted assurances as to what the UK interpretation of the provision would be.

2.135 One situation was where: (a) a dividend was paid to a UK resident by a company resident in a third country out of Australian source profits; and (b) interest was

\textsuperscript{154} Implemented in Australian law as \textit{ITAA} 1936–1947 (Cth) s160L.
\textsuperscript{155} See the discussion in notes 18 and 68 above.
\textsuperscript{156} NAA, ATO Tax Credits, ‘Article XII’ signature illegible, p39 and NAA, ATO Tax Credits, McGovern to Chifley 3\textsuperscript{rd} October 1946, p123. Under then current rates, the effect of the Australian request would have been that the limit of the credit would have been 3/- in the £ (being the difference between the UK standard rate and the Australian corporate rate) rather than 6/- in the £ (being the Australian corporate rate).
\textsuperscript{157} Inland Revenue file, p221 (two pages), Mair to Gregg, 5\textsuperscript{th} August 1946.
received by a UK resident on money secured by a mortgage over Australian real property. Here Australia was concerned about a potential conflict of source rules, recognising that, while particular types of income might be regarded as having an Australian source for Australian tax law purposes, it was possible that ‘the general law’ would determine that the source of the relevant income was in some other country. Mair noted that the understanding had been reached in discussions that the UK would give credit for the Australian tax paid in this situation.

2.136 The second situation was where an Australian holding company was interposed between an Australian subsidiary and its UK parent. The Australian inter-corporate tax rebate would mean that the recipient Australian holding company would not have any net Australian tax liability on the inter-corporate dividend. Mair sought assurances that, in calculating the amount of creditable Australian tax, the UK would take into account the underlying tax paid by the Australian subsidiary on its profits.

2.137 The third situation concerned the case of a dual resident company paying a dividend from profits which Australia regarded as having an Australian source but which the UK did not. Mair sought assurances that the UK would give credit for the Australian tax paid in this situation.

2.138 Gregg’s reply gave the requested assurances in the second and third cases but not in the first, commenting: ‘The credit system on which the Draft Treaty is founded relates to income flowing from one country to the other and I do not like the idea of extending it to income flowing to other countries which may be a contributory to a pool of profits that may be distributed by that other country in the form of dividend.’ Gregg went on to describe this as a ‘rather freak case’ and noted that Australia’s claim to tax such a dividend was rarely enforceable anyway because of its extra-territorial character. Gregg indicated that if a case arose where there were special circumstances, the UK would be prepared to consider it on its merits.\textsuperscript{158}

2.139 The exchange of letters providing the assurances requested at 2.130 and at 2.134 took place on 29\textsuperscript{th} October 1946 between the High Commissioner and the Chancellor of the Exchequer.\textsuperscript{159}

\textit{Exchange Of Information}

\textsuperscript{158} Inland Revenue file, p223 (two pages), Gregg to Mair, 6\textsuperscript{th} August 1946. On 23\textsuperscript{rd} September 1946 Mair also sought certain assurances from Gregg in relation to shipping profits, but the author has not yet located correspondence from Gregg giving the assurances requested.

\textsuperscript{159} Beasley to Dalton, 29\textsuperscript{th} October 1946, Inland Revenue file, pp294–6 and Dalton to Beasley, 29\textsuperscript{th} October 1946, Inland Revenue file, page number obscured.
2.140 The 1946 Treaty also contained an exchange of information article. In the initial negotiations, Australia had accepted the offer of an exchange of information article with alacrity.\textsuperscript{160} The exchange of information article in the original UK draft followed the equivalent article in the 1945 UK – US Treaty. In a cable to McGovern dated 20\textsuperscript{th} May 1946, Mair noted that the UK was not prepared to unequivocally exchange information required by each taxing authority.\textsuperscript{161}

2.141 Australia requested the deletion of the reference to ‘against legal avoidance’. The UK would not agree to this as it was strongly opposed to the extension of the purposes for which information could be exchanged. One of the United Kingdom’s main concerns was that continental countries with which they expected to conclude double tax treaties would require an exchange of information article in similar terms and that, as a consequence, they would carry a heavy administrative burden in disclosing information about taxpayers to continental authorities.

2.142 The UK did agree to amendments to the article which ensured that information could be divulged to a Court in addition to a Board of Review. These amendments were implemented in the draft of 19\textsuperscript{th} July 1946, and amounted to another variation, initiated by Australia, from the 1945 UK – US Tax Treaty. Mair’s view remained that Australia could relate the great majority of its enquiries to one of the purposes stated in the article and that the matter of extending the purposes for which information could be sought should not be pressed.\textsuperscript{162}

Residence Issues

2.143 The definitions of ‘UK resident’ and ‘Australian resident’ in the treaty as finally signed referred to persons who were residents for the purposes of UK or Australian tax respectively and who were not residents of the treaty partner country for its tax purposes. The basic approach to defining ‘resident’ by reference to the domestic law of each treaty partner was contained in the UK draft of 6\textsuperscript{th} May 1946, which followed the approach that had been used in the 1945 UK – US Tax Treaty. However, the end result of the drafting process was that dual residents were not treaty residents although, as will be seen below, the treaty did provide benefits to dual residents in particular circumstances. Drafting devices\textsuperscript{163} were used to avoid some dual residence problems that were identified by the ATO administrative committee, but the treaty did not contain any general dual residence tie-breakers.

\footnotesize{\textsuperscript{160} ‘Australia’ by Willis, above n 66, 73–4.\textsuperscript{161} Mair to McGovern, 20\textsuperscript{th} May 1946, NAA, ATO Cables of draft agreement, p36.\textsuperscript{162} Mair to McGovern, 8\textsuperscript{th} July 1946, NAA, ATO Cables of draft agreement, p92.\textsuperscript{163} See the discussion at 2.149 and 2.150.}
Unlike every other taxation treaty that the UK entered into in this period, the treaty did not contain the second limb of the definition which had the effect of deeming a company to be resident where it was managed and controlled. The provision had been contained in the original draft submitted by the United Kingdom and was then amended in Draft II dated 22nd May 1946. The amended provision reflected the test of Australian corporate residence in ITAA 1936 (Cth) s6(1).

When the amended provision was circulated within the ATO, several comments noted that dual corporate residence was possible under the amended provision, for example, in the situation where an Australian incorporated company was managed and controlled in the United Kingdom. Mair also noted this in a cable to McGovern on 9th May 1946, observing that dual residence would not cause difficulty where taxation was on a source basis as the other residence country would give credit, but that the position where a residence basis applied would be considered further when dealing with the tax credit article.

McGovern cabled Mair suggesting that the definition could be broken up into separate paragraphs dealing with: 1. UK residents other than a company; 2. Australian residents other than a company; 3. UK companies; and 4. Australian companies. Prior to receiving the comments from Australia, however, Mair and Willis had agreed to delete the provision referring to corporate residence entirely.

Mair noted that Willis ‘was experiencing difficulty in deciding what, under U.K. law, is a company. They use the term ‘body of persons’ in their Act. We eventually decided that it was unnecessary to include therein any reference to a company’. Mair commented in the same cable, ‘It is not practicable to make a rule to avoid ‘double residency’ cases, as neither U.K. nor Australia could give up its existing principles of determining whether an individual or a company is resident of its territory. We must, therefore, accept as inescapable the case of the double resident. The proportion of such cases will, I feel sure, prove to be very small.’

See the discussion of UK tax treaties of the time in Avery Jones, below note 169.


NAA, ATO Progressive Draft, p50. A handwritten note on p52 (the first page of the draft) states, ‘This was first draft worked on in Australia’.

Mair to McGovern, 9th May 1946, NAA, ATO Cables of draft agreement, p16.

McGovern to Mair 30th May 1946, NAA, ATO Cables of draft agreement, p42.

Extract from letter of Second Commissioner dated 11th June 1946, NAA, ATO Tax Credits, pp73–4. See also Mair to McGovern, 11th June 1946, NAA, ATO Cables of draft agreement, pp53–4. John Avery Jones has pointed out that all other UK tax treaties of the time had no difficulty in defining a company and suggests that either Willis used this as an excuse for not agreeing to an Australian proposal, possibly the redrafted provision referred to at 2.109, or that this was an excuse by Mair to McGovern as Commissioner for not achieving a dual
2.148 The ATO administrative committee of Belcher and Mills then comprehensively analysed double taxation possibilities that might arise in cases of dual corporate residence. Differing source rules on dividends between Australia and the UK could result in cases of unrelieved double taxation where the paying company was a dual resident. Belcher and Mills suggested that, while the problem would be overcome if the United Kingdom, for purposes of the treaty, adopted the Australian source rule for dividends, they noted that this might produce another potential double taxation problem if an Australian company paid a dividend to a UK resident where part of the profits of the paying company were derived in a third country such as NZ. Belcher and Mills noted that it appeared that the UK would agree to allow a credit in the first case and that, in the circumstances, an exchange of letters on the point would be sufficient considering the relative importance of the matter. This suggestion ultimately led to the third of the assurances sought from Gregg to Mair on 6th August 1946.

2.149 A further problem that was recognised was where a dual resident received income that had been derived in a third country. Here Article XII(3) provided that a proportional credit would be allowed by each contracting government. The drafting device used in this situation was to refer to ‘a resident of Australia for the purposes of Australian tax, who is also a resident of the UK for the purposes of UK tax’ and not to ‘Australian resident’ nor to ‘UK resident’ as defined in Article II. The intention was that dual residents would have the benefit of a proportionate credit in this situation but as they were neither Australian residents nor UK residents as defined would not have treaty benefits generally.

2.150 Similarly, the reductions in source taxation in the dividend article applied where the paying company was a ‘resident of Australia (whether or not also a resident of the UK or elsewhere)’ or a ‘resident of the UK (whether or not also a resident of Australia or elsewhere)’. Again, the effect of the drafting was that relief would still be available where the paying company was a dual resident even though a dual resident was not a treaty resident. As Belcher noted, however, the distinction between ‘Australian residence tie-breaker. John F Avery Jones, ‘Defining and Taxing Companies 1799 to 1965’ in John Tiley (ed), Studies in the History of Tax Law (Hart Publishing, 2012) vol 5, 1 at fn 2 and accompanying text.

170 Article XII(2) of the Treaty, although not the original draft, deemed, for the purposes of the credit provisions, a dividend paid by a company resident in the UK to be derived from sources in the UK, thus applying the same source rule for inbound dividends to Australia as the UK applied to dividends.


172 See the discussion at 2.137.
resident’ and ‘UK resident’ on the one hand and ‘resident of Australia’ and ‘resident of the United Kingdom’ was not apparent from the treaty itself.  

The Signing Of The Treaty And Its Entry Into Force In Australian Law

2.151 The treaty was signed in London on behalf of the UK by Hugh Dalton, as Chancellor of the Exchequer, and on behalf of Australia by John (Jack) Beasley, as Australian Minister in London on 29th October 1946. The treaty was given the force of law in Australia as the Third Schedule to ITAA 1936 (Cth) by s37 of ITAA (No 1) 1947 (Act No 11 of 1947). Article XV of the Treaty provided that it had effect in Australia as respects tax for the year beginning on 1st July 1946 and all subsequent years.

Significance Of The Treaty For Australia's Subsequent Taxation Treaty Policy And Practice

2.152 The significance of the 1946 UK Treaty for Australia’s subsequent treaty policy and practice cannot be overstated. The perception as to why the treaty was necessary and the terms that Australia agreed to under it made a significant contribution to Australia's reluctance to enter into further taxation treaties at least until the early to mid 1960s.

2.153 Although the UK initiated the negotiations for the treaty, Australia saw it as preferable to the previous system of Dominion Income Tax Relief, which by 1945 was no longer fully relieving international double taxation of non-portfolio dividends and was seen as inhibiting UK post war investment in Australia. From this perspective, the most significant benefit that Australia obtained was the granting of a full foreign tax credit, including a credit for Australian underlying corporate tax irrespective of the level of shareholding. However, the most significant concession that Australia made in obtaining this benefit, exempting dividends paid by wholly owned Australian subsidiaries of UK companies from source taxation, was a key factor in inhibiting Australia from entering into tax treaties with the US, Canada and NZ in the 1940s despite receiving requests for tax treaties from each of those countries in that period.

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173 ‘Dual Resident’, signed by Belcher, 24/6/1946, NAA, ATO Definitions, pp32–3. It is unclear whether the UK or Australia initiated the inclusion of this provision. Mair advised McGovern of the addition of Article XII(3) by cable dated 8th July 1946 and indicated that he considered the provision equitable but gave no clear indication of who initiated the amendment. Mair to McGovern, 8th July 1946, NAA, ATO, Cables of draft agreement. McGovern on 12th July 1946 advised Mair of agreement with the principle of Article XII(3) and suggested amendments clarifying the method for calculating the credit, which were reflected in the final version of the article. McGovern to Mair, 12th July 1946, NAA, ATO, Cables of draft agreement.

174 See the discussion at 2.28–2.30.

175 See the discussion at 2.92 and 2.129.
2.154 The Treaty also established a structure which was to persist virtually intact in Australian treaties until the end of the 1960s and which did not entirely disappear until 1980. This structure involved: defining industrial or commercial profits in terms that excluded other items of income which were not necessarily dealt with under the distributive articles of the treaty; not having an interest article; not having a capital gains article; and not having an ‘other income’ article.

2.155 Throughout the negotiations leading to the ministerial agreement, Australian politicians, while wanting to encourage direct UK investment in Australia, reaffirmed the Australian emphasis on source basis taxation and, while conceding significant reductions in source taxation of dividends paid to parents of wholly owned subsidiaries and a residence basis on shipping and aircraft profits, maintained full source country taxing rights on other key areas such as interest and mineral royalties. Chifley, at least, was aware of the economic reality of Australia as a net capital importer underpinning the emphasis on source basis taxation.

2.156 The politicians were also concerned with preserving the operation of Australia’s domestic law on the taxation of film business and of insurance business controlled abroad; an attitude that was to persist in subsequent Australian taxation treaty policy and practice.

2.157 It is arguable that the terms on which the UK had recently negotiated treaties with Canada and South Africa appear to have influenced the overall bargain that Australia agreed to in the 1946 UK Treaty.

2.158 Similar but not identical influential factors are evident in discussions between officials and between officials and ministers prior to the ministerial agreement. In briefing Evatt, Jackson had stressed the importance of obtaining full relief from international double taxation in the parent–subsidiary situation. The importance of relieving trade from double taxation was also recognised by Coombs in his meeting with Gregg. A clear emphasis on source taxation can be seen at several points. The status of Australia as a net capital importer is raised in Jackson’s briefing of Evatt.

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176 See the discussion at 2.40–2.43, 2.57, 2.72–2.76 and 2.90.
177 See the discussion at 2.42.
178 See the argument to this effect in 2.80 and 2.90.
179 See the discussion at 2.66.
180 Coombs meeting with Gregg is discussed at 2.89.
181 See the discussion at 2.47, 2.59 and 2.62–2.66.
182 See the discussion at 2.68.
and Gregg’s letter to Trend also indicates that Australia referred to its status as a net capital importer.  

2.159 Jackson, in his meetings and correspondence with Gregg and Willis, also raises the different structures of the Australian and UK systems of corporate-shareholder taxation as an argument against exempting dividends paid by wholly owned subsidiaries. In discussions with Gregg and Willis, but not with Australian politicians, Jackson argued against provisions which would have resulted in discrimination against Australian companies and raised political considerations as a reason for not agreeing to a shipping exemption. Although Gregg had justified residence basis taxation of shipping as a League of Nations principle and as something with which Canada and Eire had agreed, Jackson does not appear to have been influenced by these arguments.

2.160 At the technical drafting level, a desire to maximise source basis taxation, a concern to preserve the operation of domestic law provisions having that effect, and concerns about anticipated technical problems relating to the interaction of the Treaty with Australian domestic law all intertwine with no clear dominant emphasis on any one of these objectives in particular being evident. Australian officials were concerned with preserving the operation provisions of domestic law (such as ITAA 1936 s136) and with dealing with anticipated technical problems that were products of the interaction of the treaty with Australian domestic law. This could be seen in the extended correspondence and negotiations in relation to undistributed profits tax, credit issues and dual residence issues. Both the attitude and, to varying degrees, the drafting techniques were to influence subsequent Australian treaty practice particularly to the end of the 1950s but, to a lesser extent, under the entire period reviewed in this thesis.

2.161 A large proportion of variations from the OECD Model in currently operative Australian tax treaties can be traced directly to the 1946 UK Treaty. Half of these were the result of following the UK draft following the 1945 UK – US Tax Treaty. Six of the variations from the OECD Model which were not the result of following the

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183 Gregg’s letter to Trend is discussed at 2.86.
184 See the discussion at 2.61.
185 As discussed at 2.63, this was Jackson’s argument in response to the UK request to exempt UK companies from Australian undistributed profits tax on Australian sourced income.
186 See the discussion at 2.64.
187 See the discussion at 2.54.
188 See the discussion at 2.115–2.126.
189 See the discussion at 2.109–2.114.
190 Discussed at 2.127–2.139.
191 Residence issues in the Treaty are discussed at 2.143–2.150.
1945 UK – US Tax Treaty were initiated by the UK, although five of these were modified by Australia in the drafting process, and the remaining four were initiated by Australia. Therefore, of the ten variations from the 1945 UK – US Tax Treaty, nine were either initiated or modified by Australia.

2.162 All of the structural features of the treaty described at 2.102 to 2.103 were found in the first UK draft and were readily accepted by Australia. Australia’s acceptance of the structure is explained by its consistency with the emphasis on the primacy of source basis taxation made by both Australian politicians and officials throughout the negotiations. The absence of an equivalent to OECD Model Article 21 was initiated by the UK and, like 80% of the variations from the current OECD Model initiated by the United Kingdom, was consistent with the 1945 UK – US Tax Treaty.

2.163 In one respect, however, a variation, although appearing in the initial UK draft, appears to have been the product of the ministerial agreement discussed at 2.90. This was the absence of an ‘interest’ article. The initial UK proposals and the 1945 UK – US Tax Treaty both included an ‘interest’ article.

2.164 A variation from the 1945 UK – US Tax Treaty that was part of the initial UK draft but which does not appear to have been the subject of any discussion was the absence of a capital gains article. The most likely explanation for both the absence of the article and discussion of its omission is that, at the time, neither the UK nor Australia had a general capital gains tax.

2.165 The final structure of not having an interest article, not having a capital gains article and not having an ‘other income’ article enabled effect to be given to the ministerial agreement discussed at 2.90 in relation to items where full source country taxing rights were retained; in that sense, the structure was indirectly initiated by Australia. Other than the omission of an interest article and restricting the scope of residence taxation of royalties, the variations that Australia initiated or modified were all concerned with the intertwining of concerns to maximise source basis taxation, to preserve the operation of certain domestic law provisions and to avoid anticipated technical problems associated with the interaction of domestic law with the Treaty.

2.166 Unlike the negotiations that led to the system of Dominion Income Tax Relief, this was a bilateral negotiation in which concessions on particular articles could be traded.

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192 The initial UK proposals were discussed at 2.33–2.39.
193 See the argument to this effect at 2.106.
194 The negotiations leading to the system of Dominion Income Tax Relief were discussed at 2.22–2.26.
against each other and in which the practice of the treaty partner (the UK in this instance) and of third countries (particularly the US) or of international organisations (in this instance the League of Nations) could be and was used as a precedent for the appropriate treatment. Australian politicians and officials learnt that hard bargaining, intransigence and reference to precedents could produce favourable results. These attitudes were to be evident in varying degrees in most of Australia’s subsequent taxation treaty negotiations in the period examined in this thesis.

2.167 Finally, the negotiation and drafting of the Treaty established a process which, in broad terms, was followed in subsequent Australian taxation treaties in the period reviewed in this thesis. Politicians were responsible for and interested in the broad framework of the Treaty as it affected Australian revenues and foreign direct investment. Up to this point there is little evidence (other than the involvement of H C Coombs\(^\text{195}\) in the archives examined by the author of the Australian Department of the Treasury having a significant advisory role in relation to these broad policy issues. The ATO team, led by either the Commissioner or a Second Commissioner, was to be the principal technical negotiator with drafting assistance being provided by the Crown Solicitor’s office and with technical issues and revenue estimates being referred to ATO committees and Deputy Commissioners for comment. The major change in process that occurs in the period reviewed in this thesis is the increasing role of the Department of the Treasury in relation to broad policy issues. That increase in role began to become evident when Australia considered how to respond to requests for tax treaties received from the US and other countries in the 1940s and 1950s.

2.168 The next chapter discusses the negotiation and drafting of the two Australian tax treaties entered into in the 1950s. Emphasis is placed on the negotiation and drafting of the 1953 US Tax Treaty but brief consideration is also given to the 1957 Canada Tax Treaty. The chapter includes a discussion of: (a) the economic and strategic background to these treaties; (b) Australia’s reluctance to enter into further tax treaties between 1946 and 1953; and (c) the distinctive features of Australian tax treaty practice that can be traced to these treaties.

\(^{195}\) Coombs’ involvement is discussed at 2.81, 2.89 and 2.90. As discussed above note 99, Coombs had previously been a Treasury economist.
CHAPTER THREE: AUSTRALIA’S TAX TREATIES NEGOTIATED IN THE 1950s

3.1 Following the 1946 UK Treaty, Australia did not enter into another tax treaty until the 1953 US Treaty. The 1957 Canada Treaty was the only other tax treaty that Australia entered into in the 1950s, although the negotiation and drafting of the 1960 NZ Treaty commenced in the 1950s. This was notwithstanding the fact that the United States, Canada and NZ first offered to enter into a tax treaty with Australia in 1947 and 1945 respectively. Australia also received offers of tax treaties from several European countries in the 1950s.

3.2 Clearly, Australia was reluctant to enter into any tax treaties at all between 1946 and 1950, and for the rest of the 1950s Australia took a cautious approach to entering into tax treaties. This raises a question which this chapter shall endeavour to answer: What factors influenced Australia’s cautious approach to tax treaties in this period?

3.3 Some of the distinctive features of Australian tax treaty practice emerged in this period, while other distinctive features having their origins in the 1946 UK Treaty were consolidated and refined in this period. Chapter 4 will show that the Australian model circulated to potential treaty partners in the early 1960s was influenced by the Australian treaties of this period.

3.4 Australia’s three tax treaties negotiated in the 1950s have many features in common. The 1953 US Treaty formed the basis for the 1957 Canada Treaty and the 1960 NZ Treaty. This chapter begins with a discussion of the history of the development of the Australian economy and taxation system and

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1 Correspondence on a potential tax treaty with the US is summarised in Australian Department of External Affairs memorandum to the Minister for External Affairs dated 20th December 1949, NAA, External Affairs file, Part 1. The 1947 Canadian request for a bilateral tax treaty with Australia is discussed in C John Taylor, ‘The Negotiation and Drafting of the First Australia–Canada Taxation Treaty (1957)’ (2013) 61 Canadian Tax Journal 915 at 922–8. The negotiations in the 1940s with New Zealand are summarised in a memorandum by E M W Visbord to Mr Pryor dated 28th November 1958. The earliest correspondence on a possible tax treaty was Tom D’Aton, High Commissioner for New Zealand to H V Evatt, Minister for External Affairs (no date, but from a memorandum forwarding copies of the letter to other departments, it appears that the date received was 21st August 1945). All these documents are in ‘Taxation With Other Countries – Australia – New Zealand Double Taxation’, NAA, Series Number A571, Control Symbol 1956/1469 Pt 1.

2 ‘Confidential for Cabinet: Double Taxation Agreements With Other Countries: Submission 305: Harold Holt, Treasurer, 16th July 1962’, NAA, Series Number A5818, Control Symbol: Volume, Agendum 305 submission noted that requests for tax treaties had been received from several countries including Japan, the Federal Republic of Germany, Denmark, Greece, Malaya, Singapore, South Africa and Egypt.
discusses Australian strategic policy in the period from 1945 to 1950. It then examines the Australian reluctance to enter into tax treaties in the period between 1945 and 1950 and the change of policy with the election of the Menzies government in 1949.

3.5 The chapter then examines the negotiating and drafting of the 1953 US Treaty. Rather than discussing the negotiation and drafting of the 1957 Canada Treaty in detail, the chapter discusses the significance of the 1957 Canada Treaty for the key questions examined in this thesis. The chapter, due in part to a paucity of archival material, does not discuss the negotiation and drafting of the 1960 NZ treaty.3

The 1953 Australia – US Tax Treaty: Economic And Strategic Background – Australian Economic And Strategic Policy, 1945–50

3.6 The US–Australia alliance is popularly regarded as beginning in 1941 with Prime Minister John Curtin’s declaration:

'Without any inhibitions of any kind, I make it quite clear that Australia looks to America, free of any pangs as to our traditional links or kinship with the UK.'4

Nonetheless, in the last two years of his prime ministership, Curtin had been distrustful of American plans for the Pacific and had returned to emphasising the British Empire as the base for Australia’s military and economic security, emphases that were to be continued by the Chifley government.5

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3 Files have been located at the National Archives of Australia and at Archives New Zealand relating to the negotiation and drafting of the treaty, but the major content of these files relates to an earlier Heads of Agreement for a tax treaty which would have attempted to resolve problems associated with the use at the time of different systems of corporate-shareholder taxation by Australia (classical) and NZ (dividend exemption). Difficulties in reconciling different types of corporate-shareholder taxation systems will be identified in Chapter 7 as one of the factors that influenced Australian tax treaty policy and practice during the period reviewed in this thesis. The files in the National Archives of Australia and Archives New Zealand clearly show that difficulties in reconciling the systems of corporate-shareholder taxation and disagreements as to how this should be done were the major reasons why Australia did not enter into a tax treaty with NZ until 1960.


5 Curtin’s change of stance is discussed in Day, above n 4, ch 38 in particular 577–83. The continuity of the Chifley government’s policies with those of the Curtin government in this respect is discussed in D Day, Chifley (Harper Collins Publishers, 2001) 451.
3.7 Australian policymakers during the Second World War had low expectations for the anticipated post war recovery. Notwithstanding the Chifley government's restrictive approach to sources of funding for economic expansion, Australia's economic performance in the years 1945 to 1949 significantly exceeded these expectations. What had been a complementary relationship between Australia as a producer of raw materials and agricultural produce and the UK as a producer of manufactured goods and a consumer of agricultural products had been significantly challenged by the expansion of Australia's manufacturing industry.

3.8 High wool prices led to Australia having a balance of payments surplus with the UK. This coupled with immigration and UK capital investment led to continued economic growth, inflation and a surge in demand for both capital and consumer goods which the UK was unable to satisfy fully by 1949. The restoration of the convertibility of the pound sterling in 1947 brought on a dollar crisis in consequence of which, following the suspension of convertibility, countries in the Sterling Area (such as Australia) resolved to reduce their dollar imports.

3.9 In the late 1940s, the US was the only reliable supplier of capital and consumer goods; however, the import restrictions on dollar goods, introduced following the convertibility crisis, meant that sufficient US goods could not be imported. By 1949, Australia needed both debt and equity investment in dollars if it were to continue with a policy of economic growth through immigration and the development of its manufacturing industry. The Chifley

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7 See the discussion at 2.5 and 2.6.

8 See the discussion in Robertson, above n 6 and in particular Rooth, 1999, above n 6.

9 The response of Australia and other countries in the Sterling Area to the 1947 convertibility crisis is discussed in Robertson, above n 6, 96–8 and in P L Robertson, 'Australia, Britain and the Sterling Area, 1945–52' (2997) 37 *Australian Economic History Review* 91.

government, however, was averse to borrowing from the US or Canada or from international institutions such as the World Bank.\footnote{See the discussion in Robertson, above n 6, 100–01. See also the discussion at 2.5 of the background to the Australian and particularly the Chifley government's distrust of the United States.}

### 3.10
Prior to its election in 1949, the Menzies Liberal/Country Coalition argued that 'acute dollar restrictions' were limiting Australia's development and that Australia should borrow dollars from either the World Bank, the Export-Import Bank of the United States or the New York market.\footnote{See the discussion in Robertson, above n 6, 100–01.} Following the Coalition victory in 1949, Menzies consulted with UK ministers in London for advice, then visited Washington and secured a loan of $100 million on favourable terms from the World Bank.\footnote{See the discussion in Robertson, above n 6, 100–03 and in Singleton and Robertson, above n 10, 59–63.} In other respects, however, particularly with its emphasis on development of the manufacturing industry and immigration, the initial economic policies of the Menzies government represented a development of, rather than an abrogation of, those of the Chifley government.\footnote{For a summary, see the discussion in Singleton and Robertson, above n 10, 72–4, who note, however, that there was a shift to a greater emphasis on agriculture from 1952 onwards. R G Menzies had previously been Prime Minister in a United Australia Party government from 1939 to 1941. Menzies and others formed the Liberal Party of Australia in December 1944. Menzies was Prime Minister in a Liberal–Country Party Coalition for a record term from December 1949 to his retirement in January 1966. Allan Martin, 'Sir Robert Gordon Menzies' in Michelle Grattan (ed), Australian Prime Ministers (New Holland Publishers, 2000), 175–205.}

**The Australian Income Tax System Between 1945 and 1951**

### 3.11
No fundamental changes were made in the basic structure of the Australian income tax system between 1950 and 1953 from that described in Chapter 2.\footnote{See the discussion at 2.7 to 2.17.} The deduction for foreign tax paid on dividends received by individuals had been replaced with a rebate of foreign tax in 1947.\footnote{ITAA 1936 former s45 introduced by ITAA 1947 (Cth).} The rebate under s46(2A)\footnote{The rebate was discussed at note 19 in Chapter 2.} for dividends paid out of profits which had borne super tax was repealed with the abolition of super tax discussed below. Undistributed profits tax on non-private companies was abolished in 1951.\footnote{The provisions dealing with further tax on undistributed income of non-private companies had been contained in ITAA 1936 Part IIIA, which was omitted by s18 of the Income Tax and Social Services Contribution Assessment Act 1951 (Cth).}
3.12 Tax rates changed during the period. Super tax and the corporate rate were unchanged between 1945 and 1948, but War-Time (Company) Tax ceased to apply from 30th June 1947. A progressive rate for companies applied between 1948 and 1950, with tax being levied at a rate of 25% on the first £5000 of taxable income and at a rate of 30% thereafter. Super tax was not applied from 1st July 1951, but non-private companies were taxed at a flat rate of 35% and in addition were required to pay a special levy of 10%. The progressive rate scale was continued for private companies in 1951, with the rate on taxable income above £5000 increasing to 35%.  

The 1951 Decision To Negotiate A Taxation Treaty With The United States  

3.13 The decision to negotiate a taxation treaty with the US has to be seen against the more general economic policy background outlined above and against Australia’s somewhat negative experience in negotiating the 1946 UK Treaty. While that treaty contained provisions which became distinctive features of Australian treaty practice, it exempted from source taxation dividends paid by wholly owned subsidiaries. Australian agreement to such a restrictive approach to source taxation of dividends occurred because this was part of a total package of offsetting compromises which, taken as a whole, was

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19 War-Time (Company) Tax Assessment Act 1940 (Cth) s13 as amended by War-Time (Company) Tax Assessment Act 1942 (Cth) had imposed war-time (company) tax ‘up to and including the financial year in which the present war terminates’. War Time (Company) Tax Assessment Act 1942 (Cth) included a definition of ‘the present war’ in s3 of the War-Time (Company) Tax Assessment Act 1940 (Cth). The definition of ‘the present war’ was removed by War-Time (Company) Tax Assessment Act 1947 (Cth), which amended s13 of the Principal Act by replacing the words ‘next succeeding that in which the present war terminates’ with the words ‘which commenced on the first day of July, One thousand nine hundred and forty six’. In addition, s3 of the War-Time (Company) Tax Act 1947 (Cth) amended s6 of the War-Time (Company) Tax Act 1940 (Cth) stating, in effect, that the tax was to be imposed up to and including the financial year which began on 1st July 1946.

20 Company rates applying between 1945 and 1951 are summarised in N E Challoner and C M Collins, Income Tax: Law and Practice (Commonwealth) (Law Book Co. of Australasia Pty Ltd, 1953) 317. The House of Representatives Explanatory Note to the Sixth Schedule of the Resolution to Declare the Rates of Income Tax and Social Services Contribution for the Financial Year 1951–1952 mentions that for the financial year 1950–51, public companies were liable to pay super tax at the rate of 5% on income above £5000. The Sixth Schedule did not impose super tax as such for the 1951–52 financial year, but paragraph 10 of the Sixth Schedule imposed additional tax at the rate of 20% on the taxable income of companies other than private companies, trustees, mutual life assurance companies, co-operative companies, and non-profit companies prohibited from making distributions to their members.
perceived to place Australia in a better position than had been the case under the UK’s system of Dominion Income Tax Relief.\textsuperscript{21}

**The Chifley Government’s Reluctance To Negotiate**

3.14 The US informally raised the possibility of a taxation treaty with Australia as early as 1945. A formal approach was made by the US in October 1947, followed by the submission of a detailed proposal in September 1948. On 24\textsuperscript{th} February 1949, the Australian government advised the US that Australia was not disposed to enter into a treaty which went beyond formalising the existing arrangements and that there appeared to be little scope for an agreement which could show a balancing of advantages in any apparent form.\textsuperscript{22}

3.15 In this period, the technical answer of the Australian Treasury and ATO to these offers was that the Australian exemption system and the US unilateral foreign tax credit system meant that double taxation did not really exist between Australia and the US. While Australia saw advantages in a bilateral treaty which preserved the existing mechanisms in each country for preventing international double taxation, it did not favour any treaty which involved further adjustments. The view of Australian officials was that any double taxation that did occur was caused by differences in tax rates between the two countries rather than the absence of appropriate mechanisms for relieving international double taxation. Therefore, any double taxation could only be relieved by reducing Australian tax rates, particularly on dividends paid to foreign shareholders. Based on the precedent of the 1946 UK Treaty, Australia believed that the required concessions, particularly in relation to dividends paid to parents by wholly owned subsidiaries, would cost revenue and would to some extent provide benefits to the US treasury and not to US investors.\textsuperscript{23}

3.16 Exacerbation of Australia’s dollar difficulties through a repatriation of profits by US direct/non-portfolio investors was another factor that the Chifley government and officials took into account. The attitude was that good

\textsuperscript{21} See the argument to this effect at 2.166.

\textsuperscript{22} The history of the correspondence is summarised in an Australian Department of External Affairs memorandum to the Minister for External Affairs dated 20\textsuperscript{th} December 1949, NAA, External Affairs file, Pt 1.

\textsuperscript{23} See Acting Commissioner of Taxation to The Secretary of the Treasury, 4\textsuperscript{th} January 1950 in NAA, External Affairs file Pt 1 and McGovern, Commissioner of Taxation, to the Commonwealth Treasurer (Arthur Fadden), 26\textsuperscript{th} January 1950, NAA, External Affairs file, Pt 1.
relations between Australia and the US would not depend on the existence of a bilateral taxation treaty in which the US obtained an annual monetary advantage. 24 The US Ambassador considered that the Labor government generally, and Chifley in particular, focused too much of the revenue cost of a treaty to Australia and were insufficiently aware of the wider benefits that the US considered would flow from a taxation treaty. 25

The Menzies Government’s Reconsideration Of The Position

3.17 Several factors in combination led to a reconsideration of Australia’s attitude following the election of the Menzies government. One was certainly the more positive attitude, discussed above, of the Menzies government to US investment generally. Nonetheless, for a time, concerns remained about the effect of profit repatriations by direct investors on Australia’s limited dollar reserves. 26 Concerns also lingered about the inflationary effects of increased US direct investment given the shortages in labour, raw materials and essential services produced by the rapid post war growth in Australia. 27

3.18 The general geopolitical context was also relevant. The Australian Department of External Affairs was in favour of entering into a double tax treaty with the US to maintain good relations with Australia’s important World War II ally. 28 The victory of the Communists in China in 1949 focused US

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24 See McGovern to Fadden, 26th January 1950, above n 23. The letter also mentions that the former Treasurer (J B Chifley) took this view. Similar views are expressed in Acting Commissioner of Taxation to The Secretary of the Treasury, 4th January 1950, above n 23.


26 An internal memo dated 23rd March 1950 of the Australian Department of External Affairs to the Minister notes that the second report of the Interdepartmental Committee on Dollar Receipts (on which the Department of External Affairs was not represented) tentatively recommended against a taxation treaty with the US on the grounds of revenue cost and diminution of scarce dollar reserves. NAA, External Affairs file, Pt 1.

27 See the discussion in Singleton and Robertson above n 10, 60–1.

28 On 22nd December 1949 Norman Makin, the then Australian Ambassador to the United States, in the context of discussing a possible double taxation treaty with the US (among other issues) had recommended to the Australian Minister for External Affairs that ‘Australia’s efforts should be directed towards making itself an important, if not essential, country in the US strategic, commercial and financial thinking.’ Norman Makin, Ambassador, Australian Embassy, Washington, DC to External, 22nd December 1949, The draft submission to Cabinet for the Minister for External Affairs dated approximately 22nd February 1951 began with the following comment: ‘An urgent decision by Cabinet is desirable on the question of a Tax Convention with the
strategic attention to the Asia-Pacific where Australia as a European outpost assumed greater strategic and economic importance than the size of its population and economy would have otherwise warranted. The Korean War broke out on 25th June 1950 and, following involvement of the US and pursuant to a United Nations Security Council resolution, Australia announced that it would contribute militarily to the conflict. The early commitment of Australian forces to the Korean War enhanced US goodwill towards Australia.29

3.19 Research based on archival sources from the period argues that the US actively sought regional military treaties as part of overall resistance to Communism and that Australia too, since the Chifley government, had desired a formal military alliance with the US as a means of ensuring its own security. These mutually compatible objectives led to the 1951 ANZUS Treaty between Australia, the US and NZ.30

3.20 The Korean War led to a boom, fuelled by a steep rise in wool prices, in the Australian economy which lasted until May 1951.31 The resulting inflation was to be a contributing factor to the Fadden ‘horror budget’ of 1951–52.32

USA. In view of the current negotiations with the US on a Japanese peace settlement and security arrangements in the Pacific area, the importance of demonstrating to the US Government that we are approaching outstanding problems in a co-operative spirit is more than ever apparent. The negotiation of a convention for the avoidance of double taxation, which for more than three years has been constantly urged on us as a mutually beneficial arrangement is an important means of achieving this object.” Both documents are contained in NAA, External Affairs file, Pt 1.

29 Points made by Singleton and Robertson, above n 10, 73.
30 D McLean, ‘Australia in the Cold War: A Historiographical Review’ (2001) 23 International History Review 253 at 307–08 outlines the conventional interpretation of historians that Australia’s early military involvement in the Korean War, ahead of the British commitment of ground forces, enhanced US goodwill towards Australia and led a somewhat reluctant US to the 1951 ANZUS Treaty. McLean’s own research (D McLean, ‘ANZUS Origins: A Reassessment’ (1990) Australian Historical Studies 64 and D McLean, ‘From British Colony to American Satellite?: Australia and the US during the Cold War’ (2006) 52 Australian Journal of Politics and History 64), which was based on subsequently released archival material, argues that Australia saw a formal military alliance with the US as fundamental to its national security and would have agreed to one during the period of the Chifley government. McLean further argues that the archival evidence indicates that the US favoured membership of regional treaties as a means of consolidating US leadership of the smaller Pacific powers in the fight against Communism. The ANZUS Treaty was concluded on 1 September 1951 and came into force on 29 April 1952. McLean (2001) provides a critical review of the extensive literature (much of it partisan) on the Australia–US alliance.

31 The boom in this period is analysed in A M C Waterman, Economic Fluctuations in Australia 1948 to 1964 (Australian National University Press, 1972) 76–82. The importance of the US as a trading and investment partner for Australia increased significantly during this period. Australian exports to the US were 8.2% of total
3.21 Menzies’ 1950 visit to Washington to negotiate a dollar loan coincided with the outbreak of the Korean War and Australia’s military commitment to it. Apparently, the US deliberately refrained from mentioning the taxation treaty issue during Menzies’ visit. Nevertheless, it is hard to believe that the assistance given by the US in the obtaining of that loan could have been absent from the minds of Australian ministers and officials considering whether to agree to the US request for a taxation treaty. Indeed, Percy Spender reported to the US State Department officials that J W Hughes had expected that Menzies would be pressed for a tax treaty during his visit and was disappointed that he had not been.

3.22 There was also significant lobbying by US businesses and their existing Australian subsidiaries in favour of a double tax treaty with Australia. US business and to some extent US officials were more concerned with the discrimination against US business when compared with UK business than with double taxation on non-portfolio investment, an attitude that Australian External Affairs officials were cognisant of.

exports in 1949–50, a figure that increased to 15.2% in 1950–51 and then started to decline to 11.4% in 1951–52. R A Foster, Australian Economic Statistics: 1949–1950 to 1994–95 (Reserve Bank of Australia, 1996) 9, Table 1.4. The UK was still the major source of imports to Australia in 1949–50 at 53.1% of total imports; the US was second at 9.9% of total imports, but by 1966–67 imports from the US at 25.8% of total imports outs tripped imports from the UK at 23.8% of total imports. In 1952–53, the US was Australia’s second-largest source of imports at 16.5% of total imports compared with the UK’s 41.7% of total imports. Foster, Australian Economic Statistics: 1949–50 to 1994–95, 13, Table 1.6. As far as foreign investment was concerned, in 1949–50 the UK represented 48.2% of inflow of foreign investment at $106 million while the US (including Canada in this period) represented 9.5% at $21 million. The UK remained the major source of inbound foreign investment throughout the 1950s but was first surpassed by the US in 1961–62 when the UK represented 41.4% of inbound foreign investment ($125 million) and the US 47.4% ($143 million). Foster, Australian Economic Statistics: 1949–50 to 1994–95, 42, Table 1.17.


A draft Cabinet submission for the Minister for External Affairs written on approximately 22nd February 1951 notes that ‘while the question had not been raised with the Prime Minister during his visit to Washington this omission was deliberate in order to avoid any suggestion of a bargain in connection with his financial negotiations’, NAA, External Affairs file, Pt 1.

At the time, Spender was Minster for External Affairs in the Menzies government. Hughes was an Australian Deputy Commissioner of Taxation. As discussed at 3.23, he and E S Spooner were appointed by Fadden to report on whether Australia should enter into a tax treaty with the United States.


See E S Spooner and J W Hughes to A W Fadden M.P., Commonwealth Treasurer, 30th August 1950. NAA, External Affairs file, Pt 1. Numerous letters and memoranda
Against this background the Australian treasurer, A W Fadden, commissioned J W Hughes\(^{38}\) and E S Spooner\(^{39}\) to report on whether Australia should enter into a double tax treaty with the United States. Hughes and Spooner concluded that Australia should do so and estimated that the likely revenue loss to Australia of £1,750,000 would be offset somewhat by taxing dividends at the rates that the US had agreed with other British Commonwealth countries – namely, 5% for non-portfolio and 15% for other dividends – and by increased revenues flowing from greater US investment in Australia. The report noted that the US was seeking a closer relationship with Australia and that many large organisations were interested in permanently establishing or in expanding business in Australia.\(^{40}\)

The Treasurer’s submission to Cabinet was less optimistic, noting that existing US businesses operating in Australia would introduce additional capital in the absence of a treaty and that new US investment in Australia was likely to be of a transient nature and of restricted value to the Australian economy. The submission stated that negotiation of a taxation treaty with the US could not be justified on taxation principles, but it was necessary to consider political implications arising out of the relationships between the two countries in the then current circumstances;\(^{41}\) this was a possible reference to the dollar loan, the Korean War and the ANZUS alliance. On 15th March 1951, Cabinet resolved to commence taxation treaty negotiations with the United States.\(^{42}\)

The Negotiation And Drafting Of The 1953 Australia – US Taxation Treaty

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38 At the time, Hughes was a Deputy Commissioner of Taxation.
39 At the time, Spooner was Chairman of the Commonwealth Committee on Taxation.
40 Spooner and Hughes, above n 37.
41 A W Fadden, Treasurer, ‘For Cabinet Sub-Committee, Income Tax and Estate Duty, Double Taxation of Income Flowing Between Australia and the US of America; Double Estate Duty Imposed on Assets Having Their Situs in Australia Owned by Persons Dying Domiciled in the United States’, 2nd March 1951. NAA, External Affairs file, Pt 1. Fadden became Treasurer with the election of the Menzies government in 1949. He had previously, briefly, been Prime Minister from August to October 1941.
42 NAA, External Affairs file, Pt 1 copy of Cabinet decision dated 15th March 1951.
The Excess Foreign Tax Credit Problem For US Non-Portfolio Investors

3.25 A key consideration leading government and business in Australia and the US to favour a taxation treaty between the countries was the excess foreign tax credit problem that US non-portfolio investors encountered. The Spooner and Hughes report concluded that this problem was significantly impeding direct investment by US companies in Australia.43

3.26 The excess credit position of US companies investing in Australia through subsidiaries44 was a product of the interaction of Australian rates of tax on corporate profits and dividends with limitations on the direct and indirect foreign tax credit allowed by the US to non-portfolio outbound foreign investment.45

3.27 In 1952, the US relieved international juridical double taxation through a foreign tax credit system. US taxpayers were required to use the lesser of an overall or a per country limitation. In the former case, the credit was limited to the same proportion of the taxpayer’s overall US tax liability as was the proportion that foreign source income represented of the taxpayer’s global income. In the latter case, separate calculations were made in relation to each foreign jurisdiction in which the taxpayer invested, with the credit limit for income from each jurisdiction being the proportion of the taxpayer’s overall US tax liability that was the same proportion that income from that foreign jurisdiction represented of the taxpayer’s global income.46

3.28 Indirect credits were available where a US corporation owned 10% or more of the voting stock of a foreign corporation from which it received a dividend. An

43 Spooner and Hughes, above n 37.
44 In practice, equivalent problems did not exist when the US investment was through an Australian branch as the absence of a branch profits tax in Australia meant that Australian tax did not generate excess foreign tax credits for US companies. Memorandum from P S McGovern, Commissioner of Taxation to the Commonwealth Treasurer (A W Fadden) 15th April 1952, NAA, ATO file, Pt 3, 3, paras 14 and 17 and 4, para 19.
45 Memorandum from P S McGovern, above n 44, 3, paras 15 and 16 and 4, paras 19–21.
46 See the discussion of the history of the US foreign tax credit limitation in Michael J Graetz and Michael M O’Hear, ‘The “Original Intent” of US International Taxation’ (1997) 46 Duke Law Journal 1021 in particular at fn 141. For a discussion of US rules in 1957–58 see B Magill and WC Schaab, ‘American Taxation of Income Earned Abroad’ (1957–1958) 13 Tax Law Review 115. Shortly after the signing of the Australia – US taxation treaty of 1953, the overall limitation on the foreign tax credit was repealed in 1954. In 1960, taxpayers were given the option to use an overall limitation or a per country limitation. The per country limitation was repealed in 1976. A basket system of limitation was introduced in 1986. The number of baskets was reduced to two in 2006.
indirect foreign tax credit was also available for underlying tax on dividends received from a second-tier foreign corporation when 50% or more of its voting stock was owned by a first-tier foreign corporation in which a US corporation held 10% or more of the voting stock.47

3.29 Australia recognised that this problem could be dealt with by a reduction in Australian taxes on dividends paid to US companies making direct investments in Australia. However, Australia wanted to ensure that the reduction was only to such a level as would benefit the US investor rather than the US Treasury.48

The Initial Negotiations In Canberra In 1952

3.30 Negotiations for the treaty began in Canberra on 17th March 1952. Eldon P King, Special Deputy Commissioner of the US Bureau of Internal Revenue, led the US delegation, which also included Peter J Mitchell and Earl A Ruth.49 The Australian delegation was led by the Commissioner of Taxation, Patrick McGovern. Other members of the Australian delegation were Mair, Belcher, Hunt, Worland, Orriell, and Beikoff from the ATO and Pryor and Garrett from the Australian Treasury.50 The following discussion of the negotiations is based on McGovern’s report to Fadden and on the first draft of the treaty produced in those negotiations.51

3.31 McGovern reported that the US position was that the 1946 UK Treaty should be regarded as setting the pattern of Australia’s agreements with nations from whom investment capital for development was to be encouraged. Exceptions were in areas where the US legislature had established a precedent in previous US treaties that it was unlikely to be willing to vary.52

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49 McGovern, above n 44, 1, paras 1 and 2.
50 ‘List showing names of persons attending the discussions between US and Australian Tax Officials’ Federal Taxation Office, 20/3/52. NAA, External Affairs file, Pt 3. Belcher was Assistant Commissioner of Taxation at the time.
51 The author has not been able to locate a day to day record of the negotiations, in either the National Archives of Australia in Canberra or the US National Archives and Records Administration. The draft annexed to McGovern’s letter to Fadden is the earliest draft of the treaty that the author has been able to locate in either the National Archives of Australia or the US National Archives and Records Administration at College Park, Maryland, USA.
52 McGovern, above n 44, 4, para 22.
3.32 The Australian objective was to ascertain the minimum terms acceptable to the US that would remove the deterrent to direct investment by US companies in Australia. The reduction in Australian tax on direct investment by US companies in Australia was governed by the US corporate rate, because Australian taxes at this level would not deter US investment in Australia and reductions below this level would, through the US foreign tax credit system, produce benefits for the US Treasury rather than the US investor.53

3.33 Australia opposed provisions which ‘violated the prior right of the country of origin of the income to tax’ and which could do little or nothing to encourage US investment in Australia. Nonetheless, McGovern considered that in some areas, most importantly shipping and aircraft profits, taxation on a residence basis had become so widely recognised as to be the conventional method of taxing rather than being based on any principle of taxation.54

3.34 Notwithstanding these differences in objectives and approach, McGovern noted that the initial discussions produced ‘a very substantial degree of agreement upon the matters which might be confidently submitted to the two Governments for their consideration and a draft Convention was prepared’.55

The Draft Of The Treaty Developed In The Initial Negotiations56

3.35 The following discussion of the draft of the treaty developed during the negotiations in Canberra in 1952 will highlight similarities to and differences from the 1946 UK Treaty, particularly in relation to provisions that are relevant to distinctive features of Australia’s taxation treaty policy or practice or which are evidence of factors influencing that policy or practice.

Definitions

Resident

3.36 The definition of ‘Australian resident’ in the draft was substantially the same as in the 1946 UK Treaty; however, as the US taxed on the basis of

53 McGovern, above n 44, 5 paras 27 and 28.
54 McGovern, above n 44, 4 para 29.
55 McGovern, above n 44, 6 para 30.
56 This draft of the treaty is Annexure C to McGovern’s Memorandum above n 44. A summary of the result of the negotiations is contained in McGovern’s letter to Fadden. The author has to date been unable to locate a daily record of the negotiations either in the National Archives of Australia or in the US National Archives and Records Administration.
citizenship, a US citizen was expressly excluded from being an Australian resident. While McGovern considered that it would have been preferable to have avoided this result, he noted that it had been achieved by the US in all of its previous treaties and that it was a principle on which the US was likely to be unyielding. As the effect on Australian revenue would necessarily be negligible, he did not consider that it warranted Australian rejection.

3.37 Following the definition in the 1946 UK Treaty meant that dual residents were not treaty residents. This was because, as was the case with the 1946 UK Treaty, a taxpayer would only be a resident of one of the contracting states if the taxpayer were resident in that contracting state for tax purposes but was not resident in the other contracting state for its tax purposes.

3.38 Unlike the 1946 UK Treaty, the draft contained a specific provision dealing with the residence of companies. Under the draft, a ‘US corporation’ was not an Australian resident. A ‘US corporation’ was defined as meaning ‘a corporation, association or other like entity created or organized in or under the laws of the United States’. A ‘US resident’ included ‘any US corporation … being a corporation … which is not a resident of Australia for purposes of Australian tax’.

3.39 The combined effect of the definitions of ‘Australian resident’, ‘US corporation’ and ‘US resident’ appears to have been that a US corporation which carried on business in Australia and was centrally managed and controlled in Australia was not an Australian resident for treaty purposes; however, as it was a resident of Australia for purposes of Australian tax, it was not a US resident for treaty purposes either. On the other hand, as the US determined corporate residency solely on the basis of place of incorporation, a company incorporated in Australia could only be an Australian resident for treaty purposes. McGovern merely commented that the reference to ‘US corporation’ in the definition of ‘Australian resident’ was consistent with the Australian approach and was included for ease in drafting.

Industrial And Commercial Profits

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57 See the discussion at 2.143.
58 See the discussion at 2.144 to 2.147.
59 McGovern, above n 44, 7, para 42. The statement that the reference to ‘US corporation’ was consistent with the Australian approach was presumably a reference to the fact that one of the tests of corporate residency under Australian tax law at the time was incorporation in Australia. See ITAA 1936 (Cth) s6(1) definition of ‘resident of Australia’.
3.40 As was the case with 1946 UK Treaty, industrial and commercial profits were defined in terms which specifically excluded dividends, interest, rent and royalties. In addition, the definition excluded ‘management charges’ and ‘remuneration for personal services’.

Permanent Establishment

3.41 The definition of ‘permanent establishment’ was similar to the equivalent definition in the 1946 UK Treaty, but, in McGovern’s words, it had been ‘broadened in conformity with Australian aims’. Clearly, Australia’s aims in this respect were to maximise source based taxation of the Australian branches of foreign enterprises. In addition to indicia of a permanent establishment under the 1946 UK Treaty, the draft proposed that a permanent establishment should include a workshop, oilwell, office, an agency, a management and the use of substantial equipment or machinery.

3.42 The most interesting addition to the definition of ‘permanent establishment’ was the specific reference to the use of substantial equipment. The same reference had been included in the 12th June 1950 Supplementary Convention to the 1942 US – Canada Taxation Treaty, but had not been included in any other US treaty up to 1952 and was not included in any other US treaty for the rest of the 1950s. However, specific reference to ‘substantial equipment’ was included in several other Canadian treaties of the 1950s.

3.43 It is unclear whether the broadening of the definition in this respect ‘in conformity with Australia’s aims’ was initiated by Australia or the United States. Canada had apparently requested the inclusion of the substantial equipment provision in the 1950 Supplementary Convention between the

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60 McGovern, above n 44, 7 para 46.
61 McGovern had noted, above n 44, 5 para 29, that in the negotiations Australia had offered opposition to provisions which violated the prior right of the source country to tax and which could do little or nothing to encourage US investment in Australia. McGovern also noted, above n 12, 7 para 44, that it was in the interests of Australia to have the term ‘permanent establishment’ cover a wide variety of the means by which a resident of one country can conduct business operations in the other country.
62 Previous scholarship has traced the origins of the inclusion of substantial equipment provisions in Australian treaties to the 1953 US Treaty. See R J Vann, ‘Hill on Tax Treaties and Interpretation’ (2013) 28 Australian Tax Forum 87. The question of whether the inclusion was at the request of the US or at the request of Australia does not appear to have been the subject of detailed analysis previously.
63 See paragraph ‘o’ of Supplementary Convention 12th June 1950 to US – Canada Taxation Convention of 1942.
64 Canada – South Africa Taxation Treaty, 1956, Article II(1)(j); Australia – Canada, 1957, Article II(1)(l); Belgium – Canada, 1958, Article II(1)(l)(bb); Finland – Canada, 1959, Article II(1)(j).
United States. A reasonable conclusion is that Australia argued for the inclusion of a substantial equipment provision on the basis that the US had agreed to such a provision in its Supplementary Convention with Canada in 1950.

The Industrial Or Commercial Profits Article

This article was similar to its equivalent in the 1946 UK Treaty, and, like that article, specifically reserved Australia’s right to continue its existing methods of taxing film business and profits of non-resident insurance companies. Consistent with the 1946 UK Treaty, the article included a saving provision preserving the right to apply domestic law where information was inadequate for determining an arm’s length price.

In some respects, the Industrial or Commercial Profits article in the draft treaty differed from the equivalent article in the 1946 UK Treaty.

At the request of the United States, the draft applied a force of attraction principle in taxing industrial or commercial profits once a permanent establishment was found to exist in the source country. McGovern commented that, while not materially affecting Australian revenue, over a period of time, the force of attraction principle was likely to be more favourable to Australia, and hence Australia did not oppose the US request.

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65 This would appear to be the case from the comments on the ‘substantial equipment’ provisions in the 1950 Supplementary Convention in the letter of transmittal by the Secretary of State (Dean Acheson) to the Senate, Tax Analysts, *Worldwide Tax Treaties*, United States, Canada, Report of the Secretary of State, 29th June 1950.

66 To date the author has been unable to locate archival evidence, in either the National Archives of Australia, the US National Archives or the Canadian National Archives in Ottawa, indicating which country was the originator of the inclusion of a substantial equipment provision in the definition.

67 McGovern, above n 44, 8, para 57. Division 14 of Part III of *ITAA 1936* included 10% of the gross income of film businesses controlled by non-resident controllers in the taxable income of the relevant non-resident controller. Division 15 of Part III of *ITAA 1936* included 10% of gross premiums in the taxable income of non-resident insurance companies carrying on business in Australia but which did not have a principal office or branch in Australia. These provisions, as they applied in 1953, are discussed in N E Challoner and C M Collins, above n 20, 907–28.

68 McGovern, above n 44, 8, para 55, makes it clear that the request to tax industrial or commercial profits using a force of attraction principle was made by the United States. This was US taxation treaty practice at the time. See the discussion of the rationale behind the practice in David R Tillinghast, ‘The Revision of the Income Tax Convention between the US and the Federal Republic of Germany’ (1965–66) 21 *Tax Law Review* 399 at 420–9.

69 McGovern, above n 44, 8, para 56.
The article provided for deduction of all deductible expenses, including executive and general administrative expenses reasonably attributable to the permanent establishment in calculating its income. The article specified that it was 'subject to the principle underlying Section 38 of the Income Tax and Social Services Contribution Assessment Act', although McGovern did not expressly mention this point in his report to Fadden. McGovern commented that the provision provided a safeguard to enterprises of both countries but would not involve revenue cost to Australia as it was consistent with existing practice under Australian domestic law. Equivalent provisions had been included in US taxation treaties from 1948 onwards, although the provision in the draft omitted the words 'wherever incurred' and in this respect followed an earlier variant of the US provision.

Inter-connected Companies/Associated Enterprises

This Article was similar to the equivalent Article in the 1946 UK Treaty. A substantive variation, made at the request of the United States, was that both countries were prohibited from taxing under the treaty any greater amount than would be possible under their domestic tax law. McGovern commented that this had been requested for administrative reasons and that as it would be open to Australia to amend its domestic tax laws its right to tax was not restricted and the proposal was not opposed.

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70 Section 38 of the ITAA 1936 dealt with the importation and sale in Australia by a manufacturer of goods, and read as follows:

‘Where goods manufactured out of Australia are imported into Australia and the goods are, either before or after importation, sold in Australia by the manufacturer of the goods, the profit deemed to be derived in Australia from the sale shall be ascertained by deducting from the sale price of the goods the amount for which, at the date the goods were shipped to Australia, goods of the same nature and quality could be purchased by a wholesale buyer in the country of manufacture, and the expenses incurred in transporting them to and selling them in Australia.’

A contemporary commentary on s38, N E Challoner and C M Collins, above n 20, 303, noted that it appeared to embody the principle laid down by the High Court in FCT v W Angliss & Co Pty Ltd (1931) 46 CLR 417. This view would see the principle of s38 as being concerned with how much of a profit from an international sale of goods transaction was sourced in particular jurisdictions. Challoner and Collins went on to comment at p303, ‘The effect of s38 is that overseas manufacturing profit, i.e., the difference between the overseas manufactured cost and the wholesale purchase price, is not derived from a source in Australia.’

71 McGovern, above n 44, 9, para 64.


73 McGovern, above n 44, 8, para 59.
Shipping And Aircraft Profits

3.49 Australia, in negotiating the 1946 UK Treaty, had argued strongly but unsuccessfully against taxing shipping on a residence/place of registration basis. McGovern described the US representatives as being persistent in pressing for a similar article to the one in the 1946 UK Treaty and took this as illustrating the importance to the US of taxing shipping and aircraft profits on a residence basis. In McGovern’s view, even if the US negotiators could be persuaded to tax these profits on a source basis, the US Congress would ‘almost certainly’ decline to ratify the treaty.\(^74\)

3.50 McGovern reported that, while he had pressed the US representatives to have regard to the fact that, as Australia had no ships trading with the United States, the proposal would merely benefit the US at the expense of Australia, he admitted that residence basis taxation of shipping and aircraft profits had now become so common as to have become traditional. He could see no prospect of obtaining a treaty which did not concede a residence basis for the taxation of these profits.\(^75\) The resultant annual loss of revenue to Australia was estimated to be £100,000.\(^76\) McGovern’s position is an early example of Australia reluctantly modifying its preference for source based taxation in response to developing international practice.

Concessional Rate Of Tax On Dividends

3.51 In 1952 Australia still taxed dividends paid to non-residents on an assessment basis at the then current rate of 35%. Taking into account the special levy of 10%, the Australian tax rate on non-private companies was 45%. In the 1946 UK Treaty with the UK, Australia had agreed to exempt from Australian tax dividends paid by wholly owned subsidiaries and to reduce its tax rate on other dividends paid to UK residents by 50%.\(^77\) Hence in 1952 the rate of Australian tax payable on dividends paid by Australian companies, other than wholly owned subsidiaries, to UK residents was 17.5%.\(^78\)

3.52 In negotiations, the US argued for a 5% limit on source country taxation of dividends paid by 95% Australian subsidiaries to their US parents. Australia successfully argued for a uniform 15% source country tax rate on all dividends.

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\(^74\) McGovern, above n 44, 9, para 67.
\(^75\) McGovern, above n 44, 9–10, para 68.
\(^76\) McGovern, above n 44, 10, para 69.
\(^77\) See the discussion at 2.90.
\(^78\) McGovern, above n 44, 10, para 76.
One of the arguments put by Australia was that differential rates in the parent – 95% subsidiary situation would discourage US companies from proposals for joint participation with Australian residents in Australian companies.\textsuperscript{80}

McGovern commented that a uniform rate on all dividends flowing from Australia to the US would mean that US–Australian ventures could operate without the US shareholders suffering taxation disadvantages.\textsuperscript{81} This was because the US corporate tax at the time was 52% but was increased to 55.7% when a subsidiary paid a dividend to its parent, although the rate was reduced to 54% if both companies elected to file a joint return.\textsuperscript{82}

The combined effect of the Australian corporate rate of 45% and the treaty rate of 15% on dividends was an overall Australian tax rate on dividends flowing from a subsidiary to a parent company of 53.25%.\textsuperscript{83} In these circumstances, the effect of the US indirect foreign tax credit was that very little additional US tax was payable when an Australian subsidiary paid a dividend to its US parent. McGovern noted that prior to recent rate increases, when the corresponding Australian rate had been approximately 54%, there had been a substantial flow of US capital to Australia.\textsuperscript{84}

McGovern understood that the US had not previously agreed to a rate of 15% on parent–subsidiary dividends.\textsuperscript{85} In McGovern’s view, if Australia had not agreed to the 15% rate or had obtained a higher rate of source taxation of dividends, the treaty with the US could have had little or no beneficial effect on capital investment in Australia.\textsuperscript{86} Imposing a uniform rate of 15% on dividends was clearly perceived to be a key benefit of the treaty by promoting US non-portfolio investment without creating the ‘Treasury effect’.\textsuperscript{87}

\textsuperscript{79} McGovern, above n 44, 10–12 in particular paras 77 and 90.
\textsuperscript{80} McGovern, above n 44, 11, para 84.
\textsuperscript{81} McGovern, above n 44, 11, para 85.
\textsuperscript{82} McGovern, above n 44, 11, para 80.
\textsuperscript{83} McGovern, above n 44, 11, para 81.
\textsuperscript{84} McGovern, above n 44, 11, para 82.
\textsuperscript{85} McGovern, above n 44, 12, para 90.
\textsuperscript{86} McGovern, above n 44, 12, para 92.
\textsuperscript{87} What was described as the ‘Treasury effect’ exists when a source country reduces its rate of tax below the rate of tax in the residence country when the residence country uses a foreign tax credit system for preventing international juridical double taxation. In these circumstances, the foreign tax credit system will mean that residence country tax equal to the excess of the residence country rate over the reduced source country rate will be payable by the investor. This means that the benefit of the reduction in
3.56 Reduction in source taxation on all dividends paid to the US would have a revenue cost, which McGovern estimated at £1,000,000 per annum, but this compared favourably with the revenue cost of £1,650,000 that would have applied if the rates on dividends in the 1946 UK Treaty had been followed.

*Undistributed Profits Tax*

3.57 Article VIII stated that the Australian undistributed profits tax on private companies was the amount that would have been assessable if Articles VI(1) and VII(1) (which imposed limitations on source taxation of dividends) had not been included in the treaty. An equivalent provision had been included in the 1946 UK Treaty. McGovern pointed out that undistributed profits tax in 1952 was calculated as though the undistributed profits were distributed as dividends. Hence the article meant that the reductions in source taxation of dividends in Articles VI and VII did not operate to reduce the undistributed profits tax payable at source. McGovern commented that the sole purpose of Article VIII was to protect Australian revenue.

3.58 At the time, the US also imposed an accumulated earnings tax on corporations (other than personal holding companies, foreign personal holding companies and tax exempt corporations), imposed an undistributed profits tax on personal holding companies and included a share of the income source country tax below the residence country rate has flowed to the Treasury of the residence country rather than to the investor.

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88 McGovern, above n 44, 11, para 87.
89 McGovern, above n 44, 11, para 88.
90 See the discussion at 2.109 to 2.114.
91 McGovern, above n 44, 12, paras 94–6. Undistributed profits tax was amended by the *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, the Bill for which was introduced into Parliament on 18th September 1952. The effect of the amendments was that from the year ending 30 June 1952, Part III Division 7 of the *ITAA 1936* imposed tax on the undistributed profits of private companies after allowing a deduction of a retention allowance. For the 1951–52 year, undistributed profits tax was levied at a flat rate of 10/- in the £ or 50%. Undistributed profits tax as it applied in the 1951–52 year of income is discussed in N E Challoner and C M Collins, above n 20, 725–79. At the time McGovern was writing, the rate of undistributed profits tax on private companies was based on the tax that would have been payable by its shareholders if a distribution had been made. Hence the drafting of Article VIII reflects a concern which would have applied prior to the 1951–52 year, namely that, as the rate of tax was based on the tax that would have been payable if a dividend distribution had been made, the limitations on source taxation of dividends in Articles VI and VII of the treaty would have applied to undistributed profits tax in the absence of Article VIII. Undistributed profits tax on private companies as it applied prior to the 1951–52 year is discussed in J A L Gunn, O E Berger, J M Greenwood and R E O'Neill, *Gunn's Commonwealth Income Tax Law And Practice* (Butterworth & Co (Australia), 2nd ed, 1948) 1212. As noted at 3.11, undistributed profits tax on public companies had been repealed in 1951.
of foreign personal holding companies in the gross income of their US shareholders. While these taxes were calculated on a different basis to the Australian undistributed profits tax, they reflected a shared understanding between Australia and the US of problems in classical corporate-shareholder tax systems associated with the avoidance of shareholder tax through accumulations of profit at the corporate level.92

*Culture Royalties And Industrial Royalties*

**3.59** The treatment of royalties differed from that in the 1946 UK Treaty and provides an example of Australia arguing that the treatment in the earlier treaty should be distinguished. Initially, the US had argued for residence taxation of all royalties including industrial royalties.93 Australia had agreed to taxation of cultural (other than film) and industrial (but not mineral) royalties on a residence basis in the 1946 UK Treaty.94 McGovern estimated that taxing all royalties on a residence basis in the Australia–US context would have produced an annual Australian revenue loss of £350,000.95

**3.60** Australia distinguished the 1946 UK Treaty because UK businesses, unlike US businesses, did not frequently exploit their patents by granting licences to Australian residents. As a result, no great Australian revenue loss had resulted from the royalty article in the 1946 UK Treaty. The Australians had

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92 US accumulated earnings tax, undistributed profits tax on personal holding companies and the treatment of undistributed profits of foreign personal holding companies as they stood at this time are discussed in Boris I Bittker, *Federal Taxation of Corporations and Shareholders* (Federal Tax Press, 1st ed, 1959) ch 6. Liability for accumulated earnings tax depended on a finding that the corporation was formed for the purpose of avoiding income tax on its shareholders by accumulating earnings rather than distributing them as dividends. That earnings and profits were allowed to accumulate beyond the ‘reasonable needs of the business’ was determinative of this purpose unless the corporation proved the contrary through a preponderance of evidence. Accumulated earnings tax was imposed at the rate of 27.5% on the first $100,000 of accumulated income and at the rate of 38.5% on accumulated income above $100,000. Accumulated income was defined as the corporation’s taxable income minus the dividends paid deduction and an accumulated earnings credit under which a corporation was permitted to accumulate $100,000 during its lifetime. Undistributed profits tax on personal holding companies was imposed at the rate of 75% on the first $2000 of the company’s undistributed personal holding company income and at the rate of 85% thereafter. A company’s undistributed personal holding company income was its taxable income less dividends paid and some other adjustments. Companies were able to pay dividends after their undistributed personal holding company tax liability had been determined and to then obtain a refund of the tax paid. US shareholders in foreign personal holding companies included their proportionate share of the undistributed profits of the foreign personal holding company in their gross income.

93 McGovern, above n 44, 15, para 124.

94 See the discussion at 2.90.

95 McGovern, above n 44, 15, para 124.
pointed out to the US delegation that a £350,000 per annum revenue loss was likely to be far in excess of what the Australian government was willing to concede.\footnote{McGovern, above n 44, 16, para 125.} When pressed, the US delegation withdrew their insistence on residence basis taxation of industrial royalties but continued to insist on residence basis taxation for cultural royalties.\footnote{McGovern, above n 44, 16, para 126.} Hence Australia could continue to tax industrial royalties on a source basis while the US would give a foreign tax credit for the Australian tax thus bearing the cost of relieving international juridical double taxation.\footnote{McGovern, above n 44, 16, para 127.}

3.61 McGovern estimated the Australian revenue cost of taxing cultural royalties in the Australia–US context on a residence basis as being £50,000 per annum.\footnote{McGovern, above n 44, 16, paras 127–128.} As the country in which the creator of a cultural work resided was normally the country in which the cultural work was performed, in McGovern’s view, taxation of cultural royalties on a residence basis was ‘not unduly divergent in principle’ from taxation of the income on a source basis.\footnote{McGovern, above n 44, 16, paras 128 and 129.}

3.62 Article VIII did not apply where a resident of one of the countries carried on business through a permanent establishment in the other country. Nor, consistently with the 1946 UK Treaty, did the article apply to royalties and other payments relating to motion picture films.\footnote{McGovern, above n 44, 16, para 131.}

Mineral Royalties

3.63 Article XII taxed royalties for minerals and other natural resources on a source basis. No article in the 1946 UK Treaty dealt with mineral royalties. McGovern considered that, under that treaty, such income could be taxed by the source country with the residence country giving a foreign tax credit to relieve double taxation.\footnote{McGovern, above n 44, 16, para 132.} The main function of Article XII was to ensure that the country of source only levied tax on a net basis on mineral royalties.\footnote{McGovern, above n 44, 16, para 134.} At the time, Australia taxed royalties on a net basis,\footnote{McGovern, above n 44, 16, para 135.} but the US imposed a

\footnote{McGovern, above n 44, 17, para 136. In 1952, s26(f) of the \textit{ITAA 1936} included ‘any amount received as or by way of royalty’ in a taxpayer’s assessable income. Jurisdictional limits were not expressly stated in s26(f). Expenses relevant to the derivation of royalty income were allowable as deductions under s51(1) of the \textit{ITAA 1936}. Although no withholding tax applied to payments of royalties to non-residents}
30% gross basis withholding tax on rents and royalties. Article XII permitted Australian residents deriving mineral royalties from the US to continue to be taxed on a 30% gross withholding tax basis or to lodge a return claiming expenses and to have tax imposed at a rate appropriate to the net income. McGovern commented that the article favoured Australia and was considered satisfactory.

**Tax Credits**

3.64 Article XVI obliged the residence country to allow a foreign tax credit in respect of income derived in the source country. The limit of the credit was the lower of the tax in the source country or the tax payable in the residence country. McGovern commented that the article corresponded, in principle, with the equivalent article in the 1946 UK treaty, but there were significant differences in the drafting due to differences in the taxing codes of the countries concerned.

3.65 The US proposed to allow such credits as its own laws in operation as at the date of signature permitted. McGovern commented that this would ensure that the US would not in the future impose a less favourable basis for granting credits for Australian tax. McGovern also pointed out that ‘Article XXI would require the US to allow any liberalized basis of credit which it may adopt in the future.’

3.66 McGovern commented that, as Article XVI would not apply where income was taxed in only one of the countries, Australia would not allow a credit for exempt foreign source income as no double taxation would, in fact, exist. Hence the article would have little or no effect on Australian revenue, except in the case of dividends received by individuals who received a foreign tax

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under *ITAA 1936* s256(1), the Commissioner could require the payor to retain an amount from the royalty in respect of tax due or which might become due by the non-resident. Section 256(1) as it applied in 1952 is discussed in N E Challoner and C M Collins, above n 20, 1365.

105 McGovern, above n 44, 17, para 137.
106 McGovern, above n 44, 17, para 138.
107 McGovern, above n 44, 17, para 139.
108 McGovern, above n 44, 18, para 151.
109 McGovern, above n 44, 18, para 152.
110 McGovern, above n 44, 18, para 152. Article XXI of this draft read as follows:

‘The provisions of this Convention shall not be construed to restrict in any manner, any exemption, deduction, credit or other allowance now or hereafter accorded by the laws of one of the Contracting States in the determination of the tax payable in that State.’

111 McGovern, above n 44, 18, para 154.
credit under *ITAA 1936* s45, but it would bind the US to continue to allow credits thus reducing taxation deterrents to overseas investment by US residents and corporations.\(^{112}\)

3.67 Article XVI also contained source rules for remuneration for services and rules which deemed film profits and profits from insurance with non-residents that were taxed in Australia under specific provisions to have an Australian source. Both source rules were consistent with the 1946 UK Treaty. McGovern commented that the former rule would assist in the application of the credit provisions,\(^{113}\) and that the latter rule was inserted because of Australia’s representations. The latter rule would ensure that the US granted an appropriate credit for Australian tax assessed under the specific provisions and placed no obligations on Australia.\(^{114}\)

3.68 McGovern considered that the credit provisions as they applied to undistributed profits tax were not entirely satisfactory.\(^{115}\) Australian undistributed profits tax would be credited against US tax on the profits of the company. In situations where Australia would be levying corporate tax and undistributed profits tax, the overall limitation on the US foreign tax credit might mean that the full amount of the Australian tax paid would not be allowed. When profits which had been subject to undistributed tax were distributed as a dividend Australia did not, in effect, tax the dividend and hence the US would tax the whole of the dividend without allowing any credit.\(^{116}\)

3.69 In McGovern’s view undistributed profits tax was, in effect, a substitute for the tax on the ultimate dividend. Hence Australia had argued that the US should so treat it in granting credits. The US delegation had not conceded the point, but it was known that Canada was pressing the US on ‘an almost identical matter’. McGovern did not consider that the issue would justify holding up the treaty, but if there were to be further discussions, then it might be appropriate to reopen the issue with a view to reversing the US attitude.\(^{117}\)

*Reciprocal Collection Of Taxes*

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\(^{112}\) McGovern, above n 44, 19, para 158.

\(^{113}\) McGovern, above n 44, 18, para 155.

\(^{114}\) McGovern, above n 44, 18, para 156.

\(^{115}\) McGovern, above n 44, 19, para 159.

\(^{116}\) McGovern, above n 44, 19, para 160.

\(^{117}\) McGovern, above n 44, 19, para 161.
3.70 Article XVII required each country to collect on behalf of the treaty partner taxes due because of incorrect allowance of a concession provided for in the treaty. McGovern considered that the issue would arise principally in relation to the concessional rate of tax of 15% on dividends under the treaty. A Canadian resident could, in the absence of the article, take advantage of this concession by having the dividend paid to an address care of a US bank or sharebroker and pay Australian tax at the treaty rate of 15% instead of paying Australian tax as high as 35% on dividends received. In converse circumstances the US would suffer the loss of revenue. McGovern characterised the article as an ‘acknowledgment of a principle’ and recognised that its expression and its means of implementation might raise a number of legal difficulties which would require its revision.

No equivalent article had been included in the 1946 UK Treaty and the UK had successfully resisted US requests for the inclusion of an equivalent provision in the 1945 US – UK Tax Treaty.

Exchange Of Information

3.71 Article XVII was an exchange of information article. McGovern commented that no information which would disclose a trade secret or trade process could be exchanged, and that the secrecy provisions of each country would prohibit disclosure of information obtained from the other country. An identical provision had been included in the 1946 UK Treaty and McGovern regarded it as being required for the satisfactory operation of any treaty that might be entered into with the United States.

3.72 It is interesting that neither Australia nor the US appears to have pressed for a broader exchange of information article. The US had originally wanted a broader article in its 1945 treaty with the UK, and Australia in negotiating the 1946 UK Treaty had unsuccessfully sought to extend the purposes for which information could be exchanged but had successfully broadened the persons to whom disclosure could be made. As Australia had eventually

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118 McGovern, above n 44, 19, para 163.
119 McGovern, above n 44, 19, paras 165 and 166.
121 McGovern, above n 44, 19–20, para 167.
122 McGovern, above n 44, 20, para 168.
123 See the discussion in Avery Jones above n 120, 237–9.
124 See the discussion at 2.140 and 2.142.
come to the conclusion in the 1946 negotiations that the provision was adequate for its needs, it possibly decided to not press for any change from the article. It is also notable that, while the article appears to have been regarded as normal and required, there is no indication in any of the correspondence that it was regarded as being one of the key benefits of a taxation treaty.

Other Provisions

3.73 Article XIX was the equivalent of what is now the Mutual Agreement article in the OECD Model Treaty. McGovern indicated that Article XIX had been requested by the US delegation, who regarded it as a ‘desirable gesture to taxpayers’. Article XX authorised the taxation authorities in the two countries to consult directly with each other (as opposed to consultation at the taxpayer’s request) for the purpose of giving effect to the treaty. Notwithstanding the absence of an equivalent article in the 1946 UK Treaty, communication had taken place and was considered to be essential for the smooth carrying out of the obligations under that treaty. In McGovern’s view, the article was not essential but was considered desirable. Article XXI provided for the continuation of exemptions, deductions, credits and other allowances, and in the event that more liberal provisions were introduced into either country’s domestic law, for the new provisions to apply. McGovern commented that the article would have little effect on Australia but was considered desirable in relation to tax credits granted by the United States.

The Australian Cabinet Decision

3.74 On 3rd June 1952 the draft treaty was submitted to the Australian Cabinet, which decided:

(a) that the Government should enter into agreements with the US of America for the relief of double taxation by the two countries in respect of income tax, estate duty and gift duty;

(b) that the proposals outlined in the Treasurer’s submission and in the supporting documents should be the basis of the agreements with the United States.

125 McGovern, above n 44, 20, para 170.
127 McGovern, above n 44, 20, para 177.
The supporting documents included McGovern’s memorandum to the Treasurer dated 15th April 1952.\textsuperscript{128}

**The Australian Second Draft Treaty**

3.75 McGovern sent the first draft of the treaty to the Deputy Commissioners in each Australian State.\textsuperscript{129} Extensive written comments were made by each Deputy Commissioner.\textsuperscript{130} In March 1952 a memorandum titled ‘Australia–US Draft Income Tax Agreement – Matters Requiring Attention’ (hereafter referred to as ‘the Memorandum’) was prepared in Canberra, evidently by the ATO Central Office.\textsuperscript{131}

3.76 McGovern advised Fadden on 21st November 1952 that an Australian review of the draft had disclosed that a ‘considerable number of detailed matters will require further consideration’. McGovern regarded the more important of these as relating to: (a) credits; (b) the rate of tax on dividends; (c) collection of tax; (d) shipping and aircraft profits; and (e) Governmental remuneration.\textsuperscript{132} There were also ‘some 30 to 40 matters of detail’ on which McGovern considered further face to face negotiation would be desirable.\textsuperscript{133}

3.77 McGovern recommended advising the US that Australia would sign a treaty on the broad lines agreed at the meeting in Canberra in March 1952 and would be willing to have the remaining matters discussed between officials to prepare a document to be dealt with as early as practicable in the new year. McGovern suggested that Fadden point out that senior Australian taxation officials would be visiting Canada in about April 1953 and that it would be possible for them to have negotiations in Washington either before or after that.\textsuperscript{134}

\textsuperscript{128} The terms and date of the Cabinet resolution are set out in McGovern to Fadden 21st November 1952, ATO file, Pt 4, p1. Copies of the Cabinet submission are contained in NAA, ATO file, Pt 3, and in NAA, External Affairs file, Pt 4.

\textsuperscript{129} This was consistent with McGovern’s practice during the negotiation of the 1946 UK Treaty, as discussed in Chapter 2.

\textsuperscript{130} This correspondence is contained in NAA, ATO file, Pt 3.

\textsuperscript{131} NAA, ATO file, Pt 3, 94–9. In the footnotes this document is hereafter referred to as ‘Strictly Confidential’.

\textsuperscript{132} McGovern, above n 128, 1–4.

\textsuperscript{133} McGovern, above n 128, 4.

\textsuperscript{134} McGovern, above n 128, 4–5.
McGovern then wrote to the Commonwealth Solicitor General (Kenneth Bailey) requesting that the draft be examined, and invited comments on legal and drafting aspects which might require further consideration.\(^{135}\)

A second, undated, draft of the treaty was then prepared in Australia. The draft also included comments (evidently by the drafter) on the changes that had been made from the first draft.\(^{136}\) Only those comments relevant to the questions examined in this thesis will be discussed here.

**Article II – Interpretation**

Several significant changes were made to this article.

‘resident of Australia’ and ‘Australian resident’

A definition of ‘resident of Australia’ was not included in the first draft. The definition in the second draft was that the term ‘has the meaning which it has under the laws of Australia relating to Australian tax’. The definition was identical to the definition of ‘resident of Australia’ in the 1946 UK Treaty.\(^{137}\) The drafter commented that the definition was included ‘to ensure that it has the same meaning as in Commonwealth income tax law’.\(^{138}\) As was the case with the 1946 UK Treaty, the term ‘Australian resident’ was separately defined, although slightly more concisely than in that treaty, in terms which

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\(^{135}\) McGovern to Bailey, 24th November 1952, NAA, ATO file, Pt 4. Bailey’s reply indicated that he had arranged for H F E Whitlam, who had been involved in drafting the 1946 Treaty with the UK and who was still a consultant to the Department, to take primary responsibility for examining the treaty from a legal viewpoint. Whitlam would be available for discussions with officers of the ATO and would confer with the Parliamentary Draftsman and the Crown Solicitor. Bailey also indicated that he would personally be available for consultation at any time. Bailey to McGovern, 25th November 1952, NAA, ATO file, Pt 4.

\(^{136}\) The correspondence from Bailey to McGovern, discussed in the text accompanying above note 135, would indicate that H F E Whitlam was primarily responsible for commenting on the first draft from a legal and drafting viewpoint. It is not clear, however, that Whitlam made the actual drafting changes in the second draft. Clearly, the principal assistant parliamentary draftsman C Comas drafted Article XVII of the second draft because Comas sent J Q Ewens (the Parliamentary Draftsman) a memorandum dated 1st April 1953 on a draft of Article XVII that he had prepared following a conference between Comas, Ewens, D D Bell (the Crown Solicitor) and Mr Belcher (the Assistant Commissioner of Taxation). The draft of Article XVII attached to the memorandum is identical with Article XVII in the second draft of the treaty. The memorandum and draft Article XVII are contained in NAA ATO file, Pt 4. The second draft is also contained in NAA, ATO file, Pt 4. Hereafter, the second draft will be referred to as ‘the second draft’ and references will be given to page numbers within the second draft itself.

\(^{137}\) See the discussion at 2.149 and 2.150.

\(^{138}\) Second draft, drafter’s comments, p6. The drafter also commented that this meant it was practicable to omit the words ‘for the purposes of Australian tax’ at a number of points in the treaty. Second draft, drafter’s comments, p6.
excluded persons who were residents of the US for treaty purposes. Hence, under the second draft, as was the case with the 1946 UK Treaty, a dual resident could not be an ‘Australian resident’ (or, for that matter, a ‘US resident’) but could be a ‘resident of Australia’.

‘Industrial or Commercial Profits’

3.82 The definition of ‘industrial or commercial profits’ in the second draft expressly excluded ‘income from the operation of ships or aircraft’. Income in the form of dividends, interest, rent, royalties, management charges, or remuneration for personal services had been excluded from the definition in the first draft. Capital gains were not expressly excluded from the definition in either draft.

3.83 The drafter commented that the exclusion of income from the operation of ships or aircraft from the definition was ‘in order to ensure that Article III (Industrial or Commercial Profits) does not apply to those profits’. Article V of the second draft provided for exclusive taxation of shipping and aircraft profits on a residence basis. The exclusion of such profits from the definition of ‘industrial or commercial profits’ was aimed at simplifying the drafting of Article V, but both the exclusion and the original drafting of Article V reflected a concern that, in the absence of express exclusions, shipping and aircraft profits could be taxed as part of industrial or commercial profits despite the exclusive residence basis of taxation adopted in Article V.

‘Permanent Establishment’

3.84 The second draft changed the wording ‘or the use of substantial equipment or machinery’ to ‘a place where or in the locality of which— (i) operations involving the use of substantial equipment or machinery are conducted; or (ii) substantial equipment is installed for the purposes of a contract’. The drafter’s comment on this change was merely, ‘expression “use of substantial equipment” expanded and broadened’.  

3.85 The memorandum of March 1952 indicates that another consideration motivating the change referred to in 3.84 was that ‘a US company may fulfil a contract to erect, say, a powerhouse, by having machinery manufactured in or delivered to Australia and then installing it’. The Memorandum noted that the

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139 See the discussion at 2.143.
140 Second draft, drafter’s comments, p6
141 Second draft, drafter’s comments, p6.
US company would not make ‘use’ of the plant and hence might not have a permanent establishment in Australia under the first draft. This explains the express reference to substantial equipment being ‘installed’ in the second draft.

**Article III – Industrial or Commercial Profits**

3.86 The second draft made four changes to the Industrial or Commercial Profits article. Paragraphs (1) and (2) were redrafted so that ‘profits’ rather than the entity that made them were exempted. The drafter commented, ‘This accords with the U.K.– Australia agreement and with the Commonwealth income tax law, which exempts income, not businesses.’

3.87 Paragraphs (1) and (2) were amended so that the reference to a permanent establishment being 'situated therein' now referred, in paragraph (1), to a permanent establishment ‘in the United States’ and, in paragraph (2), to a permanent establishment ‘in Australia’. The drafter commented, ‘It is not desired to imply that a permanent establishment needs to be situated at one site.’

3.88 The proviso to paragraph (3) was transferred to Article XXI. The purpose of the transfer was to ensure that Article XI (dealing with royalties other than film royalties) would not interfere with the application of ITAA 1936 (Cth) Part III Division 14 (films). The proviso became paragraph (b) of Article XXI, which read as follows:

The provisions of this Convention shall not –

(a) be construed as restricting in any manner any exemption, deduction, credit or other allowance now or hereafter accorded by the laws of one of the Contracting States in the determination of the tax payable in that State; or

(b) affect the operation of Divisions 14 and 15 of Part III of the Australian Income Tax and Social Services Contribution Assessment Act 1936–1953 (or that Act as amended from time to time) relating to film business controlled abroad and insurance with

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143 Second draft, drafter’s comments, p8.
144 Second draft, drafter’s comments, p8.
145 Second draft, drafter’s comments, p8.
non-residents, or the corresponding provisions of any statute substituted for that Act.

3.89 The fourth change concerned the saving provision in paragraph (5) of the article preserving the operation of discretionary powers in domestic law which applied in non-arm’s length transactions where information was insufficient to determine the profit of a permanent establishment. The change omitted the words ‘in accordance with the foregoing provisions of this Article’. The drafter merely commented that the omitted words were not included in the 1946 UK Treaty.\(^{146}\)

**Article IV – Inter-Connected Companies/Associated Enterprises**

3.90 The second draft amended the deemed source rule in the inter-connected companies article. In the first draft, the deemed source rule was:

(2) Profits included in the profits of an enterprise of one of the Contracting States under paragraph (1) of this Article shall, unless contrary to the laws of that Contracting State, be deemed to be income derived from sources in that Contracting State and shall be taxed accordingly. [Emphasis added]

In the second draft, paragraph (2) of Article IV was replaced by:

(2) Subject to the provisions of Article XXI of this Convention, profits included in the profits of an enterprise of one of the Contracting States under paragraph (1) of this Article shall be subject to tax by that State as income of that enterprise.

(3) For the purposes of Article XVI (credits) of this Convention, profits taxed in accordance with this Article shall be deemed to be income derived from sources in the Contracting State which imposes that tax.

3.91 Both the Memorandum and the drafter’s comments indicate that the US pressed for the words ‘unless contrary to the laws of that Contracting State’ to be retained.\(^ {147}\) The US gave the example of a US parent company with an Australian subsidiary which traded both in Australia and NZ. If Article IV applied, Australia would tax the adjusted profits, which in the absence of the

\(^{146}\) Second draft, drafter’s comments, p8. The drafting of the corresponding saving provision in the 1946 UK Treaty was discussed at 2.115 to 2.126.

\(^{147}\) Second draft, drafter’s comments, p10; Strictly Confidential, p3.
words ‘unless contrary to the laws of that Contracting State’ would be deemed to have an Australian source. However, NZ might also tax the same amount and, the drafter commented, in equity *ITAA 1936* (Cth) s23q should have applied but could not because the adjustment would be deemed to be Australian source income.\(^{148}\)

3.92 The drafter’s comments on the redraft regarded the words ‘unless contrary to the laws of the Contracting State’ as nullifying the whole paragraph, and indicated that the proposed amendments aimed to ensure that Australia had the right to tax the adjusted income and deemed it to have an Australian source when it had not been taxed in the country of origin.\(^ {149}\) The operation of the deemed source rule was confined to the credit provisions.

*Article VII – Dividends*

3.93 The drafter indicated that a policy issue requiring resolution was whether the 15% tax envisaged should be on gross dividends, on dividends included in taxable income, or on gross dividends less direct deductions and a proportion of concessional deductions. The same question had been raised by the ATO Memorandum, which argued that ‘The present Australian method of determining the tax payable is to have different rates of tax on various income brackets. Article VII should not specify a maximum rate of 15% and so leave a lower rate to be charged on the lower income brackets – that is, it should be an overall rate not exceeding 15%.’\(^ {150}\) The comment reflects the fact that Australia still assessed dividends paid to non-residents on a net assessment basis, not on a gross withholding basis.

*Article VIII – Australian Undistributed Profits Tax*

3.94 The second draft made no substantive changes to this article, but the drafter and the Memorandum commented that, as Australian undistributed profits tax was now at a flat rate, the article had become redundant.\(^ {151}\) The drafter commented that retention of Article VIII could only be justified as protection against [sic] a possible return to the previous method of assessing

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\(^{148}\) Second draft, drafter’s comments, p10 and Strictly Confidential, p3.

\(^{149}\) Second draft, drafter’s comments, p10.

\(^{150}\) Second draft, drafter’s comments, p12 and Strictly Confidential, p4.

\(^{151}\) Second draft, drafter’s comments, p12 and Strictly Confidential, p4. The comments reflect the effect of amendments to undistributed profits tax enacted in 1952, as discussed above n 91.
undistributed profits tax based on the tax that shareholders would have paid if the undistributed profit had been distributed.\textsuperscript{152}

\textit{Article XI – Cultural Royalties}

3.95 The second draft completely redrafted the royalty article. The article in the first draft was:

Royalties for the right to use copyright of, or in respect of the right to produce or reproduce, any literary, domestic, musical or artistic work (but not royalties or other payments relating to motion picture films) derived from sources within one of the Contracting States by a resident of the other Contracting State not engaged in trade or business in the former State through a permanent establishment, shall be exempt from tax by the former State.

The article in the second draft was:

Royalties (not being royalties in relation to motion picture films or the reproduction by any means of images or sound produced directly or indirectly from those films) for the use, production or reproduction of, or the privilege of using, producing or reproducing a literary, dramatic, musical or artistic work in which copyright subsists shall, if derived from sources within one of the Contracting States by a resident of the other Contracting State not engaged in trade or business in the former State through a permanent establishment in that State, be exempt from tax in the former State.

The drafter commented that it was inappropriate to refer to royalties for the right to use copyright or the right to produce or reproduce. The drafter noted that the right to tax under Part III Division 14 of \textit{ITAA 1936} (Cth) was preserved by Article XXI, and pointed out that the redrafted article aimed to make it clear that film royalties were not exempt from source basis taxation. An attempt had been made, presumably by the inclusion of the clause ‘or the reproduction by any means of images or sound produced directly or indirectly

\textsuperscript{152} Second draft, drafter’s comments, p12.
from those films’ to cover royalties relating to the adaption of films for television purposes, but the drafter indicated that the matter was still being looked into.\textsuperscript{153}

\textit{Article XVI – Credits}

\textbf{3.96} The second draft substituted a new opening clause in paragraph (2) for the original paragraph (2). The original opening clause in paragraph (2) read:

\begin{quote}
(2) Subject to provisions in force in Australia on the date of signature of this Convention and to such provisions (which shall not affect the general principle hereof) as may be enacted in Australia,
\end{quote}

The new opening clause read:

\begin{quote}
(2) Subject to any provisions of the law of Australia which may from time to time be in force and which –

(a) relate to the allowance of a credit against Australian tax of tax payable outside Australia; and

(b) do not affect the general principle of this paragraph.
\end{quote}

The drafter commented that in the original draft the granting of the credit was subject to existing Australian credit provisions, including \textit{ITAA 1936} (Cth) s45, even if such provisions were contrary to the general principle of the credit article. Section 45 conflicted with the principle of the credit article because s45 would not allow credit for US tax paid by an Australian resident on a dividend paid by a US company out of Australian source profits.\textsuperscript{154} Section 45 only allowed a credit for foreign tax paid where the whole or part of the dividend was paid out of ex Australian source profits. Where part was paid from ex Australian source profits, the credit was the amount which bore the same proportion to the credit otherwise allowable as the ex Australian source profits bore to the total profits of the paying company.\textsuperscript{155} The drafter commented that the redraft would not permit the application of any Australian provision which affected the general principle of the credit article.

\begin{flushright}
\textsuperscript{153} Second draft, drafter’s comments, p16.
\textsuperscript{154} Second draft, drafter’s comments, p18.
\textsuperscript{155} See the discussion of s45 in 1953 in N E Challoner and C M Collins, above n 20, 336.
\end{flushright}
3.97 The drafter went on to list the following points for further discussion with US officials:

(a) allowance of Division 7\textsuperscript{156} (undistributed profits) tax in US assessments of US shareholders;

(b) allowance of credit by the US for tax paid under s125 (dealing with interest paid by a resident company to a non-resident\textsuperscript{157}) with credit being allowed to US residents entitled to the interest which had been taxed under s125;

(c) the basis for allowing credit for provisional tax.\textsuperscript{158}

Crediting Division 7 tax had been raised at the earlier discussions in Canberra with US officials, and the drafter noted that the US was unlikely to concede this point.\textsuperscript{159}

*Article XVII – Assistance In Collection*

3.98 The Assistance in Collection article in the original draft read as follows:

‘Each Contracting State shall collect on behalf of the other Contracting State an amount, due to that other State in relation to taxes which are the subject of this Convention, sufficient to ensure that an exemption or reduced rate of tax granted under this Convention shall not be enjoyed by persons not entitled thereto.’

The second draft proposed to substitute the following for the original article:

‘Each of the Contracting States may collect such amounts in respect of taxes, which are the subject of this Convention, imposed by the other Contracting State as are sufficient to ensure that an exemption or reduced rate of tax granted under this Convention by that other

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\textsuperscript{156} See the discussion of Australian undistributed profits tax above n 91.

\textsuperscript{157} For a discussion of s125 in 1953 see N E Challoner and C M Collins, above n 20, 869–80.

\textsuperscript{158} Second draft, drafter’s comments, p18.

\textsuperscript{159} Second draft, drafter’s comments, p18.
Contracting State shall not be enjoyed by persons not entitled to that benefit.'

Australia had previously indicated to the US officials that, from Australia’s perspective, the original article might need to be redrafted completely and that its form might need to be determined ‘in the light of constitutional questions and the need, if any, of Australia to give effect to the article by legislation’. The drafter pointed out that the redrafted article was not mandatory. This was evident by the substitution of the word ‘may’ for ‘shall’ in the first line. It is also notable that the redraft omits the phrase ‘due to the other State’ and instead refers to taxes, the subject of the treaty, which are ‘imposed by the other State’. The change of wording would appear to be to avoid an implied admission that the taxes referred to were actually due to the other State.

**Article XXI – Savings Provision**

3.99 The second draft amended this article to read:

The provisions of this Convention shall not –

(a) [as per the original draft]; or

(b) affect the operation of Division 14 and 15 of Part III of the *Australian Income Tax and Social Services Assessment Act 1936–1953* (or that Act as amended from time to time) relating to film business controlled abroad and insurance with non-residents, or the corresponding provisions of any statute substituted for that Act.

The drafter commented that a proviso from Article III(3) had been transferred to Article XXI to ensure that neither Article III(3) nor Article XI would impinge on Division 14.

3.100 The drafter also commented that paragraph (a) might cause Article IV (dealing with inter-connected companies) to be ineffective except to permit *ITAA 1936 s136* to continue to operate. The drafter’s reasoning was that

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160 This is consistent with the view expressed in N E Challoner and C M Collins, above n 20, 327, that under English Private International Law no action lies for the recovery of foreign taxes.

161 Second draft, drafter’s comments, p19.

162 Second draft, drafter’s comments, p21.

163 *ITAA 1936 s136* empowered the Australian Commissioner to determine the taxable income of a business carried on in Australia that was either: (a) controlled principally by non-residents; (b) carried on by a company in which the majority of shareholders were non-residents; or (c) carried on by a company which (directly or through
paragraph (a) might prohibit Australia from taxing any income which it did not now tax. The drafter's concern may have been that the absence of Australian tax under domestic law in the circumstances dealt with in Article IV(1), other than under s136, might be construed as an 'exemption' for the purposes of Article XXI(a). Alternatively, the drafter may have thought that the calculation of profit under domestic law in the absence of Article IV(1) and s136 may have involved a 'deduction' for the purposes of Article XXI(a).

3.101 In addition, the drafter commented that paragraph (a) in conjunction with Article IV(2) as revised might require Australia to continue to apply the exemption in s23q (dealing with foreign source income of residents not exempt from tax in the source country) to the adjustments made in Article IV notwithstanding a subsequent repeal of s23q.

3.102 It appears that the drafter considered that a resident company that was an inter-connected company for purposes of Article IV might be able to argue that the s23q exemption should continue to apply in calculating its profit under Article IV(2) notwithstanding its subsequent repeal on the basis that the Convention could not be construed as restricting the operation of the existing exemption. Only in a determination and taxing the profit of the company on an arm's length basis (without taking into account the s23q exemption) under Article IV(2) could it be said that the Convention was restricting the exemption.

3.103 Notwithstanding these concerns, the drafter did not propose any changes to paragraph (a) of Article XXI.

The Negotiations In Washington, 1953

3.104 McGovern and King corresponded between 20th November 1952 and January 1953 to arrange a second round of negotiations to be held in Washington.

nominees) held the majority of the shares of a non-resident company. ITAA 1936 s136 is discussed in more detail at note 133 accompanying 2.115.

Second draft, drafter's comments, p21.

ITAA 1936 s23q exempted foreign source income (other than dividends) which was not exempt from tax in the source country.

Second draft, drafter's comments, p21.

ITAA 1936 s23q provided that income was exempt from tax where it was derived by an Australian resident from foreign sources provided it was not exempt from tax in the source country or where the Australian resident was liable to pay royalty or export duty in any foreign country in respect of any sale of goods from which the income was derived.
Eventually, following suggestions by King,\(^{168}\) arrangements were made for an Australian delegation comprising McGovern, Belcher and Bell to visit Washington, New York and Ottawa in March and April of 1953 to discuss the US and Canadian treaties and to attend the meeting of the United Nations Fiscal Committee. McGovern was given plenipotentiary powers to sign the treaties.\(^{169}\)

3.105 On 28\(^{th}\) April 1953, McGovern advised that the text of the treaties had been settled at Washington and that only formal steps in preparation of the documents for approval and signing remained to be completed.\(^ {170}\) The treaties were signed on 14\(^{th}\) May 1953 by Sir Percy Spender and Mr Bedell Smith.\(^ {171}\)

**The Final Version Of The Treaty**

3.106 The ATO file on negotiation of the treaty currently does not contain any document forwarding the second draft of the treaty to US officials. Nor does the file contain any account of the content of the negotiations. The author has been unable to locate any account of the content of the negotiations in files relating to the treaty in the US National Archives and Records Administration. Hence it is necessary to make inferences as to the content of the negotiations by comparing the final version of the treaty with the first and second drafts.

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\(^{168}\) King to McGovern, 23\(^{rd}\) January 1953 and King to P S McGovern, 19\(^{th}\) February 1953, NAA, ATO file, Pt 4.

\(^{169}\) Several items of correspondence in combination support the statements made in the text. These are: Fadden to Casey, 5\(^{th}\) March 1953; G A Jockel, for a Secretary, Department of External Affairs, Memorandum for Commissioner of Taxation, Department of the Treasury, 19\(^{th}\) March 1953; Copy, Casey to His Excellency Mr Pete Jarman, Ambassador of the US of America, Canberra, 12\(^{th}\) March 1953; McGovern to The Secretary, Department of External Affairs, 27\(^{th}\) March 1953; J Plimsoll (Acting Secretary) Memorandum for the Australian Embassy, Washington, 1\(^{st}\) April 1953; Copy Note, Department of External Affairs to Embassy of the US of America, 31\(^{st}\) March 1953; Cablegram, Department of External Affairs to Australian Embassy, Washington, 14\(^{th}\) April 1953. All of these documents are contained in NAA, ATO file, Pt 4.

\(^{170}\) Cablegram, Australian Consulate General, New York, for Mair, 28\(^{th}\) April 1953, NAA, ATO file, Pt 4. Mair was Acting Commissioner of Taxation at the time. Correspondence from Mair to the Commonwealth Treasurer on 29\(^{th}\) April 1953 indicates that the sender of the cable was McGovern.

\(^{171}\) ‘For Press, Embargo – Not for release before midnight Thursday, 14\(^{th}\) May 1953, Tax Convention With USA’, Cablegram, from Australian Embassy, Washington to Min & Dept EA, Treasury, Taxation, PM’s, 14\(^{th}\) May 1953; and Department of State, For the Press, No.261, Signing of Three Tax Conventions With Australia, 14\(^{th}\) May 1953. All these documents are contained in NAA, ATO file, Pt 4. Spender was Australian Ambassador to the US at the time and Bedell Smith was Acting US Secretary of State.
The following comparison will be confined to the articles previously discussed in this chapter.

Definitions

'Resident'

3.107 The definitions of ‘resident of Australia’ and ‘Australian resident’ and the definition of ‘US resident’ follow the second draft. As a consequence, the words ‘for the purposes of Australian tax’ were omitted at several points throughout the final version of the treaty.

'Industrial or Commercial Profits'

3.108 The change described at 3.83 to the definition of ‘industrial or commercial profits’ in the second draft was incorporated into the final version of the treaty.

'Permanent Establishment'

3.109 The stylistic changes to the ‘substantial equipment’ provision in the second draft were not found in the final version of the treaty, which corresponds with the first draft except that it refers to substantial equipment being ‘installed’. Thus, the final version of the treaty accommodated the principal concern about the substantial equipment provision expressed in the memorandum of March 1952.

Industrial Or Commercial Profits

3.110 The change described at 3.86 was not adopted in the final version of the treaty, which followed the first draft in this respect. The change described at 3.87 was adopted in the final version of the treaty. Presumably, the Australian argument mentioned in the drafter’s notes, namely to avoid an implication that a permanent establishment needed to be situated at one site, was effective here. Consistently with the second draft, the proviso to paragraph (3) was omitted and transferred to Article XX (the renumbered Article XXI). The change discussed at 3.89 was implemented by omitting the words, ‘in accordance with the foregoing provisions of this Article’.

3.111 The final draft differed from both the first and second drafts in that, understandably, the proviso to paragraph (3) which applied the principle
underlying s38 of ITAA 1936 was confined in its operation to determinations by Australia.

**Article IV – Inter-connected Companies**

3.112 The final version of the article differed from both the first and second drafts. Consistent with the second draft, the words ‘unless contrary to the laws of the Contracting State’ were omitted. The difficulty identified by the drafter in relation to paragraph (2) of the first draft, as discussed at 3.91, was dealt with by deleting the deemed source rule and by making the paragraph subject to Article XX, which preserved the operation of certain domestic law provisions.

**Article VII – Concessional Rate Of Tax On Dividends**

3.113 Paragraph (1) of Article VII (dealing with Australian tax on dividends) differed from both the first and second drafts by adding the words ‘of the dividend’ after ‘15 percent’. The addition only related to Australian tax on dividends and implies that the tax would be 15% of the gross dividend thus resolving one of the questions raised in the Australian drafter’s comments.

**Article VIII – Undistributed Profits Tax**

3.114 The final version of Article VIII differed from both the first and second drafts by covering US undistributed profits tax. The extension is not the subject of specific comment in either the US or Australian files that have been examined by the author. The US may have asked for the article to be extended to its undistributed profits tax in case the US changed to the former Australian method of calculation at some future time.

**Article X – Cultural Royalties**

3.115 Article X adopted the wording of the second draft discussed at 3.95.

**Article XV – Tax Credits**

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172 As discussed at 3.91, the perceived difficulty was that ITAA 1936 s23q could not apply in a situation where, in equity, it should, because of the deemed source rule in the article.

173 The former Australian method of calculating undistributed profits tax was discussed at 2.12 and at note 91 to 3.57.
3.116 The amendment to paragraph (2) of the article proposed in the second draft\textsuperscript{174} was adopted in the final version. No changes were made to either the first or second draft versions of the article to deal with the additional issues\textsuperscript{175} raised in the drafter's comments on the article.

\textit{Article XVI – Assistance In Collection}

3.117 The Assistance In Collection article differed from both the first and second drafts. As was the case with the equivalent article in the first draft, it used the mandatory verb ‘shall’ instead of the permissive verb ‘may’ used in the second draft. The article in the final draft read:

‘Each Contracting State shall, so far as it is practicable to do so, collect, and pay to the other Contracting State amounts equivalent to the amounts due to the other Contracting State by way of taxes which are the subject to this Convention, being amounts the collection of which is necessary in order to ensure that the benefit of exemptions from tax, or of reductions in rates of tax, provided for by this Convention is not received by persons not entitled to that benefit.’

Changes from the previous drafts reflect awareness of technical and practical difficulties associated with collecting tax for the other contracting state and also aim to clarify operational aspects. Practicalities are evident in the insertion of the words ‘so far as it is practicable to do so’. The drafting reflects the technicality that what was to be collected was an amount equivalent to the tax due to the other contracting state, not the tax itself. The obligation now only applied where the assistance in collection was ‘necessary’ to ensure that the benefits of the Convention were not received by persons not entitled to them. In the first two drafts, by contrast, the obligation had applied where assistance in collection was ‘sufficient’ for those purposes.

\textit{Article XX – Savings Provision For Exemptions, Deductions, Credits and Allowances in Domestic Law}

\textsuperscript{174} As discussed at 3.97, this proposed amendment aimed to overcome difficulties associated with the application of \textit{ITAA} 1936 s45.

\textsuperscript{175} As discussed at 3.98, the drafter's comments related to: credit for US shareholders for Australian undistributed profits tax; credit for US residents for Australian tax paid under \textit{ITAA} 1936 s125; and the basis for allowing credit for provisional tax.
3.118 The final version of this article adopted the changes proposed in the second draft discussed at 3.99 but did not make any change to paragraph (a) in response to the drafter’s comments discussed at 3.100 and 3.101.

Inferences Drawn From Comparing The Final Treaty With The Earlier Drafts

3.119 With the exceptions of the gross basis taxation of dividends,\(^\text{176}\) the failure to adopt all the suggested changes to the tax credit provisions\(^\text{177}\) and the changes made to the assistance in collection article,\(^\text{178}\) all of the changes from the second draft can be regarded as alternative drafting approaches to the problems identified in the drafter’s comments on the second draft. The changes are all consistent with an acknowledgement of the validity of the Australian concern, but they adopt a different drafting approach to deal with the problem.

3.120 The changes to Article VIII dealing with undistributed profits tax acknowledge the validity of the Australian argument by making the article reciprocal. The changes to the Assistance in Collection article give the distinct impression of redrafting being done during the negotiations, reflecting the accumulated wisdom of experienced tax administrators. Applying the flat rate of source tax to the gross dividend\(^\text{179}\) was inconsistent with Australian domestic law and the Memorandum, but it was an option that the drafter’s comments had left open.

3.121 The only other point of substance in which the Australian revisions in the second draft did not carry the day were in relation to the conceptually difficult issue of characterising the Australian undistributed profits tax, \(s\)125 tax and Australian provisional tax for US foreign tax credit purposes.\(^\text{180}\)

The US Senate Foreign Relations Committee Report

3.122 The President submitted the signed treaty to the US Senate on 3\(^\text{rd}\) June 1953\(^\text{181}\) and the Senate ratified the treaty on 19\(^\text{th}\) July 1953.\(^\text{182}\) The Senate
Foreign Relations Committee submitted a report (hereafter ‘the Report’) on the treaty to the Senate. The Report highlights aspects in which the treaty was consistent with and varied from then current US taxation treaty practice.

3.123 The Report noted, with obvious approval, that the treaty, unlike some US treaties such as the 1945 US – UK Tax Treaty, did not contain any provisions for the exemption from US tax of capital gains or taxes on accumulated earnings. The Report noted that the treaty was substantially identical with US treaties then in force, but drew attention to distinctive features of the treaty.  

3.124 Principal among the unusual features, from both the US and Australian perspectives, was the flat rate of 15% of source taxation on dividends. The Committee commented:

‘This omission is one to which American taxpayer groups may take exception and, as a matter of fact, several witnesses commented on this point. It is understood, however, that US representatives in their negotiations with Australia made determined efforts to secure the reciprocal exemption. They were unable to do so because of the Australian position that reciprocal reduction of the tax on dividends to 15 percent provides more favorable [sic] treatment generally than does the corresponding provision of Australia's tax convention with the UK.’

3.125 McGovern and King had corresponded on this issue prior to the Committee’s hearing. McGovern had forwarded a memorandum which explained the context (as discussed in Chapter 2) in which Australia had made the concession of the exemption from source taxation on dividends paid by wholly owned subsidiaries to their parents in the 1946 UK Treaty. McGovern pointed out that the 15% rate in the Australia–US treaty represented a greater concession to dividends other than those paid by subsidiaries than in the 1946 UK Treaty, where the rate of source taxation on such dividends was reduced by one half to a rate of 17.5% on dividends paid to UK companies and a rate of up to 37.5% on dividends paid to UK individuals.

3.126 In addition, difficulties had been experienced in the UK treaty in defining a wholly owned subsidiary (particularly on the question of the appropriate

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184 Ibid.
treatment of preference shares in a definition) and due to the fact that having a preferential rate on dividends paid by wholly owned or 95% owned subsidiaries would mean that such companies would not seek Australian equity investment.\footnote{In reply, King commented that McGovern’s explanation ‘stood me in good stead in the final stages of the income tax convention’.\footnote{In reply, King commented that McGovern’s explanation ‘stood me in good stead in the final stages of the income tax convention’.}} In reply, King commented that McGovern’s explanation ‘stood me in good stead in the final stages of the income tax convention’.

\textbf{3.127} The Committee noted that, in contrast to some other US taxation treaties, the reciprocal exemption in the royalty article in the Australian treaty did not extend to industrial royalties or film rentals; the Committee pointed out that a similar exclusion of film rentals from the reciprocal exemption for cultural royalties was found in the United States’ treaties with Canada and Finland. Nor did the Australian treaty, unlike some other US treaties, provide for the reciprocal reduction of source taxation of interest. It is reasonably clear from this comment and the general tenor of the Committee’s report that the Committee’s view was that source countries retained full taxing rights in relation to categories of income not specifically dealt with in the relevant treaty.\footnote{In reply, King commented that McGovern’s explanation ‘stood me in good stead in the final stages of the income tax convention’.}

\textbf{3.128} The Committee also noted that under both the Australian and Belgian treaties (which it was also examining at the same time):

\begin{quote}
‘the articles providing for the mutual assistance in the collection of taxes extends [sic] only to such cooperation as will insure that the exemption or reduced rates of tax granted under the convention shall not be enjoyed by persons not entitled to such benefits.’\footnote{In reply, King commented that McGovern’s explanation ‘stood me in good stead in the final stages of the income tax convention’.}
\end{quote}

\textbf{Date Of Entry Into Force}

\textbf{3.129} In Australia, the treaty became the Second Schedule to \textit{Income Tax (International Agreements) Act 1953} (Cth), which came into force on 11th December 1953. The effect of s6 of the \textit{Income Tax (International Agreements) Act} was that the treaty had the force of law in Australia as from

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\footnote{The undated memorandum, titled ‘Taxation of Dividends Paid by US Corporations’, and McGovern’s covering letter, McGovern to King, 19th June 1953, are both contained in NAA, ATO file, Pt 4.}

\footnote{King to McGovern, above n 182. It seems likely that the reference to the ‘final stages of the income tax convention’ is to the Senate Foreign Relations Committee hearing at which King appeared. In the next sentence of the same letter, King refers to the Senate’s advice and consent to ratification as ‘final action’.}

\footnote{Tax Analysts, above n 183.}

\footnote{Tax Analysts, above n 183.}
1st July 1953, being the first day of July next succeeding the date on which the treaty became effective for US tax purposes.

The Significance Of The 1953 US Treaty For The First Two Questions Identified At 1.4

3.130 The 1953 US Treaty, while consolidating and refining the structure and some of the distinctive features of the 1946 UK Treaty, contained additional features which influenced Australian taxation treaty practice for the balance of the period under review in this thesis. The overall Australian objectives, as stated by McGovern in his report to Fadden, were to remove, at minimum revenue cost, the deterrent to US direct investment in Australia and to emphasise the primacy of source basis taxation.\(^{189}\)

3.131 The basic structure of the treaty was a carry-over from the 1946 UK Treaty. The structure was not unique. The approach taken in this treaty to defining ‘industrial or commercial profits’ can also be seen in several US taxation treaties in this period,\(^{190}\) but not in all of them.\(^{191}\) It is also common for US taxation treaties in this period to not contain an ‘other income’ article. It is reasonable to infer that this structure was one that the US would agree to even if it might not have asked for it.

3.132 In the case of the 1953 US Treaty, McGovern reported that the US attitude was that, in general, the 1946 UK Treaty should be regarded as setting the pattern of tax treaties between Australia and countries from whom investment capital was sought.\(^{192}\) One consequence of allowing the 1946 UK Treaty to set the pattern may have been the adoption of the overall structure of that treaty.

3.133 Although the ATO would subsequently describe taxation treaties that had these characteristics as following a ‘Colonial Model’,\(^{193}\) the better view appears to be that these structural features were also common in US taxation

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\(^{189}\) See the discussion at 3.32.

\(^{190}\) See, for example, US–Canada 1942; US–NZ 1948; US–Ireland 1948; US–Germany 1954.


\(^{192}\) See the discussion of this aspect of McGovern’s report at 3.31.

\(^{193}\) See Taxation Ruling TR 2001/12 Income tax and capital gains tax: capital gains in pre CGT tax treaties.
treaties in the 1940s and 1950s and in the taxation treaties of other English speaking countries of that period.\footnote{If anything, the model might be called the ‘Baby Boomer Model’ rather than the ‘Colonial Model’. The post World War II baby boom is usually regarded as beginning with births in 1945 and ending with births in 1965 thus corresponding almost exactly with the period in which Australian treaties have all the features of the model.}

3.134 Other features that were carried over from the 1946 UK Treaty included: (a) the savings provisions in respect of \textit{ITAA 1936} s136, the taxation of film income, and the taxation of profits of foreign controlled insurance companies; (b) the approach to dealing with residence issues (enhanced in the case of corporate residence); (c) quarantining Australian undistributed profits tax from the limitations on source taxation in other distributive articles; and (d) the deletion of the phrase ‘same or similar conditions’ from the arm’s length adjustment provisions. It does seem likely that these particular features, like the overall structure of the treaty, were a product of following the 1946 UK Treaty.

3.135 Several respects in which the treaty differed from the 1946 UK Treaty were to become part of Australian taxation treaty practice for the period reviewed in this thesis. The most important difference was agreeing to a flat 15\% gross source tax on all dividends. From an Australian perspective, this rate encouraged the right level of US equity participation in Australian companies without producing the ‘Treasury effect’. It is clear that this was a product of Australia’s argument in original negotiations with the US for a 5\% rate on nonportfolio dividends.\footnote{See the discussion at 3.51 to 3.56.}

3.136 Another development was the broadening of the definition of ‘permanent establishment’, particularly by the inclusion of a ‘substantial equipment’ provision. Although the author has not located direct documentary evidence on the point, US tax treaty practice in the 1940s and 1950s and subsequent Australian tax treaty practice make it likely that the request for the inclusion of a ‘substantial equipment’ provision came from Australia. The final form of the provision was a composite of the original draft and the second draft developed by Australia.

3.137 A third feature that was to continue to be part of Australian treaty practice in the period under review was the express reference to either \textit{ITAA 1936} s38 or to its content in the calculation of industrial or commercial profits. While
McGovern reported on the inclusion of the provision, he did not specify which country initiated the insertion.\textsuperscript{196} As similar provisions had been included in other US tax treaties from 1948 onwards, it seems likely that the initiative came from the United States. It is highly likely, though, that the express reference to the principle underlying s38 was initiated by Australia.

\textbf{3.138} The negotiation and drafting of the treaty consolidated an approach that had been used in negotiating and drafting the 1946 UK Treaty,\textsuperscript{197} although, so far as can be judged from the correspondence, the negotiations appear to have been much more convivial. In part, this may have been due to the greater similarity between the Australian and US income tax systems at the time (both classical systems with undistributed profits taxes and only allowing such deductions as the legislation permitted) as compared with the Australian and UK taxation systems (same common law concept of income but different corporate-shareholder tax systems and different approach to allowing deductions in respect of business income).

\textbf{3.139} The involvement of politicians was less direct, with there being no directly relevant meetings involving ministers of both countries. Nonetheless, the Australian decision to enter into negotiations was clearly made by politicians, and geopolitical considerations appear to have been relevant factors influencing that decision.\textsuperscript{198}

\textbf{3.140} As might be expected, there is also some evidence that Australian negotiators paid attention to previous US taxation treaty practice (for example, the substantial equipment provision might be derived from the 1950 US – Canada Supplementary Convention\textsuperscript{199}) and certainly expected the US to have regard to the 1946 UK Treaty. The negotiators and drafters continued to be concerned with technical problems associated with the interaction of the treaty with Australian domestic law in the areas of residence\textsuperscript{200} and credits.\textsuperscript{201}

\textbf{3.141} Unlike the case with the 1946 UK Treaty, the primary motivation for entry into the treaty was not to prevent international double taxation; rather it was to prevent credit overspill in the US and to encourage US direct investment in Australia by reducing source basis taxation.

\begin{itemize}
\item[196] See the discussion at 3.47.
\item[197] See the discussion at 2.167.
\item[198] See the discussion at 3.17 to 3.24.
\item[199] See the argument to this effect at 3.42.
\item[200] See the discussion at 3.81.
\item[201] Discussed at 3.97.
\end{itemize}
3.142 Both of the objectives referred to in 3.142 could have been achieved by a comprehensive and unilateral lowering of Australian tax rates; however, in the economic and political environment of the early 1950s, the most viable source of additional direct foreign investment in Australia was the United States. Hence a targeted approach through a bilateral treaty, which minimised revenue cost, was favoured over unilateral and comprehensive rate reductions. Encouraging investment while at the same time minimising revenue cost and the erosion of source basis taxation were again the major policies that influenced both politicians and officials.

The Significance Of The 1957 Australia – Canada Tax Treaty For The First Two Questions Identified At 1.4

3.143 Although the negotiation and drafting of the 1957 Canada Treaty is not discussed in detail in this thesis, the author has, as a result of research undertaken towards this thesis, previously published an article on that subject.\(^\text{202}\) In several respects, examining archival material relating to the 1957 Australia – Canada Tax Treaty has significance for the first and second questions identified at 1.4.

3.144 The request for a treaty was initiated by Canada,\(^\text{203}\) which sought a treaty dealing with shipping profits and air transport. Australia, concerned about a potential loss of revenue and with its emphasis on the primacy of source basis taxation, rejected this approach outright as providing advantages to Canada and no corresponding advantages to Australia. Australia advised Canada that, given the unilateral provisions in both countries for relief of international double taxation, there ‘did not appear to be any great need for such an agreement’.\(^\text{204}\) Australia was still seeing the primary purpose of tax treaties as the prevention of international juridical double taxation.

3.145 After the election of the Menzies government in 1949, the Australian attitude changed and Cabinet authorised commencing negotiations with Canada. The considerations that influenced the Australian Cabinet and officials were the promotion of closer relations with Canada and possible encouragement of

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\(^{202}\) The author has discussed the negotiation and drafting of the 1957 Australia – Canada Tax Treaty in detail in Taylor, above n 1. In the discussion that follows, references will be made to this publication to support the analysis and argument.

\(^{203}\) In every treaty that Australia entered into in this period, the initial request for a tax treaty came from the potential treaty partner.

\(^{204}\) The initial approach by Canada is discussed in detail in Taylor, above n 1, 922–8.
Canadian investment in Australia based, in part, on lobbying by significant Canadian businesses.\textsuperscript{205} From a foreign relations perspective, the Treasurer's submission to Cabinet observed that it would be difficult and perhaps embarrassing in any treaty to deny broadly comparable terms to Canada to those proposed to be agreed with the United States.\textsuperscript{206}

\subsection*{3.146} The Australian Treasury played a greater advisory role in relation to the 1957 Canada Treaty than it had in relation to Australia's previous tax treaties. The Cabinet submission, drafted by Treasury, saw the negative aspects of a tax treaty with Canada as a loss of revenue and a loss of dollars due to increased remittances by Canadian companies taking advantage of the lower treaty rate of source taxation.\textsuperscript{207} After the broad terms of the treaty had been finalised, but before settlement of the final draft, a clear division emerged between the Australian Treasury, which, unconvinced that direct Canadian investment would be encouraged or was desirable, now opposed entering into the treaty, and the ATO, which considered that the treaty might encourage Canadian direct investment in Australia at a relatively small revenue cost and that it would now be embarrassing to not enter into the treaty.\textsuperscript{208} The Australian Minister for External Affairs was in favour of the treaty throughout, for foreign

\textsuperscript{205} Most notably the Ford Motor Company of Canada, which was the parent company of the Ford Motor Company of Australia. The Ford Motor Company of Canada was 49\% Canadian owned and operated relatively independently from the Ford Motor Company of the United States. Another significantly affected Canadian company was Massey Harris Ferguson. Lobbying of Australian ministers by major Canadian companies is discussed in Taylor above n 1, 962. An apparent reference to the Ford Motor Company in Fadden's 1952 Cabinet submission is noted in Taylor, above n 1, 932. Lobbying of Canadian ministers and officials by Ford and Massey Harris Ferguson, and by Canadian shipping interests, is discussed in Taylor, above n 1, 950, 958 and 975.


\textsuperscript{207} The Treasurer's submission to the Australian Cabinet Administrative Committee is discussed in Taylor, above n 1, 931–2.

\textsuperscript{208} In August 1956, the Commissioner of Taxation drafted a submission to the Treasurer (Arthur Fadden) to submit to Cabinet. After receiving a letter from the First Assistant Secretary of the Treasury (R J Randall), the Treasurer withdrew the Cabinet submission and asked the Commissioner of Taxation and the Secretary of the Treasury to prepare a statement of pros (prepared by the Commissioner of Taxation) and cons (prepared by Randall) in relation to entering into a taxation treaty with Canada. The correspondence, the statement of pros and cons and the subsequent Australian decision are discussed in Taylor, above n 1, 962–7.
relations reasons, and also believed that the treaty might encourage Canadian direct investment in Australia.\textsuperscript{209}

3.147 Several aspects of the negotiation and drafting of the treaty highlight the importance that Australian tax officials placed on the primacy of source taxation and on a desire to protect the operation of specific features of Australian domestic law. Principal among these was Australia’s desire to preserve its undistributed profits tax on private companies. Disagreement on this issue was the major cause of the delay between the initial negotiations in Ottawa in May 1953\textsuperscript{210} and the eventual signing of the treaty in October 1957\textsuperscript{211} even though undistributed profits tax was unlikely to ever apply to subsidiaries of major Canadian companies.\textsuperscript{212}

3.148 These emphases can also be seen in technical features of the treaty such as: the inclusion of a ‘substantial equipment’ provision in the definition of ‘permanent establishment’;\textsuperscript{213} a saving provision in respect of Australian domestic law on film business controlled abroad and insurance with non-residents;\textsuperscript{214} and a saving provision for domestic law in the industrial or commercial profits and associated enterprises articles in cases where information was inadequate to ascertain an arm’s length profit.\textsuperscript{215} While each of these features was a carry-over from either or both of Australia’s two earlier tax treaties, their presence in both drafts prepared by Australia in relation to the 1957 Canada Treaty shows that in this instance the initiative for each of them came from Australia.

3.149 The provision having its origin in this treaty which remains a distinctive feature of Australian tax treaty practice was Article II(2).\textsuperscript{216} This was inserted at Australia’s request in response to the Australian Board of Review decision in *Case 110* (1955) 5 CTBR (NS) 656 and was consistent with an emphasis on the primacy of source basis taxation and with the previous Australian

\textsuperscript{209} The involvement of R G Casey as Minister for External Affairs in supporting entry into a tax treaty with Canada is discussed in Taylor, above n 1, 930–1, 947 and 962.

\textsuperscript{210} See the discussion of the Ottawa negotiations in Taylor, above n 1, 933–43.

\textsuperscript{211} See the discussion of the signing of the treaty in Taylor, above n 1, 974–5.

\textsuperscript{212} See the discussion of disagreements concerning Australian undistributed profits tax in Taylor, above n 1, 938–42 and 946–9.

\textsuperscript{213} The inclusion of a substantial equipment provision in the treaty is discussed in Taylor, above n 1, 938.

\textsuperscript{214} This aspect of the treaty is noted in Taylor, above n 1, 981.

\textsuperscript{215} This aspect of the treaty is noted in Taylor, above n 1, 982.

\textsuperscript{216} Article II(2) is discussed in Taylor, above n 1, 968–9 and 981.
practice\textsuperscript{217} of drafting treaty provisions in response to Australian court and board of review decisions.

3.150 The 1957 Canada Treaty continued the ‘baby boomer’ structure that had been established in Australia’s two earlier tax treaties.\textsuperscript{218} In this instance, clearly Australia initiated that structure, which was adopted in the two drafts that Australia sent to Canada. The structure was consistent with the principle of the priority of source taxation that Australia stressed.\textsuperscript{219}

3.151 The treaty also consolidated the approach of uniform source country taxation of dividends at 15% that Australia had argued for in the 1953 US Treaty.\textsuperscript{220} That Canada, understandably given its own prior tax treaty practice, agreed to this without apparent difficulty may have reinforced the belief of Australian negotiators that rates at this level could consistently be achieved in bilateral treaty negotiations.

3.152 The negotiation and drafting of the 1957 Canada Treaty also shows that Australian officials were willing to modify their initial stance in relation to items which were important to Canada (such as shipping and aircraft profits and undistributed profits tax) as a means of obtaining concessions on items (such as a uniform rate on source taxation of dividends) which were important to Australia. Australia bowed to the emerging international standard on shipping profits, characterising not using its arbitrary domestic basis for taxing them as a major concession.\textsuperscript{221} In the case of undistributed profits tax, Australia’s concession was limited to omitting the equivalent of Article VIII of the 1953 US Treaty\textsuperscript{222} from the 1957 Canada Treaty without prohibiting Australia from levying undistributed profits tax.\textsuperscript{223}

3.153 The respects in which the 1957 Canada Treaty differed from the 1953 US Treaty are instructive. The inclusion of a ‘force of attraction’ rule in the first Australian draft and its apparently ready agreement to omit that rule from the

\textsuperscript{217} See, for example, the discussion at 2.161.
\textsuperscript{218} The ‘baby boomer’ structure of the treaty is discussed in Taylor, above n 1, 984–5 and the discussion at 3.132.
\textsuperscript{219} See the argument to this effect at 2.162.
\textsuperscript{220} A point noted in Taylor, above n 1, 981–2. See also the discussion of this aspect of the 1953 Australia – US Tax Treaty at 3.51 to 3.56, 3.93 and 3.113.
\textsuperscript{221} See, for example, the discussion of McGovern’s correspondence with Canadian officials on this issue in Taylor, above n 1, 951.
\textsuperscript{222} Article VIII of the 1953 Australia – US Tax Treaty was discussed at 3.57, 3.93 and 3.113.
\textsuperscript{223} For a more detailed analysis of this aspect of the treaty see Taylor, above n 1, 982.
second draft shows that Australia was not particularly concerned with the
presence or absence of the rule.\footnote{1}{224}

\textbf{3.154} The provisions relating to royalties also differed from those in the 1953 US
Treaty. No specific provision in the 1957 Canada Treaty preserved the
operation of Australian domestic legislation in relation to film royalties,
although the credit article deemed income covered by those provisions to
have an Australian source. As the royalty article in these treaties did not
extend to film and television royalties, thus leaving full taxing rights with the
source country, the end effect of the two treaties was substantially the
same.\footnote{1}{225}

\textbf{3.155} In the case of mineral royalties, the draft that Australia sent to Canada did not
contain an equivalent to Article XI of the 1953 US Treaty,\footnote{1}{226} which had
apparently been inserted to counteract the effect of provisions in US domestic
law. It may be that Australia did not have similar concerns about provisions in
Canadian domestic law.\footnote{1}{227}

\textbf{3.156} Unlike the 1953 US Treaty the 1957 Canada Treaty, consistent with prior
Canadian tax treaty practice, did not contain even a limited assistance in
collection article nor had one been included in the Australian draft sent to
Canada. This omission of this article from the Australian draft reinforces the
impression that the assistance in collection provision in the 1953 US Treaty
was inserted at the request of the United States.\footnote{1}{228}

\textbf{3.157} The negotiations with Canada show that for most of the 1950s Australia was
still developing its process for negotiating tax treaties. Negotiating tax treaties
was still a novel experience for Australia, and officials clearly believed that
authorisation from Cabinet was required to enter into negotiations and for the
draft to be used in negotiations. Shortly after they were concluded, McGovern
provided a detailed report of the initial negotiations to Fadden. The author has
found no evidence of action by Fadden in response to a key recommendation
by McGovern at the time on the article dealing with the calculation of

\footnote{1}{224} See the discussion of the initial inclusion and subsequent omission of the ‘force of
attraction’ rule in Taylor, above n 1, 935–7, 969 and 981.
\footnote{1}{225} See the discussion in Taylor, above n 1, 982–3.
\footnote{1}{226} See the discussion at 3.63. In the version of the 1953 Australia – US Tax Treaty
discussed at 3.63, this article was numbered XII.
\footnote{1}{227} See the discussion in Taylor, above n 1, 982–4.
\footnote{1}{228} See the discussion at 3.70, 3.97 and 3.116.
undistributed profits tax which, if acted upon, may have led to an earlier conclusion of the treaty.\textsuperscript{229}

3.158 The factors that influenced the decision to enter into a tax treaty with Canada, the long delay in making that decision, the delay in reaching agreement with Canada, the division between Australian government departments on the issue, and the lack of clarity as to roles of officials and ministers in the process are all evidence of the nascent state of Australian tax treaty policy, practice and processes at the time. Economic, revenue, tax technical, foreign policy and political factors were all interacting without any of them assuming decisive significance and without any of the departments which championed particular factors becoming clearly dominant.

3.159 Having now entered into three tax treaties Australia in the late 1950s, through the Department of the Treasury working with the ATO, began to develop formal policies in relation to concluding tax treaties and developed an Australian model treaty. Chapter 4 discusses the 1959 - 1964 review of Australian tax treaty policy and the development of the first Australian model tax treaty.

\textsuperscript{229} Taylor, above n 1, 985–7, discusses this issue and contrasts the Australian process with the Canadian process at the time.


4.1 In mid 1959, the Australian Treasury commenced a general review of policy on concluding further tax treaties.¹ That review led ultimately to the development of the first Australian model tax treaty, which was sent to several European countries. The model was also used as the basis for the ATO’s review of the draft tax treaty that the UK sent to Australia in 1966 as part of the negotiations which led to the 1967 Australia – UK Tax Treaty. The model also was a reference point and a source of precedents for Australian negotiators during that negotiation.² This chapter will discuss the correspondence, meetings, Cabinet submissions, Cabinet decisions, reviews and drafts which led up to the development of this first Australian model tax treaty.

4.2 The review process began when M W O’Donnell³ wrote to the Commissioner of Taxation⁴ on 3rd December 1959 indicating that Treasury was preparing a draft Cabinet submission on the general approach that should be taken in response to requests for tax treaties. O’Donnell requested that McGovern provide a statement in relation to countries which had made or were likely to make approaches for tax treaties with Australia, indicating: (a) the nature and extent of the double taxation which existed; (b) the difficulties (including loss of revenue) associated with concluding tax treaties with such countries; and (c) the advantages in concluding such treaties. O’Donnell also indicated that Treasury would welcome any comments concerning the general policy on concluding tax treaties.⁵

¹ M W O’Donnell, Assistant Secretary, Department of the Treasury to The Treasurer (Harold Holt) 16th August 1962, 2, para 6. ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. The review was initiated following a request from Japan for a tax treaty.
² See the discussion at 5.12, 5.14, 5.30 and 5.56.
³ M W O’Donnell was First Assistant Secretary of the Australian Treasury at the time.
⁴ Patrick McGovern was still Australian Commissioner of Taxation in 1959.
⁵ M W O’Donnell, above n 1.
McGovern made a lengthy reply to the Secretary of the Treasury on 8th April 1960. McGovern identified residence–source conflicts as the principal cause of international double taxation, noting that, while the burden of taxation could be increased in dual residence situations and by conflict of source rules, these cases were ‘infrequent’ and did not call for consideration in a general review of double taxation. McGovern identified the five ‘recognised means’ for the relief of double taxation as: (a) exemption at source; (b) exemption by the state of residence; (c) allowance of credit by the residence state for source tax; (d) exemption of a portion of the income by each state; and (d) allowance of the source country tax as a deduction by the residence state.

McGovern summarised the almost complete unilateral relief from international double taxation which Australia provided under domestic law. In the case of the ITAA 1936 s45 credit, McGovern conceded that where the dividend was funded from Australian source profits, the lack of availability of the s45 credit meant that double taxation was not relieved in the absence of a tax treaty. McGovern pointed out that Australian companies receiving dividends from foreign companies did not (except for private companies in rare circumstances) pay tax on the dividend, but that redistributions of the dividend to Australian shareholders bore tax at the shareholder level. While the position was modified where a tax treaty reduced the foreign tax on the dividend received by the Australian company, there were ‘few cases of this nature’ and the need for Australian residents in this situation to be relieved from international double taxation was ‘not pressing’.

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6 Patrick McGovern, Commissioner of Taxation to The Secretary, Department of the Treasury, Canberra, ACT, 8th April 1960. ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. McGovern’s reply was based on information received from Deputy Commissioners. McGovern had written to each Deputy Commissioner on 15th December 1959. Memorandum to the Deputy Commissioner of Taxation from Commissioner of Taxation, 15th December 1959. ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. In addition to the information that O’Donnell had required, McGovern also requested that the information supplied include: (a) the classes of income which flowed between Australia and the country in question; (b) an estimate of the revenue gain or loss to Australia of entering into a tax treaty with the country in question, assuming that the treaty followed the lines of the Australia–Canada tax treaty; and (c) any other factor which the relevant Deputy Commissioner might consider relevant.

7 McGovern, above n 6, paras 3 and 4.

8 McGovern, above n 6, para 5.

9 The unilateral provisions providing relief from international double taxation were discussed at 2.7, 2.9 and 2.13.
McGovern then summarised the unilateral relief from international double taxation provided by selected foreign countries and provided estimates of the revenue cost to Australia of concluding a tax treaty with each of these. All the countries discussed (other than Greece and Egypt) provided relief using one or a combination of methods; however, McGovern noted that, in some instances, the unilateral relief provisions in the foreign country did not completely eliminate international double taxation.

McGovern then observed that ‘it has become conventional in double taxation agreements to relieve the weight of tax on dividends flowing between the two countries that conclude an agreement’. McGovern opined that this was ‘the most important feature of the agreement so far as concerns overseas investors wishing to place their capital with Australia and enterprises operating through subsidiary companies incorporated in Australia. It is thought to have done much more to attract capital to Australia than all the other provisions in the agreement.’ McGovern considered that the non-treaty level of Australian tax on distributions ‘may well deter investment in Australia by an overseas enterprise wishing to establish a subsidiary in this country’, but that the rates of company tax in other countries were generally high enough to not encourage companies (for tax reasons) to keep their capital at home rather than invest in Australia at treaty rates.

McGovern’s overall conclusion was that: (a) there was little unrelieved double taxation for Australian taxpayers; (b) countries seeking treaties with Australia did not provide unilateral relief on a basis as satisfactory as that provided in treaties; and (c) in the absence of treaty rates on dividends the weight of Australian tax on company profits distributed to non-residents (particularly to parent companies) was a deterrent to overseas investment in Australian companies.

The countries discussed (in this order) were the Federal Republic of Germany, Japan, Sweden, The Netherlands, France, Norway, Italy, Switzerland, Ireland, Denmark, Greece and Egypt.

No information was available on the domestic law provisions for unilateral relief in these countries.

McGovern made specific mention of the position of Dutch and Swedish investors.

McGovern had provided information about the effects of the reduction in source taxation of dividends under Australia’s existing tax treaties and of the effect of dividend withholding tax.
McGovern considered that the principal difficulty in concluding tax treaties had been the cost to Commonwealth revenue. It was estimated that the cost of entering into tax treaties with the countries that had requested them would be £640,000 per annum and that of this, £544,000 would be attributable to taxing shipping profits on a residence basis and £82,000 would be attributable to reducing the tax on dividends to 15%. Statistics were not available to make a reliable estimate of the cost of Australia’s existing tax treaties, but on a comparable basis of estimation, the cost would have been several times £640,000. The cost of the NZ tax treaty was estimated to be £150,000. Tax treaties with Malaysia, Pakistan and Burma would be expected to result in a small revenue gain for Australia. McGovern observed that virtually the whole revenue cost of tax treaties was attributable to taxing shipping profits on a residence basis and reducing the rate of withholding tax on dividends.\[16\\]

McGovern then outlined the classes of income that were taxed on a residence basis in Australia’s existing tax treaties and pointed out that, except in the case of taxation of industrial royalties in the 1946 Australia – UK Tax Treaty, all but a negligible portion of the revenue costs associated with residence basis taxation were attributable to taxation of shipping profits on a residence basis.\[17\\]

McGovern then outlined the policy arguments for and against residence basis taxation and the particular arguments put in favour of residence basis in the case of shipping profits.\[18\\] McGovern noted that, where a foreign tax credit system was in operation, taxation on a residence basis frequently provided more assistance to the foreign Treasury than it did to foreign investors. In the case of shipping profits, in some situations double taxation still arose in the absence of a treaty because Australia imposed tax at 5% on gross freights while residence countries typically allowed credit against and up to their own tax, which was calculated on the basis of profits.\[19\\]

There are indications in the letter that McGovern did not favour continuing Australia’s arbitrary approach to taxing shipping profits stating:

‘There would be few countries today, however, and possibly only those without a merchant marine service of their own, who would be sympathetic with the policy at present followed by Australia in relation

\[16\\] McGovern, above n 6, paras 52–8.
\[17\\] McGovern, above n 6, paras 59–60.
\[18\\] McGovern, above n 6, paras 61–4.
\[19\\] McGovern, above n 6, paras 66 and 67.
to shipping profits. All the model double tax agreements emerging from United Nations agencies and other international advisory bodies accept without exception the doctrine of assessment of profits on a residence basis.’\textsuperscript{20}

Given that Australia had already, through its existing treaties, considered it not appropriate to tax a large proportion of ships visiting Australia, ‘rejection of proposals for agreements on the grounds of revenue costs in relation to ships has become more difficult to justify, especially where an agreement could be expected to encourage an inflow of capital or to assist trade.’\textsuperscript{21}

\textbf{4.11} Turning to the effect of reduced treaty rates on dividends on Australian revenues, McGovern pointed out that the cost to the Australian revenue of these concessions in the UK and US treaties was £3,850,000 per annum as compared with the estimated cost to Australian revenue of £82,000 if similar concessions were made to all the other countries currently seeking tax treaties with Australia.\textsuperscript{22} Since the conclusion of the 1953 tax treaty with the US, the profits of General Motors-Holden’s Ltd had increased from £689,154 in 1948 to £15,343,107 in 1958, and its dividend distributions had increased from nil in 1948 to £7,437,500 in 1958. The total dividends paid to US residents had also increased during the period in which the 1953 treaty had been in operation.\textsuperscript{23} While acknowledging that there could be other explanations for General Motors-Holden’s Ltd’s dividend policy, McGovern considered that the better view was that, ‘General Motors Holden regarded the pre-double tax agreement rate of tax on distributed profits as excessive and it was content to use its profits for development purposes in the almost certain knowledge that Australia’s need to attract development capital would in the long term make it necessary to reduce the tax rates’.\textsuperscript{24} Whatever the reason for the change in the General Motors-Holden’s Ltd’s dividend policy, Australia was now collecting more tax from dividends paid to US residents than it did before the treaty was concluded, notwithstanding that the rate of tax was limited to 15% on the dividends.\textsuperscript{25}

\begin{itemize}
  \item \textsuperscript{20} McGovern, above n 6, para 69.
  \item \textsuperscript{21} McGovern, above n 6, para 70.
  \item \textsuperscript{22} McGovern, above n 6, para 72.
  \item \textsuperscript{23} McGovern, above n 6, para 74.
  \item \textsuperscript{24} McGovern, above n 6, para 75.
  \item \textsuperscript{25} McGovern, above n 6, para 76.
\end{itemize}
McGovern then commented on the extent to which the ‘Treasury effect’ was, or was likely to be, produced in Australia’s current and proposed tax treaties. In most cases, McGovern’s conclusion was that relevant foreign companies would obtain at least some benefit from the rate reduction but that usually individuals would not.26

McGovern concluded with several general observations about treaty practice and policy. One difficulty associated with concluding a treaty could be co-ordination with the laws of the country concerned. McGovern cited difficulties that had been encountered in attempting to conclude a tax treaty with NZ when NZ exempted dividends from taxation and had a higher level of corporate tax.27

McGovern believed that Australia’s tax treaties with the UK, the US and Canada had improved the climate for the flow of investment capital from those countries into Australia. In part, this was because the ‘more or less permanent’ nature of the treaties ‘engendered a feeling of confidence’ that both countries were determined to avoid double taxation and that there would not be dramatic changes in taxation principles affecting foreign investors without notice to amend or abandon the treaty being given.28

McGovern also considered that tax treaties were an indication to foreign investors that Australia no longer saw them as exploiters to be penalised by the taxation law. In McGovern’s view, it was only with the negotiation of tax treaties that Australia provided modest encouragement in its taxation laws for the foreign investor who, ‘because he makes no claims upon Australia for social services, education or personal protection, requires relatively little Commonwealth expenditure in his interest’.29

McGovern explained that the zero rate of source taxation on dividends paid by Australian wholly owned subsidiaries to UK parent companies in the 1946 UK Treaty was a means of providing neutrality of tax treatment for UK branch and subsidiary operations in Australia, given that UK companies had traditionally invested through branches. By contrast, US and Canadian companies had not tended to use branches to invest in Australia, and hence a

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26 McGovern, above n 6, paras 78–84.
27 McGovern, above n 6, para 86.
28 McGovern, above n 6, paras 88 and 89.
29 McGovern, above n 6, para 90.
zero rate had not been adopted in these treaties nor in the proposed tax treaty with New Zealand.

4.17 McGovern did not favour exempting dividends paid by wholly owned subsidiaries of foreign companies, as this discouraged the formation of companies with joint Australian and foreign equity participation.30

4.18 Since the reduction in Australian tax on dividends under the treaties, McGovern noted that there had been an increase in the number of foreign companies conducting business in Australia through subsidiaries. He saw this as a step towards a position in which Australian residents would increase their influence in such companies through management and equity participation.

4.19 In McGovern's view, treaty rates of taxation on dividends would not discourage foreign investment and, at the same time, would provide a substantial contribution to Australian revenues without prohibiting subsequent increases in Australian corporate tax.31 McGovern's concluding paragraph was highly supportive of tax treaties:

‘The flow of capital and consequent expansion of the Australian economy lead to greater industrial knowledge and develop new manufacturing techniques. Double taxation agreements have, I believe, contributed in part to those advantages to Australia and it does not seem too much to suggest that, in some circumstances, they have advantages in the fields of trade, defence and diplomacy.’32

The Process Of Drafting The Cabinet Submission

4.20 Treasury officials were more sceptical of the value of tax treaties. On receipt of McGovern's letter, E M W Visbord33 prepared a summary of it, which he sent to F C Pryor34 with the comment:

‘I do not think that we would be entirely in agreement with this general attitude on double taxation agreements. The main value of the Commissioner's document seems to be in the facts that it sets out

30 McGovern, above n 6, para 92.
31 McGovern, above n 6, paras 93 and 94.
32 McGovern, above n 6, para 95.
33 The author has been unable to ascertain the precise position that Visbord held in the Australian Treasury at the time, but it is clear from the correspondence that he was a Treasury official.
34 Pryor was Acting First Assistant Secretary in the Australian Treasury at the time.
rather than in its analysis. I think that what is needed is an analytical paper based, to some extent, on the Commissioner's document, but transferring much of the detailed information to attachments. I have prepared a draft document on this basis and it also is attached to this minute.

In view of the character of the Commissioner's document, I think it would be preferable for a paper based on my draft, rather than the Commissioner’s document, to be made the subject of discussion between ourselves and the taxation branch.35

4.21 A draft Cabinet submission was subsequently prepared by R Daniel36, settled by R J Randall37 and forwarded to the Commissioner of Taxation on 23rd September 1960 asking for suggestions to ensure that the facts were 'fairly stated' and seeking any general comments that the Commissioner had.38 Through a long process of inter-departmental correspondence and meetings involving Treasury, the ATO, External Affairs, Trade and the Prime Minister's Department, the submission was further developed and was ultimately made available to Cabinet by the then Treasurer39 on 16th July 1962. Despite the inter-departmental consultation, the Treasury view dominated the overall argument of the final submission.

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35 Minute Paper, Visbord to Pryor, 17th May 1960, paras 3 and 4, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 1. A document which is evidently the draft that Visbord refers to is also contained in this file.

36 Minute Paper, R Daniel to Acting Secretary (Richard Randall) 21st September 1960, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 1. The Minute Paper indicates that Daniel had prepared a draft submission for Randall’s approval and suggested that it be sent to the Taxation Office to ensure that the factual statements within it were accurate. What was evidently Daniel’s draft is filed immediately after his Minute Paper. From Visbord’s report to Randall, referred to at 4.20, it may be that Visbord’s draft referred to in that report may have formed the basis for Daniel’s draft.


38 R J Randall, Acting Secretary of the Treasury, to the Commissioner of Taxation, Canberra, ACT, 23rd September 1960, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 1.

39 Harold Holt was Treasurer at the time. Ian Hancock, ‘Harold Edward Holt’ in Michelle Grattan (ed), Australian Prime Ministers (New Holland Publishers, 2000) 271–84 at 276 to 277.
Treasury officials were not persuaded by the written responses of the other departments (particularly those of the Department of External Affairs and the Department of Trade) to the draft submission.

The Prime Minister’s Department was regarded as agreeing with the general tenor of the draft submission, as making some minor suggestions for additional information and as not offering any major criticism.  

Jarasius, a Treasury official, considered that the responses from the Department of External Affairs and the Department of Trade did not take into account the three main arguments in the submission. These were that: (a) there was not much benefit to Australia in entering into tax treaties and there would be a loss of revenue if concessions were made; (b) Australian domestic law provided residents with almost complete protection against international double taxation; and (c) the main objective of European countries wanting tax treaties with Australia was to obtain a shipping exemption. The suggestion, incorrectly attributed to the Department of External Affairs instead of the Prime Minister’s Department, that other countries’ experiences could form a guide to Australia’s attitude was characterised as ‘rather far-fetched’ on the basis that treaties would have to be negotiated on the basis of mutual benefit and ‘could not be guided by the past experiences of any other country’.

Various considerations were seen as making a policy of having special provisions for migrant supplying countries difficult to implement.

A Department of Trade argument that, despite the ‘Treasury effect’, foreign investors still wanted tax treaties because of the certainty they provided was characterised as being ‘not quite clear’ on the basis that rates of tax did ‘not appear’ to be covered in treaties and that, in Jarasius’ view, a treaty could not be a deterrent to policy changes by the contracting parties.

Jarasius concluded that the Department of External Affairs and the Department of Trade wanted tax treaties for the purpose of better foreign

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40 Minute Paper, B Jarasius to Mr Visbord, 8th March 1962, p1, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2.
41 Jarasius to Mr Visbord, above n 40, 1.
42 Jarasius to Mr Visbord, above n 40, 1.
43 Jarasius to Mr Visbord, above n 40, 1. The considerations mentioned were: discrimination, pressure from other countries, differing characteristics of various migrant supplying countries, and the changing mix of migrant supplying countries.
44 Jarasius to Mr Visbord, above n 40, 2.
relations and that while this was a ‘highly commendable objective, the price seems nevertheless too high’.45

4.28 Treasury then convened a meeting on 4th May 196246 between officials from Treasury, External Affairs, Trade, Prime Minister’s and Taxation Departments to discuss the draft submission with a view to reaching consensus on the recommendations to be made to Cabinet.47 Craik, of Treasury, opened the meeting by explaining the Treasury view that Australia should be prepared to enter into negotiations but that its objective should be to enter into agreements which offered advantages (in the widest sense) to Australia. Craik acknowledged that the draft submission would need to be revised to make this attitude ‘quite clear’.48 The Treasury ‘Note for File’ of the meeting records that all present agreed to this general policy.49

4.29 The meeting then discussed advantages (such as Commonwealth relations, civil aviation, immigration, and intangibles in the form of goodwill) to Australia from tax treaties not measurable in financial terms and agreed that these should be covered in the submission. It was recognised that indirect gains could not be expected after treaties had been entered into and hence would need to be sought at the time a treaty was being negotiated.50

4.30 Kemp, of the Department of Trade, indicated that it might be possible to use tax treaty negotiations to secure benefits for shipping lines trading with

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45 Jarasius to Mr Visbord, above n 40, 2.
47 ‘General Attitude to Further Double Taxation Agreements’, no author, no date, p1, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2. The document indicates what Treasury’s purpose was in calling the meeting, and it is clear from its content that it was written prior to the meeting. The document largely reiterates previous Treasury views expressed in the draft submission. Treasury was represented by Mr Craik, Mr Stone and Mr Visbord, External Affairs by Mr Peachey, Trade by Mr Kemp, Prime Minister’s by Mr Salter and Miss Seawright and Taxation by Mr Belcher and Mr Hill. ‘Note for File’, above n 46, 1.
48 ‘Note for File’, above n 45, 1. The ‘Note for File’ above n 46 indicates that notes used in Craik’s presentation were attached to it. These notes appear to be the document titled ‘General Attitude to Further Double Taxation Agreements’, above n 47. A one-page summary of these notes, titled ‘Double Taxation Agreements’ and likely used for the purposes of an oral presentation, is also contained in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2.
49 ‘Note for File’, above n 46, 1.
50 ‘Note for File’, above n 46, 1.
Australia with associated freight reductions. It appears likely that Kemp had in mind special tax treatment of shipping companies in their country of residence in exchange for Australia agreeing to taxation of shipping on a residence basis.

4.31 Peachey, of the Department of External Affairs, emphasised that a willingness to enter into negotiations was almost from a diplomatic perspective even if a treaty was not ultimately entered into. It was agreed that the submission should emphasise that Australia was willing to enter into negotiations with countries that sought treaties with it.

4.32 The meeting recognised that negotiations would have to be authorised by Cabinet, that treaties would have to be ratified by Cabinet and that interdepartmental discussions would be necessary on the wider aspects associated with particular treaties. Notwithstanding this, it was also recognised that bargaining 'on financial lines' would have to be carried out by expert representatives.

The Cabinet Submission Of July 1962

4.33 Harold Holt presented the finalised submission to Cabinet. The submission pointed out that Australia’s four existing treaties reflected ties with countries ‘with which our political and economic relationships are especially close’. The submission argued that Australia’s existing treaties should not necessarily provide a model for treaties with other countries requesting treaties with whom Australia did not have the same close ties. The

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51 ‘Note for File’, above n 46, 2.
52 This point had been made in A T Carmody, Deputy Secretary, Department of Trade to M W O’Donnell, First Assistant Secretary, Department of the Treasury, Canberra, ACT, 5th February 1962, p1, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2, as representing the view of the Department of Trade. The relationship between tax treaties and landing rights that Qantas had in other countries was also discussed. ‘Note for File’, above n 46, 2.
53 ‘Note for File’, above n 46, 1.
54 ‘Note for File’, above n 46, 2.
55 Holt was Federal Treasurer at the time.
56 ‘Confidential for Cabinet: Double Taxation Agreements With Other Countries: Submission 305: Harold Holt, Treasurer, 16th July 1962’, NAA, Series Number A5818, Control Symbol: Volume, Agendum 305. (hereafter ‘Cabinet Submission 305’). A copy of the submission is also contained in ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. The submission noted that requests for tax treaties had been received from several countries, including: Japan, the Federal Republic of Germany, Denmark, Greece, Malaya, Singapore, South Africa and Egypt. This inclusive list of countries that had requested taxation treaties with Australia is on page one of the submission.
submission also considered that the countries that it listed were not so
dissimilar in their relationships with Australia that Australia could agree to
enter into treaties with one or two of them and not with the others.\textsuperscript{57} As a
matter of general principle, Australia should enter into treaty negotiations with
countries seeking treaties even if the prospects of a satisfactory treaty being
concluded were limited. The submission argued, however, that it was
necessary to determine the general approach that would be taken in future
negotiations. The overarching approach argued for was that Australia should
enter into taxation treaties when advantages, associated with taxation and of
other types, would be gained by Australia.\textsuperscript{58}

4.34 After outlining the system of double taxation relief through credits, the
submission noted that to arrive at an acceptable apportionment of tax on
income between two contracting countries, it was customary for the source
country to reduce the tax on, or to exempt some classes of income from, tax
thus increasing the tax that the residence country collected. The submission
observed that, ‘it is in the interests of the country towards which there is a net
flow of income to have such limitations included’.\textsuperscript{59} As there was a substantial
outflow of income between Australia and its existing treaty partners and most
of the countries requesting tax treaties, there would be a loss of Australian
revenue when limitations on source taxation were inserted into Australia’s
taxation treaties.\textsuperscript{60} The submission observed that, ‘almost without exception’,
the countries seeking taxation treaties with Australia, wanted Australia to
reduce or eliminate tax on ‘certain important items of income which, as the
country of origin of income, it has the prior right to impose’.\textsuperscript{61}

4.35 The submission considered that Australia’s existing treaties contained
substantial concessions by Australia, and that while these, in part, reflected
the closeness of Australia’s relationship with the countries concerned,
concessions made in the UK treaty (which influenced subsequent treaties)
‘probably arose from the rudimentary double taxation arrangements which
had been entered into with the UK in 1922’.\textsuperscript{62} The view was that Australia had

\textsuperscript{57} The list of the countries in the submission is set out in note 56 above.
\textsuperscript{58} Cabinet Submission 305, p1.
\textsuperscript{59} Cabinet Submission 305, p3.
\textsuperscript{60} Cabinet Submission 305, p3.
\textsuperscript{61} Cabinet Submission 305, p4.
\textsuperscript{62} Cabinet Submission 305, p4. An ATO internal memorandum, by J Hill, had
questioned whether the concessions made in the UK, US, Canada and New Zealand
treaties arose, as the draft submission had suggested, from the ‘rudimentary’
entered into its existing taxation treaties notwithstanding the loss of revenue that they entailed, because they were perceived to provide other benefits mainly in the form of increased foreign investment in Australia. The submission pointed out, however, that to the extent that increased foreign investment would have occurred in the absence of the treaties and would only be marginally affected by them, the costs of that marginal effect was high in terms of revenue foregone.\textsuperscript{63}

4.36 The submission largely repeated the analysis of the revenue costs of tax treaties that had been provided in McGovern’s letter. The main causes of revenue losses were identified as the shipping exemption and reduced source tax rates on dividends. The revenue losses arising from the introduction of dividend withholding tax were noted. McGovern’s comments on whether the foreign investor or the foreign Treasury benefitted from reductions in source taxation were largely repeated.\textsuperscript{64}

4.37 While recognising that some investment into Australia would not have occurred without Australia’s four existing taxation treaties, the submission asserted that tax considerations did not appear to be a major determining factor for the bulk of overseas investment into Australia. Investment from non-treaty countries (such as Germany, The Netherlands, France and Japan) had been increasing rapidly for the three years from 1957/58 to 1959/60 and represented roughly one-eighth of total direct investment other than retention of profits.

arrangements that had previously existed with the UK. Hill expressed the view that the UK treaty followed the League of Nations London and Mexico drafts, and that the only significant departure from them was the exemption of dividends paid to UK parent companies by wholly owned Australian subsidiaries and that this originated from ‘the practical application of Australian Income Tax Law to profits of Australian branches of U.K companies’. Hill considered that the submission as it stood suggested, incorrectly, that there had been ‘sloppy thinking’ by the Australian negotiators of the 1946 UK Tax Treaty. Memorandum by J Hill, 7/9/61. ‘General Review of Double Taxation Policy, Revised Draft Cabinet Submission’ in ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. It appears that view was not conveyed to the Treasury officials drafting the submission or, if it was, it did not produce an alteration in the submission. The statement that the 1946 Australia – UK Tax Treaty followed the League of Nations London and Mexico drafts is not consistent with the research in Chapter 2 of this thesis. The only direct reference to the League of Nations in archival materials relating to those negotiations was discussed at 2.54 and 2.119. The archival material, as noted at 2.98 to 2.108, does indicate that the UK proposals were based on the 1945 UK – US Tax Treaty.

\textsuperscript{63} Cabinet Submission 305, p4.
\textsuperscript{64} Cabinet Submission 305, p6. McGovern’s letter was discussed at 4.3 to 4.19.
4.38 The exemption of shipping profits, in the view taken in the submission, involved a direct and visible loss of revenue without any offsetting benefits.\textsuperscript{65} If the direct loss of revenue, from the concessional rate on dividends, were seen as a cost of obtaining inbound investment then, the submission observed, that cost would continue for the life of the treaties and would progressively increase with the flow of dividends. In addition, it was an unrequited cost where the investment would have been made in the absence of the concessional rates.\textsuperscript{66}

4.39 The submission noted that little revenue would be lost by entering into further treaties which did not include concessions on shipping profits and dividends. This raised the question of whether Australia, in further treaties, should extend the same concessions on shipping profits and dividends as it had previously.\textsuperscript{67}

4.40 The submission argued that European countries wanted taxation treaties with Australia principally to obtain an exemption from Australian tax on shipping profits. The arguments in favour of source country concessions on shipping profits in taxation treaties were: (a) models from the United Nations and ‘other international advisory bodies’ accepted residence basis taxation of shipping profits; (b) a strong element of discrimination currently existed because more than 50% of the cargoes shipped from Australia were carried in ships registered in one of Australia’s four existing taxation treaty countries; and (c) as shipping profits arose almost exclusively from carriage on the high seas, did not have a source in any particular country and as ships paid port dues and related charges in ports of call, exclusive taxation on a residence basis was appropriate.\textsuperscript{68} While these arguments would be attractive to a country wishing to have its shipping profits exempted from Australian taxation, the submission considered that there were no compensating benefits to be gained from the Australian viewpoint, noting that foreign shipping still seemed to find it profitable to trade in Australia despite the profits being subject to double taxation.

4.41 The submission further argued that, in the absence of a binding undertaking, significant reductions in fares and freights for Australian passengers and

\textsuperscript{65} Cabinet Submission 305, p7.
\textsuperscript{66} Cabinet Submission 305, p7.
\textsuperscript{67} Cabinet Submission 305, p9.
\textsuperscript{68} Cabinet Submission 305, p10.
cargoes would not follow from agreeing to taxing shipping profits on a residence basis.\(^{69}\) The submission recommended that, as a starting point in negotiations, Australia should maintain its present method of source taxation of shipping profits. At the same time, the submission recognised that, in the course of negotiations, some concessions, short of total exemption, could be made where there were commensurate advantages to Australia.\(^ {70}\)

4.42 The submission noted that, prior to the introduction of dividend withholding tax in Australia, foreign resident shareholders in non-treaty countries were taxed on an assessment basis at normal rates. Following the introduction of dividend withholding tax, these shareholders were now taxed at a rate of 6/- in the £ (that is, 30%). However, under the treaties with the US, Canada and NZ the rate of withholding tax was reduced to 3/- in the £ (that is, 15%), and the UK tax treaty, which reduced source taxation of dividends by 50% (except for dividends paid by wholly owned subsidiaries that were exempt from source taxation), had substantially the same effect.\(^ {71}\)

4.43 Countries that were capital exporters to Australia would be likely to seek similar concessions in taxation treaties with Australia, arguing that the concessions would promote further investment in Australia by their residents. This argument was regarded as valid in situations where the domestic law of the potential treaty partner exempted foreign source dividends. However, where the potential treaty partner relieved international juridical double taxation using a credit system, the benefit of reductions in dividend withholding tax was seen as accruing to the foreign Treasury rather than to the foreign investor.\(^ {72}\)

4.44 In relation to non-portfolio foreign investment in Australia, the submission pointed out that the investment could either be through branch or subsidiary operations. In the former case, the non-resident was taxed on income from Australian sources in the same way and at the same rates as Australian residents with no concession being allowed under Australia’s existing taxation

\(^ {69}\) Cabinet Submission 305, p11.
\(^ {70}\) Cabinet Submission 305, p11.
\(^ {71}\) Cabinet Submission 305, p11. Dividend withholding tax was introduced by \textit{Income Tax and Social Services Contribution Act (No 3) 1959} and applied to dividends paid by Australian companies to non-resident shareholders on or after 1 July 1960.
\(^ {72}\) Cabinet Submission 305, pp11–12.
treaties, although there was no further taxation of remissions of branch profits to the parent organisation. By contrast, in the absence of a taxation treaty an Australian subsidiary of a foreign company bore Australian corporate tax and was then subject to Australian dividend withholding tax of 6/- in the £ (30%) on dividends remitted to a foreign parent, bringing the total Australian tax to 11/- 7d in the £ (approximately 58%). Under Australia’s existing taxation treaties, the withholding tax was reduced to 3/- in the £ with the effect that the total Australian tax was reduced to 9/- 9d in the £ (48.75%).

4.45 The submission then commented that ‘the relative magnitude of the withholding tax concession arising from the present agreements is, therefore, somewhat less than it might appear to be at first sight’. This assumed that dividends paid to foreign parents were wholly funded from profits subject to Australian corporate tax.

4.46 The submission considered that reductions in withholding tax in further taxation treaties would be likely to make investment via subsidiaries more attractive relative to investment via branches and to increase remittances by Australian subsidiaries to foreign parents (with the benefit of increased collections of withholding tax but at the expense of net foreign investment), particularly where little unilateral relief from international juridical double taxation was currently granted by the foreign parent’s country.

4.47 The submission argued that the price at which portfolio foreign investors purchased Australian equities reflected investment returns to Australian investors, which took account of the absence of credit for Australian corporate

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73 While true in the case where the non-resident was trading through an Australian branch, this was misleading as, in the absence of a taxation treaty, Australia claimed the right to tax Australian source business profits whether or not they were attributable to a permanent establishment.

74 Cabinet Submission 305, p13. At the time, Australia applied progressive scales to companies and applied different scales to public and private companies and to resident and non-resident public companies. For resident public companies, the rate was 35% on the first £5000 of taxable income and 40% thereafter. For non-resident public companies, the rate was: (a) 30% on so much of the taxable income consisting of dividends as did not exceed £5000; (b) 35% on so much of the taxable income not consisting of dividends as did not exceed the amount (if any) by which the taxable income consisting of dividends was less than £5000; and (c) where neither (a) nor (b) applied, the rate was 40%. For private companies (whether resident or non-resident), the rates were 25% on the first £5000 of taxable income and 35% thereafter. Undistributed profits tax at the rate of 50% was payable by private companies. The rates of corporate tax at the time are discussed in J A L Gunn and O E Berger, Gunn’s Commonwealth Income Tax Law and Practice (Butterworths, 7th ed, 1963) 1211 and 1212.

75 Cabinet Submission 305, pp13–14.
tax. Therefore, the only tax that foreign portfolio investors paid was dividend withholding tax at 6/- in the £. Hence, the submission argued, reductions in withholding tax under taxation treaties ‘was an outright concession in the case of this type of investment’. The submission also noted that the UK system of corporate-shareholder taxation meant that UK portfolio investors in Australian equities obtained credit for Australian corporate tax and that this gave them advantageous returns when compared with Australian investors in Australian equities. The submission’s conclusion on the treaty treatment of dividends was that, if concessions were to be offered in future, then, so far as was practicable to do so, they should only be offered to non-portfolio investors.

4.48 The overall conclusion in the submission on the concessional treatment of dividends in taxation treaties was negative. While it might be that the concessions would lead to some increase of foreign direct investment into Australia, they would add significantly to the cost to Australia of that investment, a cost which would be likely to increase over the life of treaties with a ‘more or less interminable nature’. As Australia had recently provided tax benefits to all foreign investors through the introduction of the system of withholding taxes on dividends, the submission considered that Australian taxpayers would not welcome a further reduction in the tax paid by foreign investors, particularly portfolio investors. The emphasis in the submission is on pragmatic revenue considerations rather than on a theoretical or principled analysis of taxing rights in the international context.

4.49 The submission concluded with a nine-point summary derived from the earlier arguments within it. The nine points were:

1. Australian residents were already provided (via ITAA 1936 s23q) with almost complete protection from double taxation of foreign source income.

2. The especially close ties that Australia had with its existing treaty partners meant that those treaties were not necessarily precedents for Australian treaties with other countries.

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76 Cabinet Submission 305, p14.
77 Cabinet Submission 305, pp14–15.
78 Cabinet Submission 305, p15.
79 Cabinet Submission 305, pp15–16.
3. The recently introduced dividend withholding tax limited Australian tax on dividends and thus benefitted investors resident in non-treaty countries deriving Australian source dividends.

4. The chief purpose of relieving double taxation through treaties was served by defining the areas of income to be taxed by each country and the relief to be given by each country to its residents for income derived in the treaty partner; this meant that there was no need for 'concessions' by either country but that there was 'everything to be said' for treaties 'as an aid to ordering the flow of income derived from everyday trade and commerce'.

5. The effectiveness of treaties in relieving double taxation would not be impaired if they did not exempt foreign shipping profits from Australian tax and did not reduce the rate of tax on dividends.

6. Exemption of shipping profits from Australian tax, the main object of many approaches Australia had received, would have a considerable revenue cost to Australia and, at least in relation to taxation, would not produce offsetting benefits.

7. Reduction of Australian tax on dividends, particularly non-portfolio dividends, might provide some encouragement to foreign investment in Australia, but, as much of the benefit of the reductions would flow to foreign Treasuries, the effect on the inflow of capital would 'undoubtedly be marginal'.

8. Australia should 'stand ready' to enter into negotiations with any country seeking a treaty with Australia subject to the proviso that, if preliminary bilateral discussions made it clear that no useful purpose would be served by formal negotiations as there would be no hope of success, then formal negotiations should not be proceeded with.

9. Before the conclusion of any treaty, particularly if it contains significant concessions, the government should satisfy itself that the treaty would offer a balance of advantages to Australia. Up to a point, such advantages could be non-tax advantages.\(^\text{80}\)

\(^\text{80}\) Cabinet Submission 305, pp16–18.
The submission argued that it would usually be in Australia’s interest to enter into further treaties which did not exempt shipping profits and did not reduce the rate of tax on dividends derived in Australia. The submission identified Commonwealth countries (such as Malaysia) with whom Australia did not have existing treaties and other Asian countries (other than Japan) as potential partners for such treaties on the basis that to them ‘these two aspects are of little importance’.  

For other countries, the submission stated that some concessions on shipping profits and on the rate of Australian tax on dividends could be considered at least where commensurate direct advantages, some of which might be unrelated to taxation, could be negotiated for Australia. Negotiations would always require Cabinet’s authorisation, and the treaties themselves would require Cabinet’s approval and would be preceded by discussions between officials. The stages in the process should mean that all considerations associated with treaties would be taken into account. Nonetheless, the submission then stated:

‘As a starting point, however, I think that we should endeavour to avoid having concessions in respect of shipping profits and dividends included in any further double taxation agreements and, unless there are compelling reasons for doing so, I certainly think that we should avoid including in further agreements concessions going so far as those in our existing agreements.’

The submission recommended that this general approach be used when the question of negotiating a tax treaty with a potential partner arose and that, following departmental consideration, proposals to open negotiations, and the basis on which they were to be conducted, be submitted to Cabinet for approval.

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81 Cabinet Submission 305, p18. The statement is consistent with the recognition by the Department of External Affairs during the drafting of Cabinet Submission 305 that there would be little loss of revenue in granting concessions to countries where Australia was a net capital exporter. R A Peachey, for The Secretary, Department of External Affairs, to The Secretary, Department of the Treasury, Canberra, ACT, 9th January 1962, p1, para 2, in Double Taxation Agreements With Other Countries, Policy, NAA, Series Number A571, Control Symbol 63/3972 Part 2, pp1–2, paras 3 and 4.

82 Cabinet Submission 305, p18.

83 Cabinet Submission 305, p19.

84 Cabinet Submission 305, p19.
4.51 The submission noted that a further relevant consideration was the UK’s moves to join the EEC. As entry of the UK into the EEC would affect Australia’s relations with European countries generally, the submission recommended that further discussions on treaties with the ‘countries concerned’ should be deferred until the result of the UK’s moves was clear.85

The 1962 Cabinet Decision

4.52 On 10th August 1962 the Australian Cabinet agreed that, in deciding whether Australia should enter into any further tax treaties, the government should be guided by the considerations discussed at paragraph 4.49, with individual cases being examined carefully on their merits as they arose. The same approach was to apply to renegotiation of existing treaties. Any proposals to open negotiations and the basis on which negotiations were to be conducted were to be submitted to Cabinet for approval.86

4.53 Following the Cabinet decision, M W O’Donnell87 wrote to Holt88 pointing out that, in view of the Cabinet decision discussed in 4.52, approaches by the European countries identified in the Cabinet submission could be ‘put aside for the time being’.89 This left Japan, South Africa and the countries of South-East Asia as countries with which ‘negotiations might be pressed forward’.90

4.54 The immediate problem was seen as opening negotiations with Japan, given that the review of policy had been initiated when a request for a tax treaty was received from Japan in mid 1959 and that Japan was ‘probably the most important trading nation for Australia with which we do not have an agreement’.91 A Japanese mission was currently visiting New Zealand to negotiate a tax treaty, and the Japanese Embassy had ‘expressed a strong

86 Cabinet Minute, 10th August 1962, Decision Number 386. A copy of the Cabinet minute is contained in ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1.
87 O’Donnell was then Assistant Secretary, Department of the Treasury.
88 Holt was Treasurer at the time.
90 M W O’Donnell, above n 89, 2, para 5.
91 M W O’Donnell, above n 89, 2, para 6.
desire’ for its officers to discuss the possibility of a tax treaty with Australia when the mission was passing through Canberra en route to Japan.\textsuperscript{92} O’Donnell recommended that there be a preliminary exchange of information about the Japanese and Australian tax systems with the Japanese delegation when it visited Canberra, to be followed by inter-departmental discussions of the issues involved in negotiating a tax treaty with Japan.\textsuperscript{93} The discussions would be ‘very preliminary’ and would not amount to opening negotiations with Japan but rather would be taking advantage of an opportunity to obtain information on Japanese tax law.\textsuperscript{94}

4.55 O’Donnell also recommended the reopening of the subject of tax treaties with South Africa and with South-East Asian countries with a view to an early commencement of negotiations.

4.56 O’Donnell’s third recommendation was that, in accordance with Cabinet’s decision, any action on approaches by European countries be deferred.\textsuperscript{95} Holt then made decisions giving effect to these recommendations.\textsuperscript{96}

**Australia’s First Assessment Of The 1963 Draft OECD Model**

4.57 During this period, the OECD was in the process of developing what was to become the 1963 draft OECD Model Convention. On 27\textsuperscript{th} February 1963, O’Donnell requested that the Commissioner of Taxation advise on the acceptability to Australia of the various articles already adopted by the OECD. The Commissioner was asked to distinguish between the effects of accepting the OECD draft on Australia’s existing tax treaties and on those yet to be negotiated.\textsuperscript{97}

\textsuperscript{92} M W O’Donnell, above n 89, 2, para 6.

\textsuperscript{93} M W O’Donnell, above n 89, 2, para 8.

\textsuperscript{94} M W O’Donnell, above n 89, 2, para 7.

\textsuperscript{95} M W O’Donnell, above n 89, 2, para 8.

\textsuperscript{96} M W O’Donnell, Assistant Secretary, Department of the Treasury to The Secretary, Department of External Affairs, Canberra, ACT, 20\textsuperscript{th} August 1962 and M W O’Donnell (Assistant Secretary, Department of the Treasury) to the Commissioner of Taxation, Canberra, ACT, 20\textsuperscript{th} August 1962, note the Treasurer’s affirmative decision in relation to each of the recommendations made in O’Donnell’s letter to the Treasurer dated 16\textsuperscript{th} August 1962. ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1.

\textsuperscript{97} M W O’Donnell, First Assistant Secretary, Department of the Treasury to the Commissioner of Taxation, Canberra, ACT, 27\textsuperscript{th} February 1963, ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 3.
4.58 M J Belcher, Assistant Commissioner of Taxation, replied on 5th March 1963. Belcher’s reply was based on the OECD material then available to the ATO, namely four reports of the Fiscal Committee published between September 1958 and August 1961. After outlining the methods by which the OECD draft provided for avoiding double taxation, Belcher went on to examine the effect of modifying Australia’s existing tax treaties to accord with the OECD draft.  

4.59 Belcher’s analysis began by noting that there might be advantages in extending the scope of Australia’s treaties to include sub-national taxes in line with the OECD draft as a counter to a tax planning strategy that had been developed by professors and teachers visiting the US who were exempt from US tax under the 1953 Australia–US Tax Treaty but who argued that they were exempt from Australian tax under ITAA 1936 s23q when they paid a small amount of State Income Tax in the US.  

4.60 Belcher considered that an extension of taxes covered to payroll tax as envisaged under the OECD Model would involve some loss of Australian revenue but that this would be likely to be small. Belcher noted that the OECD draft included taxes on capital, and observed that the intention was evidently to prepare model treaties on death and estate duties but that there was no indication of what the content of these would be.  

4.61 Belcher made interesting comments concerning the definition of ‘permanent establishment’ in the OECD draft and in Australia’s existing treaties, noting that the definitions were ‘not constant’, had been ‘developed in the light of experience’ and reflected the viewpoint both of Australia and the relevant treaty partner. Belcher then commented: ‘In the case of the UK a wider definition would have been adopted if the UK had agreed but in the case of NZ it was not in Australia’s interest to seek a wide definition.’ Belcher then observed that the definition in the OECD draft appeared to favour capital exporting countries and that it would be advisable to have a definition at least as wide as that in Australia’s existing tax treaties with the US, Canada and New Zealand.

98 M J Belcher, Assistant Commissioner of Taxation, to M W O’Donnell, First Assistant Secretary, Department of the Treasury, 5th March 1963, pp1–2, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 3.  
100 Belcher to O’Donnell, above n 98, 3, para 13.  
Paragraph 1 of Article II of the OECD draft, in Belcher’s view, was ‘clearly designed’ to attribute to a permanent establishment the ‘essential characteristic of having a distinct situs; a fixed place of business’. Noting that the OECD Commentary described the examples referred to in paragraph 2 as ‘prima facie’ instances of a permanent establishment, Belcher considered that this raised the possibility that a branch or an agency might not, in some cases, ‘due to the strongly explicit terms of paragraph 1’, be considered to be a permanent establishment. Belcher did not regard the possibility as strong but considered that the article as a whole was sufficiently ambiguous for the point to be argued.\(^{102}\)

Belcher commented that Article II(2)(g), which regarded a building site or construction project that existed for twelve months as a permanent establishment, was satisfactory from an Australian viewpoint.\(^{103}\)

On balance, Belcher concluded, the OECD draft definition of permanent establishment was less favourable to Australia than the equivalent definition in any of Australia’s existing tax treaties.\(^{104}\)

Turning to the definitions of ‘resident’ in the OECD draft, Belcher noted the tie-breaker provisions but considered that some of the tests could give rise to practical difficulties and differences of opinion with the relevant treaty partner. Belcher commented that the OECD definitions would clearly ‘be major departures from the definition in our law and from the concept of residence as it applies to some aspects of existing agreements’.\(^{105}\)

Belcher was concerned that the non-discrimination article might prevent Australia from discriminating against non-residents by denying them an inter-corporate rebate under ITAA 1936 s46(1). Belcher observed that this would have a ‘tremendous impact’ on revenue if applied to Australia’s existing tax treaties as, under those treaties, only dividends paid by a wholly owned subsidiary to a UK parent were exempt from Australian tax at source.\(^{106}\)

\(^{102}\) Belcher to O’Donnell, above n 98, 3, para 15. The 1977 OECD Commentary was subsequently to make clear that the examples contained in OECD Art 5(2) only constitute permanent establishments if they meet the requirements of OECD Art 5(1) and that to meet the requirements of Art 5(1) the place of business must be ‘fixed’. 1977 OECD Commentary on Article 5(1) paragraph 5 of the commentary and 1977 OECD Commentary on Article 5(2) paragraph 12 of the commentary.

\(^{103}\) Belcher to O’Donnell, above n 98, 3, para 16.

\(^{104}\) Belcher to O’Donnell, above n 98, 3, para 16.

\(^{105}\) Belcher to O’Donnell, above n 98, 3–4, paras 17–18.

\(^{106}\) Belcher to O’Donnell, above n 98, 4, para 19.
Belcher considered that this interpretation of the non-discrimination article might not have been intended and that it would be important to have the position clarified before agreeing to the article.\textsuperscript{107}

4.67 The OECD draft shipping and aircraft profits article provided for exclusive taxation by the country where the place of effective management of the relevant enterprise was located.\textsuperscript{108} Under existing Australian tax treaties, shipping and aircraft profits were exempt from tax at source if the ship or aircraft was registered in the relevant treaty partner country in which the owner or charterer resided. Belcher noted that the provision in the draft OECD Model would widen the exemption, because only the place of effective management of the relevant enterprise and not the place of registration of the ship or aircraft would be relevant.\textsuperscript{109}

4.68 Agreeing to a provision of this nature would, on Belcher’s calculations, be likely to produce an annual loss of revenue to Australia of £100,000 per year under Australia’s existing agreements without any compensating tax gain to Australia.\textsuperscript{110} If Australia were to enter into tax treaties containing this provision with several identified European countries, the additional loss of Australian revenue would be £500,000 per year.\textsuperscript{111}

4.69 Belcher noted that the income from the Immovable Property article would enable Australia to continue to tax rents of foreign owned property situated in Australia and royalties from foreign owned natural resources situated in Australia. Belcher considered that the article was satisfactory to Australia.\textsuperscript{112}

4.70 Turning to the business profits article, Belcher noted that source taxation of profits attributable to a permanent establishment in the source state broadly corresponded with the basis adopted in Australia’s existing tax treaties with the UK, the US and Canada.\textsuperscript{113} The comment appears to be odd in relation to the 1953 Australia – US Tax Treaty under which, as noted at 3.46 a force of attraction basis applied to source taxation of industrial or commercial profits once a permanent establishment existed in the source country. The same

\begin{footnotes}
109 Belcher to O’Donnell, above n 98, 4, para 22.
110 Belcher to O’Donnell, above n 98, 4, para 23.
111 Belcher to O’Donnell, above n 98, 4, para 24.
112 Belcher to O’Donnell, above n 98, 5, para 28.
113 Belcher to O’Donnell, above n 98, 5, paras 30–1.
\end{footnotes}
basis also applied to taxation of industrial or commercial profits under the 1960 Australia – NZ Tax Treaty.

4.71 Belcher pointed out that Australia’s existing tax treaties preserved Australia’s rights to tax film businesses controlled abroad and insurance with non-residents under *ITAA 1936* divs 14 and 15 respectively, and that this protection of Australian revenue would be lost if the OECD draft were adopted.

4.72 Belcher anticipated that there would be large annual revenue losses for Australia if the Business Profits article in the OECD draft were applied without reservation. On the computation of business profits attributable to a permanent establishment, Belcher commented that existing Australian tax treaties gave ‘a greater degree of protection to Australia’ than did the draft OECD provisions. Belcher pointed out that the OECD draft articles would probably prevent the application of *ITAA 1936* s136, the operation of which had been expressly preserved in Australia’s existing tax treaties. Belcher also considered that the OECD draft articles might interfere with the operation of the Australian general anti-avoidance provision, *ITAA 1936* s260. Loss of Australian revenue in both these cases was indeterminate.

4.73 Similarly in relation to the income of Associated Enterprises article, Belcher commented that the provision was broadly comparable to equivalent provisions in existing Australian tax treaties but, for the reasons stated in relation to the Business Profits article, provided less protection for Australian revenue than those provisions.

4.74 Belcher contrasted the maximum rate of source country tax of 5% on non-portfolio dividends allowed under the dividend article in the OECD draft article with the 15% rate that applied in Australia’s existing tax treaties other than the 1946 Australia – UK Tax Treaty where dividends paid by a wholly owned subsidiary were exempt from source country tax while source country tax on all other dividends was reduced by one half. Belcher noted that the loss to Australian revenue of adopting the OECD draft article would, on the basis of

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115 The background to the insertion of the saving provision for *ITAA 1936* s136 in the 1946 Australia – UK Tax Treaty was discussed at 2.124 to 2.126.
116 Belcher to O’Donnell, above n 98, 6, para 36.
118 Belcher to O’Donnell, above n 98, 7–8, paras 43–8.
1960–61 statistics, be £1.75m per year, and considered that the revenue cost could be ‘very appreciably’ above £1.75m per year in the future.119

4.75 Belcher also pointed out that the 1946 Australia – UK Tax Treaty allowed Australian shareholders to gross up dividends for underlying UK corporate tax and to receive a credit for that tax, a procedure that was not required under the OECD draft. Adoption of the OECD draft would require revision of the basis of Australian tax on dividends paid by UK companies to Australian shareholders.120

4.76 Belcher pointed out that the Interest article in the OECD draft had no equivalent in Australia’s existing tax treaties, which allowed interest to be taxed on a source basis with the residence country providing a credit for the source tax. Belcher’s comment on the 10% limit on source country taxation of interest in the draft OECD Model was: ‘This is obviously disadvantageous from an Australian revenue viewpoint and the article would, if revenue is the sole yardstick, be unacceptable.’121 Belcher estimated the revenue loss from agreeing to the OECD draft article as being tentatively £1.0 million per year.122

4.77 The royalty article in the OECD draft only permitted source taxation of royalties if they were effectively connected with a permanent establishment in the source country. Belcher noted that this was the position in relation to both industrial and cultural royalties in the 1946 Australia – UK Tax Treaty, but that in the 1953 Australia – US Tax Treaty and in the 1957 Australia – Canada Tax Treaty only cultural royalties were taxed on a residence basis. Belcher pointed out that, under all of Australia’s existing tax treaties, motion picture films were specifically excluded with the result that Australia was able to tax them under ITAA 1936 div 14. Belcher considered that the OECD draft article would generally be less advantageous to Australia, particularly in relation to film royalties. An estimate of the loss of Australian revenue in relation to industrial royalties if the OECD draft article were implemented was not available, but Belcher commented that, ‘for all practical purposes’, there would be no loss of revenue in relation to cultural royalties.123

119 Belcher to O’Donnell, above n 98, 12, PS (a).
120 Belcher to O’Donnell, above n 98, 8, para 49.
121 Belcher to O’Donnell, above n 98, 8, paras 50–1.
122 Belcher to O’Donnell, above n 98, 12, PS (b).
123 Belcher to O’Donnell, above n 98, 9, paras 53–6.
Belcher observed that the other income article, which provided for exclusive taxation in the residence country, contrasted with the position under existing Australian treaties where full source country taxing rights were retained in respect of such income. Belcher commented that the approach under existing Australian treaties was favourable to Australia in situations where there was a net outflow of income from Australia. Australia’s previous treaties had not contained any article dealing with other income, and Belcher’s conclusion as to the effect of that omission is clearly based on the view that full source country taxing rights were retained in relation to all types of income not expressly mentioned in a tax treaty.

Belcher then discussed the alternative methods in the OECD draft for relieving double taxation. After identifying exemption with progression, Belcher commented that its adoption would preclude the use of the credit method but would not involve a revenue loss for Australia. Belcher noted that exemption of foreign source income other than dividends corresponded with the then current Australian domestic law, but commented that Australia in its existing tax treaties had deliberately restrained from committing to continuing the exemption and had agreed that if Australia taxed foreign source income, a credit would be allowed for foreign tax paid. Belcher commented that the limitation on the credit for foreign tax on interest and dividends in the credit provisions in the draft, namely the amount of residence tax otherwise payable, corresponded with the limitations in Australia’s existing tax treaties and in s14 of the Income Tax (International Agreements) Act (Cth) 1953. Belcher noted that Australia had sought and obtained a credit basis of relief for all types of income in its existing tax treaties, notwithstanding that Australian domestic law only adopted a credit basis in relation to dividends. Belcher’s conclusion was that, based on Australia’s past attitude, an overall credit basis would be preferred and that no loss of revenue would be involved.

Belcher described the mutual agreement article in the OECD draft as ‘a machinery provision’ and ‘unobjectionable’, noting that the article was permissive and did not detract from appeal rights of a taxpayer under
Australian domestic law even if the taxpayer had exercised rights under the mutual agreement procedure. Belcher noted that, in relation to domestic law appeal rights, time periods in domestic legislation would still have to be observed.\footnote{Belcher to O'Donnell, above n 98, 10, paras 63–5. As noted in Appendix One of current Australian tax treaties, only the 2003 Australia – UK Tax Treaty applies time periods in domestic law in this context.}

4.81 Belcher considered that in the case of some OECD countries there would be a real possibility of Australia obtaining more favourable tax treaties than the draft OECD Model. In particular, Belcher considered that agreement might be obtained for a 15% rate on all dividends, source taxation of royalties and, in some cases, a willingness for Australia to collect some of its tax on shipping profits.\footnote{Belcher to O'Donnell, above n 98, 11, para 67.} Australia’s prior experience in negotiating tax treaties would have provided cause for hope in relation to dividends and royalties. In relation to shipping profits, the only aspect in which Australia’s prior tax treaty experience would have provided grounds for believing that greater source country taxing rights were obtainable was by making the exemption only available where the ship was registered in the treaty partner country. In Belcher’s view, it was unclear whether Australian membership of the OECD would preclude it from seeking such provisions in tax treaties, but he considered that if Australia became a member of the OECD it might be more difficult to obtain favourable results on these points.\footnote{Belcher to O'Donnell, above n 98, 11, para 67.}

4.82 In relation to non-OECD countries, Belcher commented that the most important case was Japan. In Belcher’s view, acceptance by Australia of the draft OECD Model would make it more difficult for Australia to persuade Japan to agree to allowing Australia to levy approximately 50% of its present tax on shipping and to accept a source basis of taxation in relation to other types of income, particularly interest.\footnote{Belcher to O'Donnell, above n 98, 11, para 68. As recommended by O'Donnell (see the discussion at 4.34), and as discussed at 6.4, Australian and Japanese officials had a preliminary exchange of information about their respective tax systems in August 1962.}

4.83 Belcher also noted that the draft OECD Model did not contain tax sparing provisions and commented that, while acceptance of the OECD Model would not weaken Australia’s position in negotiating with Singapore and Malaya
(both of whom sought tax sparing provisions) it was doubtful that it would provide any positive assistance.\(^{133}\)

4.84 Belcher’s overall conclusion on the draft OECD Model was that its provisions were more favourable to the capital exporting and maritime nations than they were to a capital importing country like Australia and were less favourable to Australian revenue than those in Australia’s existing tax treaties.\(^{134}\) Adoption of the draft OECD Model would involve departure in several respects from the principles approved in Cabinet decision 386. To justify the revenue losses, there would need to be non-tax benefits of OECD membership.\(^{135}\)

The 1963 Reassessment Of Australian Tax Treaty Policy

4.85 Following the suspension of negotiations concerning the UK’s initial bid to join the EEC,\(^ {136}\) Treasury officials, in August 1963, prepared a further submission on future policy relating to tax treaties.\(^ {137}\) The submission noted that, independently of whether the UK joined the EEC, there was likely to be significant change in the tax systems of countries in the EEC because it had started a program of ‘fiscal harmonisation’.\(^ {138}\)

4.86 The submission also noted the development of model tax treaty articles by the OECD and expressed concern that the OECD draft might introduce some rigidity into the negotiations. This was seen as undesirable because several provisions in the OECD draft were regarded as not being acceptable to Australia.\(^ {139}\)

4.87 Neither the uncertainty about the future of the tax systems of European countries nor the possibly widespread future use of the OECD Model (both of

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\(^ {133}\) Belcher to O’Donnell, above n 98, 11, para 69. Australia had, by this point, received draft treaties from Singapore and Malaya. The negotiations relevant to those treaties are not discussed in detail in this thesis.

\(^ {134}\) Belcher to O’Donnell, above n 98, 11, para 70.

\(^ {135}\) Belcher to O’Donnell, above n 98, 11, para 71. Cabinet decision 386 was discussed at 4.52.

\(^ {136}\) For a discussion of Australia’s response to the UK’s second bid to join the EEC see Andrea Benvenuti, “Layin’ Low and Sayin’ Nuffin”: Australia’s Policy Towards Britain’s Second Bid to Join the European Economic Community’ (2006) 46 Australian Economic History Review 155 and the discussion in Singleton and Robertson, above n 85, chs 9 and 10.

\(^ {137}\) ‘Confidential for Cabinet, Double Taxation Agreements With European Countries: Submission 871: Harold Holt, Treasurer: 26th August 1963.’ A copy of the submission is contained in ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. Hereafter the submission is referred to as ‘Cabinet Submission 871’.

\(^ {138}\) Cabinet Submission 871, p1, para 3.

\(^ {139}\) Cabinet Submission 871, pp1–2, para 3.
which had been characterised as being ‘some distance away’) were seen as
constituting sufficient grounds for refusing to negotiate with European
countries. On the contrary, the submission suggested that there might be
advantages in negotiating tax treaties with European countries before their
tax systems and their attitudes to articles usually included in tax treaties
became too rigid.140

4.88 After pointing out that officials had held preliminary discussions with Japan
and anticipated holding discussions with Malaysia once the Federation was
established, the submission considered that Australia could hardly decline to
negotiate tax treaties with European countries until the pattern of European
economic relations had been more firmly established.141

4.89 Hence the submission recommended that Cabinet remove the barrier,
introduced by Cabinet decision 386, against entering into negotiations with
European countries so that proposals from whatever source would, in future,
be examined on their individual merits.142 On 10th September 1963, Cabinet
accepted the recommendations in the submission.143

The Development Of The 1965 Australian Model Tax Treaty

4.90 In anticipation of the Cabinet decision of 10th September 1963, O’Donnell
wrote to the Commissioner of Taxation noting that Japan (as discussed in
more detail in Chapter 6), Singapore and Malaya, in the recent preliminary
discussions on tax treaties, had provided draft treaties to serve as a starting
point. O’Donnell considered that there would be advantages if initial
negotiations were based on a draft that reflected Australia’s viewpoint. While
recognising that there could be no ‘universal draft’, as Australia’s interests
would differ for different countries, O’Donnell believed that suitable initial
drafts should be prepared for negotiations with European countries and with
Malaysia.144

140 Cabinet Submission 871, p2, para 3.
141 Cabinet Submission 871, pp2–3, para 4.
142 Cabinet Submission 871, p3, para 5.
143 Cabinet Minute, Decision 1009, Canberra, 10th September 1963. A copy of this
minute is contained in ‘General Review of Double Tax Proposals, Part 1’ NAA, Series
Number A7073, Control Symbol J245/68 Pt 1.
144 M W O’Donnell (First Assistant Secretary, Department of the Treasury) to the
Commissioner of Taxation, Canberra, ACT, 28th August 1963, in ‘General Review of
Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68
Pt 1. In the case of Malaysia, O’Donnell noted that drafts had been received from
In the case of European countries, if Cabinet agreed to the recommendations in the submission of 26th August 1963, then Australia might be faced with a large number of requests for tax treaties at short notice. If so, O'Donnell considered, there would be advantages in having a draft treaty which could be sent to European countries. As the European countries might consider that any tax treaty should be based on the draft OECD Model, it would be desirable for the Australian draft to embody as much of the OECD Model as was ‘acceptable to us’. O'Donnell pointed out that, of course, any draft would have to take into account the review of tax treaty policy by Cabinet decision 386. O'Donnell closed by requesting the Commissioner's views on the subject.\(^{145}\)

**The Draft By M J Belcher**

In response to O'Donnell’s request, Belcher prepared a draft for use as the basis for Australian tax treaty negotiations with European countries.\(^{146}\) While Belcher’s covering letter included comments on some articles in his draft,\(^{147}\) it did not systematically catalogue differences between his draft and the OECD Model and did not draw O'Donnell’s attention to the history of many of the distinctive features of his draft.

The substantive content and overall structure of Belcher’s draft closely resembles the 1960 tax treaty between Australia and NZ, but in some presentational aspects and with some, probably not significant, verbiage it follows the 1963 draft OECD Model. In some instances, Belcher’s draft gives greater source country taxing rights to Australia than had been the case under prior Australian treaties. This is most notably the case with the treatment of dividends, interest and royalties as a consequence of complying with Australian Cabinet decision 386.

\(^{145}\) M W O'Donnell, above n 144, 1.

\(^{146}\) Belcher’s draft is contained in General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1. The document is hereafter referred to as ‘Belcher’s draft’.

\(^{147}\) M J Belcher, First Assistant Commissioner to W M O'Donnell, First Assistant Secretary, Department of the Treasury, Canberra, ACT, 9th March 1964, in ‘General Review of Double Tax Proposals, Part 1’ NAA, Series Number A7073, Control Symbol J245/68 Pt 1.
4.94 Belcher began by commenting that his draft followed the OECD Model Convention in that it permitted source taxation of industrial or commercial profits only to the extent that they were attributable to a permanent establishment in the source country. This, Belcher noted, was consistent with Australia’s existing treaties with the UK and Canada but differed from Australia’s treaties with the US and NZ, which applied a force of attraction approach. Belcher’s comment on the two approaches was: ‘No strong preference as between the two approaches is felt and if European countries wish to adopt the OECD model there seems no reason for Australia to resist.’ 148

4.95 Belcher’s letter does not point out that Article III(2) of his draft preserved the operation of divs 14 and 15 of ITAA 1936 dealing with film businesses controlled abroad and insurance with non-residents respectively. Nor does Belcher point out that Article III(5) of his draft preserved the right to apply domestic law provisions giving tax authorities power to determine industrial or commercial profits attributable to a permanent establishment using discretion or on the basis of estimates in situations where information was inadequate to determine them.

4.96 Belcher also noted that the OECD Model contained a broadly corresponding provision to Article III(4) of his draft that allowed for deductions of expenses, reasonably attributable to the permanent establishment, in calculating industrial or commercial profits. Belcher merely commented that the paragraph ‘does not go any further in allowing deductions than is the practice under the present Australian law’ 149 and did not point out that the paragraph included a savings provision in relation to ‘the principle underlying’ s38 of ITAA 1936.

4.97 Belcher’s draft reflected the policy decisions made in Cabinet decision 386. Thus Belcher’s draft did not contain provisions limiting source taxation of dividends or shipping or aircraft profits. The definition of industrial or commercial profits expressly excluded dividends and profits from the operations of ships or aircraft. 150 Belcher considered that this meant that, in

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148 Belcher to O’Donnell, above n 147, para 5.
149 Belcher to O’Donnell, above n 147, para 6. As discussed in Chapter 3, the first Australian tax treaty to contain a provision to this effect was the 1953 US Treaty.
150 The definition of ‘industrial or commercial profits’ was contained in Article II(1)(h) of Belcher’s draft and expressly excluded, inter alia, ‘dividends’ and ‘income from operating ships or aircraft’.
combination with the absence of an ‘other income’ article in the draft, full source country taxing rights would be maintained in relation to dividends and to shipping and aircraft profits.\textsuperscript{151}

4.98 Belcher did not appear to be in favour of this aspect of the policy Cabinet decision 386, commenting that European countries might expect concessions by the source country in relation to these items of income and might not enter into treaties consistent with Belcher’s draft in these respects.\textsuperscript{152} He did consider that some European countries might permit Australia to retain some of the tax that it had been collecting from ships carrying passengers and cargo from Australia.\textsuperscript{153}

4.99 Belcher’s draft did not contain a provision dealing with the taxation of royalties, with the consequence, in Belcher’s view, that full source country taxing rights would be retained. Belcher noted that European countries might be opposed to the Australian position. Belcher considered that Australia could offer to adopt a residence basis in relation to copyright royalties but that ‘[i]t has not been thought necessary to offer this at the outset’.\textsuperscript{154}

4.100 Belcher’s draft contained the same structural features as earlier Australian treaties, with industrial or commercial profits being defined in terms that excluded particular categories of income, with no interest article, no capital gains article and no other income article. The definition of ‘industrial or commercial profits’ was critical to this structure and was identical to the definition in the Australia – NZ Tax Treaty of 1960, which itself had developed the definition in earlier Australian tax treaties by adding to the list of types of income excluded from being industrial or commercial profits; that is, ‘income arising from, or in relation to contracts or obligations to provide the services of public entertainers such as stage, motion picture, television or radio artists, musicians and athletes’.\textsuperscript{155}

4.101 Consistent with earlier Australian treaties, under Belcher’s draft dual residents were not treaty residents and there was no dual residence tie-breaker. The

\textsuperscript{151} Belcher to O’Donnell, above n 147, para 3 (comment on reflecting principles in Cabinet decisions), paras 7 and 8 (shipping and aircraft profits), para 9 (dividends), and para 16 (other income).

\textsuperscript{152} Belcher to O’Donnell, above n 147, para 8 (shipping and aircraft profits) and para 9 (dividends).

\textsuperscript{153} Belcher to O’Donnell, above n 147, para 8.

\textsuperscript{154} Belcher to O’Donnell, above n 147, para 15.

\textsuperscript{155} Belcher’s draft, Article II(1)(h), which was identical to Article II(1)(h) in the 1960 NZ Treaty.
provisions dealing with residence in Belcher’s draft were identical to those in the 1957 Australia – Canada Tax Treaty and in the 1960 Australia – NZ Tax Treaty. Like those two treaties and the 1953 Australia – US Tax Treaty, Belcher’s draft did not contain an equivalent to the provision for proportional credits for tax on third country income contained in the 1946 Australia – UK Tax Treaty.

4.102 The definition of ‘permanent establishment’ in Belcher’s draft represented a consolidation, refinement and extension of definitions in earlier Australian treaties. It opened with language that largely followed Article 5(1) of the 1963 draft OECD Model. The definition included, as an example of a permanent establishment, a provision identical to Article 5(2)(g) of the 1963 draft OECD Model with the addition of a reference to ‘supervisory activities for such a site or project for more than twelve months’. Earlier Australian treaties had merely referred to a ‘construction project’ as an example of a permanent establishment. Belcher’s draft narrowed the scope of the definition in prior Australian tax treaties by requiring the project to exist for more than twelve months. On the other hand, Belcher’s draft broadened the definition by referring to a ‘building site’ and to ‘supervisory activities’. As had been the case with Australia’s tax treaties with the US, Canada and NZ, the list of examples of permanent establishment in Belcher’s draft included a ‘substantial equipment’ provision identical in language to the provision in those treaties but set out as a separate paragraph in the definition.

Article II(1)(c) of Belcher’s draft stated that Australian resident ‘means a person who is a resident of Australia and is not a resident of (X country)’. This was identical to the definition of ‘Australian resident’ in Article II(1)(c) of the 1957 Australia – Canada Tax Treaty and to the definition in Article II(1)(c) of the 1960 NZ Treaty. ‘Resident of Australia’ was defined in Article II(1)(n) of Belcher’s draft as having the meaning that it had under the laws of Australia relating to Australian tax. The definition was identical to the definitions of ‘resident of Australia’ in Article II(1)(n) of the 1957 Canada Treaty and in Article II(1)(n) of the 1960 NZ Treaty.

The opening words of the definition of ‘permanent establishment’ in Article II(1)(l) of Belcher’s draft were: “‘permanent establishment’ in relation to an enterprise means a fixed place of business in which the business of the enterprise is wholly or partly carried on and includes …’. By contrast, the opening words of the definition in Article II(1)(m) of the 1960 NZ Treaty were: “‘permanent establishment’ means a branch, agency or other place of business and includes …’. The opening words of the definition in Article II(1)(h) of the 1957 Canada Treaty and in Article II(1)(o) of the 1953 US Treaty were: “‘permanent establishment’ means a branch, agency, management or fixed place of business and includes …’. The opening words in Article II(1)(j) of the 1946 UK Treaty were: ‘The term “permanent establishment”, when used with respect to an enterprise of one of the territories, means a branch or other fixed place of business and includes …’.
4.103 It is unclear whether Belcher understood the separate paragraphs in his draft as merely being examples of fixed places of business which would be permanent establishments or as being business operations which were deemed to be permanent establishments notwithstanding that they might not be fixed places of business. The specific paragraphs followed on immediately from the opening words of Article 2(l) of Belcher’s draft and were proceeded merely by the words ‘and includes’. This was in contrast to Article 5(2) of the 1963 draft OECD Model, where the examples are contained in a separate paragraph that opens with the words, ‘The term permanent establishment shall include especially’. Later comments by officials suggest that the ATO may have understood the sub-paragraphs in Article 5(1) of Belcher’s draft as deeming provisions.159

4.104 The definition of ‘permanent establishment’ in Belcher’s draft, other than in presentational aspects, also followed the Australia–Canada and Australia–NZ treaties and differed from the 1963 draft OECD Model Article 5(3) by stating that where the activities specified in Article II(l)(x) to (xiii) of the draft occurred, ‘the enterprise shall not, merely by reason thereof, be deemed to have a permanent establishment in that other Contracting State’. By contrast, Article 5(3) of the 1963 draft OECD Model stated that ‘The term “permanent establishment” shall be deemed not to include’ before proceeding to list excluded activities. Moreover, the list of activities in Belcher’s draft followed the Australia–Canada and Australia–NZ treaties in being narrower than the list of excluded activities in Article 5(3) of the 1963 draft OECD Model.

4.105 Belcher’s draft followed the Australia–Canada160 and Australia–NZ treaties by including a specific provision deeming there to be a permanent establishment in the situation in Case 110 (1955) 5 CTBR (NS) 656. No equivalent provision was in the 1963 draft OECD Model.

4.106 Consistent with prior Australian treaties from the 1953 tax treaty with the US onwards, and in contrast to the 1963 draft OECD Model, the credit article in Belcher’s draft contained deemed source rules in relation to personal (including professional) services, and amounts included in taxable income

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159 See the discussion by O’Reilly (as Acting Second Commissioner of Taxation) of this aspect of the 1966 UK draft treaty at 5.16.

160 As discussed at 3.149, the first Australian tax treaty to contain a provision of this nature was the 1957 Canada Treaty.
under either div 14 or 15 of ITAA 1936 relating to film businesses controlled abroad and insurance with non-residents.

4.107 Belcher’s draft contained exchange of information and communication between taxation authorities articles identical to the equivalent articles in the Australia–Canada and Australia–NZ tax treaties. However, like those treaties and unlike the Australia–US tax treaty, his draft did not contain an assistance in collection article; and unlike the US tax treaty and the 1963 draft OECD Model, it did not contain a mutual agreement procedure article in addition to the article dealing with communication between taxation authorities.

The Revised Draft

4.108 Following the receipt of Belcher’s draft, A D Ross from the Treasury and J Hill from the ATO developed a revised draft which largely followed Belcher’s draft in language and technical content but followed the OECD draft in the order of articles and other presentational matters.161 Ross and Hill prepared a schedule comparing the OECD draft, Belcher’s draft and the revised draft. The schedule included comments by Hill on variations between the OECD draft and Belcher’s draft.

4.109 In forwarding the schedule and the revised draft to Visbord, Ross commented that he preferred the wording of Belcher’s draft, which he regarded as far more specific than the OECD draft. Adhering more closely to the OECD draft would have, in Ross’ view, involved a ‘waste of roundabout verbiage’ in many areas. Ross also commented that the revised draft, like Belcher’s draft, did not contain any provisions dealing with dividends, interest, royalties, shipping and transport profits, but that Australia’s attitude on these issues would be best conveyed in a covering letter when the final draft was sent to potential tax treaty partners.162 The comments in the schedule on articles relevant to this thesis will be discussed in the following paragraphs.

161 Early and final versions of the revised draft (hereafter referred to as the ‘revised draft’) and the schedule (hereafter referred to as the ‘comparative schedule’) comparing the OECD draft, Belcher’s draft and the revised draft are contained in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.

162 E A Ross to Mr Visbord, 22nd March 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5. This memorandum makes it clear that Ross consulted with Hill in developing the revised draft and the schedule and that Hill wrote the comments in the comparative schedule.
4.110 The comments reflected the continued Australian practice of excluding dual residents from being treaty residents and its unwillingness to include tie-breaker provisions on dual residence. Thus, in relation to Article 1 of the OECD draft the comment was made: ‘The article does not appear to add to the effectiveness of the convention. By virtue of its reference to persons who are residents of both Contracting States it necessitates the procedures and definitions of article 4. The taxation draft does not seek to remove the problem of dual residence.’

4.111 The dislike for dual residence tie-breakers continued with the following comment on paragraph 1 of article 4 of the OECD draft: ‘The OECD draft, like the Taxation draft, defines residence by reference to national taxation practice, but in attempting to cater for dual residence involves itself in the complexities of para. 2.’ The full disdain of the ATO for dual residence tie-breakers was apparent in the following comment on paragraph 2 of article 4 of the OECD draft: ‘This provision is reminiscent of the trouble-shooting charts issued to non-mechanically minded troops, even down to the referral to Third Line Workshops in (d).’

4.112 The comments confirm the emphasis on source taxation underlying the Australian approach to defining ‘industrial or commercial profits’: ‘The Taxation definition, as opposed to normal definitions of “industrial or commercial profits”, sets out those classes of income which Australia wishes to tax even where a permanent establishment exists.’

4.113 The definition of ‘permanent establishment’ in the revised draft was identical to the definition in Belcher’s draft. The comment was simply that the list in Belcher’s draft was more extensive to cater for Australian conditions.

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163 Comparative schedule comment on OECD draft article 1.
164 Comparative schedule comment on OECD draft article 4(1).
165 Comparative schedule comment on OECD draft article 4(2).
166 Comparative schedule comment on article II(1)(h) in Belcher’s draft. It appears likely that the author of the schedule meant to insert the word ‘no’ immediately before ‘permanent establishment’ in the comment. Belcher’s draft and the revised draft, consistent with previous Australian treaties, define ‘industrial or commercial profits’ in terms which exclude items such as dividends, interest, rent royalties, etc. Belcher’s draft and the revised draft would have given Australia the right to tax these items in the absence of them being effectively connected with an Australian permanent establishment. As gross basis withholding tax in Australia at that time only applied to dividends, it seems unlikely that the comment would have referred to taxation of the excluded items on a gross basis rather than on a net basis as industrial or commercial profits.
167 Comparative schedule comment on OECD draft article 5(1).
4.114 On the exclusions from the definition of permanent establishment in Article 5(3) of the OECD draft, the comment was that ‘the OECD draft takes four paragraphs … to cover what is dealt with (on a verbally more economic and more readily intelligible basis) by the single Taxation clause’. The comments then go on to criticise each of the paragraphs in OECD draft Article 5(3).

4.115 The comment on Article 5(3)(e) of the OECD draft reflects the usual Australian concern with maximising source basis taxation: ‘The activities listed are said to be so far antecedent to the actual realisation of profits by the parent body that no profits can be allocated to the place of business which performs them. The OECD recognises, however, that such a place of business could shift from an ancillary function to a profit making function (selling or order-taking, for example, or manufacture in the case of a laboratory).’

4.116 The revised draft followed Article 5(5) of the OECD draft by adding the words ‘or any other agent of an independent status’ immediately after the word ‘broker’ in Belcher’s draft. The comment was that the use of this phrase in the OECD draft was a ‘useful addendum’.

4.117 The revised draft included the additional provision in Belcher’s draft which aimed to deal with the situation that arose in Case 110 (1955) 5 CTBR (NS) 656. That this was the intent of the inclusion is confirmed by the comment that this provision was necessary ‘to protect Australian revenue against such operations as those of the electric light trade’.

4.118 Several of the distributive articles in the OECD draft did not have equivalents in either Belcher’s draft or the revised draft. As a consequence of Australian Cabinet decision 386, articles on dividends, royalties and shipping profits were not included. In the case of each of these articles in the draft OECD Model, a comment was made that they had been deliberately excluded from the definition of industrial or commercial profits and that mention of them was not necessary in the credit article in the revised draft. The comment is also

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168 Comparative schedule comment on OECD draft article 5(3).
169 Comparative schedule comment on OECD draft article 5(3)(e).
170 Comparative schedule comment on OECD draft article 5(5).
171 See the discussion at 4.105.
172 Comparative schedule comment on OECD draft article IV(4) of the revised draft. It is understood that Case 110 (1955) 5 CTBR (NS) 656 concerned a company which manufactured light bulbs.
made that Australia’s attitude in relation to these types of income could be best expressed in a covering letter. In the case of the dividend article, where both Belcher’s draft and the revised draft contained the equivalent to Article 10(5) of the draft OECD Model, the comment was made that the reference in the OECD paragraph to taxation of undistributed profits had been intentionally omitted from Belcher’s draft. The revised draft followed Belcher’s draft in this respect.

4.119 In addition, neither Belcher’s draft nor the revised draft included articles on capital gains, income from immovable property or capital taxes. In relation to the OECD draft capital gains article, the comment was simply: ‘This is not relevant to Australia’s present taxation provisions.’ Similarly, in the case of OECD draft Article 22, the comment was that Australia did not impose taxation on capital of any kind, but that if a treaty partner imposed a tax on capital which might bear heavily or disadvantageously on Australian residents, consideration would have to be given to the desirability and practicality of relieving Australian residents of such taxation.

4.120 In relation to the income from immovable property article, the comment was that the principle embodied in the OECD draft article was implicit in Belcher’s draft, but that including an immovable property article in the Australian model would raise the question of whether income covered by it would be identical to the Australian equivalent. A note in brackets suggested a comparison between the Australian concepts of real and personal property as opposed to movable and immovable.

4.121 Neither the revised draft nor Belcher’s draft included an ‘other income’ article. The comment on Article 21 in the draft OECD Model was that Canada had reserved its position on the article because it wished to maintain its right to tax certain payments by residents to non-residents. The comment suggested that Australia might take the same attitude towards the article.

173 Comparative schedule comment on OECD draft article 10(5). Article VII of the revised draft was identical to Article 10(5) of the 1963 OECD draft article 10(5).
174 Comparative schedule comment on OECD draft article 13.
175 Comparative schedule comment on OECD draft article 22.
176 It would appear that the reasoning was that by not having provisions dealing with income from immovable property, full source country taxing rights were retained, which produced the same result as Article 6 in the OECD draft Model.
177 Comparative schedule comment on OECD draft article 6.
178 Comparative schedule comment on OECD draft article 21.
4.122 Like Belcher’s draft, the revised draft did not include a non-discrimination article. The comment on OECD Draft Model Article 24 was that the article conflicted with existing (unspecified) provisions of Australian income tax law and could extend to other taxing statutes including State statutes.\footnote{Comparative schedule comment on OECD draft article 24.}

4.123 The provisions dealing with methods of relieving double taxation in the revised draft were identical to those in Belcher’s draft. The comment was made that the OECD draft evidently assumed that if the exemption method were adopted, it would be adopted by both contracting states but that the Australian practice of tax credit made the symmetrical relationship of the OECD draft irrelevant.

4.124 On the credit article, the comment was made that the OECD draft allowed credit only in the case of income (and capital) taxable under the convention, whereas Belcher’s draft allowed credit for all income (subject to the provisions of the law in force). The comments noted that there might not be much practical difference between the two drafts of the credit article in this respect, given the width of the taxes covered in the OECD draft. The comment was also made that the OECD draft referred explicitly to the limit of the credit, while the limit was only implicit in Belcher’s draft. The comments also pointed out that Belcher’s draft explicitly excluded credit for any penalty element.\footnote{Comparative schedule comment on OECD draft articles 23A and 23B.}

4.125 Belcher’s draft did not contain an article on mutual agreement procedure. The comments note that an equivalent provision to Article 25(1) of the OECD draft had been contained in the 1953 Australia – US Tax Treaty but that the exchange of information provision in Belcher’s draft provided adequate coverage. Nonetheless, an equivalent to OECD Article 25(1) (based on Article XVI of the Japanese draft used in preliminary negotiations between Australia and Japan in Tokyo in 1964) was included in the revised draft. The comment pointed out that the article in the revised draft required proof rather than postulating an alleged cause for complaint.

4.126 Neither Belcher’s draft nor the revised draft included equivalents to OECD Draft Article 25(2) and (3), with comments stating that OECD Draft 25(3) could operate to curtail the existing rights of Australian taxpayers. In substitution for Article 25(4) of the OECD draft, the revised draft used the communication between taxation authorities provision from Belcher’s draft,
the comment being that Belcher’s draft was regarded as covering the whole of the provisions of OECD Article 25.\textsuperscript{181}

4.127 The revised draft adopted the exchange of information article in Belcher’s draft, with the comments stating that Belcher’s draft covered more concisely all that the OECD draft did (with the exception of the reference to public order) and made specific allowance for disclosure to judicial authorities, something that was only in the supplementary drafting provisions of the OECD draft. The comments also considered that OECD Draft Article 26(2)(b) appeared to limit exchange of information to what was possible in the state with the poorer information facilities.\textsuperscript{182}

4.128 The revised draft was forwarded by O’Donnell to the Commissioner of Taxation for comment on 24\textsuperscript{th} March 1965.\textsuperscript{183} W J O’Reilly, as First Assistant Commissioner, replied on 14\textsuperscript{th} April 1965 commenting that, subject to an understanding that there would be flexibility to negotiate in relation to a paragraph on government remuneration which appeared in the revised draft but not in Belcher’s draft and subject to the minor drafting matters being taken into account, the revised draft was considered suitable for submission to countries seeking tax treaties with Australia.\textsuperscript{184} F C Pryor, as Acting First Assistant Secretary of the Treasury, then sent the final draft to the Commissioner of Taxation for final checking on 27\textsuperscript{th} April 1965.\textsuperscript{185} O’Reilly replied on 6\textsuperscript{th} May 1965, indicating that the final draft had been checked and found to be satisfactory so far as the ATO was concerned and that the office did not desire to offer any further comments.\textsuperscript{186}

\textsuperscript{181} Comparative schedule comment on OECD draft article 25. The relevant provision in Belcher’s draft was discussed at 4.125 and 4.126.

\textsuperscript{182} Comparative schedule comment on OECD draft article 26.

\textsuperscript{183} M W O’Donnell, First Assistant Secretary, Department of the Treasury to the Commissioner of Taxation, Canberra, ACT, 24\textsuperscript{th} March 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.

\textsuperscript{184} W J O’Reilly, First Assistant Commissioner, ATO to The Secretary, Department of the Treasury, Canberra, ACT, 14\textsuperscript{th} April 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.

\textsuperscript{185} F C Pryor, Acting First Assistant Secretary, Department of the Treasury to the Commissioner of Taxation, 27\textsuperscript{th} April 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.

\textsuperscript{186} W J O’Reilly, First Assistant Commissioner, ATO to The Secretary, Department of the Treasury, Canberra, ACT, 6\textsuperscript{th} May 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.
O’Donnell then wrote to the Treasurer, Harold Holt, enclosing a copy of the draft Australian model tax treaty. O’Donnell commented that the Australian model adhered, so far as practicable, to the 1963 draft OECD Model, explaining:

‘The reason for this is that members of the OECD naturally look to the OECD model when considering proposals for new agreements. Further, the OECD model appears to be in increasing use internationally as a guide to the form and content of double taxation agreements, so that our adoption of elements of it, principally relating to format, which were compatible with our interests, would serve to minimise the area of potential disagreement on relatively insubstantial matters and to point up the matters of real substance.’

O’Donnell pointed out that the content of the Australian model reflected the considerations set out in Cabinet decision 386 of August 1962 and 1009 of September 1963 on the renegotiation of existing tax treaties and the negotiation of new tax treaties. O’Donnell considered that, given the Cabinet decisions, Australia’s interests would be best served by commencing from a ‘no concessions’ basis with concessions to be made during negotiations to be for Cabinet’s consideration, depending on the offsetting advantages offered to Australia in particular negotiations.

O’Donnell sought the Treasurer’s approval for forwarding the Australian model to the Department of External Affairs. The department would then be directed to send the model to countries that had sought tax treaties with Australia, along with a covering letter detailing Australia’s position on dividends and shipping and aircraft profits but stating that Australia was not ‘wholly inflexible and unwilling to consider mutually satisfactory changes’. Holt gave his consent to this approach.

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187 M W O’Donnell, First Assistant Secretary, Department of the Treasury to The Treasurer, 27th May 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.
188 O’Donnell to The Treasurer, above n 187, 1, para 3.
189 O’Donnell to The Treasurer, above n 187, 1, para 4.
190 O’Donnell to The Treasurer, above n 187, 1–2, para 5.
191 O’Donnell to The Treasurer, above n 187, 2, para 6.
192 This is confirmed in O’Donnell to Mr Craik (D Steele Craik, Assistant Secretary of the Treasury), Department of the Treasury, Minute Paper, 8th June 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.
4.132 The model was sent to the Department of External Affairs with instructions consistent with those outlined in O’Donnell’s memorandum to Holt of 27th May 1965. A legal officer from the Department of External Affairs then suggested minor drafting changes, only some of which appear to have been incorporated in the Australian model. The model was then sent to several European countries, accompanied by a letter making the points suggested in O’Donnell’s memorandum to Holt of 27th May 1965.

The Subsequent Use Of The 1965 Model

4.133 The Australian model tax treaty of 1965 was not directly used in the actual negotiations of any Australian tax treaties between 1965 and 1972. Although the model was sent to Germany in 1965, a later model, influenced by the 1967 Australia – UK Tax Treaty, was sent to Germany in 1969 and was used in the negotiations which led to the 1972 Tax Treaty with Germany. Similarly, as discussed in Chapter 6, the 1969 Australian model used in the negotiations with Japan had also been influenced by the 1967 Australia – UK Tax Treaty.

4.134 It would be a mistake, however, to discount the influence of the 1965 Australian model and of the 1959 to 1964 review of tax treaty policy. As will be seen in Chapter 5, the 1965 model provided a reference point and source of drafting precedents for Australian officials in analysing the 1966 UK draft

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193 M W O’Donnell, Acting Deputy Secretary, Department of the Treasury to The Secretary, Department of External Affairs, Canberra, ACT, 22nd June 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.

194 External Affairs Minute Paper, Cavan Hague to indecipherable 13/7 encloses a copy of the model with handwritten annotations by the Department of External Affairs legal advisor, A H Body. A ‘Note for the File’ by A D Ross dated 19th July 1965 indicates that External Affairs had been told that the model had been approved by the Treasurer, had been sent to External Affairs for distribution not for comment, and could not be changed. A subsequent file note by Ross dated 16th July 1965 indicates that Body still wanted his changes incorporated, and a handwritten note at the foot of the file note indicates that Body would have a further look at the draft and would indicate any points on which he felt strongly and would advise how the issue could be resolved. All these documents are contained in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.

195 F C Pryor, Acting First Assistant Secretary, Department of the Treasury to The Secretary, Department of Civil Aviation, 499 Little Collins Street, Melbourne, C1, Vic, 23rd September 1965, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5, indicates that the Australian model was sent to: Denmark, France, Germany, Greece, Ireland, Italy, The Netherlands, Norway, Sweden and Switzerland.

196 A draft of the letter and suggested amendments are contained in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 5.
used as part of the negotiations which led to the 1967 Australia – UK Tax Treaty. The pragmatic emphasis on maximising source taxation rights was also to be evident in that negotiation and in Australia’s subsequent negotiations with Japan although, as will be seen in Chapter 5, Australian negotiations were to find that some of the more extreme positions in Australian Cabinet decision 386 would have to be abandoned if Australia wanted to enter into any further bilateral tax treaties.

**Significance Of The Review Of Australian Tax Treaty Policy 1959 to 1964 For The First Two Questions Identified At 1.4**

4.135 The increasing influence of the Department of the Treasury on tax treaty policy is evident in the 1959 to 1964 review of Australian tax treaty policy.\(^{197}\) While the ATO, the Department of External Affairs, the Department of Trade and the Department of Prime Minister and Cabinet were all consulted in the process of drafting Cabinet Submission 305,\(^{198}\) Treasury generally discounted their views and was the department primarily responsible for the drafting of the submission. Of these departments, Treasury was shown to be the most sceptical of the value of tax treaties and the least willing for Australia to enter into further tax treaties.\(^{199}\)

4.136 A concern to protect Australian revenue was central to Treasury’s attitude to tax treaties. Believing that Australian domestic law provided virtually complete protection against international double taxation,\(^{200}\) and sceptical about the effect of tax on decision-making by potential foreign direct investors,\(^{201}\) Treasury saw the typical reduction in source basis taxation in tax treaties as both costly to Australian revenue and unlikely to produce a significant increase in inbound investment to Australia. That Australia’s four existing tax treaties were with countries with which Australia had particularly close ties was seen as being a reason why those treaties could not provide a model for future Australian tax treaties.\(^{202}\)

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\(^{197}\) The review is discussed at 4.1 to 4.56. For a discussion of the rise of the Department of the Treasury as the principal source of economic advice to Australian governments post World War II see G Whitwell, *The Treasury Line* (Allen & Unwin, 1986) ch 1.

\(^{198}\) The Cabinet submission was discussed at 4.33 to 4.51.

\(^{199}\) See the discussion at 4.20 to 4.32.

\(^{200}\) See the discussion at 4.49.

\(^{201}\) See, for example, the discussion of this aspect of Cabinet Submission 305 at 4.37.

\(^{202}\) See point (2) in the nine-point summary in the submission discussed at 4.49.
4.137 There does not appear to have been significant appreciation in Treasury (in contrast to the ATO) of the need to reduce source taxation to prevent double taxation arising from credit overspill. Treasury saw tax treaties as relieving double taxation by defining the areas of income to be taxed by each country and the relief to be given by each country to its residents for income derived in the treaty partner. This meant that concessions to the potential treaty partner were viewed as unnecessary.203

4.138 As the greatest revenue cost arose from conceding residence basis of taxation on shipping and from reductions in source taxation of dividends, the Treasury view was that Australia could enter into tax treaties which did not concede exclusive residence basis taxation of shipping and did not reduce source rates on dividends without adversely affecting the means by which tax treaties prevented international double taxation.204

4.139 It is notable that other relevant Australian departments, including the ATO, had a more positive attitude to tax treaties but had little influence on Submission 305. The Department of External Affairs205 and the Department of Trade206 had both pointed to wider benefits of tax treaties, as did McGovern’s letter.207 Understandably, the ATO appears to have had the greatest appreciation of the ‘Treasury effect’,208 while Trade saw tax treaties as a means of obtaining trade concessions and saw the absence of relief from source taxation of dividends as inhibiting Australia’s ability to attract future capital. The Department of External Affairs cautioned that investment might flow towards less-developed Asian countries as they developed tax treaties and became more economically developed. The assurance function of tax treaties was also recognised in correspondence by these departments, but it was discounted by Treasury. The Prime Minister’s Department put the issue

203 See point (4) in the nine-point summary in the submission discussed at 4.49.
204 See points (5), (6) and (7) in the nine-point summary of the submission discussed at 4.49.
205 The Department of External Affairs comments on the first draft of what was to be Cabinet Submission 305 are contained in R A Peachey, for The Secretary, Department of External Affairs to The Secretary, Department of the Treasury, Canberra, ACT, 9th January 1962, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2.
206 The Department of Trade comments on the first draft of what was to be Cabinet Submission 305 are contained in A T Carmody, Deputy Secretary, Department of Trade to M W O’Donnell, First Assistant Secretary, Department of the Treasury, Canberra, ACT, 5th February 1962, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2.
207 See the discussion at 4.19.
208 See the discussion at 4.9.
into some perspective when its permanent head questioned whether the anticipated revenue loss of £82,000 worth of future dividend concessions was significant in any assessment of the costs and benefits of capital inflow.\textsuperscript{209}

4.140 Clearly, all departments and the Cabinet saw Australia’s major trade and investment relationship as still being with the UK, and this led to the decision not to enter into tax treaties with European countries until the result of the UK’s first attempt to join the EEC was determined. This meant that Japan, South Africa and British Commonwealth countries in Asia were identified as countries whose offer to enter into tax treaty negotiations Australia should accept. Treasury recognised that, except in the case of Japan, Australia’s status as a net capital exporter to each of the other countries would mean that Australia could enter into tax treaties with these countries which prevented double taxation without granting concessions on shipping or source taxation of dividends.\textsuperscript{210}

Significance Of Belcher’s Review Of The 1963 Draft OECD Model For The First Two Questions Identified At 1.4

4.141 Belcher’s assessment of the 1963 OECD draft highlighted the differences between the draft and Australia’s existing tax treaties, and it illustrates the factors that influenced one of Australia’s key negotiators in the period from 1946 to 1963 in assessing tax treaties. Belcher’s overall conclusion on the draft OECD Model – that it was more favourable to capital exporting and maritime countries than to capital importing countries like Australia\textsuperscript{211} – accurately reflected his whole approach to the assessment of the draft OECD Model. With the exception of the taxes covered article\textsuperscript{212} and the immovable property article,\textsuperscript{213} Belcher consistently preferred the drafting of corresponding articles in previous Australian treaties.\textsuperscript{214}

\textsuperscript{209} The comments of the Prime Minister’s Department on the first draft of what was to become Cabinet Submission 305 are contained in E J Bunting, Secretary, Prime Minister’s Department to The Secretary, Department of the Treasury, Canberra, ACT, 25\textsuperscript{th} January 1962, in ‘Double Taxation Agreements With Other Countries, Policy’, NAA, Series Number A571, Control Symbol 63/3972 Pt 2.

\textsuperscript{210} See the discussion at 4.49.

\textsuperscript{211} See the discussion at 4.84.

\textsuperscript{212} See the discussion at 4.59 and 4.60.

\textsuperscript{213} See the discussion at 4.69.

\textsuperscript{214} See the discussion at 4.64, 4.65, 4.67 to 4.68, 4.72, 4.73, 4.74, 4.76, 4.77, 4.78 and 4.79.
4.142 A clear theme that emerges from Belcher’s analysis of most articles in the draft OECD Model which had an equivalent in existing Australian tax treaties is that they would be less favourable to Australia because they allowed less scope for source basis taxation with consequential revenue losses. This can be seen in Belcher’s analysis of: the definition of ‘permanent establishment’, the shipping and aircraft profits article; the dividend article, and the royalties article. Belcher also made a negative assessment of the interest and other income articles in the draft OECD Model, neither of which had had equivalents in previous Australian tax treaties. The limit on source taxation of interest in the OECD draft was characterised as being unacceptable if revenue were the only yardstick. Similarly, with the other income article Belcher commented that the Australian position of retaining full source country taxing rights favoured Australia in situations where Australia was a net capital importer. Belcher’s assessment of the non-discrimination article focused on the possibility that Australia’s denial of the inter-corporate dividend rebate to non-residents might infringe the article and that this would have a ‘tremendous impact’ on revenue.

4.143 Belcher was also concerned with preserving the operation of particular provisions in Australian domestic law and with possible conflicts between provisions in the OECD draft and Australian domestic law. These concerns can be seen in Belcher’s analysis of: the definition of ‘resident’, and the business profits article.

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215 As discussed at 4.62, Belcher was concerned that the examples in Article 5(2) would be required to be fixed places of business.

216 Belcher, as discussed at 4.74, noted the significant loss of Australian revenue that would be associated with adopting the draft OECD article.

217 As discussed at 4.77, Belcher believed that only the 1946 UK Treaty taxed both industrial and cultural royalties on a residence basis and that Australia’s existing tax treaties all preserved Australia’s right to tax film royalties under ITAA 1936 s136.

218 See the discussion at 4.76.

219 See the discussion at 4.78.

220 See the discussion at 4.66.

221 As discussed at 4.65, Belcher considered the OECD approach could give rise to practical operational difficulties and would be major departures from Australian domestic law and existing tax treaties.

222 As discussed at 4.71, Belcher pointed to the preservation of Australian taxing rights under ITAA 1936 divs 14 and 15 and ITAA 1936 s136 in previous Australian tax treaties.
4.144 On credits, Belcher recommended continuing to use an overall credit basis in tax treaties, notwithstanding the use of wide exemptions under Australian domestic law.\(^{223}\)

4.145 Belcher did not favour adopting the OECD draft in future Australian tax treaties with either OECD or non-OECD countries. Belcher expressed concern about whether the OECD Model would preclude Australia from having a uniform rate of withholding tax on all dividends and from collecting some tax at source from shipping profits;\(^{224}\) he considered that adopting the draft OECD Model would make it difficult to persuaded Japan to allow some source taxation of shipping profits and source based taxation of other types of income.\(^{225}\) Despite the absence of tax sparing provisions in the draft OECD Model, Belcher doubted that adopting the OECD Model would provide any positive assistance in future tax treaties with Singapore and Malaya.\(^{226}\)

The Significance Of The 1965 Australian Model Tax Treaty For The First Two Questions Identified At 1.4

4.146 Although the Australian model tax treaty of 1965 was not directly used in the actual negotiations of any Australian tax treaties between 1965 and 1969, it (particularly given the comments by Hill in the comparative schedule\(^{227}\)) does provide evidence relevant to the first two questions identified at 1.4 in the period immediately before Australia entered into its next four pre-OECD membership tax treaties. The model was used by Australian officials in analysing the 1966 UK draft and in negotiating the 1967 Australia – UK Tax Treaty.

4.147 The 1965 model followed the OECD draft in presentational matters, but generally\(^{228}\) followed a draft developed by M J Belcher in terms of language and technical content.\(^{229}\) The reason why the OECD draft was followed in presentational matters was that the 1965 Australian model was developed with the intention of sending it to European countries. The expectation was

\(^{223}\) See the discussion at 4.79.

\(^{224}\) See the discussion at 4.81.

\(^{225}\) See the discussion at 4.82.

\(^{226}\) See the discussion at 4.83.

\(^{227}\) The comments in the comparative schedule are discussed at 4.110 to 4.128.

\(^{228}\) The only exceptions being following OECD Draft Article 5(5) by including ‘or any other agent of an independent status’ immediately after the word ‘broker’ (as discussed at 4.116) and the inclusion of an equivalent to OECD Draft Article 25(1) (as discussed at 4.154).

\(^{229}\) See the discussion at 4.108.
that the more familiar OECD layout would facilitate agreement with European
countries. Treasury officials favoured Belcher’s draft on technical issues as
providing for greater scope for source basis taxation and as being verbally
simpler and more specific.

4.148 Belcher’s draft largely represented a consolidation and refinement of previous
Australian tax treaty practice. It retained the same structural features as
Australia’s four previous tax treaties by: defining industrial or commercial
profits in terms which excluded particular categories of income; not including
an interest article; not including a capital gains article; and not including an
‘other income’ article.

4.149 The major differences between Belcher’s draft and previous Australian tax
treaties were a product of Cabinet decision 386. The result was that
Belcher’s draft expressly excluded ‘dividends’ and ‘income from operating
ships or aircraft’ from the definition of ‘industrial or commercial profits’ and did
not contain a dividend article or a royalty article. It is clear that Belcher
considered that these features would mean that Australia would retain full
source country taxing rights in relation to these categories of income.

4.150 The comments on the 1965 model stated that the capital gains article was not
relevant for Australia’s present taxation purposes. The comments, while
noting the absence of an article on taxation of capital, did consider that the
inclusion of such an article would be desirable in tax treaties with countries
which taxed capital.

4.151 Belcher was sceptical as to whether European countries would agree to enter
into tax treaties having the features referred to in 4.149 and that compromises
on shipping profits and royalties might be the best that Australia could expect
to achieve. No similar reservations were expressed in the comments, which

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230 See the discussion at 4.129.
231 These were the reasons Ross gave for following the Belcher draft when forwarding
the revised draft and the comparative schedule to another Treasury official, E M W
Visbord. See the discussion at 4.109.
232 See the discussion at 4.100.
233 4.58 discusses how Belcher’s draft was constrained by Cabinet decision 386. Cabinet
decision 386 and Cabinet Submission 305 are discussed at 4.33 to 4.52.
234 See the discussion at 4.97.
235 See the discussion at 4.119.
236 See the discussion at 4.119.
237 Belcher’s scepticism on these issues is discussed at 4.98.
merely proposed that Australia's attitude to these articles be conveyed in a covering letter.\textsuperscript{238}

4.152 Interestingly, Belcher's comments on his draft did not highlight several respects in which it followed prior Australian treaties in a manner that differed from the OECD Model. The inclusion of those features in Belcher's draft (and subsequently in the revised draft) is evidence that in subsequent Australian tax treaties where they appear, they are likely to have been requested by Australia.

4.153 Those features were: the preservation of the operation of \textit{ITAA 1936} divs 14 and 15;\textsuperscript{239} the preservation of the operation of \textit{ITAA 1936} s136;\textsuperscript{240} expressly preserving the principle underlying \textit{ITAA 1936} s38;\textsuperscript{241} following the list of exclusions in the 1960 Australia – NZ Tax Treaty definition of 'industrial or commercial profits';\textsuperscript{242} following the residence provisions in the 1957 Australia – Canada Tax Treaty and in the 1960 Australia – NZ Tax Treaty;\textsuperscript{243} including a 'substantial equipment' provision in the definition of permanent establishment;\textsuperscript{244} following the phraseology and narrower list of activities in Article 5(3) in the 1957 Australia – Canada Tax Treaty and the 1960 Australia – NZ Tax Treaty;\textsuperscript{245} including a provision deeming there to be a permanent establishment in the situation which arose in \textit{Case 110} (1955) 5 CTBR (NS) 656;\textsuperscript{246} containing deemed source rules in the credit article in relation to personal (including professional) services and amounts taxable under either \textit{ITAA 1936} divs 14 or 15;\textsuperscript{247} and exchange of information and communication between tax authorities provisions identical to those in the 1957 Australia – Canada Tax Treaty and the 1960 Australia – NZ Tax Treaty.\textsuperscript{248}

4.154 Although commenting that the exchange of information provisions in Belcher’s draft were adequate and covered the whole of OECD Draft Article 25, the
revised draft did include an equivalent to OECD Draft Article 25(1).\textsuperscript{249} The comments also compared Belcher’s draft exchange of information article favourably with its direct OECD draft equivalent, noting that Belcher’s draft was more concise, made specific allowance for disclosure to judicial authorities, and that the OECD draft appeared to limit exchange of information to what was available in the state with the poorer information facilities.\textsuperscript{250}

\textbf{4.155} The respects in which Belcher’s draft (other than in its treatment of dividends, shipping profits and royalties) differed from earlier Australian tax treaties may be evidence that those features were included in those earlier treaties at the request of the treaty partner. Belcher’s draft used an ‘attributable to’ basis rather than a ‘force of attraction’ basis in allocating industrial or commercial profits to a permanent establishment. A force of attraction basis had been adopted in the 1953 Australia – US Tax Treaty and in the 1960 Australia – NZ Tax Treaty, but Belcher indicated that no strong preference between the two approaches was felt. The first draft that Australia sent to Canada had adopted a force of attraction basis, but this was readily deleted by Australia in subsequent drafts.\textsuperscript{251} It appears likely that the adoption of a force of attraction basis in the 1953 Australia – US Tax Treaty was at the request of the US and was something that Australia would agree to but would not insist on.

\textbf{4.156} Other features of the 1953 Australia – US Tax Treaty which were not included in Belcher’s draft were the assistance in collection and mutual agreement procedure articles. The absence of these articles in the 1957 Australia – Canada Tax Treaty, in the 1960 Australia – NZ Tax Treaty and in Belcher’s draft provides some evidence that they were inserted in the 1953 Australia – US Tax Treaty at the request of the US.\textsuperscript{252}

\textbf{4.157} The other significant respect in which Belcher’s draft differed from a previous Australian tax treaty was the absence of a provision for proportional credits

\textsuperscript{249} See the discussion at 4.125.
\textsuperscript{250} See the discussion at 4.126.
\textsuperscript{252} In relation to the mutual agreement procedure article, this conclusion is consistent with McGovern’s statement (discussed at 3.73) that the article had been included at the request of the US. McGovern’s comment (discussed at 3.70) does not explicitly state that the assistance in collection article was inserted at the request of the US.
for tax on third country income contained in the 1946 Australia – UK Tax Treaty.\textsuperscript{253}

4.158 The definition of permanent establishment in Belcher’s draft differed from all previous Australian tax treaties, by including supervisory activities in relation to building or construction projects (hence broadening the definition) and by requiring the project to exist for more than twelve months (hence narrowing the definition).\textsuperscript{254} The comments in the comparative schedule pointed out that the definition in Belcher’s draft was more extensive to cater for Australian conditions and also praised its verbal economy.\textsuperscript{255}

4.159 An immovable property article was not contained in either Belcher’s draft or the revised draft. The comments considered that the principle in the OECD draft article was implicit in Belcher’s draft, and expressed concern about how the scope of the immovable property article would be determined given the existence of different concepts in Australian domestic law.\textsuperscript{256}

4.160 Neither Belcher’s draft nor the revised draft contained a non-discrimination article, with the comments expressing concern about possible conflict with taxing provisions in Australian domestic law.\textsuperscript{257}

4.161 The credit provisions in the revised draft were identical to the equivalent provisions in Belcher’s draft. The comments pointed to the fact that symmetrical approaches to relieving double taxation were inconsistent with previous Australian practice. The comments also noted differences between the Belcher and revised drafts as compared with the OECD draft in relation to creditable taxes and credit limits.\textsuperscript{258}

4.162 The 1965 Australian model implemented the policies of maximising source taxing rights and Australian revenue that were evident in Cabinet decision 386 and in Belcher’s review of the OECD Model in the detail of its drafting. The 1965 model also preserved certain features of Australian domestic law, although Belcher did not note this in his comments on his draft. The 1965

\textsuperscript{253} See the discussion at 4.101. As noted at 2.149 and accompanying notes, it is unclear from the files relating to the 1946 Australia – UK Tax Treaty whether Australia or the UK initiated the process which led to the inclusion of this provision in that treaty.

\textsuperscript{254} See the discussion at 4.102.

\textsuperscript{255} See the discussion of the comments on the comparative schedule at 4.113 and 4.114.

\textsuperscript{256} See the discussion at 4.120.

\textsuperscript{257} As noted at 4.122, the concern extended to possible conflict with State taxes.

\textsuperscript{258} See the discussion at 4.123 and 4.124.
model and the comments on it also reflect a preference for concise and what was perceived to be precise language and a strong tendency to follow existing Australian precedents. The consolidation and refinement in the 1965 model of provisions in previous Australian tax treaties which maximised source basis taxation, coupled with the omission of articles dealing with dividends, interest, royalties, capital gains and shipping profits, represented an extreme emphasis on source basis taxation which Australia was never able to achieve in any actual tax treaty.

**The Challenge To Australian Attitudes Presented By The Negotiation And Drafting Of The 1967 UK Treaty**

4.163 Australia’s extreme emphasis on source basis taxation and its dislike of many of the provisions of the 1963 Draft OECD Model were to be challenged during the negotiation and drafting of the 1967 UK Treaty which was to prove to have a most significant influence on future Australian treaties. The background to, the negotiation and drafting of, and the significance of that treaty are discussed in Chapter 5.
CHAPTER FIVE: AUSTRALIA’S SECOND TREATY WITH THE UK IN 1967

5.1 Although, as was noted in Chapter 4 and will be seen in Chapter 6, Australia had previously held preliminary discussions on possible taxation treaties with Japan and Singapore, the next taxation treaty that Australia commenced negotiations on and entered into was its second taxation treaty with the UK, in 1967.

5.2 The 1967 UK Treaty is important for several reasons. It was the first treaty that Australia entered into after publication of the draft OECD Model and was based on a UK draft that had been influenced by the OECD Model. Hence the treaty and the negotiations leading up to it are evidence of how Australia would respond, in actual treaty negotiations, to the draft OECD Model relatively shortly after its publication. Australia had previously had preliminary discussions with Japan in relation to a Japanese draft, which had been influenced by the 1963 draft OECD Model,\(^1\) and the review of Australia’s tax treaty policy between 1959 and 1964\(^2\) had considered the 1963 draft OECD Model in developing the 1965 Australian model.

5.3 Secondly, the treaty was an indication to Australia’s potential treaty partners as to how it would seek to vary several articles in the OECD Model. In particular, the treaty signalled the rates of withholding tax on dividends, interest and royalties that Australia was prepared to agree to and that Australia would not agree to a non-discrimination article. In contrast to the OECD Model and UK practice, the treaty contained structural features, particularly the replacement of the ‘other income’ article with an article confined to tax on third country income, that developed out of the distinctive features of earlier Australian treaties discussed in Chapters 3 and 4.

5.4 This chapter begins with a discussion of developments in the Australian economy and income tax system between 1960 and 1967 before examining the negotiation and drafting of the 1967 UK Treaty.

The Australian Economy 1960–1967

5.5 In 1960, while the UK was still Australia’s major trading and investment partner, its significance in both those capacities had been declining since 1950.\(^3\)

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1 The preliminary meeting with Japan is discussed at 6.4 to 6.12.
2 See the discussion at 4.57 to 4.130.
3 In 1949–50, 53.1% of Australian imports came from the UK. By 1960–61, this had declined to 31.3%. In 1949–50, 39.4% of Australian exports were to the UK; but by 1960–61, this had declined to 23.9%. In 1949–50, 48.2% of the total inflow of foreign investment in Australian enterprises came from the UK. Although this figure was little changed by 1960–61, at 47.3%, it had fluctuated significantly in the interim, reaching a high point of 91.3% in 1952–53. R A
The military and economic ascendancy of the US during the 1950s, together with the recovery of Europe (especially Germany) and Japan, meant that Commonwealth preferences and the Sterling Area came to be seen as less and less economically attractive. By the time Australia renegotiated the 1932 Ottawa Agreement as the 1957 UK – Australia Trade Agreement, the level of Commonwealth preferences in the former agreement was seen, among other disadvantages for Australia, as inhibiting Australia’s ability to negotiate trade agreements with other countries, such as Japan, with fast-growing economies. Kunkel argues that the UK’s failed first bid to join the EEC left Australian officials ‘with a more jaundiced view of the supposedly special relationship with the UK having witnessed the crumbling of assurances about the protection of Commonwealth interests’. An important consequence was a concerted export diversification drive by Australia and a renewed effort to deepen trade relations with Asia and North America.

5.6 Throughout the 1960s, while the UK’s importance to Australia as a trading and investment partner continued to decline, it still remained a major trading partner and a major source of investment in Australian enterprises. Strategically, Australia was concerned at the prospect of the UK withdrawing militarily East of Suez. The military strategic imperative affected Australia’s trade relations with the UK. Australia made a muted response to the UK’s second unsuccessful bid to join the EEC in the fear that a more robust response would antagonise the UK and dilute Australia’s message on the need for a UK military presence in the Far East. The recognition in Australia that the UK’s economic destiny lay increasingly with Europe gave further impetus to

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Foster, *Australian Economic Statistics 1949–50 to 1994–95* (Reserve Bank of Australia, 1996) 9, Table 1.4, 13, Table 1.6 and 42, Table 1.17.

4 This represented a shift from earlier policies. See the discussion of the economic policies of the Chifley and Menzies governments at 3.6 to 3.10.


6 Kunkel, above n 5, 20. There is a comprehensive discussion of the Australian and NZ responses to Britain’s first attempt to join the European Economic Community in Singleton and Robertson, above n 5, chs 7 and 8.

7 See the discussion in Singleton and Robertson, above n 5, ch 9. These points are also made by Kunkel, above n 5, 20.

8 By 1969–70, the UK accounted for only 11.8% of Australian exports and was the source of 21.8% of Australian imports. The UK was the source of 33.1% of foreign investment in Australian enterprises by 1969–70. Foster, above n 3, 9, Table 1.4, 13, Table 1.6 and 42, Table 1.17.

9 Points made by Andrea Benvenuti, ‘“Layin’ Low and Sayin’ Nuffin”: Australia’s Policy Towards Britain’s Second Bid to Join the European Economic Community’ (2006) 46 *Australian Economic History Review* 155. See also the discussion in Singleton and Robertson, above n 5, chs 9 and 10.
Australia’s efforts at import diversification and import replacement through local manufacturing.


5.7 Between 1953 and 1966, incremental changes were made to the Australian taxation system from the system described at 3.11 to 3.12 and at 3.57. Machinery provisions relevant for credits under Australia’s tax treaties and for the credit for individuals for foreign tax on dividends under ITAA 1936 s45 were relocated from the International Agreements Act 1953 and became former Division 19 of ITAA 1936 (Cth).10 The method of calculating undistributed profits had been altered in 1952.11 A withholding tax regime for dividends had been introduced in 1959, although the regime still gave shareholders an option to file a return and to be taxed on an assessment basis.12

5.8 The corporate tax rate was changed in 1957 to 32.5% for the first £5000 of taxable income of resident public companies, with a rate of 37.5% applying to taxable income above £5000. For non-resident public companies, the rate was 27.33% for the first £5000 of dividend income and 32.5% for the first £5000 of income other than dividends. A rate of 37.5% applied to taxable income of non-resident public companies above £5000. For resident and non-resident private companies, the rate was 22.5% for the first £5000 of taxable income and 32.5% thereafter. Undistributed profits tax on private companies which did not make a sufficient distribution was 50%. Corporate rates were increased in 1960, with a rate of 35% applying to the first £5000 of taxable income for resident public companies and a rate of 40% applying thereafter. For non-resident public companies, a rate of 30% applied to the first £5000 of dividend income, a rate of 35% applied to the first £5000 of non-dividend income and a rate of 40% applied to all taxable income over £5000. For resident and non-resident private companies, a rate of 25% applied to the first £5000 of taxable

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10 These changes were made by Act No. 17 of 1961 and by Income Tax (International Agreements) Act (No 2) 1960. The background to the changes is discussed in Explanatory Memorandum to Income Tax and Social Services Contribution Assessment Bill 1960, Income Tax and Social Services Contribution Bill 1960 and Income Tax (International Agreements) Bill 1960. The change coincided with the introduction of income tax in the Australian Territory of Papua New Guinea, as a consequence of which former ITAA 1936 div 18, which provided Australian residents with a credit for Papua New Guinea tax, was also introduced in 1959.

11 As noted at Chapter 3, n 91 to paragraph 3.57.

12 ITAA 1936 s128B(1) introduced by Income Tax and Social Services Contribution Assessment Act (No 3) 1959.
income, with a rate of 35% applying thereafter. The rate of undistributed profits tax was unchanged.\textsuperscript{13}

The Negotiation And Drafting Of The 1967 Australia – UK Treaty

The 1966 Changes To UK Corporate-Shareholder Taxation And The Decision To Renegotiate The 1946 Australia – UK Treaty

5.9 Due to proposed changes in its system of corporate-shareholder taxation, in late 1965 the UK sought modifications to its existing bilateral taxation treaties, including the 1946 UK Treaty. Under the 1946 UK Treaty, the UK provided a foreign tax credit for underlying Australian corporate tax irrespective of the level of shareholding.\textsuperscript{14} In 1946, the UK operated what was, in effect, a form of dividend imputation system. The UK introduced unilateral relief provisions in 1950, which allowed credits for underlying tax irrespective of the level of voting power held by the recipient where the paying company was a resident of a Commonwealth country.\textsuperscript{15} In 1965, the UK introduced a corporation tax that was regarded as a separate tax from the tax on shareholders. As a consequence, the UK sought to limit foreign tax credits for underlying corporate tax in its double taxation treaties by renegotiating the credit provisions in treaties through protocols. The general UK policy was to require a minimum 10\% voting power before an underlying credit was available in a treaty with a Commonwealth country.\textsuperscript{16} The policy was consistent with amendments to the UK’s unilateral relief provisions, effective from 5\textsuperscript{th} April 1966, under which the recipient was required to be a UK company with a minimum voting power of 10\% where the paying company was a Commonwealth resident.\textsuperscript{17}

\textsuperscript{13} Corporate tax rates for the period 1\textsuperscript{st} July 1957 to 30\textsuperscript{th} June 1962 are summarised in J A L Gunn, O E Berger and M Maas, \textit{Gunn’s Commonwealth Income Tax: Law and Practice}, Butterworths, Sydney, 1963, at [1210] to [1212].

\textsuperscript{14} See the discussion at 2.129.

\textsuperscript{15} See the discussion in John E Talbot and G S A Wheatcroft, \textit{Corporation Tax, and Income Tax Upon Company Distributions} (Sweet & Maxwell, 1968) 279–80, para 18-01. See also the discussion in C N Beattie and J C Wisely, \textit{Corporation Tax} (Butterworths, 2\textsuperscript{nd} ed, 1966) 170–1.

\textsuperscript{16} See the discussion of UK treaties in this period in Talbot and Wheatcroft, above n 15, 282–4, paras 18-07 and 18-08. In some instances, the UK required a 25\% minimum voting power in treaties with non-Commonwealth countries.

\textsuperscript{17} See the discussion in Talbot and Wheatcroft, above n 15, 284–86, paras 18-09 to 18-11 and in Beattie and Wisely, above n 15, 170–1. A minimum of 25\% voting power held by a UK resident company was required where the paying company was a resident of a non-Commonwealth country.
5.10 In 1965, the UK requested that a protocol be negotiated to take into account the effect of these changes to the UK system of corporate-shareholder taxation.\textsuperscript{18} Australia preferred that a new treaty be entered into,\textsuperscript{19} because it was dissatisfied with some features of the 1946 UK Treaty and was contemplating changes to its domestic law affecting cross-border dividends, interest and royalties.\textsuperscript{20} The UK continued to request a protocol,\textsuperscript{21} but after making arrangements to renegotiate its treaty with NZ in the northern hemisphere autumn of 1966 or in the spring of 1967 asked if Australia could indicate when it would like to undertake a complete review of the treaty.\textsuperscript{22}

The Initial UK Draft

5.11 The UK, after seeking representations from other UK government bodies, business groups and selected businesses,\textsuperscript{23} submitted a draft treaty, influenced by the 1963 draft OECD Model, to Australia for consideration on 20\textsuperscript{th} September 1966.\textsuperscript{24} Australia

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\textsuperscript{18} The earliest correspondence raising the issue that the author has been able to locate is a telegram dated 16\textsuperscript{th} September 1965 from the UK Commonwealth Relations Office to the UK High Commission in Canberra asking for the question of negotiation of a protocol to the 1946 treaty, consequent on the introduction of UK corporations tax, be raised with Australian authorities. The Secretary of the Australian Prime Minister’s Department (E J Bunting), in an undated reply to the UK High Commissioner in Canberra, stated that the government had considered the issue but would prefer that the 1946 treaty be renegotiated at a convenient time. It is clear that Bunting’s reply was received by the UK authorities by 2\textsuperscript{nd} December 1965, as it is referred to in H H Woodruff to T W Keeble Esq, Commonwealth Relations Office, dated 2\textsuperscript{nd} December 1965. All of these documents are contained in UK National Archives, Kew, ‘Revision of Double Taxation Agreement – Australia’, UK National Archives, IR 40/16741. Hereafter referred to as ‘Inland Revenue file’.

\textsuperscript{19} The Secretary of the Australian Prime Minister’s Department to the UK High Commissioner in Canberra, nd, above n 18.

\textsuperscript{20} At a meeting in Canberra between UK and Australian officials on the issue in February 1966, the Australian officials indicated that Australia had long thought that several features of the 1946 Australia – UK Treaty required revision. In particular, the exemption for dividends paid to a 100% UK parent was inconsistent with the 15% flat rate on dividends agreed to under Australia’s subsequent treaties with the US, Canada and New Zealand. Australia was concerned that the withdrawal of relief for underlying tax would remove the inducement for portfolio investment in Australia and might result in a reduction in the actual flow of portfolio investment. Inland Revenue file, ‘Notes of Meetings in Canberra 25\textsuperscript{th} February 1966’, hereafter ‘Notes of Meetings’.

\textsuperscript{21} Inland Revenue file, Johnson to Cain 1\textsuperscript{st} March 1966, Cain to Johnson 1\textsuperscript{st} April 1966, Johnson to Cain 5\textsuperscript{th} May 1966, Cain to Johnson 17\textsuperscript{th} May 1966.

\textsuperscript{22} Inland Revenue file, Johnson to Cain 24\textsuperscript{th} May 1966.

\textsuperscript{23} Letters were sent on 12\textsuperscript{th} September 1966 to the Board of Trade, the Treasury, the Confederation of British Industries, the British and Commonwealth Banks Association, the Taxation Committee of the British Insurance Association, the ANZ Banking Group and other businesses; these are contained in the Inland Revenue file. Most replies were not received, and the representations appear to have had little effect on the UK’s negotiating position. An undated summary of the representations is contained in the Inland Revenue file.

\textsuperscript{24} Inland Revenue file, Johnson to Cain 20\textsuperscript{th} September 1966, Harrison to Wearing 20\textsuperscript{th} September 1966.
by this time had developed its own draft, but there is no evidence that this was ever sent to the UK. However, there is some evidence that it influenced Australia’s analysis of the UK draft and Australia’s negotiating position.

**Australian Reactions To The Initial UK Draft**

**Australian Internal Reactions At The Official Level**

5.12 Official Australian internal reactions to the UK draft can be seen in a letter by W J O’Reilly to Sir Richard Randall and an accompanying Memorandum. In analysing the UK draft, O’Reilly and the Memorandum compared it with: the 1946 UK Treaty; the draft OECD Model Convention; previous UK treaty practice, particularly its recently concluded treaty with New Zealand; and the 1965 Australian model tax treaty.

**Corporate Dual Residence Tie-breaker**

5.13 One concern was with the proposed tie-breaker on corporate dual residence (place of effective management) in Article 3(3) of the draft. A company incorporated in Australia but centrally managed and controlled in the UK would be an Australian resident for purposes of Australian domestic law. Because of the *ITAA 1936* s46 inter-corporate dividend rebate, such a company would be effectively exempt from Australian tax on dividends it received, while Article 9 of the draft would mean that dividends that it paid to its UK parent would not be subject to Australian tax. O’Reilly considered that the problems of dual residence had been satisfactorily dealt with previously without resorting to dual residence tie-breakers. O’Reilly noted that the tie-breaker provisions had been considerably modified in the 1966 UK – NZ Taxation Treaty. The Memorandum considered this approach would be more favourable to Australia but would not eliminate the possibilities for exploitation of tie-breaker provisions.

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25 The development of this draft was discussed at 4.90 to 4.132.

26 W J O’Reilly (Acting Second Commissioner of Taxation) to The Secretary to the Treasury (Sir Richard Randall) and accompanying memorandum, 16th November 1966, Australian Treasury file. All subsequent references to ‘O’Reilly's letter’ or to ‘the Memorandum’ in paragraphs 5.13 to 5.39 are to these documents and hence separate footnotes will not be provided for those references. O’Reilly was subsequently appointed as Commissioner of Taxation in 1976 and held that position until his retirement in 1984. Leigh Edmonds, *Working for All Australians: A Brief History of the Australian Taxation Office* (Australian Taxation Office, Canberra, 2010), 154 and 175.

27 Under the UK–NZ treaty, a NZ company was defined as one that met the NZ definition of corporate residence (place of incorporation and centre of administrative or practical management in NZ or central management and control in New Zealand). Under that treaty, a UK company was a company that was centrally managed and controlled in the UK but was not a NZ company.
Permanent Establishment

5.14 O'Reilly observed that the definition was much narrower than Australia would desire and narrower than the definition in the 1966 UK – NZ Taxation Treaty. The Memorandum observed that, apart from paragraph 4, the definition of ‘permanent establishment’ in the UK draft was a copy of the definition in the OECD Model, and noted that the definition differed from its equivalent in the Australian model\textsuperscript{28} by not including the following specific instances of a permanent establishment:

- An agency;
- An oil-well;
- An agricultural, pastoral or forestry property;
- An installation project that existed for more than 12 months;
- Supervisory activities on a building site or a construction, installation or assembly project for more than 12 months; and
- The use or installation of substantial equipment or machinery by, or under contract with, an enterprise of one of the countries.

5.15 An ‘agricultural or pastoral property’ had specifically been included in the definition of permanent establishment in the 1946 UK Treaty.\textsuperscript{29} The use or installation of substantial equipment had been expressly mentioned in the ‘includes’ portion of the definition in the 1953 US Treaty, in the 1957 Canada Treaty and the 1960 NZ Treaty.\textsuperscript{30} Installation projects and supervisory activities had not been expressly mentioned in any taxation treaty that Australia had entered into prior to 1966.

5.16 The structure of earlier Australian treaties may have influenced Australian interpretation of later treaties, even though they had a different structure. In earlier Australian treaties, such as the 1946 UK Treaty and the 1953 US Treaty, the definition of ‘permanent establishment’ was a ‘means and includes’ definition; a form well known to common lawyers. Under a ‘means and includes’ definition, the items referred to after the word ‘includes’ may deem items to be covered by the defined term that would not fall within the ‘means’ portion of the definition. The definition of permanent establishment in the 1966 UK draft was structured differently and followed the OECD Model in this respect. Article 4.1 of the draft was a ‘means’ definition of permanent establishment and Article 4.2 stated that ‘permanent establishment’ ‘includes especially’ a list of specified items. Article 4.5 expressly deemed what

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\textsuperscript{28} The definition of ‘permanent establishment’ in the 1965 Australian model was discussed at 4.102 to 4.105.

\textsuperscript{29} See the discussion at 2.101 and 2.102.

\textsuperscript{30} See the discussion at at 3.41 to 3.43, 3.84 to 3.85, 3.109, 3.136 and 3.148.
would now be referred to as dependent agents to be permanent establishments. O’Reilly’s letter appears to reflect a concern that all of the items specified in his letter would have to be included in either Article 4.2 or in a specific deeming provision for them to be regarded as permanent establishments.\(^{31}\) This reflects thinking that sees Article 4.2 as functioning to deem items to be permanent establishments whether or not they were within the Article 4.1 definition. This interpretation is understandable given the ‘means and includes’ drafting of the definition of permanent establishment in Australia’s previous treaties. It is questionable whether this construction of the definition in the UK draft was appropriate given the presence of Article 4.5, which specifically deemed certain agencies to be permanent establishments. The drafting arguably reflected the view that is currently taken in the OECD Model Commentary that the equivalent of Article 4.2 merely lists examples of items that are within the equivalent of Article 4.1, that each of these will only be a permanent establishment if it is a fixed place of business, and that the only items that are permanent establishments that are not within the Article 4.1 definition are those that are expressly deemed to be permanent establishments under articles such as Article 4.5.\(^{32}\)

5.17 The Memorandum noted that, under the UK draft, unlike the 1946 UK Treaty, agricultural, pastoral and forestry properties were dealt with under Article 5 (income from immovable property) and that this, if anything, would be more favourable to a source country than would taxation as a permanent establishment under the industrial or commercial profits article.

5.18 Again unlike the 1946 UK Treaty, the UK draft did not treat an agent who filled orders on a non-resident’s behalf from a stock of goods maintained in Australia as a permanent establishment. The Memorandum noted that the absence of such a provision and the deeming of warehousing activities to not be a permanent establishment meant that Australia would be unable, in the absence of anything more, to tax such activities by a UK firm. The Memorandum also observed that the converse was also true and that the levying of UK tax on the warehousing of Australian exports in the UK had been considered by the Department of Trade to be ‘something of an obstacle’ to export market development expenditure.

5.19 The UK draft did not include an equivalent provision to Article II(2) in the 1957 Canada Treaty and the 1960 NZ Treaty. Under the 1946 UK Treaty, Australia was

\(^{31}\) As noted at 4.62, M J Belcher, the then Australian Assistant Commissioner of Taxation, raised similar concerns in his 1963 review of the draft OECD Model.

\(^{32}\) See OECD Commentary on Article 5(2) paragraph 12.
unable to tax the UK company in *Case 110* (1955) 5 CTBR (NS) 656 because it did not have a permanent establishment in Australia. The Memorandum commented that the provision in the 1966 UK – NZ Treaty dealing with this situation was an improvement on the equivalent provision in the 1960 NZ Treaty.

**Income From Immovable Property**

### 5.20

Article 5 of the UK draft was new to Australia. O'Reilly considered that it was not essential in the Australia – UK context, that its inclusion might be avoided if possible, and, if it were included, that some clarification of its scope would be required. The Memorandum noted that under Article 5 Australia could continue to tax rents from UK owned property situated in Australia and royalties from the exploitation of Australian natural resources. The article would also mean that Australia could tax profits from agricultural and forestry enterprises in Australia without having to determine if the profits were industrial and commercial profits attributable to a permanent establishment in Australia. The Memorandum commented on problems that could arise due to perceived differences between English and Australian law in relation to the classification of property as movable or immovable in the case of debts secured by immovable property. The Memorandum referred to the statements in the OECD commentary that no special provision in the income from immovable property article dealt with debts secured by immovable property as the question was settled by the provision (under the interest article) for a 10% tax in the source country.

**Industrial or Commercial Profits And Associated Enterprises**

### 5.21

O'Reilly regarded the draft industrial or commercial profits article as ‘basically satisfactory in concept’ but commented that it would be desirable for it to recognise, as all of Australia’s prior treaties had done, Australia’s right to apply *ITAA 1936* s136, where information was insufficient for the arm’s length basis provided for in the Article to be applied. The Memorandum noted that NZ secured the ability to

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33 In *Case 110* (1955) 5 CTBR (NS) 656, the Board of Review held that the UK company, which participated in the capital of an Australian company that manufactured light bulbs to the order of the UK company, was not taxable under the industrial and commercial profits article because it did not have a permanent establishment in Australia. The issue had been raised but not resolved at meetings between UK and Australian tax officials in London in 1959. See ‘Australian Double Taxation Talks; Meeting 22rd April 1959 and ‘Australian Double Taxation Talks; Meeting 11th May 1959, Inland Revenue file.

34 Article II(viii) of the UK – NZ Treaty of 1966.

35 OECD Commentary on Article 6 paragraph 2.2.

36 *ITAA 1936* s136 was discussed at n 133 to paragraph 2.115.

37 See the discussion at 2.115 to 2.126.
apply its equivalent provision in its recent treaty with the UK. The same point was raised in relation to Article 8, the associated enterprises article.

5.22 Remuneration of an enterprise for personal services, dividends, interest, royalties and rents were excluded from the definition of ‘industrial and commercial profits’ except when effectively connected with a trade or business carried on through a permanent establishment. The Memorandum pointed out that in the latter case these items would be regarded as industrial or commercial profits and thus subject to full rates of source country tax. The comment should be read in the context of the limitations on the taxing rights of the source country of these types of income that are contained in other articles in the treaty. The Memorandum commented that, under the draft treaty, regarding personal services income, dividends, interest, royalties and rents effectively connected with a permanent establishment as industrial or commercial profits would favour Australia. Neither O'Reilly’s letter nor the Memorandum made any comment on whether capital gains would be within the definition of industrial or commercial profits.

5.23 The Memorandum also questioned the appropriateness of the reference to ‘under the same or similar conditions’ in paragraph 3 of the article, pointing out that ‘It is generally because of the conditions that exist between an enterprise and its establishment that the derivation of profits can be transferred at will between one country and the other. By having to calculate the attributable profits on the basis of the conditions that do in fact exist, the country in which the permanent establishment is situated may have to work on the basis of special conditions that it ought to be able to ignore for this purpose.’ Australia had raised the same problem when it negotiated the 1946 UK Treaty and had had the phrase removed following negotiations.38

5.24 The draft allowed for the deduction of all reasonable expenses, calculated on an arm’s length basis, in determining profits attributable to a permanent establishment. The Memorandum noted that the 1953 US Treaty allowed Australia to apply the principles in ITAA 1936 s38 in calculating profit39 and suggested that it would be useful to have the s38 principle recognised in the new treaty with the United Kingdom.

5.25 The definition of industrial or commercial profits in the draft included income from the furnishing of services of employees or other personnel. The Memorandum considered that this was necessary to enable the country of source to tax profits of

38 See the discussion at 2.120 and 2.124.
39 See the discussion at 3.47, 3.111 and 3.137.
public entertainer companies and argued that a source rule, in the form adopted in the 1946 UK Treaty and the 1953 US Treaty, should be inserted in the industrial and commercial profits article. Otherwise it would be fruitless to regard ‘public entertainer’ companies as having a permanent establishment in Australia if the ordinary source rules meant that the income of the company arose outside Australia. The comment reflects concern about the operation of Australian domestic law in the absence of the article. Following the decision of the High Court in *FCT v Mitchum* (1965) 113 CLR 401, it was uncertain when the income a company which provided the services of a public entertainer would have an Australian source.

**Shipping And Air Transport**

5.26 O'Reilly's letter and the Memorandum noted that the draft article taxed shipping and air transport on a residence basis, but contrasted it with both the 1946 UK Treaty and the 1966 UK – NZ Treaty. Under the 1946 UK Treaty, the exemption only applied to ships registered in the UK and operated by a UK resident. Under the draft, and in the 1966 New Zealand – UK Treaty, the exemption would apply wherever the ship was registered provided it was operated by a UK resident. In addition, in combination with the definition of ‘international traffic’ in Article 2, the exemption in the draft applied, consistently with the 1946 UK Treaty, to ships and aircraft operated by a UK resident solely between places in Australia. Under the UK – NZ Treaty, by contrast, the exemption only applied to traffic between places in NZ where that traffic was in the course of a voyage which extended over more than one country. The Memorandum noted that these features meant that under the draft the exemption would apply to profits of a UK operator of an Australian registered tanker wholly between Australian ports. The Memorandum commented that if Australia sought to continue to confine the operation of the exemption to ships registered in the country of residence, then the UK might argue that the Australian arbitrary method of calculating shipping profits in *ITAA 1936* div 12 did not give a true measure of Australian source income; this would make obtaining a UK credit for the Australian tax paid by UK operators of ships registered outside the UK problematic. The Memorandum observed, however, that this was ‘the opposite side of the coin’ to the use of arbitrary methods by the UK in

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40 Article III(3) 1946 UK Treaty contained an actual deemed source rule, but Article III(4) of the 1953 US Treaty deemed profits attributable to a permanent establishment to be income of the permanent establishment and to be taxed accordingly.

41 The decision of the Australian High Court in *FCT v Mitchum* (1965) 113 CLR 401 is discussed in R L Hamilton, R L Deutsch and J C Raneri, *Guidebook to Australian International Taxation* (Prospect Media, 7th ed, 2001) paras 2.520 and 2.530.

42 See the discussion at n 120 to paragraph 2.102.

43 See the discussion at paragraph 2.14 and accompanying notes.
calculating the profits of life assurance companies and that 'the U.K. may not press the point'.

**Dividends**

**5.27** While not specifying rates of source country tax on dividends, the UK draft envisaged that a different, and O'Reilly presumed lower, rate would apply where the dividend was paid to a shareholder controlling 25% or more voting power. The Memorandum noted that the 1966 NZ – UK Treaty provided for a uniform 15% rate on dividends, but considered that the UK might be contemplating the rates specified in the OECD Model, namely 5% for non-portfolio dividends and 15% for other dividends. If so, Australia would be gaining revenue in the wholly owned subsidiary situation but would be losing revenue where between 25% and 100% of the shareholding in companies was controlled by a UK resident. The credit for underlying tax for UK companies having at least 10% of the voting power in the paying company would mean that the UK revenue would generally not benefit in these cases from any reduction in the Australian tax on dividends below 15%. These statements highlight the emphasis that Australian officials of the time placed on revenue considerations, and also appear to indicate an assumption that the UK would also be significantly influenced by revenue considerations. The estimate was that there would be no benefit to the Australian revenue from the UK proposals in relation to UK dividends received by an Australian company, but that there would be some benefit in the case of dividends received by Australian individuals.

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44 At the time, both UK and Australian tax law contained special provisions that taxed certain profits of life assurance companies using arbitrary methods.

45 Limits on source country taxation of dividends under the 1946 Australia – UK Tax Treaty were discussed at 2.90.

46 The combined operation of ITAA 1936 ss45 and 46 (as discussed at 2.9 and 3.11) meant that usually no Australian tax would be collected on a foreign source dividend. Article XII (2) of the 1946 UK Treaty, however, meant that Australian taxpayers other than companies could be entitled to net UK tax deducted at the standard rate. In essence, this involved allowing an Australian resident shareholder other than a company a credit for UK corporate tax irrespective of the Australian resident’s level of shareholding in the UK company. Following the introduction of corporation tax in 1965, the UK had, pending the conclusion of a new treaty, unilaterally decided to limit its tax on dividends paid by UK companies to Australian residents to 15%, being the rate of tax levied by Australia on dividends paid by Australian companies to UK shareholders. Australian authorities had been notified of this intention at a meeting of UK and Australian Inland Revenue, Tax, Treasury and High Commission officials at Canberra on 25th February 1966. See Inland Revenue file, ‘Note of Meeting in Canberra 25th February 1966. Article 21(1)(b) restricted the availability of credits in the UK for Australian underlying corporate tax to UK companies which had a 10% or more voting power in the Australian company paying the dividend. It is reasonably clear that O'Reilly was envisaging that Australian resident portfolio shareholders would not be entitled to underlying foreign tax credits on UK sourced dividends. If so, then limiting the UK tax on portfolio dividends to 15%, in contrast to deduction of tax at the standard rate of 38.75%, would, when combined with the
5.28 The Memorandum discussed the definition in the draft of dividends subject to treaty limits. The definition adopted an ‘in substance’ approach under which interest and royalties could be classified as dividends. Items were included that would not be dividends, or even taxable in some cases, for Australian domestic law purposes. When combined with Articles 10(4) and 11(4) of the draft, the effect of the definition of ‘dividend’ appeared to be that the UK could levy tax at dividend rates on certain interest and royalties that were treated as dividends under UK law. In the case of interest, this would apply where the interest was paid to an Australian company with greater than 50% control. In the case of royalties, taxation at dividend rates would apply where the royalty was paid between companies under common management where the Australian company had a greater than 50% control.

5.29 Under the draft, the concessional rates of tax on dividends were only available to beneficial owners of the dividends. The Memorandum recognised that this was an anti-avoidance provision, but observed that both Australia and the UK taxed trustees on dividends and that the solution to this problem that had been developed in the UK – NZ Treaty would mean that an Australian charitable trust would be subject to full rates of UK tax on UK sourced dividends it received.

5.30 Article 9(7) of the draft, unlike the 1946 UK Treaty, precluded Australia from taxing dividends paid by UK residents to shareholders who were not Australian residents, as distinct from the narrower subset of shareholders who were UK residents. The Memorandum commented that this was consistent with the 1957 Australia – Canada Treaty and the 1960 Australia – NZ Treaty, and with the Australian model treaty. Here the progressive development of Australian treaty practice is referred to as being consistent with UK treaty practice, as evidenced by the draft.

5.31 The Memorandum noted that Article 9(7) would free a UK private company operating in Australia from undistributed profits tax, but commented that undistributed profits tax was rarely levied on non-resident companies. Interestingly, neither O’Reilly nor the Memorandum refer to the treatment of undistributed profits tax in the negotiation of the 1946 UK Treaty, which had been the product of considerable negotiation. By

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45 foreign tax credit, have meant that more Australian tax would be collected on dividends paid by UK companies to Australian portfolio shareholders.

47 As discussed in C John Taylor, ‘The Negotiation and Drafting of the First Australia–Canada Taxation Treaty (1957)’ (2013) 61 Canadian Tax Journal 915 at 969, this variation from the 1946 Australia – UK Tax Treaty in the 1957 Australia – Canada Tax Treaty was at the request of Canada. This aspect of the 1965 Australian model is noted at 4.118 n 173.

48 See the discussion in 2.90 to 2.91 and 2.109 to 2.114.
1966, Australian undistributed profits tax did not apply to public companies\(^\text{49}\) thus limiting the prospects of it applying to an Australian branch of a UK multinational.

**Interest**

5.32 O’Reilly stressed that under the 1946 Treaty interest had not been dealt with under the distributive rules, with the intention that the source country retain full taxing rights in relation to interest.\(^\text{50}\) Draft Article 10 taxed interest on a residence basis except when effectively connected with a permanent establishment. Where the borrower and lender were not at arm’s length, the exemption from source basis taxation was not to apply to interest above a normal commercial rate. Both the Memorandum and O’Reilly observed that the 1966 New Zealand – UK Treaty did not contain an equivalent article and concluded that this meant that NZ retained full source country taxing rights in relation to interest.\(^\text{51}\)

**Royalties**

5.33 Unlike the 1946 UK Treaty, the draft royalties article meant that film royalties, in addition to other royalties, would be taxed on a residence basis. As with the 1946 UK Treaty, the definition of ‘royalties’ did not extend to mineral royalties.\(^\text{52}\) Both O’Reilly and the Memorandum contrasted the draft article with the equivalent provision in the 1966 New Zealand – UK Treaty, which imposed an upper tax rate of 10% on the source taxation of royalties except in the case of royalties effectively connected with a permanent establishment. O’Reilly commented that under the 1966 New Zealand – UK Treaty, film royalties were excluded, with the effect that they remained taxable under the domestic law of each country. The Memorandum noted that NZ currently levied taxes equivalent to 11% of the gross rentals of British films.

**Capital Gains**

5.34 Although the draft contained a capital gains article, O’Reilly commented that it had no real relevance while Australia did not have a capital gains tax. O’Reilly and the Memorandum observed that, from the UK perspective, the article added little if anything to existing UK law. The Memorandum categorised the article as applying a

\(^{49}\) See the discussion at 3.11.

\(^{50}\) See the discussion at 2.90, 2.92, 2.102 and 2.104.

\(^{51}\) The Memorandum also noted that Article 10(5) had no equivalent in other Australian agreements. The article allowed a source country to tax interest derived by a tax exempt institution from interest bearing securities traded on a stock exchange where the institution was trafficking in securities. The Memorandum commented that Article 10(5) did not appear to have any effect for Australian tax purposes.

\(^{52}\) The treatment of royalties in 1946 UK Treaty is discussed at 2.90, 2.91, 2.94, 2.155 and 2.165.
similar principle to that applied in the industrial or commercial profits article, namely that source taxation of capital gains was only permitted in relation to property which was an asset of a permanent establishment in the source country. The comment reflects differences between the draft article and the capital gains article of the draft 1963 OECD Model. Article 13(1) in the OECD Model gave the state of situs the right to tax gains from the alienation of immovable property. No equivalent provision was contained in the 1966 UK draft under which, except in the case of gains from the alienation of ships and aircraft, source taxation of capital gains was confined to situations where the gain was from the alienation of property forming part of the business property of a permanent establishment or of property pertaining to a fixed base available to a resident for the purpose of performing professional services. Such source taxation was also permitted under the OECD Model. In addition, both the draft and the OECD Model explicitly gave the source country the right to tax gains from the alienation of the permanent establishment itself or of the fixed base.\textsuperscript{53} The Memorandum commented that the practical effect of the insertion of the article would be to limit Australian source taxation of capital gains if Australia ever introduced a capital gains tax. O'Reilly commented that one advantage of the article was that it would limit the scope of future UK capital gains tax on Australian property to what was contained in the present UK law.

5.35 As the draft contemplated that capital gains on property forming part of the property of a permanent establishment were to be taxed under the capital gains article, it is clear that the draft did not intend for such capital gains to also be the subject of source taxation of a permanent establishment under the industrial and commercial profits article. In other words, the draft did not consider that capital gains were within industrial or commercial profits as defined even though (unlike dividends, interest and royalties) they were not expressly excluded from the definition. The explanation for this may be that under UK\textsuperscript{54} and Australian law, capital gains had not been included in the ordinary concept of income as a business gain and in the UK had only been taxed through the introduction of statutory provisions that explicitly taxed capital gains. An interpretation of treaties which saw industrial or commercial profits as not

\textsuperscript{53} Unlike the OECD Model, the draft did not contain provisions excluding gains on moveable property dealt with under Article 22 of the OECD draft (dealing with Taxation of Capital) from taxation under the capital gains article. The draft did not contain any equivalent to Article 22 of the OECD Model.

\textsuperscript{54} The United Kingdom treatment of capital gains prior to the introduction of capital gains tax is discussed in P G Whiteman and D C Milne, \textit{Wheatcroft and Whiteman on Capital Gains Tax} (Sweet & Maxwell, 2\textsuperscript{nd} ed, 1973) paras 1–13 to 1–26 and in P G Whiteman and G S A Wheatcroft, \textit{Whiteman and Wheatcroft on Income Tax and Surtax} (Sweet & Maxwell, 1971) paras 1–17 to 1–20.
including capital gains and which saw capital gains taxed under a separate article would thus seem natural to UK tax officials because it would mirror the structure of UK domestic law taxing capital gains.55

**Other Income**

5.36 The Memorandum noted that the other income article was new to Australia and that it taxed income from sources not otherwise mentioned in the treaty on a residence basis. Under all of Australia’s existing treaties income not expressly mentioned could be taxed in the source country, with the residence country allowing a credit for the source country tax. O’Reilly pointed out that the draft article was precisely the converse of Australia’s existing agreements. The Memorandum identified the income that would be covered by the article as the draft stood at that point.56 O’Reilly considered that, with some technical amendments, the article might prove satisfactory, depending on the general context of the treaty as concluded in other respects.

**Credits**

5.37 O’Reilly noted that the main point about the credit article was that it would withdraw credit for Australian underlying corporate tax in respect of dividends paid by an Australian company to a UK resident except where the recipient was a company that controlled 10% or more of the voting power in the Australian company. This change was in line with the amendments to the unilateral credit provisions which the UK had enacted in its domestic law. This change in the credit article was the UK’s principal objective in renegotiating the Treaty.57 The Memorandum observed that the draft contained a note to the effect that crediting of underlying tax by the UK was ‘subject to reciprocity’, but pointed out that the ITAA 1936 s46 rebate meant that dividends

55 The question of whether Australia’s pre capital gains tax treaties provided protection from Australian taxation of capital gains made by enterprises that did not have a permanent establishment was answered in the affirmative in *Virgin Holdings SA v Commissioner of Taxation* [2008] FCA 1503 and in *Undershaft v Commissioner of Taxation* [2009] FCA 41. See the discussion of these cases in R J Vann, ‘Comment on *Virgin Holdings SA v Commissioner of Taxation* [2008] FCA 1503 and *Undershaft v Commissioner of Taxation* [2009] FCA 41’ (2009) 11 International Tax Law Reports 653–72.

56 This was: income from a trust or estate; some alimony payments; and income derived from a third country. In the case of trust income, the Memorandum considered that the draft might exempt all income derived by a UK resident from Australia via a trust; if so, this would clearly be inappropriate. Here it is worth noting that the draft included ‘interest’ and ‘capital gains’ articles. If these articles had been excluded, as had been previous Australian treaty practice, then interest and capital gains would have been dealt with under the ‘other income’ article.

57 See the discussion at 5.9.
received by Australian public companies from UK companies did not bear Australian tax and that usually this would be the position in the case of Australian private companies. The Memorandum considered that, in these circumstances, the UK might not insist on reciprocity.

Non-Discrimination

5.38 The UK draft contained a non-discrimination article. Both the Memorandum and O'Reilly noted that: there was no equivalent provision in existing Australian treaties; subject to certain reservations by NZ, it was contained in the UK – NZ Treaty; and it was an OECD provision. O'Reilly went on to list examples of ways in which Australia discriminated between residents and non-residents. These were: (i) the rebate on dividends received by resident companies; (ii) limiting to residents only deductions for capital subscribed to prospecting companies; and (iii) the exemption for residents of income derived from the mining of uranium.58

5.39 O'Reilly referred to a memorandum sent to the Treasurer as part of the Japanese negotiations.59 For the reasons set out there, O'Reilly considered the article undesirable and commented: ‘Even if it were re-drafted to permit us to continue all our present “discriminations” it would still be clearly restrictive on future policy.' The Memorandum stated that acceptance of the article would preclude Australia in the future from discriminating against foreign owned companies. After noting that State taxes and other Commonwealth taxes would be within the prohibition, the Memorandum pointed out that the equivalent article in the 1966 NZ – UK Treaty only applied to the taxes covered by that treaty.60

Initial Australian Reactions At The Ministerial Level

5.40 The UK sought renegotiation of the 1946 UK Treaty because changes in the UK system of corporate shareholder taxation meant that it wanted more restricted foreign

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58 In addition, the Memorandum contained several examples of the implications of Article 22. These included that: (a) Australia might have to free from tax dividends flowing to UK companies attributable to their Australian permanent establishments; (b) capital subscribed by a non-resident to petroleum exploration companies would have to be deductible and this, presumably because of the operation of the UK's foreign tax credit system, could produce benefits for the UK Treasury rather than for the UK investor; and (c) the variation according to the status of the payer in the consequences for failure to comply with proposed withholding tax provisions on interest and royalties might be prohibited.

59 This aspect of the memorandum is discussed at 6.23.

60 As discussed at 4.66, a negative view of the non-discrimination article had previously been taken in the analysis by M J Belcher of the non-discrimination article in the 1963 draft OECD Model.
tax credit provisions.\(^{61}\) The Australian Treasurer, in a submission to Cabinet, considered that this change was one that Australia would have to agree to.\(^{62}\)

5.41 The submission considered that the UK draft (and the OECD Model on which it was based) was technically unsatisfactory at several points because its provisions had been designed to suit the situation of bi-directional income flows that existed between the main OECD countries and not the largely uni-directional flows as between the UK and Australia.\(^{63}\)

5.42 The submission argued that any treaty Australia negotiated with the UK at this time would ‘stand as something of a precedent’ for negotiating treaties with other countries, especially given the UK’s renewed interest in EEC membership.\(^{64}\)

5.43 The submission regarded the following as the key UK proposals:

1. A more restrictive definition of ‘permanent establishment’ than in the 1946 UK Treaty;
2. Shipping and aircraft profits continuing to be taxed on a residence basis but irrespective of the place of registration;
3. A reduced rate of taxation on dividends paid to residents of the other country, with a further reduction for dividends paid to companies with a 25% or more shareholding;
4. Interest and royalties (including film royalties) being taxed on a residence basis;
5. The credit for Australian underlying corporate tax being restricted to UK companies with a 10% or more shareholding in the Australian company;
6. A non-discrimination article;
7. Taxation of other income on a residence basis.\(^{65}\)

5.44 The submission and the Cabinet decision on what should be Australia’s negotiating position on key articles in the UK draft are discussed in the following paragraphs. The primary focus of the submission and of the Cabinet decision is on setting a clear

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\(^{61}\) See the discussion at 5.9.


\(^{63}\) Submission 123, pp13–14, para 24.

\(^{64}\) Submission 123, p13, para 25. For a discussion of Australia’s responses to the UK’s second attempt to join the EEC see Benvenuti (2006) above n 9 and Singleton and Robertson, above n 5, chs 9 and 10.

\(^{65}\) Submission 123, pp14–15, para 24.
initial Australian negotiating position on withholding tax rates, exemptions and the scope of definitions, with little or no consideration being given to the technical issues raised in O'Reilly's letter and the Memorandum.

**Permanent Establishment**

5.45 Regarding the definition of permanent establishment in the draft as unduly restrictive, the submission recommended pressing for a more comprehensive definition of permanent establishment. The technicalities in relation to the definition of permanent establishment were to be left to the negotiators, subject to consultation where necessary on a 'best interests' basis.

**Dividends**

5.46 The submission considered that the UK Exchequer was the principal beneficiary of the exemption from Australian tax of dividends paid by a wholly owned subsidiary to a UK parent because otherwise it was likely that UK parent companies would have most, if not all, of their UK tax on dividends received from their Australian subsidiary eliminated by the UK foreign tax credit system.

5.47 The submission recommended, and Cabinet decided, that Australia argue for a uniform maximum rate of 15% withholding tax on all dividends (except for certain special transactions through permanent establishments). This proposal was consistent with Australia's other taxation agreements of the 1950s, as discussed in Chapter 3, and with the UK's newly revised agreements with the US, NZ and Canada, but it represented a change from the Australian Cabinet decisions 386 of August 1962 and 1009 of September 1963. Eliminating the exemption for dividends paid by 100% subsidiaries to their UK parent would increase the overall tax burden on these dividends but would put them in the same position as UK companies with a 10% or more shareholding in an Australian company who would obtain a UK foreign tax credit for the underlying Australian corporate tax. This was seen as removing the strong incentive that the exemption provided for UK companies to acquire and retain 100% ownership of Australian companies. Using the same logic, Australia did not

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67 Submission 123, p24, para 48.
68 Submission 123, p18, para 23. The submission was inconsistent on this point as paragraph 10 had noted that because of the availability of the credit for underlying tax, the level of Australian corporate tax meant that no UK corporate tax would be payable on dividends in this situation.
69 Cabinet decision 386 and Cabinet Submission 305 are discussed at 4.33 to 4.52. Cabinet decision 1009 and Cabinet Submission 871 are discussed at 4.85 to 4.89.
favour the UK proposal for a further reduction in withholding tax for dividends paid to UK companies with 25% or more ownership.\textsuperscript{70}

**Interest**

5.48 The submission proposed to continue to assert full source country taxing rights to interest, but noted the proposal to introduce a withholding tax system for interest paid to non-residents.

**Royalties**

5.49 The submission was that Australia’s initial negotiating position should be that Australia should have the right to tax royalties at source through the use of a proposed withholding tax system.\textsuperscript{71}

**Shipping Profits**

5.50 The submission proposed, as a bargaining point in negotiations, that Australia have the right to tax 2.5% of the outward freight and passenger fares from shipping.\textsuperscript{72} Australia expected strong resistance on this point and was prepared to concede a residence basis of taxation of shipping generally to gain the right to tax coastal shipping, which the UK had recently conceded in treaties with NZ and Canada.\textsuperscript{73}

**Foreign Tax Credits**

5.51 The submission recognised that Australia would have to concede a minimum shareholding qualification for the UK credit for foreign underlying tax. Australia, as a bargaining ploy, proposed that the qualification be a 5% UK corporate shareholding, not the 10% minimum shareholding requirement of UK domestic law. The submission recognised that if Australia were to adopt a general foreign tax credit system, the UK would expect Australia to give credit for UK underlying corporate tax in equivalent circumstances to those where the UK gave such credit. \textsuperscript{74}

\textsuperscript{70} Submission 123, pp16–17, paras 27–29. As noted at 3.52, Australia had used a similar argument in negotiating a flat 15% source country tax rate for all dividends in the negotiations for the 1953 US Treaty. McGovern, as noted at 4.17, had continued to express this view in his 8\textsuperscript{th} April 1960 letter to the Secretary of the Department of the Treasury. As discussed at 6.19, the Australian delegation put the same argument against the use of a 5% dividend withholding tax for non-portfolio dividends in the preliminary talks with Japan in April 1964.

\textsuperscript{71} Submission 123, pp19–20, paras 35–8.

\textsuperscript{72} As noted at 5.26 and 2.14 and accompanying notes, Australia applied a presumptive tax regime to shipping profits under which 5% of the freight and fares were taxed.

\textsuperscript{73} Submission 123, pp17–18, paras 30–2.

\textsuperscript{74} Submission 123, pp20–2, paras 39–41.
In 1967, Australia’s dividend withholding tax system still permitted a non-resident to elect to be taxed on an assessment basis, with credit being given for the withholding tax deducted. For foreign tax credit purposes, the UK had refused to credit Australian dividend withholding tax and only credited Australian tax where the UK shareholder elected to be taxed in Australia on an assessment basis. The submission proposed to remove the right for non-resident shareholders to elect to be taxed on an assessment basis, expecting that the UK would thereafter credit Australian dividend withholding tax.\textsuperscript{75}

**Non-discrimination**

The submission noted that the proposed article would conflict with certain provisions of Australian law, commenting that, ‘While it might be possible to negotiate provisions with sufficient qualification to make them compatible with our law, I think it would be best to avoid any provisions on “non-discrimination”’.\textsuperscript{76}

**Correspondence Between Australian And UK Officials On The Draft Prior To Negotiations**

The Australian Commissioner of Taxation (E T Cain)\textsuperscript{77} wrote to W H B Johnson, Under Secretary of the UK Board of Inland Revenue, on 13\textsuperscript{th} December 1966 raising technical and drafting points and seeking clarification on some aspects of UK law. Cain stated that his letter did not represent the beginning of formal negotiations, that he had not had direction from ministers on the form or substance of the agreement and stressed that his letter did not refer to any major matters of policy from an Australian government viewpoint.\textsuperscript{78} Johnson made a detailed reply to Cain’s letter on 3\textsuperscript{rd} February 1967.\textsuperscript{79} In the following paragraphs, each of Cain’s points and Johnson’s response to it will be discussed together. The discussion is confined to selected articles.

\textsuperscript{75} Submission 123, pp17–18, paras 30–2.
\textsuperscript{76} Submission 123, pp20–2, paras 39–41.
\textsuperscript{77} Submission 123, p23, para 45.
\textsuperscript{78} Submission 123, p22, para 43. The election had primarily been introduced to accommodate NZ shareholders in Australian companies. The need for the election on this basis had disappeared when NZ replaced its exemption for income sourced in a Commonwealth country with a foreign tax credit system. The removal of the election had been recommended in Australia, *Report of the Commonwealth Committee on Taxation* (the Ligertwood Committee), Canberra, 1961, p110, para 543.
\textsuperscript{78} Cain to Johnson, 13\textsuperscript{th} December 1966. Inland Revenue file.
\textsuperscript{79} Johnson to Cain, 3\textsuperscript{rd} February 1966. Inland Revenue file.
Residence

5.55 Cain doubted whether the definition of ‘resident’ in the draft would include entities, such as a company incorporated in Australia or a contributor to the Commonwealth Superannuation fund, who were Australian residents by virtue of the statutory definition in ITAA 1936 (Cth). Australia had been satisfied with the residence definitions in the 1946 UK Treaty and had never found dual residence to be a serious problem under it. Cain raised the problems with the corporate dual residence tie-breaker that O’Reilly had identified\(^{80}\), but he did not refer to the then recent UK treaty with New Zealand. Johnson noted the suggestion that the definition in the 1946 treaty might be preferable, but said that his view was that it was necessary first to discuss whether it was desirable to eliminate dual residence. If Australia could accept the basic UK proposal, a solution could then be sought to the difficulties Cain had mentioned. Johnson stressed that the definitions in all new UK treaties were similar to those in the draft that followed the OECD recommendation. In addition, there would be awkward problems under UK law (as amended by changes in the corporate tax system) concerning any company with dual residence status.

Permanent Establishment

5.56 Cain regarded the definition of permanent establishment in the draft as falling short of what Australia viewed as adequate and enclosed the definition in the Australian model.\(^{81}\) Cain referred to paragraph (viii) of the definition in the 1966 UK – NZ Treaty\(^{82}\) and to equivalent articles in Australia’s treaties with Canada and NZ. The point had been raised in O’Reilly’s letter.\(^{83}\) Apparently, this request was a response to the situation that arose in Case 110 (1955) 5 CTBR (NS) 656.\(^{84}\)

5.57 Johnson responded that, while it was helpful to have Australia’s views, he was not sure that the Australian draft (particularly paragraph (2)(ii) dealing with substantial equipment) was entirely satisfactory from the UK viewpoint. Johnson considered that it ought to be possible to reach a solution acceptable to both sides in the negotiations. Johnson’s letter contained no specific comment on paragraph (viii) of the UK – NZ Treaty. The omission is interesting as the problem dealt with under the article is referred to in the UK Inland Revenue’s minutes of a meeting of Australian

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\(^{80}\) See the discussion at 5.13.
\(^{81}\) The definition of permanent establishment in the 1965 Australian model is discussed at 4.102 to 4.105 and at 4.113 to 4.117.
\(^{82}\) See the discussion at 5.19.
\(^{83}\) See the discussion at 5.19.
\(^{84}\) Case 110 (1955) 5 CTBR (NS) 656 was discussed at 5.19 n 33.
and UK officials in 1959. The omission may reflect a desire to reserve the UK’s position pending face to face negotiations rather than ignorance of the problem on Johnson’s part.

5.58 Article 4(4) (covering companies providing the services of public entertainers or athletes) dealt with a situation of concern to Australia, and Cain feared that the real profit might not be derived by the company that ‘carries on the activity of providing the services’ of the entertainer. Cain makes no mention of the need for a source rule. Johnson noted that Australia was giving further consideration to the adequacy of paragraph (4) and indicated that the UK had no objection to ‘tightening it up’.

Industial Or Commercial Profits And Associated Enterprises

5.59 On Article 6, dealing with industrial or commercial profits, Cain raised three issues which had been discussed in O’Reilly’s letter and in the Memorandum. In all three issues, both O’Reilly and the Memorandum had contrasted the 1966 UK draft with either the 1946 UK Treaty or with the 1953 US Treaty. On all three issues, Cain merely stated the point of concern to Australia without comparing the UK draft with previous Australian treaties.

5.60 First, on the ‘same or similar conditions’ point, Cain more succinctly made the same point as had been made by the Memorandum, namely that there could be circumstances in which a true arm’s length profit could only be ascertained by postulating different conditions from those which in fact applied. Johnson noted that Australia would pursue this point in negotiations.

5.61 Second, on the issue of providing for cases where information was insufficient to determine the profits to be attributed to a permanent establishment, Johnson’s response was to indicate that the UK was prepared to add a sentence in similar form to Article III(3) of the 1946 UK Treaty and Article III(3) of the then current UK treaty with New Zealand. Cain also raised the same issue in relation to Article 8 (Associated Enterprises) and received a similar response from Johnson.

5.62 Third, on Australia’s ability to apply ITAA 1936 (Cth) s38 on the basis that it was a simplification of but not a departure from the principles in Article 6(4) of the draft, Johnson’s reply was that the UK did not consider s38 in any way in conflict with

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85 Australian Double Taxation Talks, Meeting 11th May 1959, para 3, and 22nd April 1959 3(a) Inland Revenue file.
86 As discussed at 5.25, the Memorandum had also raised this issue.
87 See the discussion at 5.23.
88 See the discussion at 5.21.
89 See the discussion at 5.24.
Article 6(4), and that it would not prevent Australia from applying the principles of Article 6(4).

5.63 Cain raised several issues in relation to Article 6 which had not been raised in the same form by O'Reilly or in the Memorandum. The first concerned the geographic source of profits attributable to a permanent establishment. The Memorandum had raised this issue in the specific context of the profits of public entertainer companies, but Cain raised it in the context of industrial or commercial profits generally. Cain's letter at this point reflected concern about the adequacy of Australian source rules. Johnson responded that, following the OECD Model Article, it had not been the UK's practice to include a source rule. He questioned whether a source rule was any longer necessary, but said that if it were necessary on the Australian side to include a special source rule, then the UK would be happy to do so.

5.64 Cain pointed out that the 1946 UK Treaty had preserved the Australian bases of taxing film businesses controlled abroad and insurance with non-residents. Johnson replied that the UK noted Australia's interest in continuing the special bases for taxing these types of income and that these questions would need further discussion during the negotiations.

5.65 Another issue concerned the application of Article 6(7) in determining the profits of insurance companies, particularly in relation to relief for management expenses, the basis on which taxation would be levied and the effect of the non-discrimination article on them. Cain asked a question about the potential effect the article might have on 'the companies', clearly meaning insurance companies. Johnson replied that since the decision in Ostime v Australian Mutual Provident Society [1960] AC 459, the UK had changed its domestic law so that the position that existed prior to that decision would apply. Johnson explained that the main purpose of Article 6(7) of the UK draft was to clarify the basis of liability of Australian life insurance companies operating in the UK. In the absence of Article 6(7), the UK would be able to choose between assessing the company to corporation tax as trading profits or assessing it on investment income on property or rights held by or used by the branch plus annuity profits. If the company were assessed on an investment income basis, then chargeable gains would also be liable to corporation tax. As there were not statutory provisions relating to the method for determining investment income, Johnson indicated that the UK would probably use a formula like the one (relating to corporation tax on life insurance companies) in s430 of Income Tax Act 1952. In this

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90 See the discussion at 5.25.
situation, Australian life insurance companies would obtain relief for their management expenses but would only be able to set these against dividends received from UK companies if the treaty included a non-discrimination article.\(^{91}\)

**Dividends\(^{92}\)**

5.66 Cain indicated that Australia anticipated difficulties in relation to the ‘beneficial ownership’ test proposed for dividends, given that in Australia a trustee could be taxed on income accumulating in the trust and, as the ultimate title to the income often depended on contingencies, the beneficial ownership of dividends paid to trustees would not be clear. This could mean that an Australian trustee receiving dividends from a UK company might not be entitled to the reduced treaty rate of withholding tax.\(^{93}\) Johnson agreed that the concept of beneficial ownership was not always easy to apply in the trust context,\(^{94}\) but he indicated that a similar formula could be adopted in Australia’s case to the one that the UK had used in the 1966 NZ – UK Treaty.\(^{95}\) Johnson believed, however, that this was not necessary, because in the case Cain had mentioned, the UK considered that relief from UK tax would be

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\(^91\) In [*Ostime v Australian Mutual Provident Society*](https://doi.org/10.1093/acprof:oso/9780198788605.001.0001/9780198788605) [1960] AC 459, a majority of the House of Lords held that an Australian insurance company's taxable surpluses were ‘industrial and commercial profits’ and hence were only taxable under Article III(2) of the 1946 UK – Australia Treaty and not on a proportion of its worldwide income attributable to the UK under UK domestic law. As a consequence, the UK amended its domestic law to enable it to continue to apply a global apportionment approach to determining the income of a company engaged in the business of life assurance that was subject to UK tax. Article 6(7) in the draft treaty was a savings clause in relation to these provisions in UK domestic law.

\(^92\) In addition to the questions discussed under this heading, Cain raised three questions for Johnson concerning: (a) the exclusion of certain redeemable share capital and securities in respect of shares from the definition of ‘dividend’ in the 1966 NZ – UK Tax Treaty; (b) what were the practical means that the UK used in applying the reduced rate for dividends in tax treaties; and (c) the rationale behind Article 9(4) of the UK draft, which was an anti-dividend stripping provision. Cain’s questions and Johnson’s responses are discussed in more detail in C John Taylor, ‘The Negotiation and Drafting of the 1967 UK – Australia Taxation Treaty’ in John Tiley (ed), *Studies in the History of Tax Law* (Hart Publishing, 2012) vol 5, 427 at 453–5.

\(^93\) As discussed at 5.29, the point had been raised less explicitly in the Memorandum.

\(^94\) A note, dated 6\(^{th}\) January (apparently 1966 from the order in which it appears in the file), commented on the meaning of ‘beneficial owner’. The note points out that the expression ‘beneficial owner’ was not defined in UK statute law but had been considered by UK courts. The note indicates that, generally speaking, a beneficial owner of property may be said to be one who has the right to the use and enjoyment of property, including, on a sale, the right to the proceeds. The note goes on to point out that the beneficial owner is not necessarily the same as the legal owner. Examples from the law of trusts are given to illustrate the point. ‘Beneficial Ownership’ 6\(^{th}\) January, Inland Revenue file.

\(^95\) Article VI(3) of the 1966 NZ – UK Tax Treaty stated: ‘For the purposes of paragraphs (1) and (2) of this article, dividends in respect of which a trustee is subject to tax in NZ shall be treated as being beneficially owned by that trustee.’ Article VI(4) included the following sentence: ‘For the purposes of this paragraph, dividends in respect of which the trustee is subject to tax in the UK shall be treated as being beneficially owned by that trustee.’
available under the current draft. As an alternative, Johnson suggested that the 'subject to tax' test from the 1946 UK Treaty could be used.\textsuperscript{96}

5.67 Under paragraphs 9(5) and (6) of the draft dividend article, the reduction in the rate of tax on dividends in Article 9(1) did not apply where the dividend was effectively connected with a trade or business carried on by the non-resident through a permanent establishment in the other treaty partner country where the trade or business was such that a sale of the shareholding would be regarded as a trading receipt. Cain asked whether administrative guidelines had been set for determining when a dividend was effectively connected with a trade or business carried on through a permanent establishment. Cain assumed that Article 9(5) was not to be construed so that a company whose profit on a sale of shares would be a capital gain would not be entitled to the reduced rate on dividends.

5.68 Johnson's reply was that the UK had no formal rules for determining when a dividend was 'effectively connected' with a permanent establishment, and that the words had been taken from the OECD Model. Johnson referred Cain to the Commentary on the OECD Model in noting that the object of the language was to do away with the 'force of attraction' principle. In a narrow interpretation of 'effectively connected',\textsuperscript{97} Johnson stated that generally there should be no difficulty in identifying when interest, dividends and royalties were effectively connected with a permanent establishment. The only interest and dividends effectively connected with a permanent establishment would be when 'financial concerns' drew interest and dividends in the course of carrying on their normal business. Johnson confirmed that Article 9(5) was not intended to deprive a company whose profit on a sale of shares was treated as a capital gain from the reduced rate on dividends. The UK was prepared to apply the reduced rate on all dividends, even those effectively connected with a permanent establishment, except where the owner of the effectively connected holding was an

\textsuperscript{96} The relevant provision in the 1946 UK Treaty was Article VI(2)(b), which stated: 'Any dividend paid by a company which is a resident of Australia (whether or not also resident in the UK or elsewhere) to a company which – (a) is a UK resident; (b) is subject to UK tax in respect thereof, and (c) beneficially owns all the shares (less directors' qualifying shares) of the former company, shall be exempt from Australian tax: [a proviso followed setting out circumstances in which the exemption was not available].'

\textsuperscript{97} The interpretation of the expression 'effectively connected' given in Johnson's letter is narrow by comparison with paragraph 31 of the Commentary on Article 9(4) in the OECD Model, the relevant portion of which makes the point that Article 9(4) does not adopt the 'force of attraction' principle but goes on to merely comment that dividends are taxable as part of the profits of a permanent establishment if they are paid in respect of holdings forming part of the assets of the permanent establishment or are otherwise effectively connected with the permanent establishment. The Commentary does not limit the application of Article 9(4) of the Model to 'financial concerns' or other entities where profits from sales of particular shares were included in their taxable profits.
individual or a financial concern. Financial concerns included the proceeds of share sales in their taxable profits, and the proceeds were therefore properly described as ‘trading receipts’.

**Interest And Royalties**

5.69 Contrary to prior Australian practice, Articles 10 and 11 of the UK draft gave the residence country the exclusive right to tax interest and royalties. Cain asked for an explanation of the purposes for UK law of Articles 10(4) and 10(5) and 11(4). Johnson explained that Articles 10(4) and 11(4) (in determining character in the hands of a non-resident recipient) overrode provisions in UK law which re-characterised certain interest and royalty payments as dividends (and hence denied a deduction to the payer). The override did not apply where the recipient company was under UK control. Johnson explained that Article 10(5) was an anti-avoidance provision aimed at preventing bond washing by tax exempt bodies and paralleled similar provisions in UK domestic law.

**Capital Gains**

5.70 Cain explained that Australia did not at present have a capital gains tax and that this kind of tax was not covered by any of Australia’s existing agreements. Cain asked whether the article varied the practical effects of UK law regarding capital gains derived by non-residents. Johnson replied that the article reproduced the substance of UK law but that since drafting it, a loophole had been discovered which would enable a UK resident to go to a foreign country, such as Australia, for one year, and while there realise a capital gain on UK property tax free. Johnson indicated that to prevent this the UK would like to add a ‘subject to tax’ test in Article 12(3).

**Other Income**

5.71 Both O'Reilly's letter and the Memorandum had pointed out that none of Australia’s earlier treaties had contained an ‘other income’ article. Cain commented that the other income article in the draft would operate for UK residents in relation to income from a trust, some alimony payments, and to income derived from a third country. Australia was concerned that, under the draft, dividends derived from Australia

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98 In the subsequent Australian Federal Court decision in *Undershaft v Commissioner of Taxation* [2009] FCA 41, Lindgren J held, inter alia, that capital gains made on disposals of shares in a related entity in a corporate reconstruction were ‘industrial or commercial profits’ for the purposes of the 1967 Australia – UK Tax Treaty. The decision is inconsistent with Johnson’s interpretation of paragraphs 9(5) and 9(6) of the dividend article.

99 See the discussion at 5.36.
through a trust would have to be exempted in Australia. Cain asked what income of Australian residents the article would extend to. Johnson replied that the article was ‘a sort of long stop’ intended to regulate the treatment of types of income which had not been specifically dealt with elsewhere in the treaty. Hence it was not possible to give an exhaustive list of the types of income which it might cover. The obvious cases were trust income, alimony payments and third country income, and Johnson noted that Australia had reservations about the application of the article relating to trust income.

Credits

5.72 Cain enquired whether if Australia taxed a profit as ordinary income in circumstances where the UK taxed it as a capital gain, the UK would give credit for the Australian income tax against the UK tax on the capital gain. Johnson confirmed that credit would be granted.

5.73 Under the draft, the UK would only grant a credit for underlying corporate tax if Australia reciprocated. Cain pointed out that usually ITAA 1936 s46 freed Australian companies from tax on dividends. Johnson replied that the credit provisions in the draft simply reflected current UK law but would continue to bind the UK in the event of changes to UK domestic law. Hence the UK considered that it was entitled to ask Australia to undertake a corresponding obligation. Johnson suggested that either the credit be contingent on the continuance of Australia’s effective exemption, or that the two countries should consult to establish new rules.

5.74 Cain commented that for Australia to give credit for UK tax, it appeared to be necessary to have an election to gross up UK dividends. The issue had arisen in the negotiation of the 1946 UK Treaty. Johnson did not reply to Cain’s comment.

The Negotiations In Canberra: March–April 1967

5.75 Negotiations were held in Canberra over a ten-day period commencing on 31st March 1967. Australia was represented by Sir Richard Randall (Secretary to the Treasury), Messrs Pryor, Daniel and Ross of the Treasury, Cain (Commissioner of Taxation), Wicks, W J O’Reilly (Second Commissioner of Taxation), Boucher, and

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100 As noted at 5.37, this point had been raised by O’Reilly and in the Memorandum.
101 Johnson noted that this had been done in the UK’s treaties with Canada and New Zealand.
102 See the discussion at 2.132 to 2.133.
Hill of the ATO and Hutchinson (First Assistant Crown Solicitor) of the Attorney General’s Department. The UK was represented by Messrs Johnson (Under Secretary, Department of Inland Revenue), F P Harrison (Assistant Secretary, Department of Inland Revenue), Robertson (Principal, Department of Inland Revenue) and by Miss Harrison from the British High Commission.\(^{103}\)

5.76 Cain’s opening address emphasised that Australia, as a net importer of capital and not a maritime nation, approached many issues from a different point of view. Cain commented: ‘Much of the lore on double taxation has been built up on the experience of countries quite differently situated, and there is a limit to the extent that we can accept it.’\(^{104}\) The UK ‘Notes of Meetings’ record that in their opening remarks the Australian representatives ‘pointed out that they did not regard the OECD Model as entirely suitable to the circumstances of their country’. Cain possibly departed from his draft text and explicitly mentioned the OECD Model, but it is also possible that the UK delegation interpreted the remarks from Cain’s opening address quoted above as referring to the OECD Model. All records of the negotiations and the draft of the address itself confirm that Australia was particularly concerned about provisions in the UK draft relating to dividends, interest, royalties and shipping profits.

5.77 By agreement, the UK draft of September 1966 formed the basis for the discussions. The remainder of the first day of negotiations was devoted to an examination of the broad outline of each article of the September 1966 draft.\(^{105}\) Australian records of the negotiations report that Johnson indicated that his government had taken a very firm line on shipping profits.\(^{106}\) The following account of the negotiations will be confined to those issues on which there was significant discussion between the delegations. The account is organised topically rather than chronologically.

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\(^{104}\) ‘Draft Notes of a Statement by the Commissioner’, Australian Treasury file. ‘Opening Meeting with UK Delegation’, Australian Treasury file, confirms that Cain was scheduled to give the opening address at the conference. ‘Notes on discussions 13/3/67–14/4/67’ (hereafter ‘Notes on discussions’) Australian Treasury file, handwritten notes (apparently made by an Australian Treasury official) confirm that Cain made an opening address but do not indicate what the content of the address was.


Definitions

 Resident

5.78 Australia raised an issue concerning the corporate residence tie-breaker in the draft (place of effective management) and referred to the problem identified in O’Reilly’s letter to Randall\(^\text{107}\) and in Cain’s letter to Johnson\(^\text{108}\). The UK delegation appreciated the problem but pointed out that the tie-breakers were intended to avoid the taxation of dual resident companies by both countries. The Notes of Meetings record that ‘It might be possible to meet the Australians’ problem by provisions along the lines of those in the recent NZ agreement.’\(^\text{109}\)

5.79 The Australians subsequently raised the same issue and the same scenario, explicitly referring to proposed Article 9(7) as preventing Australia from taxing a dividend paid by the interposed company to UK residents and to the shareholder not being liable to UK tax because of the credit provisions. The Australians suggested that the definition of resident company be amended (consistently with previous Australian practice) so that a company would be a resident of Australia if it were an Australian resident under Australian domestic law and would be a resident of the UK if it were a resident of the UK under UK domestic law provided it was not a resident of Australia. The UK delegation objected that this proposed definition was too wide, given the Australian tests of company residence.\(^\text{110}\) The Notes of Meetings record that a possible compromise was: (a) that for all purposes, other than dividends paid by dual resident companies, the definition include a corporate residence test along the lines of either the September 1966 draft or the 1966 UK – NZ Treaty;\(^\text{111}\) and (b)

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\(^\text{107}\) See the discussion at 5.13.

\(^\text{108}\) See the discussion at 5.55.

\(^\text{109}\) Notes of Meetings, First Day, 31\(^{\text{st}}\) March 1967, Morning Session, p2. The Notes of Meetings do not explicitly refer to the inability of Australia to tax subsequent dividends paid by the interposed company to UK resident shareholders, but this would have been the combined effect of the tie-breaker and draft article in the circumstances contemplated. The Notes of Meetings merely record that the use of the interposed company would secure the dividend rebate and escape Australian tax on the dividends. ‘Notes on discussions’, in commenting on the discussion of Article III(3) of the draft on the first day, note that a company incorporated in Australia would be a resident for purposes of the s46 exemption but that the ‘effective management’ tie-breaker ‘cld give complete exemption’.

\(^\text{110}\) Under the definition of ‘resident’ as it applied to companies in ITAA 1936 as it then stood, a company was a resident of Australia if it: (a) was incorporated in Australia; or (b) not being incorporated in Australia, carried on business in Australia and either: (i) was centrally managed and controlled in Australia; or (ii) had its voting power controlled by Australian residents.

\(^\text{111}\) Under the 1966 UK – NZ Treaty, the definitions of corporate residence in Article II were:

\((j)\) The term “NZ company” means any company which is —
that the dividend article should provide that, in the case of dual resident companies, Australia was entitled to tax dividends paid to UK shareholders and that the UK was entitled to tax dividends paid to Australian shareholders. The initialled draft implemented this agreement, but it was subject to further amendment through correspondence following the completion of negotiations.

Permanent Establishment

5.80 The Australians indicated an intention to raise the question of including oil and gas wells and agricultural and pastoral properties in the definition of permanent establishment (PE) and also wanted a provision similar to Article II(1)(p)(viii) of the UK–NZ Agreement (which expressly included a subsidiary company engaged in trade or business in the other state whether or not through a permanent establishment) and wanted an agent who filled orders from stock to be included.

5.81 The Australians’ reasons for including agricultural and pastoral properties in the definition of PE were explained and the Australian request was agreed to. Johnson had explained that their omission from the definition of PE was due to them being dealt with in the OECD Convention under Article 5 relating to immovable property. It was noted that agricultural and pastoral properties were included in the definition of PE in the 1946 UK Treaty because it did not contain an immovable property article. Including them under the immovable property article as in the September 1966 draft meant that they were not given the protection of the rules in the industrial or commercial profits article about the allowance of reasonable expenses. It was agreed

(i) Incorporated in NZ and which has its centre of administrative or practical management in NZ whether or not any person outside NZ exercises is capable of exercising any overriding control or direction of the company or of its policy or affairs in any way whatsoever; or

(ii) Managed and controlled in New Zealand;

(k) The term “UK company” means any company which is managed and controlled in the UK and is not a NZ company.

(l)(i) The term “resident of the UK” means any UK company and any other person who is resident in the UK for the purposes of UK tax and the term “resident of New Zealand” means any NZ company and any other person who is resident in NZ for the purposes NZ tax.

Notes of Meetings, Second Day, 3rd April 1967, Afternoon Session, pp3–4. Report of discussions on 31st March 1967, the official Australian record of the discussions, is much briefer at this point and merely comments on Article 3: ‘The article was found to be technically unsatisfactory in some respects and some clauses were redrafted along lines acceptable to Australia. One clause remained unacceptable to Australia but the UK undertook to provide a form of words which it was thought would meet Australia’s requirements.’ Notes on discussions, 3rd April 1967, record that there was a drafting change to Article 3(2)(a) but that O’Reilly said that Article 3(2)(d) was ‘politically undesirable’ and suggest that Johnson agreed to take Article 3(d) out.

See the discussion at 5.147 to 5.151.

Notes on discussions, 4th April 1967.
at this point that ‘it would be preferable to deal with such property in the present article, and to add a reference to forestry’.\textsuperscript{115}

5.82 The word ‘installation’ was added to sub-paragraph 2(g) to cover a person who contracts to manufacture, supply and install equipment.\textsuperscript{116} It was agreed on the third day that provision dealing with supervisory activities as in the UK – NZ Treaty would be added. It is clear that these additions were requested by Australia.\textsuperscript{117}

5.83 At Australia’s request, the minimum period for building or construction sites and assembly projects in sub-paragraph 2(g) was agreed to be reduced to six months.\textsuperscript{118} The equivalent provision in the UK draft had contained a twelve-month minimum period for building sites or construction or assembly projects. The 1967 UK Treaty is the first Australian treaty with six months being the minimum required period for a building site, construction or assembly project to be classified as a permanent establishment.\textsuperscript{119}

5.84 Australia raised the case of a US company which had appointed a UK company as its sole distributor of its products in Australia on a commission basis. The US company licensed the UK company to manufacture its products and use its trademarks, reimbursed the costs of manufacture and loaned all the machinery necessary to manufacture its products. The US company was treated as having an Australian PE under the 1953 US Treaty where permanent establishment was defined as including ‘the use or installation of substantial equipment or machinery by, for, or under a contract with, an enterprise of one of the countries’. While the UK delegation agreed that there was some justification for treating the company as having an Australian PE in the example given, they considered that the Australian formula was too wide because it might, for example, cover plant supplied under a hire purchase agreement or ordinary plant hire and hence might ‘cut across’ the royalty article.\textsuperscript{120} No further mention is made of this request in either the UK or Australian records of the negotiations nor in the subsequent correspondence. A

\textsuperscript{115}Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Morning Session, p2. Notes on discussions, 4\textsuperscript{th} April 1967. The handwritten notes by the Australian Treasury official convey the impression that the suggested solution was proposed by Mr Johnson of the UK delegation.

\textsuperscript{116}Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Morning Session, p2. Notes on discussions, 4\textsuperscript{th} April 1967.

\textsuperscript{117}Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Morning Session, p2. Notes on discussions, 4\textsuperscript{th} April 1967. An equivalent article had been in the 1965 Australian model. See the discussion at 4.62 and 4.70.

\textsuperscript{118}Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p2.

\textsuperscript{119}This was a variation on prior Australian practice. See the discussion of the comments in the Memorandum at 5.14.

\textsuperscript{120}Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Afternoon Session, pp.2–3.
substantial equipment provision was not included in the final version of the treaty, although variants on it appear in most subsequent Australian treaties.\textsuperscript{121}

5.85 The Australians pointed out that Article 4(3)(e) (which deemed certain activities not to amount to a PE) could mean that a person who sold information through a place of business would be deemed not to have a PE. It was agreed that the draft of Article 4(3)(e) would be revised.\textsuperscript{122} The final version of the treaty, in a variation from the 1963 Draft OECD Model and subsequent versions of the OECD Model, did not contain the words ‘for the collection of information’ in Article 4(3)(e).

5.86 An Australian Treasury official’s notes indicate that Australia sought the addition of clause 8(p)(viii) of the UK – NZ Treaty and comment that this was ‘OK’.\textsuperscript{123} As is clear from the UK Notes of Meetings, the reference should have been to Article II(1)(p)(viii) of the UK – NZ Treaty.\textsuperscript{124} The final version of the Australia – UK Treaty included Article 4(8), which was identical in form to Article II(1)(p)(viii) of the UK – NZ Treaty. Article 4(8) dealt with the problem raised in Case 110 (1955) 5 CTBR (NS) 656.\textsuperscript{125}

5.87 Agreement was also reached on changes relevant to agency PEs requested by Australia. One amendment agreed to at this point was that: (a) ‘on behalf of’ be substituted for ‘in the name of’ in paragraph 5 to cover the agent who acts for an undisclosed principal.\textsuperscript{126} Paragraph 5 of the UK draft was identical to Article 5(4) in the draft 1963 OECD Model Convention. The change of language agreed upon here clearly reflects an attempt to accommodate the language of the article to the common law concept of ‘agent’.\textsuperscript{127} The Notes of Meetings also record that at this point, as

\textsuperscript{121} As shown in Appendix 3, substantial equipment provisions appear in all but five subsequent Australian tax treaties.
\textsuperscript{122} Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Afternoon Session, p3.
\textsuperscript{123} Notes on discussions, 5\textsuperscript{th} April 1967, ‘Article 4 (Cont)’.
\textsuperscript{124} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p2. There was no clause 8(p)(viii) in the 1966 UK – NZ Treaty. The author considers that the reference to this clause was a clerical error by the Australian Treasury official and that the reference should have been to clause II(p)(viii), which deemed there to be a permanent establishment in certain cases where there was a special relationship between principal and agent. Article 4(8) of the 1967 UK – Australia Treaty is identical in form to Article 2(p)(viii) of the 1966 UK – NZ Treaty. See the discussion at 5.19.
\textsuperscript{125} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p2. Notes of discussions, 5\textsuperscript{th} April 1967, ‘Article 4 (Cont)’.
\textsuperscript{126} The different concepts of ‘agent’ in common law and civil law and their implications in this context are discussed by John F Avery Jones and Jurgen Ludicke, ‘The Origins of Article 5(5) and Article 5(6) of the OECD Model’ (2014) 6 World Tax Journal 203. As Avery Jones and Ludicke at 206 point out, the expression ‘in the name of’ has no meaning in common law because a contract by an agent for an undisclosed principal will normally bind the principal. Avery Jones and Ludicke also note, at 221, that earlier OEEC and OECD drafts of Article 5(4) had used the expression ‘on behalf of’ in the second reference in Article 5(4)(a) and comment that ‘How and why the change was made is something of a mystery for which no explanation is contained in the minutes.’
requested by Australia, it was agreed to add words at the end of paragraph 6 to cover an agent who, because of a special relationship with the principal, does not charge commission at the going rate.\textsuperscript{128}

5.88 Curiously, in the final treaty the addition suggested was not made to paragraph 6. Handwritten notes by an Australian Treasury official record O'Reilly as observing that the UK draft had dropped the idea of a special relationship between an agent and his principal.\textsuperscript{129} It is likely that O'Reilly’s comment was making a comparison between the UK draft and the 1946 UK Treaty, which limited the equivalent exclusion to situations where the broker or general commission agent received remuneration at the rate customary in the relevant class of business.\textsuperscript{130} The Australian Treasury official’s notes record Johnson as replying that he regarded some cases as being covered by Article 8 (the ‘associated enterprises’ article), but that he did not see how or why a PE could be regarded as existing in these cases. The notes by the official then state, ‘Addition Agreed’.\textsuperscript{131} The absence of the agreed addition in the final version of the treaty is therefore puzzling. The UK Notes of Meetings also note that ‘It was agreed to add a sub-paragraph dealing with an agent who fills orders from stock to be a permanent establishment.’\textsuperscript{132} The Australian Treasury official’s notes make it clear that the addition was at Australia’s request.\textsuperscript{133}

5.89 Australia expressed concerns about Article 4(4) in the context of companies providing the services of public entertainers,\textsuperscript{134} fearing that Article 4(4) would not catch a company providing (possibly through an intermediary) the services of an entertainer under a slavery contract. Australia then submitted an alternative draft, which read as follows:

‘An enterprise of one of the territories shall be deemed to carry on business in the other territory though a permanent establishment situated therein in relation to income (other than dividends) which it derives from or in relation to contracts or obligations for the rendering within the other territory of the services of public entertainers or athletes such as are referred to in Article 15.’

\textsuperscript{128} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p2.
\textsuperscript{129} Notes of discussions, 5\textsuperscript{th} April 1967, ‘Article 4 (Cont)’.
\textsuperscript{130} Article II (1)(j) of the 1946 UK – Australia Treaty.
\textsuperscript{131} Notes of discussions, 5\textsuperscript{th} April 1967, ‘Article 4 (Cont)’.
\textsuperscript{132} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p2. The relevant provision in the 1967 Australia – UK Tax Treaty was Article 4(5)(b).
\textsuperscript{133} Notes of discussions, 5\textsuperscript{th} April 1967, ‘Article 4 (Cont)’.
\textsuperscript{134} As discussed at 5.58, this concern had been raised in Cain’s letter to Johnson.
The UK objected that this would deem there to be an Australian source and enable Australia to obtain tax in circumstances where this might not be possible under Australian domestic law. This was justifiable to ensure that a treaty did not open up avenues for avoidance, but it was ‘quite another matter’ to use a treaty to make good gaps in domestic anti-avoidance legislation. The Notes of Meetings then record that a solution might be to exclude supplying the services of public entertainers from the definition of industrial or commercial profits; a decision which was subsequently made. The notes of an Australian Treasury official record that this was at Australia’s request and was based on the form of the 1960 NZ Treaty, which excluded such profits from the definition of industrial and commercial profits.

5.90 Australia had already indicated on the first day that it wanted Article 15 (dealing with artistes and athletes) strengthened to cover companies which supplied the services of entertainers. It was subsequently agreed that, as it was conceivable that Australian courts might in some circumstances deem income from ‘employment, etc.’ exercised in Australia to have a non-Australian source, a source rule was necessary in Articles 13, 14 and 15 (professional services, dependent personal services and entertainers, respectively). This is an example of a continuing Australian treaty practice of deeming there to be an Australian source where there might not be an Australian source outside the treaty.

5.91 Interestingly, the UK does not appear to have objected to the existence of a deemed source rule in this context, although, as noted above, it objected to such an extension in the context of industrial and commercial profits. To be consistent with the UK’s objection to the extension in that context, having a deemed source rule in the context of Articles 13, 14 and 15 would have to be seen as preventing the treaty from otherwise opening up avenues for tax avoidance.

Industrial Or Commercial Profits

5.92 Australia wanted two further types of income to be excluded from the definition of ‘industrial or commercial profits’. These were the taxation of film businesses.
over which Australia wished to retain its current tax treatment, and coastal shipping,\textsuperscript{142} with the latter exclusion being considered necessary if Australia’s source country taxing rights over coastal shipping were to be preserved.\textsuperscript{143}

5.93 The Australians requested a source rule in the industrial and commercial profits article. The Notes of Meetings indicate that the UK was prepared to acquiesce so long as this did not mean that there was an Australian source where there was not one under Australian domestic law.\textsuperscript{144}

5.94 The Notes of Meetings on the discussion of paragraph (3) of the article (providing for the use of arm’s length in determining the profits of a PE) comment that in making this determination it ought to be possible to ignore the special relationship between a head office and a branch. The Australians doubted whether the phrase ‘under the same or similar conditions’ would allow this to be done. It was agreed to use paragraphs (3) and (4) of Article III of the 1946 UK Treaty instead. This would entail adding the source rule and the information provision that was contained in the 1946 UK Treaty.\textsuperscript{145}

5.95 The Australians commented that they did not regard paragraph (4) of the industrial and commercial profits article as being inconsistent with \textit{ITAA 1936} s38,\textsuperscript{146} but preferred to apply s38 as a short cut that saved arguments. The UK delegation undertook to consider the issue further.\textsuperscript{147} The Australians subsequently explained that s38 simplified calculations by obviating the need to analyse all elements going into a wholesale price. The UK delegation agreed to the inclusion of a s38 source rule at this point, ‘especially if it can be done on a reciprocal basis’.\textsuperscript{148} The Australians indicated that they would produce a form of words that would allow the

\textsuperscript{141} The negotiations in relation to the taxation of film businesses are not discussed in detail in this chapter.\textsuperscript{142} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p3.\textsuperscript{143} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p3.\textsuperscript{144} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p2. The relevant provision became Article 5(9) in the 1967 UK Treaty, clearly inserted at Australia’s request. The Notes of Meetings also record that the Australian domestic law source rule was ‘not very precise’.\textsuperscript{145} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session and Afternoon Session, p2. The information provision and aspects of the source rule in the 1946 UK Treaty were discussed at 2.115 to 2.126.\textsuperscript{146} \textit{ITAA 1936} s38 was discussed at 3.47.\textsuperscript{147} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p3. Notes of discussions, 31\textsuperscript{st} March 1967 contain the following comment:

‘VI source rule J (Johnson) some hesitation
(4) cf s38
film business & reinsurance (illegible)’\textsuperscript{148} Notes of discussions, 5\textsuperscript{th} April 1967.
principles of s38 to be applied. There is no further mention of discussion of the industrial and commercial profits article in the Notes of Meetings.

Associated Enterprises

5.96 The desirability of including a provision to cover estimated profits where actual figures were not available, as had been done in the 1946 UK Treaty, was discussed. The UK pointed out that the article was in the standard form adopted in almost all UK treaties. The Australians argued that the proposed wording of Article 8 was less precise than that in Article IV of the 1946 UK Treaty, which had been tested in the courts and had been found to work as intended. The meeting then decided to substitute Article IV of the 1946 UK Treaty, including the source rule and the information provision for draft Article 8.

Dividends

5.97 The draft dividend article assumed that different rates would apply to portfolio and non-portfolio dividends. The discussion of rates of withholding tax on dividends was obviously robust. On the first day the Australians proposed a rate of 15% for both portfolio and non-portfolio dividends, but the question was reserved for later discussion.

5.98 The UK suggested that the OECD rates of 15% for portfolio dividends and 5% for non-portfolio dividends apply, and that the OECD definition of the type of company qualifying for the lower rate be adopted; but it did not consider this test sacrosanct. The UK argued that the provisions in the 1946 UK Treaty, which exempted dividends paid to a 100% UK parent, were inconsistent with modern conditions and with Australia’s policy of encouraging local participation. Although the UK had agreed to a uniform 15% rate on dividends in several of its recent agreements, the situation with Australia was distinguishable because, given that dividends by wholly owned subsidiaries had been completely exempt for a long time, a large number of companies would be affected by any change and a 15% withholding tax would only

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149 Notes of Meetings, Fourth Day, 5th April 1967, Morning Session, p2. Notes of discussions, 5th April 1967. The relevant article was Article 5(4) in the 1967 Australia – UK Tax Treaty. It would appear from the Notes of Meetings that Article 5(4) was drafted by Australia and was certainly inserted at Australia’s request.


151 Notes of Meetings, Fourth Day, 5th April 1967, Afternoon Session, p3. There is no reference to subsequent discussion of the associated enterprises article in the Notes of Meetings.

152 Notes of Meetings, First Day, 31st March 1967, Morning Session, p.3.

add to their tax burden. The UK balance of payments would suffer both from the reduction in the rate on outbound portfolio dividends and from an increase in Australian tax on inbound dividends from 100% subsidiaries. The Voluntary Program was already restricting the increase in UK investment in Australia, but a 15% withholding tax on dividends paid to direct investors would be a positive discouragement of it. The UK argued that there should be broad equality of treatment between a branch and a subsidiary. Hence Australian tax on subsidiary dividends should be kept to a minimum as a high rate would encourage UK businesses to convert their subsidiaries to branches.

5.99 The Australians’ response was that Australia had long been unhappy with the exemption for dividends paid by 100% subsidiaries. All of Australia’s other agreements had a uniform 15% rate on dividends. To concede a lower rate on dividends paid to UK parents would cause Australia difficulties in negotiations with other countries, and political opinion in Australia was strongly against it. Given the imbalance of income flows between the two countries, a low rate of tax on subsidiaries’ dividends would cause a substantial loss to the Australian revenue. By contrast, a 15% rate would not cause a loss to the UK revenue because the extra tax would be borne by the companies concerned. A 15% rate on dividends taken with the Australian rate of corporate tax produced a total rate of around 51% on non-portfolio dividends, which Australia did not regard as exorbitant. Australia was not concerned about possible avoidance, because Australia would not be any worse off than it was now given that it was not collecting any tax on dividends paid by wholly owned subsidiaries.

5.100 The Australians agreed to make a submission to their ministers for a reciprocal 10% rate on interest and royalties and a uniform 15% rate on dividends. The Notes of Meetings do not record any discussion of the reasons behind the shift in the UK’s attitudes to the taxation of dividends. Given that the submission for a uniform rate of 15% on all dividends was to be made along with submissions for rates of 10% on

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154 The Voluntary Program was a UK program introduced in 1965 to control direct UK investment in developed Sterling Area countries. UK National Archives, T295/524, OIG (66)2, “Guidelines for overseas investment”, 9 February 1966.
157 Presumably because of limitations on the UK's foreign tax credit, although this is not stated in the Notes of Meetings.
158 Although not expressly stated in the Notes of Meetings, a reasonable inference is that the tax avoidance would be through converting subsidiaries to branches.
interest and royalties, it may be that Australia’s agreement to the latter rates was regarded as a matching concession for the UK conceding its position on non-portfolio dividends. While the rates of tax on interest and royalties were high by OECD standards, they did represent a reduction in Australian source taxation of these items of income which had previously been taxed at full marginal rates.\textsuperscript{161}

5.101 The initial discussion of effectively connected dividends confirmed that sales of shares in a 100% subsidiary would not normally constitute trading receipts.\textsuperscript{162} The discussion then turned to the treatment of banks. The UK pointed out that under Australian law Australian banks received an inter-corporate dividend rebate under \textit{ITAA 1936} s46, but UK banks operating through branches in Australia did not. The UK submitted that this meant that UK banks were at a competitive disadvantage when compared with Australian banks and that this should be removed in the treaty. Taxing UK banks under the industrial or commercial profits article effectively involved giving the branch analogous treatment to an Australian resident company so far as the inclusion of dividends in assessable income was concerned, but analogous treatment was not given in the case of the inter-corporate dividend rebate under s46. The Australian reply was that Australia could levy dividend withholding tax on dividends paid by a resident company to a non-resident shareholder, but could not do this in the case of branches and hence took the tax where it could.\textsuperscript{163}

5.102 The Australians indicated that they were not happy with Article 9(7) applying to Australian undistributed profits tax. The UK view was that the ban on undistributed profits tax was complementary to the ban on taxation of dividends paid by a non-resident company to a non-resident shareholder and that the Australian definition of private company meant that a wide range of companies, some of them quite substantial, were exposed to undistributed profits tax.\textsuperscript{164} Subsequently, it was noted that UK private companies were seldom, if ever, caught by undistributed profits tax. Australia was concerned that if it were to renounce undistributed profits tax on UK private companies in the treaty, then UK private companies would be able to ‘plough back tax free’ a greater amount of retained profits than would similarly placed Australian companies.\textsuperscript{165} The UK response was that this was essentially an anti-

\textsuperscript{161} This aspect of prior Australian tax treaty practice is discussed at 2.90, 2.102, 2.104, 3.127, 4.93 to 4.100, 4.109 and 4.148.

\textsuperscript{162} This was consistent with Johnson’s earlier advice to Cain discussed at 5.68.

\textsuperscript{163} Notes of Meetings, Second Day, 3\textsuperscript{rd} April 1967, Morning Session, p2. It is likely that this represents the UK reporter’s interpretation of what the Australian delegation said. It seems unlikely that the Australian delegation would use the words ‘took the tax where it could’.

\textsuperscript{164} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p3.

\textsuperscript{165} Notes of Meetings, Second Day, 3\textsuperscript{rd} April 1967, Morning Session, p2.
avoidance issue that was properly a matter for the residence country. If the UK close
country would undertake to levy only the same tax on non-residents as on
residents. It is unclear which delegation proposed this compromise. It was later
decided to substitute a provision similar to Article VI(8) of the NZ Treaty for
paragraph (7). Article VI(8) of the NZ Treaty restricted a source country from
imposing tax on dividends paid by a non-resident company to a non-resident
shareholder, but did not in terms prevent the source country from imposing
undistributed profits tax on the non-resident company.

5.103 The treatment of dividends paid in the ‘New Broken Hill’ situation (where a UK
resident company paid dividends funded solely from Australian source profits to
Australian resident shareholders) was a major point of disagreement in the
negotiations and was not finally resolved until several months after the negotiations
were otherwise concluded. The Australians asked for a provision similar to Article
9(8) of the UK – Canada Treaty, arguing that there should be no UK tax on the
dividends in the New Broken Hill situation simply because Australian source profits
had passed through a conduit UK company en route to Australian shareholders.

5.104 The UK response was that to give shareholders relief because dividends were
funded from a particular geographic source of profit would be inconsistent with the
separate entity theory that now underpinned both Australian and UK corporate-
shareholder taxation. Furthermore, the New Broken Hill situation was merely a
variant on a company which had profits from several jurisdictions, and in the latter
case it was impossible to apportion dividends according to the source of profits. The
UK delegation indicated that their ministers would have to be consulted before a
decision could be made.

5.105 The Australians raised the New Broken Hill issue again towards the end of the
negotiations, stating that if the UK was willing to drop the non-discrimination article
and tax on dividends in the New Broken Hill situation, Australian ministers were

168 Article VI(8) of the UK – NZ Double Taxation Treaty of 11th August 1966 read as follows:
‘VI(8) The Government of one of the territories shall not impose any form of taxation, in
addition to tax on the company’s profits, on dividends paid by a company which is
resident of the other territory to persons not resident in the first mentioned
territory.’
prepared to accept, though with considerable reluctance, a shipping exemption. The Australians further indicated that they would like a decision on the New Broken Hill situation before the end of discussions, but that if no decision was reached by then they were authorised to initial the draft, with the shipping exemption, on the basis that the matter could be raised again at government level. The UK’s response was that their ministers might take the view that, except for Broken Hill relief, the agreement was merely a standard agreement without a non-discrimination article and might want some matching concession from Australia.\footnote{Notes of Meetings, Sixth Day, 7th April 1967, Morning Session, p1.}

5.106 The Australians pointed out technical problems that would be involved in giving effect to a New Broken Hill concession if the UK were to agree to one. The Notes of Meetings comment that the problem would have to be resolved by providing that where the 90% rule applied Australia would not treat the company as a resident for the purposes of the ‘criss-cross’ rule.\footnote{Notes of Meetings, Sixth Day, 7th April 1967, Morning Session, p2.}

5.107 When the position in relation to trusts was discussed, the Australians explained that Australia taxed the trustee of a discretionary trust and the trustee of estates in the course of administration where no beneficiary was presently entitled to the trust income. The Australians envisaged that the UK draft might open up opportunities for tax avoidance, giving the example of a UK trust set up with a fund of Australian shares and Australian beneficiaries. The Australian view was that under the draft Australia would only get 15% withholding tax on the dividends, the UK might have to give up its tax on the winding up of the trust, and Australia would get nothing more as it did not tax distributions out of trust accumulations.\footnote{Notes of Meetings, Second Day, 3rd April 1967, Morning Session, p2.} It was agreed to not put any special provision for trusts in the dividend article and to consider excluding trust income from the ‘sweep up’ (that is, other income) article as had been done in the NZ Agreement.\footnote{Where no beneficiary was presently entitled to the income of the trust estate or to any part of the income of the trust estate, under ITAA 1936 s99, as it then stood, a trustee was assessed and liable to pay tax on the net income or the relevant part of the net income. At that time, no provision in ITAA 1936 taxed beneficiaries on subsequent distributions of accumulated income.}
Interest

5.108 Subject to some exceptions, principally where payment was made to a permanent establishment, the UK draft exempted interest from source taxation.\(^{175}\) This represented a very significant change from the 1946 UK Treaty where full source country taxing rights in relation to interest were retained.

5.109 The Notes of Meetings record that the current Australian system of taxing interest paid to non-residents at marginal rates was easily avoided because tax was not payable where interest was paid on a contract, enabling the lender to enforce payment without deduction of tax.\(^{176}\) Australia was proposing to introduce a withholding tax likely to be at a 10% rate. Australia argued for a reciprocal limitation of the rate to the proposed rate of Australian withholding tax. The UK objected that this would allow Australia but not the UK to tax at its full statutory rate and thus it might be preferable to drop the interest article altogether.\(^{177}\)

5.110 When the interest article was discussed again the Notes of Meetings record that, although Australia was not prepared to surrender its right to tax interest to the residence country entirely, it would accept a reciprocal rate of 10%. This was agreed and the Australians undertook to produce a revised draft of Article 10. It was also noted that, as Australian borrowers received a deduction for interest paid, Article 10(4) needed to be reciprocal.\(^{178}\) The Notes of Meetings contain no explanation of the change in the UK’s attitude.

Royalties

5.111 Australia and the UK had diametrically opposed views on the taxation of royalties. The Notes of Meetings record that large amounts of royalties and know-how payments were leaving Australia but that Australia was unable to tax them either because the contracts were arranged so that it was difficult to allege an Australian source or because they were ‘dressed up’ as industrial and commercial profits. The Australians indicated that the government intended to legislate to define royalties in similar terms to those used in Article 5 of the UK draft, and to deem them to have an Australian source and tax them on an assessment basis when exploited in Australia.

\(^{175}\) Article 10 of UK Draft, September 1966.
\(^{176}\) At the time of the negotiations in Canberra in 1967, Australian treatment of interest paid to non-residents was unchanged from the treatment that applied in 1945. See the discussion of that treatment at 2.15.
\(^{178}\) Notes of Meetings, Third Day, 4th April 1967, Morning Session, p1. The interest article is not mentioned subsequently in the Notes of Meetings. Note that, as discussed at 2.19, the UK did not allow a deduction for interest paid.
Australia's view was that the country of source ought to have the right to tax, but it was prepared to concede a reduced rate of tax in the treaty.\textsuperscript{179}

5.112 By contrast, the UK's view was that royalties should be taxed on a residence basis, as the gross royalty did not represent true profit because it took no account of expenses. Only the country of residence was in a position to tax royalties fairly, because only the country of residence was able to say what expenses ought to be allowed.\textsuperscript{180}

5.113 The Australians claimed the right to tax royalties at source: (a) on the basis that the royalties were (i) paid out of Australian source profits and (ii) deductible from the payer's Australian source profits; and (b) because Australia provided the conditions under which the licensor could exploit knowledge. The outflow of royalties to the UK was considerable, with the Australian estimate being $A10 million to $15 million while the UK estimate was $A7 million gross. The UK reiterated their previous arguments for taxation on a residence basis, adding that exemption in the source country encouraged the free interchange of technical knowledge. Nonetheless, the UK agreed to source taxation providing that the Australians would make a submission to Australian ministers that the rate on royalties (including copyright royalties) not exceed 10% and that there be a uniform 15% rate on dividends.\textsuperscript{181} The source country rates on these three types of income were probably arrived at through a process of matching concessions.\textsuperscript{182} It seems likely that the key concession made by Australia was to tax royalties at a flat 10% rate, because the proposed treaty rate for interest was the same as the foreshadowed Australian domestic law rate and because the UK originally sought a 5% rate on non-portfolio dividends.\textsuperscript{183}

5.114 It was also agreed that 'information' be added after 'rights or property' in Article 11(3) to cover title to receive payments from know-how. The Notes of Meetings record that a definition along the lines of the definition in the 1966 UK – NZ Treaty would

\textsuperscript{179} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p3.
\textsuperscript{180} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p4.
\textsuperscript{181} Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Morning Session, p1.
\textsuperscript{182} See the discussion of balancing concessions at 5.133 to 5.140.
\textsuperscript{183} As Australia in 1967 was still taxing royalties paid to non-residents on a net basis, it is possible that deductions may have meant that taxation on a net basis under domestic law might have been less than the 10% gross basis permitted under the treaty. Hence, agreeing to a 10% gross basis might in fact not have been such a significant concession by Australia. Vann and Oliver make a similar point about taxation of leasing of substantial equipment under the treaty (taxed under the royalty article in this treaty) in R J Vann and J D B Oliver, 'The New Australia–UK Tax Treaty' [2004] \textit{British Tax Review} 194 at 221–4. Admittedly, the point is stronger in the case of equipment leasing where significant deductions (interest and depreciation) for equipment are available.
conform more closely to the new definition proposed for Australian domestic law. Hence it was agreed to redraft Article 11(3) accordingly.\textsuperscript{184}

\textit{Shipping And Air Transport}

\textbf{5.115} Australian ministers had given instructions that Australia should have the right to tax UK shipping profits in accordance with Australian domestic law. The UK would not agree to this and produced a written statement of the UK view.\textsuperscript{185} The UK was prepared to agree to allow Australia to tax the profits of ships engaged in coastal trade, but wanted to give further consideration to whether this should include voyages between Australia and Papua New Guinea.\textsuperscript{186} The Australians wanted to examine the definition of ‘international traffic’ to ensure that it would allow Australia to tax the profits of voyages solely between Australian ports.\textsuperscript{187}

\textbf{5.116} The Australian record of the discussions notes that when shipping profits were discussed again there was ‘a total opposition of views, which was not resolved’.\textsuperscript{188} This record notes that the Australians stressed that ministers had given firm directions on the taxation of international shipping and that any question of derogation from this position would have to be referred back to ministers.\textsuperscript{189} The UK ‘Notes of Meetings’ record that the Australian delegation commented that ‘their Ministers might be more inclined to accept the UK views on the taxation of shipping if they could report a favourable solution to the dividend question’, something on which the UK had not yet reached a final decision.\textsuperscript{190} The treatment of shipping profits was only finally resolved through correspondence, discussed below, following the conclusion of the negotiations.

\textsuperscript{184} Notes of Meetings, Third Day 4\textsuperscript{th} 1967, Morning Session, p2. The royalties article is not mentioned subsequently in the Notes of Meetings.
\textsuperscript{185} Both the Notes of Meetings and the official Australian Report of discussions refer to the UK circulating a paper on the first day setting out its views on the international taxation of shipping and air transport. The author has been unable to locate the paper in either the UK National Archives or the National Archives of Australia.
\textsuperscript{186} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Morning Session, p4.
\textsuperscript{187} Notes of Meeting, First Day, 31\textsuperscript{st} March 1967, Morning Session, p1.
\textsuperscript{188} Report of discussions on 4\textsuperscript{th} April 1967.
\textsuperscript{189} Report of discussions on 4\textsuperscript{th} April 1967.
\textsuperscript{190} Notes of Meetings, Third Day, 4\textsuperscript{th} April 1967, Morning Session, p1. The only subsequent mention of the shipping and air transport article in the Notes of Meetings is in the morning session of the 9\textsuperscript{th} day under the heading ‘General’. The reference to the ‘dividend question’ clearly is to the rate of withholding tax on dividends as distinct from the ‘dividend question’ associated with the New Broken Hill situation. Shipping profits were the first item discussed in the morning session of the third day but, as discussed at 5.95, the UK later in that session apparently agreed to a uniform 15% dividend withholding tax.
Immovable Property

5.117 Income from immovable property was originally dealt with in Article 5 of the UK draft of September 1966. The Notes of Meetings record that the article ‘dealt with agricultural enterprises but there might be some advantage in transferring to Article 4’. Clearly, this suggestion came from the Australians. As noted above, the Notes of Meetings also record that the Australians indicated that they intended to raise the issue of including agricultural and pastoral properties in the definition of PE. When the article was discussed again, the Australian view was that the disadvantage of dealing with agricultural enterprise under the immovable property article as in the draft was that this did not give the protection of the rules in the business profits article about the allowance of reasonable expenses. It appears that the UK then agreed with the Australian suggestion on this point.

5.118 When the article was discussed again, it had been renumbered as Article 8. The Notes of Meetings record that it had been agreed that the article should be amended to allow ‘agricultural enterprises etc to have their expenses in accordance with the principles in article 6’. Difficulties in the interpretation of the article and possible conflicts with article 6(7) (which taxed effectively connected rents as business profits) were noted. As the article did not ‘secure any result other than that achieved under domestic law’, a decision was made to delete it.

Capital Gains

5.119 The UK draft had included a capital gains tax article. The Australians explained that although Australia had no capital gains tax at present, the existence of the article would ‘tie their hands’ in relation to the UK if they ever introduced one in the future. The UK pointed out that the draft article was reciprocal but that an article based on the OECD Model was an alternative if Australia did not like the draft article. The Australians questioned the need for the article and preferred that the article be dropped altogether, which the UK delegation indicated they would consider.

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191 Article 5 of UK Draft, September 1966.
192 Notes of Meetings, First Day, 31st March 1967, Morning Session, p2. Article 4 contained the definition of permanent establishment. Including agricultural enterprises within the definition of PE would mean that they were taxed under the industrial and commercial profits article, which was Article 6 in the draft of September 1966.
193 Notes of Meetings, Third Day, 4th April 1967, Morning Session, p2. As noted at 2.102, agricultural and pastoral properties had been included in the definition of permanent establishment in the 1946 Australia – UK Tax Treaty.
Handwritten notes by an Australian Treasury official observe that the political climate was against CGT and that the inclusion of the article might prevent passage of the treaty through the Senate.\textsuperscript{196} The article is not mentioned again in either official record of the discussions until the fifth day, when both official records confirm that the article was to be omitted.\textsuperscript{197}

\textbf{5.120} It is clear from the notes of the meeting that the Australian delegation considered that by not including a capital gains tax article in the treaty, Australia would retain full rights to levy capital gains tax on UK residents if it subsequently introduced a capital gains tax. In this context, it should also be noted that the view of the delegations was that capital gains on realisation of shares in a 100\% subsidiary would not normally be considered ‘trading receipts’ and hence would not amount to industrial or commercial profits.\textsuperscript{198}

\textit{Other Income}

\textbf{5.121} The UK draft contained an ‘other income’ article giving the country of residence exclusive right to tax income not expressly mentioned in other articles.\textsuperscript{199} The Australians stated that they considered that this article only needed to cover tax on third country income and that they were concerned about its application in the case of trusts.\textsuperscript{200}

\textbf{5.122} The Notes of Meetings subsequently record that the article ‘contradicts Australia’s general philosophy concerning the taxation of income flowing abroad and they cannot accept it as it stands’. The Australians were prepared to accept the results of the article as regards tax on third country income. While this would mean that there would be nothing in the treaty dealing with alimony, this was seen as being of comparatively minor importance. Restricting the article to tax on third country income would not create problems in relation to trusts because both the UK and Australia treated income flowing through a trust in which beneficiaries had an absolute interest as retaining its original identity. The Notes of Meetings comment that the absence of another income article would only be felt in the case of discretionary trusts, which would be treated on an ‘empirical basis’, and record that ‘It was in consequence

\begin{flushleft}
\textsuperscript{196} See also Notes of discussions, 31st March 1967.
\textsuperscript{197} Notes of Meetings, Fifth Day, 6th April 1967, Morning Session, p1. Report of discussions on 6th April 1967. The Australian record makes it clear that the article was omitted at Australia’s request.
\textsuperscript{198} As noted at 5.68 n 98, in \textit{Undershaft v Commissioner of Taxation} [2009] FCA 41 Lindgren J subsequently came to the opposite conclusion.
\textsuperscript{199} Article 20 of UK Draft, September 1966, Inland Revenue file.
\textsuperscript{200} Notes of Meetings, First Day, 31st March 1967, Afternoon Session, p5.
\end{flushleft}
agreed that the Article should be amended to restrict its scope to tax on third country income.\textsuperscript{201}

5.123 By restricting the other income article to tax on third country income, both parties considered that they would retain full taxing rights in relation to income not otherwise dealt with in the treaty. This is particularly evident from the Australian comment that the original article, which gave exclusive taxing rights to the residence country, contradicted Australia’s general philosophy concerning the taxation of outbound income.

Credits

5.124 The major reason why the UK wanted the treaty reviewed was to restrict the circumstances in which it would, following the introduction of UK corporation tax, grant a foreign tax credit for underlying foreign corporate tax.\textsuperscript{202} The draft credit article limited the availability of credits for underlying corporate tax to situations where the recipient of the dividend was a company holding a 10% or greater interest in the paying company. Draft Article 22(1)(b) indicated that the UK would grant credit for Australian corporate tax in this situation. A marginal note in the draft indicated that the inclusion of (b) was subject to reciprocity and indicated that the reciprocal provision was to be drafted by Australia.

5.125 The Australians proposed that the minimum percentage shareholding for an underlying foreign tax credit should be reduced to 5%.\textsuperscript{203} The UK saw no logic in this, as the reason for the minimum shareholding requirement was to limit credit for underlying tax to dividends from ‘trade investment’. It was unlikely that a trade investor would have a less than 10% shareholding, but it was possible that a portfolio investor might hold 5%.\textsuperscript{204}

5.126 On the question of reciprocity, the Notes of Meeting record that the UK’s preferences were in the following order:

(1) to write in each country’s domestic laws;
(2) to link the UK commitment to the continuance of the present Australian exemption; and

\textsuperscript{201} Notes of Meetings, Fifth Day, 6th April 1967, Afternoon Session, p2. The other income article is not mentioned subsequently in the Notes of Meetings.
\textsuperscript{202} See the discussion at 5.9.
\textsuperscript{203} As discussed at 5.51, this was a bargaining ploy recommended to Cabinet in the Treasurer’s submission.
\textsuperscript{204} Notes of Meetings, First Day, 31st March 1967, Morning Session, p5.
(3) to have a consultation provision on the NZ model.\textsuperscript{205}

The Notes of Meeting indicate that Australia’s preference at this stage was for (3).\textsuperscript{206}

5.127 When the credit article was discussed again, Australia was no longer pressing for a reduction in the minimum shareholding percentage for an underlying foreign tax credit. The Australians explained their reasons for rejecting approaches (1) and (2) at 5.127 to reciprocity. The first alternative, of writing in each country’s domestic laws, would remove their freedom of action for a considerable time in the future. They were concerned that the second alternative, of linking the UK’s commitment to the continuance of the present Australian exemption, might mean that the UK could be released from its obligation to provide an underlying foreign tax credit if Australia did nothing more than change its law by adopting a foreign tax credit system which provided for underlying foreign tax credits. The UK accepted the Australian proposal that there should be consultation to establish the new rules if and when Australia’s existing rules were changed.\textsuperscript{207}

5.128 The Notes of Meetings record that rules would be needed to resolve conflicts between the UK and Australian law on the source of interest and royalties to enable credit to be given for tax deducted from ‘criss-cross’ dividends paid by dual resident companies.\textsuperscript{208} The credit article was also briefly discussed in the afternoon session of the sixth day. Here it was agreed to amend Article 21(4) so that it could apply where Australia gave relief in the form of: (a) credit (as in the case of dividends); or (b) exemption. Source rules for dividends, interest and royalties were also inserted.\textsuperscript{209}

\textit{Non-Discrimination}

5.129 The UK draft contained a non-discrimination article. None of Australia’s previous tax treaties had contained a non-discrimination article, and a non-discrimination article

\begin{itemize}
\item \textsuperscript{205} The relevant provision in the 1966 UK – NZ Treaty was Article XVIII(2)(b), which read as follows: ‘In the event that the Government of NZ should impose a tax on dividends received by companies which are resident in NZ the Contracting Governments will enter into negotiations in order to establish new provisions concerning the taxation of such dividends derived from sources in the UK.’
\item \textsuperscript{206} Notes of Meeting, First Day, 31\textsuperscript{st} March 1967, Morning Session, p5.
\item \textsuperscript{207} Notes of Meetings, Fifth Day, 6\textsuperscript{th} April 1967, Afternoon Session, p2.
\item \textsuperscript{208} Notes of Meetings, Fifth Day, 6\textsuperscript{th} April 1967, Afternoon Session, p2. The Notes of Meetings also record that the insertion of source rules in Articles 13, 14 and 15 meant that the source rule in paragraph (3) of the credit article was no longer necessary so far as it related to personal and professional services, but that it needed to be kept for services on board ships and aircraft.
\item \textsuperscript{209} Notes of Meetings, Sixth Day, 7\textsuperscript{th} April 1967, Afternoon Session, p3. At this session it was also agreed to amend the source rule in Article 21(4) dealing with services aboard ships and aircraft to make it consistent with Article 14(3).
\end{itemize}
had not been requested by Australia’s treaty partner in any of those treaties. All prior Australian analysis of and experience with non-discrimination articles had been negative.\textsuperscript{210} In the negotiations in Canberra the non-discrimination article emerges as one which divided the delegations, more at the level of principle and policy than practicality, and as one which proved to be the fulcrum on which the overall balance of concessions in the treaty pivoted.

5.130 The Notes of Meetings record that the article was not acceptable to Australian ministers. Although Australia did not discriminate on the basis of nationality, the notes list a number of examples of ways in which Australia did discriminate against non-residents.\textsuperscript{211} Including a non-discrimination article in the treaty was seen as likely to be highly embarrassing by adding fresh fuel to political controversy over whether Australia should have a branch profits tax.\textsuperscript{212}

5.131 The UK responded that one function of a double taxation agreement was to do away with discrimination against non-residents and that a non-discrimination article was therefore ‘a natural constituent of an agreement’. Similar articles were contained in their agreements with the US, Canada and New Zealand. Nothing in the draft article would prevent Australia from ‘refusing the dividend rebate’, and the article could be amended so as to enable the exemption for uranium mining to be continued in its present form. The UK pointed out that the absence of a non-discrimination article would mean that Australian insurance companies would not be able to get full relief for their management expenses.\textsuperscript{213} On the argument that the inclusion of the article would restrict Australia’s freedom in the future, the UK delegation responded that this was true of any article in the agreement.\textsuperscript{214}

5.132 When the non-discrimination article was discussed again, the UK reiterated its earlier arguments but added that the article would override the Finance Act provision which denied a resident company a deduction for interest paid to a non-resident. The UK then linked the non-discrimination article with the negotiations over the treatment of

\begin{itemize}
  \item \textsuperscript{210} As discussed at 4.66, Belcher, in reviewing the 1963 OECD draft, had been concerned at the revenue impact of a non-discrimination article if it required extension of the inter-corporate dividend rebate. As discussed at 4.122, the 1965 Australian model did not contain a non-discrimination article. As will be discussed at 6.11, Australian officials in preliminary discussions with Japan in 1963 had rejected a non-discrimination article.
  \item \textsuperscript{211} The discriminatory treatments listed were: (a) the inter-corporate dividend rebate; (b) the exemption for profits for uranium mining; and (c) the tax reliefs to residents who subscribe capital for mineral exploration.
  \item \textsuperscript{212} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Afternoon Session, p5.
  \item \textsuperscript{213} See the discussion of Ostime v Australian Mutual Provident Society [1960] AC 459 and the UK’s legislative responses in relation to this issue at 5.65.
  \item \textsuperscript{214} Notes of Meetings, First Day, 31\textsuperscript{st} March 1967, Afternoon Session, p6.
\end{itemize}
dual resident companies and the rates of withholding tax on dividends. The UK would be prepared to consider relief in the dual resident company case if there was a matching concession by Australia on either the non-discrimination article or in agreeing to the OECD rate on dividends.\textsuperscript{215}

\textbf{5.133} In response to the request for a balancing concession, the Australians raised the issues of the treatment of shipping profits and the UK’s wish to withdraw underlying tax relief for portfolio dividends.\textsuperscript{216} As the withdrawal of credits for underlying tax for portfolio dividends was the issue that had generated the negotiations in the first place, the Australians were on strong ground with this argument. The Australians argued that the concessions the UK offered were not adequate compensation for the UK tax system being less favourable to overseas investment as a result of the introduction of corporation tax.\textsuperscript{217}

\textbf{5.134} The UK’s reply was that credits for underlying tax would still be available for direct investment (presumed to be the form of investment of greatest concern to Australia) and, subject to certain conditions, for insurance company portfolio dividends, which could be written into the agreement if necessary. The UK also pointed out that any source tax on subsidiary dividends would be a disincentive to investment as it would fall on the parent company.\textsuperscript{218} The UK undertook to put to ministers Australia’s compromise proposal that New Broken Hill dividends should be exempt but that the exemption should be withdrawn if Australia subsequently introduced a branch profits tax.\textsuperscript{219}

\textbf{5.135} The Australian delegation subsequently indicated that if the UK would drop the non-discrimination article and exempt New Broken Hill type dividends, and provided there were no other matters in the agreement adverse to Australia, then Australian ministers would, with great reluctance, accept a shipping exemption. The Australians indicated a preference for a decision on the New Broken Hill issue before the end of the discussions, but that if none was forthcoming they were authorised to initial the agreement with a shipping exemption on the understanding that the New Broken Hill issue would be taken up at a government level.\textsuperscript{220} The UK replied that they would telegraph home for instructions, but commented that their minister might regard the agreement, without the New Broken Hill clause, as being merely a standard

\textsuperscript{215} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p1.
\textsuperscript{216} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p1.
\textsuperscript{217} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p1.
\textsuperscript{218} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p1.
\textsuperscript{219} Notes of Meetings, Fourth Day, 5\textsuperscript{th} April 1967, Morning Session, p2.
\textsuperscript{220} Notes of Meetings, Sixth Day, 7\textsuperscript{th} April 1967, Morning Session, p1.
agreement without a non-discrimination article and might want some matching concession.221

5.136 Johnson sent a telegram to Brookes of Internal Revenue on 7th April 1967, stating that the Australians were ‘anxious that dividends paid to their residents by U.K. companies operating almost wholly in Australia should be exempt from U.K. withholding tax’ and giving New Broken Hill as an example of such a company. The exemption sought in the New Broken Hill situation would be withdrawn if Australia ever imposed a branch profits tax. Johnson indicated that the Australians were very reluctant to exempt international shipping profits.

5.137 Johnson summarised what he saw as the likely content of any agreement with Australia. There would be: uniform reciprocal rates of 15% on dividends; 10% on interest and 10% on royalties; credit relief for underlying tax for portfolio shareholders would be withdrawn; and no non-discrimination article (‘because the Australians refuse to commit themselves in this way’). Australia would retain the right to tax premiums for the reinsurance in London of Australian risks. Johnson commented that he had made what case he could for a 5% rate on subsidiary dividends, but had to concede that ‘a 15 per cent rate was in line with a common pattern’. Johnson reported that the Australians had indicated that if Johnson could be given the authority to concede New Broken Hill relief, they would initial a text containing a shipping exemption while reserving the right to reopen the matter at a government level. The Australians had requested that Johnson seek the necessary authority and wanted the matter settled, if possible, during the discussions in Canberra. Johnson considered that, as a last resort, the UK should accept the bargain proposed by the Australians but noted that it was possible, if unlikely, that if the Australians were left to raise the matter at a government level the UK could secure a reduction of tax on non-portfolio dividends as well as the shipping exemption.222

5.138 In response to Johnson’s telegram, some ‘back of the envelope’ calculations were undertaken by Inland Revenue officers to determine the likely net revenue effect of the Australian proposal.223 Brookes replied to Johnson by telegram on 11th April 1967, indicating that New Broken Hill relief could not be conceded without ministerial authority and that it was impossible to obtain the Chancellor of the Exchequer’s decision at that time due to Budget preparations. In addition, ‘we should have to

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221 Notes of Meetings, Sixth Day, 7th April 1967, Morning Session, p1.
222 Telegram, Canberra to Commonwealth Office, Following for Brookes, Inland Revenue, from Johnson, U.K. team, 7th April 1967. Inland Revenue file, Part II.
223 File notes dated 7th April 1967, Inland Revenue file, Part II.
square treasury first on balance of payments aspects'. Brookes’ advice was that it would be wiser not to initial anything, because initialling would involve accepting Australia’s view on non-discrimination, non-portfolio dividends, and insurance. The Australian reservation on shipping meant that their initialling of that article was worthless. There was no objection to settling the drafting of these and other articles without prejudice to the policy.²²⁴

5.139 The next time that the non-discrimination article is mentioned, the Notes of Meetings record that the UK communicated the gist of the reply from London, summarised above.²²⁵ The Australians replied that they had authority to initial an agreement with a shipping exemption, provided there was no non-discrimination article and provided that the agreement was satisfactory in other respects. If there was no concession on the New Broken Hill issue, they reserved the right to raise the matter at a government level independent of the agreement.²²⁶ The UK’s response was that under this approach their minister might want a quid pro quo elsewhere in the agreement and that they would not want to do anything at this point that would inhibit him from seeking this.²²⁷ Hence it was agreed that the treaty be initialled on the terms provisionally accepted but accompanied by a covering memorandum stating that if the New Broken Hill issue was raised, ministers were free to reopen other matters.²²⁸

5.140 Johnson sent a telegram to Brookes on 12th April 1967 reporting Australia’s offer to initial a text which did not contain New Broken Hill relief but which did include a shipping exemption, and which dealt with other matters in the manner set out in Johnson’s telegram of 7th April 1967 on the basis that the Australian government might raise the issue of New Broken Hill relief with the Chancellor of the Exchequer separately on the condition that they would not seek to change other items if New Broken Hill relief was refused. Johnson considered the proposed treaty acceptable and reported that the delegates had agreed, subject to Brookes’ approval, to initial the draft text on the basis offered by Australia. The non-discrimination article was probably of little practical significance, the UK had a uniform 15% rate on dividends in other agreements, had conceded insurance to Australia and to other countries in previous agreements and the UK now had its own desire to reverse the decision in

Ostime v Australian Mutual Provident Society.229 Brookes’ brief telegram in reply dated 12th April 1967 simply stated ‘Content you should initial’ on the terms set out in Johnson’s telegram.230 A draft was evidently initialled at this point and members of the UK delegation left Australia on 16th April 1967.231

The Subsequent Correspondence And Drafting

5.141 Following the conclusion of the negotiations, Australia prepared a draft which was initialled by the delegations and forwarded to the UK. Major issues and detailed drafting amendments were then eventually resolved through correspondence without further meetings between officials.

5.142 The initial recommendation from Inland Revenue to the UK Treasury noted that although there were benefits for the UK in the treaty (removal of the requirement to give credit for underlying corporate tax and the exemption of shipping and aircraft profits from source taxation), it did not contain a non-discrimination clause and made a number of other concessions to Australia, particularly in relation to the level of source taxation permitted on dividends, royalties and interest. The uniform rate of 15% source taxation on dividends contrasted with the exemption of subsidiary to parent dividends in the 1946 UK Treaty. The revenue cost was estimated at £1.5 million, but the greater part of this was expected to fall on UK parent companies rather than on the Exchequer. At a cost of £0.25 million, royalties were to be taxed at 10% at source in contrast to the complete exemption under the 1946 UK Treaty. Interest was to be subject to 10% taxation at source which, while an improvement on the 1946 UK Treaty, represented a ‘derogation from our ideal, which is again complete exemption’. The recommendation noted, however, that the overwhelming proportion of interest received by UK residents from Australia was on Australian government securities exempt from source taxation. The recommendation was for the Chancellor of the Exchequer to refuse any special relief in the New Broken Hill situation for the present time and to wait for a further approach from Australian ministers in the expectation that it was ‘just conceivable’ that Australia might then

229 Telegram from Canberra to Commonwealth Office, Following For Brookes From Johnson, 12th April 1967, Inland Revenue file, Part II.
230 Telegram from Commonwealth Office to Canberra, For Johnson Inland Revenue Team from Brookes Inland Revenue, 12th April 1967, Inland Revenue file, Part II.
231 Telegram from Canberra to Commonwealth Office, Following For Inland Revenue (J.M. Green), 14th April 1967, Inland Revenue file, Part II.
offer something in exchange, such as a reduction in the withholding tax rate on dividends paid by Australian subsidiaries to their UK parent.\textsuperscript{232}

**New Broken Hill**

\textbf{5.143} Correspondence continued between UK officials and between UK and Australian officials on the New Broken Hill issue.\textsuperscript{233} Eventually, Cain accepted a proposal by Johnson of 4\textsuperscript{th} September 1967 and the draft of 11\textsuperscript{th} October 1967 prepared by Australia excluded dual resident companies from the 90\% New Broken Hill relief.\textsuperscript{234} Finally, on 28\textsuperscript{th} October 1967 Cain advised Johnson by telegram that, ‘subject to Government approval of agreement as a whole your proposal on N.B.H.C. is accepted’ and indicated that action was being taken to put the complete text before the Australian Cabinet.\textsuperscript{235}

**Other Matters**

\textbf{5.144} Cain’s letter to Johnson of 16\textsuperscript{th} June 1967 enclosed a revised draft treaty incorporating a total of 48 amendments proposed by Australia accompanied by notes explaining the rationale behind the amendments.\textsuperscript{236} Johnson advised Cain of the UK response to the amendments by letter on 4\textsuperscript{th} September 1967.\textsuperscript{237} Most of the Australian amendments dealt with stylistic or grammatical matters and were readily agreed to by the UK. Other amendments either dealt with issues which the countries continued to discuss through correspondence before reaching final agreement or dealt with drafting features which, although readily agreed to by the UK, were significant from an Australian perspective and had longer term effects on Australian tax treaty practice.

**Credits For Withholding Tax On Dividends Paid By Dual Resident Companies**

\textbf{5.145} It had been agreed during the negotiations in Canberra\textsuperscript{238} that where a dual resident company paid a dividend to a shareholder resident in Australia then the UK would levy withholding tax on the dividend and that Australia would levy withholding tax

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\textsuperscript{232} Memorandum, ‘PS 1152/67Mr Baldwin’, Inland Revenue file, Part II. From the content of the memorandum it is clear that this is from Inland Revenue to Treasury. From the content, the location in the file and from the context of surrounding documents it appears likely that this was the first memorandum sent by Inland Revenue to Treasury after the conclusion of the discussions in Canberra.

\textsuperscript{233} The correspondence is discussed in detail in Taylor, above n 92, 487–92.

\textsuperscript{234} Draft of 11.10.67 Articles 4 and 8, Inland Revenue file, Part II.

\textsuperscript{235} Telegram, For Johnson, Board Room, Inland Revenue, Somerset House, From Cain. 28th October 67, Inland Revenue file, Part II.

\textsuperscript{236} Cain to Johnson, 16\textsuperscript{th} June 1967, Inland Revenue file, Part II.

\textsuperscript{237} Johnson to Cain, 4\textsuperscript{th} September 1967, Inland Revenue file, Part II.

\textsuperscript{238} See the discussion at 5.128.
where a dividend was paid by a dual resident company to a UK resident. It had also been agreed that the country of the shareholder’s residence would give credit for the withholding tax. These were described as the ‘criss-cross dividend’ provisions. The UK Chief Inspector (Company Taxation) had raised technical difficulties that would be associated with the implementation of the draft article using existing UK law. Implementation problems were confirmed through subsequent legal advice. The UK Inland Revenue view was that amending relevant UK legislation was ‘presumably out of the question’ and that the Australians would have to be told that it would not be possible to gross up a dividend from a dual resident company subject to Australian withholding tax in calculating the recipient’s Schedule F tax and to then give credit for the Australian tax against the Schedule F tax. The Inland Revenue considered that, if UK Treasury agreed, giving New Broken Hill relief could be offered to the Australians on the condition that there would be no credit for Australian withholding tax on dual resident companies. Following further correspondence in which Johnson advised Cain of the impossibility under UK domestic law of giving effect to the criss-cross dividend provisions, Cain acknowledged the UK’s difficulties and agreed to a rule governing single residents whether or not New Broken Hill relief was agreed to. Cain proposed a further amendment aimed at: accommodating the situation where dividends were beneficially owned but not received by a shareholder: and overcoming difficulties associated with the undefined expression ‘residents of the first-mentioned territory’ in the case of a dual resident. This amendment was the final version of Article 8(7) and 8(8) used in the treaty. Cain commented that the UK’s amendment to the credit article had ‘proved troublesome to us’, but the conclusion had been reached that the amendments could be accepted. Johnson agreed to the proposal in a telegram to Cain dated 29th September 1967.

Trusts

5.146 Difficulties associated with accumulation trusts had been considered but not resolved during the Canberra negotiations. Cain’s letter outlined again the planning strategy that Australia had identified during the Canberra negotiations and asked Johnson...
how UK law would operate in the situation contemplated. Further internal UK discussions and correspondence between Johnson and Cain followed, which exposed differences between the Australian and UK interpretations of ‘beneficially owned’. Eventually, Cain conceded, stating: ‘In all circumstances willing to revert to original text and apply your interpretation. In event either country finds actual evidence of exploitation matter could presumably be looked at again.’ Hence the final version of the treaty contained the original text of Article 8(1).

Residence

5.147 The compromise in relation to corporate residence discussed during the negotiations had been implemented in the initialled version of the treaty. In the initialled draft, the expressions ‘resident of the UK’ and ‘resident of Australia’ were defined as having the meaning that those terms had under, in the former case, UK tax laws and in the latter under Australian tax laws. The notes explained that if these expressions were not defined in this manner, there would be difficulties when one country had to interpret the other’s ‘residence’ term. The expression ‘resident of the UK’ had no special meaning for Australia. The amendment, based on the approach taken in the 1960 Australia – NZ Treaty, overcame this difficulty by defining the expressions by reference to the domestic law of the country in which it appeared.

5.148 A related amendment added the phrase ‘being a resident of Australia’ to the definition of ‘Australian company’ in Article 3(1)(a)(i). The reason for the amendment was that, otherwise the definition of ‘Australian company’ could include a company which was not an Australian resident. The amendment meant that to be an Australian company for treaty purposes, a company had to be a resident of Australia for purposes of Australian domestic law. Cain’s explanation cited an example of a company incorporated in NZ and carrying on business there but which was centrally managed and controlled in Australia. Cain considered that, prior to the amendment the company would be an Australian company for purposes of the treaty, because it was centrally managed and controlled in Australia, but would not be an Australian resident for domestic law purposes (presumably because the Australian notes did not regard it as carrying on business in Australia). Cain considered that this would enable

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246 Cain to Johnson, 16th June 1967, Inland Revenue file, Part II. The planning strategy that Australia identified in the Canberra negotiations was discussed at 5.107.

247 Telegram, Cain to Johnson, 7th October 1967, Inland Revenue file, Part II.

248 The discussions and correspondence on this issue are discussed in detail in Taylor, above n 92, 495–6.

249 UK – Australia Double Taxation Agreement, Notes on Australian Drafting Amendments, Note on Amendment 2, Inland Revenue file, Part II (hereafter ‘Notes on Australian Drafting Amendments’).
the company to receive a reduced rate of UK tax on, say, interest while Australia would not be taxing the interest because the recipient company would not be an Australian resident for domestic law purposes.\textsuperscript{250} Although the amendment was agreed to by the UK without question, Cain’s reason for seeking it is interesting in that it was not until 2004 that the ATO released a ruling\textsuperscript{251} clearly stating that a company in a situation analogous to the example given by Cain would not be an Australian resident.

\textbf{5.149} As the definitions of ‘Australian company’ and ‘UK company’ were mutually exclusive, it was not possible for companies to be dual residents.\textsuperscript{252} These provisions meant that a company incorporated in Australia with its centre of administrative and practical management in Australia would be an Australian company and not a UK company, even if it were managed and controlled in the UK. Where a company was not incorporated in Australia, it could only be an Australian resident for treaty purposes where it was managed and controlled in Australia. Where it was managed and controlled in the UK, then it would be a UK resident for treaty purposes. Where management and control was both in Australia and the UK, the effect of the definitions was that the company was an Australian resident. Where it was managed and controlled in neither Australia nor the UK, it would be neither an Australian company nor a UK company as defined. It could still, however, be an Australian resident as ‘a person (other than a UK company) who is a resident of Australia’. Hence, in the situation where a company was not incorporated in Australia, was not managed and controlled in either Australia or the UK, but carried on business in Australia and had its voting power controlled by Australian shareholders, the company would be a resident of Australia for both Australian domestic law purposes and treaty purposes.

\textbf{5.150} Ironically, the convoluted drafting would not in all cases have dealt with the problems previously raised by Australia.\textsuperscript{253} Where the interposed company was centrally managed and controlled in the UK, and where (as might have been the case with a mere holding company) its centre of administrative or practical management was not

\begin{flushleft}
\textsuperscript{250} Cain to Johnson, 16th June 1967, Inland Revenue file, Part II and Notes on Australian Drafting Amendments, Note on Amendment 4.

\textsuperscript{251} Taxation Ruling TR 2004/15 Residence of companies not incorporated in Australia – carrying on business in Australia and central management and control.

\textsuperscript{252} In addition to the discussion in the text see R W Parsons, ‘Tax Problems Relating to a UK Business Operating In Australia’ [1968] \textit{British Tax Review} 177 at 183–4. As discussed at 2.143, dual residents were not treaty residents under the 1946 Australia – UK Tax Treaty although, as discussed at 2.149 and 2.150, that treaty did provide benefits to dual residents who received income that had been taxed in a third country.

\textsuperscript{253} See the discussion at 5.13, 5.55, 5.78 and 5.79.
\end{flushleft}
in Australia, it would be a UK company and hence a UK resident for treaty purposes. Nonetheless, as a company incorporated in Australia it would still be an Australian company for Australian domestic law purposes and hence be entitled to the s46 inter-corporate dividend rebate. Nor was the UK’s concern about the breadth of the definition of Australian resident company under Australian domestic law entirely met. Where a company was ‘a person, other than a UK company, who is a resident of Australia’, it would have been an Australian resident for both Australian domestic law and treaty purposes. It may be that the UK did not regard this situation as raising significant issues from a UK perspective given that it contemplated a company that was not managed and controlled in the UK. The definition represented a compromise from the initial positions of both countries where a company was incorporated and had its centre of administrative or practical management in Australia notwithstanding it being centrally managed and controlled in the UK. The definition represented a compromise by the UK where the central management and control of a company was divided between the UK and Australia.

5.151 Unlike the relevant provisions in the 1966 UK – NZ Treaty, the 1967 UK Treaty included an additional tie-breaker, which stated:

(3) Where by reason of the provisions of paragraph (1) of this Article a person other than an individual is both a UK resident and an Australian resident –

(a) it shall be treated solely as a UK resident if it is managed and controlled in the UK;

(b) it shall be treated as an Australian resident if it is managed and controlled in Australia.

It was not possible for a company to be a dual resident, because the terms ‘Australian company’ and ‘UK company’ were mutually exclusive. The tie-breaker was directed at entities such as trusts.

Tax On Third Country Income

5.152 Pursuant to the agreement in Canberra, Article 18 (the ‘other income’ article) had been redrafted and was confined to tax on third country income. Australia now

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254 By contrast, if the parent had directly owned shares in the Australian company conducting active business operations, the parent would not have received the s46 inter-corporate dividend rebate because only Australian resident recipient companies were entitled to the rebate. In these circumstances, the dividend would have been subject to Australian withholding tax at the treaty rate of 15%.

255 See the discussion at 5.121 to 5.123.
sought an amendment so that the article only applied to dual residents of Australia and the UK. If the provision applied to single residents, a resident of the UK (for example) could arrange to ensure that income flowing to Australia was sourced in a third country and hence subject to UK but not Australian tax. In reply, Johnson did not consider that the initialled draft was 'likely to lead to untoward results', but he had no objection to making it more precise. Johnson identified an additional problem that could arise with dual residents in connection with dividends, interest and royalties. If an individual who was a UK resident under the ordinary law but who was an Australian resident under the treaty received dividends from a company in a third country, the UK could not tax the dividend; however, if he received dividends from an Australian company (that was not a UK resident) then there was nothing in the initialled or revised Article 18 which would prevent the UK from taxing the dividend up to a rate of 15%. Johnson suggested a further amendment to Article 18 aimed at resolving this problem by extending the exemption to include income derived from sources in the other Contracting State in addition to income derived from a third country. Cain’s telegram in reply accepted the UK amendment but commented that where income had a dual source, Australia assumed that the source rule of the country to which residence was allotted would apply. In Cain’s view there were other situations where the provision could apply, such as rent from Australia derived by a dual resident whose residence the treaty allotted to Australia.

Miscellaneous

5.153 Other amendments in the Australian draft of 16th June 1967, which were either readily accepted by the UK or the UK accepted subject to modifications, affected subsequent Australian treaty practice for some years. A deemed source rule for interest and royalties was included in the credit article consequent on Australia taxing interest and royalties at source without technically requiring the relevant income to have an Australian source. Australia sought specifically to exclude from the

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256 Notes on Australian Drafting Amendments, Note on Amendment 31.
257 Johnson to Cain, 4th September 1967, Inland Revenue file, Part II. The suggested amendment to Article 18(2) was:

"Where such a person is treated for the purposes of this Agreement solely as a resident of one of the territories he shall be exempt in the other territory from tax on any income in respect of which he is subject to tax in the first-mentioned territory if the income is derived:

(a) from sources in the first-mentioned territory; or

(b) from sources outside both territories.

258 Cain to Johnson, undated copy of telegram, Inland Revenue file, Part II.
259 Cain to Johnson, 4th May 1967. Inland Revenue file, Part II had advised Johnson of the terms of the proposed changes to Australian treatment of outbound interest and royalties. Notes on Australian Drafting Amendments, Note on Amendment 38 indicated that this was to align with
operation of the industrial or commercial profits article any income taxed under Australian domestic law provisions dealing with insurance with non-residents and film business controlled abroad.\textsuperscript{260} The UK accepted this with a relatively minor drafting change.\textsuperscript{261} Other changes were proposed by Australia, but the final form was a product of further amendment by the UK. In Article 4(8) (definition of PE), Australia had proposed the deletion of the phrase ‘in the other territory’ to deal with situations like those in Case 110 (1955) 5 CTBR (NS) 656.\textsuperscript{262} The UK response proposed that ‘in the other territory’ be replaced by ‘a person in the other territory’.\textsuperscript{263} Likewise, Australia had proposed substituting ‘might be expected to accrue’ for ‘would have accrued’ in Article 7(1) to provide a more practical measure of the profits which could be taxed to an enterprise.\textsuperscript{264} A similar change was made in paragraph 4 of Article 19 dealing with credits, despite the UK’s preference for the language in the initialled text.\textsuperscript{265} The UK would have preferred that this change not be made and suggested the final wording ‘might have been expected to have accrued’, that was used in the treaty.\textsuperscript{266} The Australian redraft amended the definition of ‘royalties’ to allow for the apportionment of lump sum payments and to include any payment in respect of films or videotapes for use in connection with television, or tapes for use in connection with radio.\textsuperscript{267} The UK indicated the amendment was acceptable in principle, but considered the term ‘any payment’ too wide because it could potentially cover a payment to an airline for transporting a film. The UK’s preferred language was, ‘and
includes any payments of any kind to the extent to which they are paid as consideration for the use of, or the right to use, motion picture films, which became the phraseology used in the final version of the treaty.

Significance Of The Treaty

5.154 The 1967 UK Treaty was the first Australian treaty entered into after the publication of the 1963 draft OECD Model and was the first Australian treaty to come into force after the introduction of Australian interest and royalty withholding tax. Two major policy messages were apparent from the treaty. First, the treaty gave a clear signal on what Australia’s position was on rates of withholding tax. Despite the fact that these rates were higher than those suggested in the draft OECD Model, Australia managed to maintain them in almost all the treaties that it entered into until the 2001 Protocol to the treaty with the US. Second, the 1967 UK Treaty also signalled that Australia would not agree to the non-discrimination article, a position that Australian adhered to (with the exception of the 1982 US Treaty) until the 2003 UK Treaty.

Policy on withholding tax rates was determined at a ministerial level and was influenced by prior Australian Treaty practice and by economic and revenue considerations relevant to current and expected trade and investment flows between the two countries. Policy on the non-discrimination article also was determined at a ministerial level and was primarily influenced by Australian domestic law considerations.

5.155 The treaty continued structural features that had characterised earlier Australian treaties. It did not have an ‘other income’ article, did not have a capital gains article and defined industrial and commercial profits as excluding specified items. Instead of an ‘other income’ article, it contained an article dealing with tax on third country income that found its way into several Australian treaties up to the 1980 treaty with Canada, which was the first Australian treaty to contain a general ‘other income’ article. The policy decision to continue these structural features appears to have

268 Johnson to Cain, 4th September 1967, Inland Revenue file, Part II.

269 Article 23 of the 1982 US Treaty is a non-discrimination article, but prior to amendments in 2011 the effect of s6 of the International Tax Agreements Act 1953 was that Article 23 did not have the force of law in Australia.


272 Australia – Canada Treaty 1980, Article 21. This article applied to items of income of a resident of one of the countries which was not expressly mentioned in the earlier articles. Unlike the OECD ‘other income’ article, however, this article gave the source state a right to tax other income arising in it.
been made at the official level and reflects a belief that the absence of a general ‘other income’ article and the exclusion of specified types of income from the definition of ‘industrial and commercial profits’ meant that full source country taxing rights were maintained in relation to items of income not expressly mentioned in the Treaty. This, too, was the thinking behind the exclusion of a ‘capital gains’ article. It is clear from the negotiations that the Australians considered that omitting a capital gains article would leave Australia’s ability to tax capital gains in the future unrestricted. It is also reasonably clear from the negotiations that neither delegation considered items that ordinary concepts would characterise as capital gains to fall within the definition of ‘industrial or commercial profits’.

5.156 Past Australian treaty practice was a major factor in continuing this structure, but economic and Australian domestic law considerations also appear to have had an effect. While Australia was responsible for the exclusion of the ‘other income’ and ‘capital gains’ articles and the introduction of the ‘tax on third country income’ article, the UK draft defined industrial or commercial profits as excluding specified items.

5.157 Several features of the detailed drafting of the treaty were to find their way into subsequent Australian treaties, particularly in the period before Australia joined the OECD. Some, such as Article 4(8) dealing with the situation in Case 110 (1955) CTBR (NS) 656, were refinements or continuations of the drafting of prior Australian treaties while others, such as the way ‘resident of Australia’ was defined and the adjustments in the interest and royalty articles to accommodate the language of the new Australian withholding tax provisions, were developed as part of these negotiations. Another significant development was the broadening, consistently with Australia’s emphasis on source basis taxation, of the definition of permanent establishment. Five of the variations, initiated by Australia, from the OECD Model currently operative Australian tax treaties concerned the definition of permanent establishment. The treaty also saw a further development of the Australian treaty practice of including deemed source rules which, in this instance, were extended to items that did not necessarily have an Australian source under domestic law.

5.158 Prior Australian treaty practice, Australian domestic law considerations, prior UK treaty practice and the prior treaty practice of other countries (particularly New Zealand) appear to have been the dominant influences on the detailed drafting.

AV8, AV9, AV12, AV13 and AV14. Details are set out in Appendices 3 and 5.
Interestingly, the New Broken Hill provisions, which, apart from the non-discrimination article, were the subject of the most extensive negotiations and correspondence, were not replicated in any subsequent Australian treaty. New Broken Hill represented a then unusual situation of a UK resident company with most of its income derived from Australian sources and with a high percentage of Australian shareholders. An exact repetition of those precise circumstances was unlikely to recur. Economic considerations appear to have been dominant for both Australia and the UK in relation to the New Broken Hill issue. Some other drafting features of the treaty were never repeated in subsequent Australian treaties, with some of these being the product of unusual features of the UK draft or of particular features of UK domestic law.275

As will be seen in Chapter 6, the treaty formed the basis for the draft that Australia sent to Japan in 1968. Australia was evidently pleased with the treaty as a whole. In its first negotiation dealing with a draft influenced by the OECD Model, it managed to continue a policy of high levels of source basis taxation through the agreed rates on dividends, interest and royalties through the broad definition of permanent establishment. Saving provisions preserving the operation of particular features of Australian law were introduced or refined. Australia achieved relief from UK tax on dividends in the New Broken Hill situation, and managed to not agree to a non-discrimination article but had to concede residence taxation of shipping. The latter concession would prove to be damaging to Australia in its next tax treaty negotiations with Japan. Chapter 6 discusses the background to, the negotiation and drafting of, and the significance of the 1969 Japan Treaty. This was Australia’s first tax treaty with an Asian country and, as is argued in Chapter 6, in some respects represents the ‘high water mark’ of Australian exceptionalism.

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275 See the discussion in Taylor, above n 92, 502.
CHAPTER SIX: THE 1969 TREATY WITH JAPAN

6.1 Australia's first taxation treaties with Asian countries were with Japan and Singapore, and both were concluded in 1969. The influence of the 1967 UK Treaty (discussed in Chapter 5) can be seen in both treaties, despite there being preliminary discussions in relation to them before the 1967 UK Treaty was entered into. This chapter is confined to the negotiation and drafting of the 1969 Japan Treaty. At the time, Australia was a net capital exporter to Singapore, which was a new and developing country recovering from the effects of World War II. As a result, the 1969 Singapore Treaty contained several features (most notably a tax sparing provision) which were atypical of Australia taxation treaties in the period discussed in this thesis.

The Increasing Importance Of Japan As An Australian Trading Partner

6.2 Australia and Japan entered into an Agreement on Commerce in 1957,1 which granted Australia access to the Japanese market for raw materials but reserved the right to impose restrictions on Japanese imports that might damage Australian industries. A 1963 Protocol to that agreement removed this restriction, and contemporary comment regarded it as effectively placing Japan in an equivalent trade position in relation to Australia as the United Kingdom, Canada and New Zealand.2

6.3 By the end of the 1960s, Japan was Australia’s major export destination. In 1949–50, 4% of Australia’s total exports were to Japan, with 18.9% and 8.2% of total exports being to the UK and US respectively. By 1962–62, exports to Japan, at 16.1% of the total, had nearly drawn level with exports to the UK, at 18.7%, and had surpassed exports to the US, at 12.3% of total exports. By 1969–70, Japan was the major destination of Australian exports, at 25% of exports, dwarfing exports to the UK, at 10.9% of exports, and exports to the US, at 13.4% of exports.3 Japan increased in importance as a supplier of imports to Australia in the same period without becoming the major source. In 1949–50, 1.3% of Australia’s imports came from Japan compared with 53.1% from the UK and 9.9% from the US. By 1969–70, 12.4% of

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Australia’s imports came from Japan while 21.8% came from the UK, with 24.9% coming from the US.\(^4\)

1964 Preliminary Negotiations For A Treaty With Japan

6.4 As discussed at 4.1, Australia received a proposal for a tax treaty from Japan in 1959. Following Australian Cabinet decision 386 on 10\(^{th}\) August 1962,\(^5\) Australia took advantage of a visit by a Japanese delegation to NZ to have an exchange of information about the two countries’ tax systems in Canberra in August 1962. Following these discussions, the Australian Cabinet on 28\(^{th}\) November 1962 agreed that:

‘preliminary discussions and correspondence between officials with the Japanese should continue, without commitment on either side, with a view to defining the issues involved and the points of difference which might be likely to arise in any formal negotiation. At a later stage the Treasurer will give the Cabinet an opportunity to consider the issues involved and decide whether or not it would be desirable to enter into formal negotiations with Japan for such an agreement.’\(^6\)

Correspondence between Australian and Japanese officials continued, with the Japanese providing a draft taxation treaty to the Australians in March 1964.\(^7\) An Australian delegation of officials led by D L Canavan, Commissioner of Taxation,\(^8\) met with Japanese officials (including the Director of the Tax Bureau and the Chief of the International Tax Affairs section of the Tax Bureau) in Tokyo from 20\(^{th}\) to 30\(^{th}\) April 1964.\(^9\) The following discussion of the negotiations is based on: Canavan’s

\(^4\) Foster, above n 3, 13, Table 1.6.
\(^5\) Cabinet decision 383 was discussed at 4.52.
\(^6\) The Cabinet minute is quoted in D L Canavan (Australian Commissioner of Taxation) to The Commonwealth Treasurer (H E Holt) 27\(^{th}\) July 1964, paragraph 1 in NAA, ATO file, Pt 1, 83. Canavan was appointed as Commissioner of Taxation in January 1963 and held that position until his retirement in November 1964. Leigh Edmonds, Working for All Australians: A Brief History of the Australian Taxation Office (Australian Taxation Office, Canberra, 2010) 134.
\(^7\) Canavan, above n 6, 83, para 2. The draft, dated 28\(^{th}\) February 1964, is Annexure B to Canavan, above n 6, and is hereafter referred to as ‘the 1964 Japanese Draft’.
\(^8\) D L Canavan (Commissioner of Taxation, hereafter referred to as ‘Canavan’), Belcher (First Assistant Commissioner of Taxation), D S Craik (Assistant Secretary, Treasury), W J R Hill (Assistant Executive Officer, Taxation) accompanied by G H Clark of the Australian Embassy as an interpreter. The names of the Taxation and Treasury officials present at the discussions in Tokyo are set out in Canavan, above n 6, 60, addendum. That Clark accompanied the delegation as an interpreter is stated in ‘Double Taxation, Australia – Japan, Record of Tokyo Talks’ [hereafter ‘Record of 1964 Tokyo Talks’] in NAA, ATO file, Pt 1, 41, para 1.
\(^9\) Canavan, above n 6, 83, para 3. The full Japanese delegation is listed in Record of 1964 Tokyo Talks, 41, para 2.
report to the Treasurer; the 1964 Japanese Draft; and the Record of 1964 Tokyo Talks.

6.5 Canavan’s report noted that because of Australia’s provisions for unilateral relief from international double taxation, Australian residents did not generally require relief from international double taxation. However, as the Japanese foreign tax credit system did not extend to the 10–11% local ‘enterprise tax’, a Japanese company might, in some circumstances, need greater credit than Japanese law allowed to ensure adequate relief from double taxation, and Japanese shipowners trading with Australia could also find the present position unsatisfactory.

6.6 The Japanese draft was used as the basis for the discussions. The draft had clearly been influenced by the 1963 draft OECD Model. The Japanese draft contained three structural features which differed from the 1963 draft OECD Model but which were consistent with previous Australian treaties. These were: (a) the presence of a definition of ‘industrial or commercial profits’; (b) the absence of an ‘other income’ article; and (c) the absence of a capital gains or alienation of property article. Nonetheless, the draft contained some articles (dealing with interest and non-discrimination), derived from the 1963 draft OECD Model, which had not been in previous Australian treaties. Canavan drew the Treasurer’s attention to the features of the draft that were most likely to raise important policy issues, particularly given the Australian Cabinet decision 386 and the then Treasurer’s and Treasury view that, as a starting point, Australia should avoid making concessions on shipping profits and dividends absent compelling reasons for doing so. The features specifically identified were: (a) a residence basis of taxation for income from the operation of ships and aircraft; (b) limiting source country taxation to 10% on

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10 At the time, foreign source income (other than dividends) was exempt from Australian income tax under ITAA 1936 (Cth) s23q where it had been subject to tax in a foreign country. Australia gave a foreign tax credit under ITAA 1936 s45 for dividends received by residents sourced in non-Australian profits. No credit was given where a dividend sourced in Australian profits was paid by a foreign company to an Australian resident. The Commissioner noted that, to this extent, double taxation was imposed on Australian residents investing in Japan, but pointed out (Canavan, above n 6, 82, para 10) that this situation had not arisen in practice.

11 Canavan, above n 6, 82, para 11.
12 Canavan, above n 6, 82, para 8.
13 Canavan, above n 6, 82, para 11. Record of 1964 Tokyo Talks, 3–7 contains further details of Japanese taxes and of the Japanese system of corporate-shareholder taxation at the time.
14 Canavan, above n 6, 81, para 16 and Record of 1964 Tokyo Talks, 41, para 4.
15 See the discussion at 4.49 and 4.52.
16 Canavan, above n 6, at pp80–1, para 17.
17 Article V of the 1964 Japanese Draft.
dividends paid by a 25% or more subsidiary to a parent;\textsuperscript{18} (c) limiting source country
tax on other dividends to 15%;\textsuperscript{19} (d) limiting source country tax on interest to 10%;\textsuperscript{20}
(e) limiting source country tax on royalties to 10%;\textsuperscript{21} and (f) a non-discrimination
article.\textsuperscript{22} While Canavan’s letter discussed each article in the draft in more detail, the
discussion here is confined to Canavan’s conclusions on the preliminary
negotiations.

**Commissioner’s Conclusions On The Preliminary Negotiations**

6.7 Canavan believed there was a genuine desire on the part of Japan to conclude a
taxation treaty with Australia. Shipping and air transport, dividends, and industrial or
commercial profits were the major areas where significant issues still needed to be
resolved.

6.8 The biggest issue concerned the treatment of shipping and air transport. The draft
gave exclusive right to tax shipping and aircraft profits to the residence country of the
operator (whether owner or charterer) irrespective of the place of registration of the
ship or aircraft. Australian acceptance of a residence basis in all of its previous
treaties had only been in respect of ships and aircraft registered in the residence
country of the operator. There would be a gain to Japanese shipping companies of
£225,000 annually from tax concessions proposed in the draft. While there would be
gains to Qantas and Dominion Navigation Co. Ltd, these would not offset the
revenue loss to Australia of a treaty consistent with the draft. Canavan speculated
that the Japanese, as they had done with NZ, might agree to a 50% exemption for
shipping and air transport. In the NZ context, this meant a NZ source country tax rate
of 5% on shipping and air transport. This was the current source country rate on
shipping and air transport under Australian domestic law, but the Tokyo discussions
did not suggest that the Japanese would be satisfied with the status quo on shipping
and air transport.\textsuperscript{23}

6.9 Canavan considered that, while Japan would continue to press for a lower source
country rate on non-portfolio dividends, it might agree to a uniform rate of 15% on all
dividends paid by Australian companies to Japanese residents. The revenue cost to

\textsuperscript{18} Article VI(1) of the 1964 Japanese Draft.
\textsuperscript{19} Article VI(1) of the 1964 Japanese Draft.
\textsuperscript{20} Article VII of the 1964 Japanese Draft.
\textsuperscript{21} Article VIII of the 1964 Japanese Draft.
\textsuperscript{22} Article XVIII of the 1964 Japanese Draft.
\textsuperscript{23} Canavan, above n 6, paras 162 and 163.
Australia would at that time be small but might ‘ultimately assume large proportions’.  

### 6.10

Whether industrial or commercial profits should be taxed on an ‘attributable to’ basis, as required by the draft, or on a ‘force of attraction’ basis as adopted in the Australian draft, did not at that time involve any significant revenue problem. Canavan expressed the theoretical justification for a force of attraction basis in these terms: ‘It might be said that once an enterprise sets up a permanent establishment in a country, it should be taxed on its full income in the same manner as applies to a resident, except where a specific exemption is granted.’ While considering that the force of attraction basis was more appropriate, Canavan nonetheless suggested that Australia could concede the ‘attributable to’ basis if a matching concession were to be made by Japan.

### 6.11

Canavan made only brief concluding comments on other articles in the draft. The discussions had not significantly clarified the Japanese attitude to interest and royalties. The draft proposed a 10% limit on source taxation of interest and literary royalties, whereas Australia’s previous treaties had not restricted source taxation of interest but had taxed some royalties on a residence basis. As some changes were being considered in Australian law, the Australian delegation could not press these issues. Canavan recommended that ‘the view in relation to these classes of income may need further revision if discussions are to be resumed’. There were matters still to be resolved in relation to other classes of income, but these would not stand permanently in the way of a treaty. The use of the credit method to relieve double taxation was seen as being sound in principle, but some matters of detail would need to be resolved. Canavan opposed inclusion of a non-discrimination article, describing the need for it as not being apparent and commenting that, in practice, it would conflict with existing provisions in both Australian and Japanese law.

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24 Canavan, above n 6, para 164.
25 Canavan, above n 6, para 166. It is unclear what ‘Australian draft’ Canavan was referring to here. The 1965 Australian model discussed in Chapter 4 adopted an ‘attributable to’ rather than a ‘force of attraction’ basis. Previously, Australia had assessed likely revenue impacts of treaties with potential partners on the basis that a treaty concluded with them would follow the 1957 Canada Treaty. That treaty also used an ‘attributable to’ basis. Australia’s most recently concluded treaty at the time of Canavan’s letter was the 1960 NZ Treaty, which adopted a ‘force of attraction basis’. A ‘force of attraction’ basis had been adopted in the draft Australia sent to Canada as part of the negotiations leading to the 1957 Canada Treaty.
26 See the discussion at 2.90 and at 3.59 to 3.63 and 3.127.
27 Canavan, above n 6, para 165.
28 Canavan, above n 6, para 166.
29 Canavan, above n 6, para 168.
30 Canavan, above n 6, para 169.
6.12 The Japanese proposed to report to their government, and Canavan presumed that the Japanese government would suggest further negotiations in Canberra and considered that further detailed and extensive negotiations would be required before a treaty could be approved by the Commonwealth government. The revenue cost to Australia of a treaty consistent with the Japanese draft would be £232,500 annually but would trend upwards. Of this, £225,000 would come from the exemption for shipping and aircraft profits and £7000 would come from reductions in source country tax on dividends (the remaining £500 would come from other concessions). With a 50% reduction in source country taxation of shipping and air transport instead of a total exemption, the revenue cost would be £120,000 annually and would again trend upwards. Canavan considered that any treaty with Japan would ‘almost certainly be put forward as a pattern for agreements with other countries. In particular, countries with mercantile marine could be expected to seek in relation to shipping a concession at least as favourable as any that may be granted to Japan.’

The Decision To Commence Formal Negotiations

6.13 Following the Tokyo talks in 1964, between August 1964 and November 1965 the Australian Treasury, with limited liaison with the ATO, drafted a Cabinet submission
recommending that Australia enter into formal negotiations for a taxation treaty with Japan. The submission and a memorandum by the Acting Secretary of the Treasury\textsuperscript{35} to the then Treasurer\textsuperscript{36} recognised that in the negotiations, difficulties were likely to arise in relation to the taxation of shipping profits, dividends, interest and royalties. Consistent with Cabinet submission 305, tax treaties were clearly seen by Australian Treasury officials as being primarily concerned with preventing double taxation.\textsuperscript{37} As Australia unilaterally prevented residence source double taxation, international double taxation was not seen as a significant problem for Australia. Japan was regarded as seeking concessions that would affect Australian revenues adversely and would raise serious questions of principle.\textsuperscript{38} A summary of the main issues accompanying the submission recognised that unilateral credit provisions did not remove all international double taxation conflicts (conflicts of source rules and issues concerning the allocation of head office and branch expenses are explicitly

\textsuperscript{35} R J Randall was Acting Secretary of the Treasury at the time.

\textsuperscript{36} The Treasurer at the time was Harold Holt.

\textsuperscript{37} Cabinet Submission 305 was discussed at 4.33 to 4.51.

\textsuperscript{38} Draft ‘Confidential for Cabinet, Submission, Double Taxation Agreement – Japan/Australia’, Harold Holt, Treasurer, undated and Minute Paper by R J Randall, Acting Secretary, 10\textsuperscript{th} November 1965, ‘The Treasurer, Proposed Double Taxation Agreement – Japan/Australia’. Both documents are contained in NAA, Treasury file, Pt 2. A copy of the draft submission is also contained in NAA, ATO file, Pt 1. Randall’s Minute Paper records that the draft submission and a draft attachment setting out the main issues had been prepared in co-operation with the taxation branch.
mentioned) and that taxation treaties had an ‘assurance’ function of maintaining, for the duration of the treaty, a consistent treatment in the taxation of cross border activities by the treaty partner. Nonetheless, the document ‘Japan/Australia – The Main Issues’ observed that:

’Some countries, including Japan, view double taxation agreements also as a means of achieving a re-distribution of the taxation revenue arising from income flowing between countries which are parties to an agreement. To this end, a mutually [emphasis in the original] satisfactory allocation is sought by means of a re-arrangement of classes of income which each country is free to tax and by the restriction of the rate of tax which may be charged in the country of source of income. Such countries want Australia to reduce (or in some cases eliminate completely) its taxation on certain classes of income – and in particular on shipping profits and dividends. We are a capital importing country and dependent on foreign shipping so that the flow of dividends, interest and shipping profits from Australia to other countries greatly exceeds any inflow of these kinds of income. Consequently were we to grant these requests without obtaining something in return we would reduce our revenues by a substantial and, over the years, growing amount.’

6.14 Japan/Australia – The Main Issues recommended, and Cabinet approved, application of the 1962 policy that, generally, Australia should not make concessions on shipping profits and dividends unless ‘some clearly commensurate advantage could be negotiated for Australia’, but that the Australian concessions should not go as far as they had in Australia’s previous treaties. Commensurate advantages ‘in the taxation field’ were to be preferred, and in any case, when negotiating with a capital exporting maritime nation the onus should be on the other country to suggest an appropriate commensurate advantage. Foreign relations considerations were dismissed as

40 See the discussion at 4.49 and 4.52 of the content of the 1962 Cabinet decision.
41 Main Issues, pp3–5. Treasury and ATO officials consistently expressed the view in internal correspondence that they could see no commensurate advantages for Australia in a tax treaty with Japan having regard to the revenue losses associated with a shipping exemption and a reduced rate of source taxation on dividends. The ATO view was that Japan would not agree to a treaty which did nothing more than formalise the credit arrangements, and that unless the Australian view that no concessions would be granted was made clear to the Japanese prior to negotiations, then undesirable acrimony might result during the actual negotiations. For an example of the ATO view see M J Belcher, Second Commissioner of Taxation to M W O’Donnell Esq, First Assistant Secretary, Department of the Treasury, Canberra, ACT, 21st May 1965, NAA Treasury file, Pt 1. Examples of the Australian Treasury view can be seen in: Minute Paper to Mr Craik from E M W Visbond, 28th September 1964, NAA, Treasury file, Pt
reasons for entering into taxation treaties. Providing an incentive for foreign non-portfolio investment was no longer seen as a benefit of a taxation treaty. Rather, taxation treaties were seen as setting dangerous precedents, with the existing treaties being ‘somewhat of an embarrassment’. The concessions sought by Japan and provided in Australia’s existing taxation treaties would be attractive to countries either with maritime fleets calling at Australia or with equity investments in Australia. A treaty granting such concessions to Japan, unless commensurate benefits were secured for Australia, was regarded as making it ‘more difficult than ever to refuse similar treatment to other countries’.

6.15 Neither the draft submission nor Randall’s memorandum nor Japan/Australia – The Main Issues envisaged any commensurate advantage to Australia of a treaty with Japan. Nonetheless, the draft submission recommended that, as the Japanese still sought formal negotiations notwithstanding their awareness of Australia’s attitude, Australia should agree to the Japanese request. The draft submission recommended that the Australian negotiators should make it clear that Australia’s attitude to the concessions Japan sought had not changed since the Tokyo talks. The Japanese would have an opportunity to either offer commensurate advantages to Australia or enter into a treaty which did little more than formalise the existing unilateral provisions relieving international double taxation between Australia and Japan. Based on the Tokyo talks, it was considered that agreement would be reached on items other than the main issues in dispute, namely: shipping and aircraft profits; dividends; interest; royalties; taxes covered; and non-discrimination. The revenue cost of Australia adopting the concessions sought by the Japanese was estimated at £257,500.

6.16 The draft submission and Japan/Australia – The Main Issues recommended a hard line on all the contentious issues. Revenue cost is given overwhelming importance in these documents. Revenue cost is seen as trumping all other considerations unless they produce a commensurate (and implicitly, tangible) benefit to Australia.

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1; Minute Paper to Mr Craik from A D Ross, 18th September 1964, NAA, Treasury file, Pt 1; and Minute Paper to Mr Craik from A D Ross, 24th August 1964.

42 Japan/Australia – The Main Issues contained the observation: ‘I do not think our relations with, say, the U.K. or the U.S.A. are demonstrably better today because over ten years ago we agreed to concessions in double tax agreements which cost our revenue more and more each year.’ Main Issues, p6.

43 Main Issues, pp6–7.

44 Main Issues, p7.

45 This is particularly clearly stated in the draft submission, pp3–4. Similar points are also made in Randall’s memorandum and in Main Issues.

46 Main Issues, pp8–9; draft submission, pp2–3.
6.17 On shipping and aircraft profits, Japan/Australia — The Main Issues, after summarising the Japanese arguments for residence taxation, commented: 'None of these arguments alters the plain fact that if Australia were to grant the Japanese request it would mean an immediate loss of Australian revenue of about £250,000 per annum, a loss which would increase as shipping grows between the two countries.' Japan/Australia — The Main Issues then observed that while the Japanese shipping companies were in a loss position, residence taxation would benefit them; however, once they became profitable, it would benefit the Japanese Treasury, and commented that it was ‘difficult to see why Australian taxpayers should be called upon to subsidise the Japanese Treasury’. Although Australia had conceded a residence basis of taxation in its first four agreements (on more restrictive terms than Japan proposed), those could be distinguished because the latter three all followed a precedent set by the 1946 UK Treaty, which was entered into ‘when our special ties with the UK were extremely strong’ and replaced the arrangements under the Dominion Income Tax Relief System,\(^{47}\) which was characterised as being ‘more onerous’. Although Japan was a ‘very good customer of ours’, and although the balance of payments was in Australia’s favour, granting concessions to Japan in a taxation treaty would not, Japan/Australia — The Main Issues suggested, have a significant effect on Japan’s trading with Australia. As long as Australia’s prices were competitive and its supplies adequate, Japan would continue to buy from Australia irrespective of the existence or otherwise of a taxation treaty. Having bought from Australia, Japan would ensure that ships were available to transport the goods to Japan. The Japan — NZ Taxation Treaty, and the statements by Japanese officials on shipping profits at the Tokyo talks, raised the possibility that Japan might agree to a 50% reduction of source taxation of shipping profits, but that this should only be agreed to if Japan were to offer an acceptable direct commensurate concession.\(^{48}\) Japan/Australia — The Main Issues recommended that, irrespective of the outcome of the Japanese negotiations, Australia should renegotiate the complete exemption of shipping profits in its existing treaties, because they provided an ‘awkward precedent’ in discussions with other countries and cost Australia substantial revenue, particularly in relation to the UK.\(^{49}\)

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\(^{47}\) The Dominion Income Tax Relief System was discussed at 2.22 to 2.30.

\(^{48}\) Main Issues, pp11—14 and draft submission, p4.

\(^{49}\) Main Issues, p14.
6.18 The attitude on aircraft profits was the opposite. There, since Australia would gain a revenue benefit from adopting a residence basis, the recommendation was to accept this aspect of the Japanese proposal.\textsuperscript{1}

6.19 The response to Japan's request for a reduced rate of source country tax on non-portfolio dividends was clearly affected by political issues of economic nationalism. Rather than neutrality between different forms of business organisation being the objective, the emphasis was on encouraging local (as distinct from foreign) investment. The comment on the Japanese proposal in Japan/Australia – The Main Issues was: 'I think we might first look at this last proposition (the 10% source country rate request on non-portfolio dividends), which touches on fundamental questions of our attitude to overseas investment and local participation. I do not wish to open up this controversial question in this context. But I do not think that we could seriously contemplate giving a concession in respect of dividends paid by an Australian resident company because not less than 25 per cent of the shares are owned by a company resident in Japan. Still less could we justify such a concession on dividends paid by a wholly-owned Japanese subsidiary. I recommend strongly that in negotiations we do not accept this clause.'\textsuperscript{2}

6.20 In the case of dividends generally, despite Japanese arguments that a reduction of source country taxation on dividends to 15% would encourage investment and was consistent with both Australia's previous taxation treaties and the 1963 draft OECD Model, the view in Australia/Japan – The Main Issues was that the Japanese foreign tax credit meant that few, if any, Japanese investors were subject to double taxation. The recommendation was that Australia should not concede 15% on dividends unless the Japanese could offer something commensurate in return that would also grow in value at a similar rate to the cost of a 15% dividend rate to Australia.\textsuperscript{3} The UK and Canada had requested that Australia not levy undistributed profits tax on their companies with Australian branch profits. In those negotiations, the request had been rejected 'with vigour' and the recommendation was again to refuse to limit Australia’s taxing jurisdiction by agreeing to the similar Japanese request.\textsuperscript{4}

6.21 Hard lines were recommended in the case of interest and royalties where the Japanese had requested that source taxation be limited to 10%. Despite the Japanese argument that gross basis taxation of interest above 10% would render on-

\textsuperscript{1} Main Issues, p14.
\textsuperscript{2} Main Issues, p15 and draft submission, p4.
\textsuperscript{3} Main Issues, p16
\textsuperscript{4} Main Issues, p17.
lending uneconomic, adopting the Japanese proposal was seen as creating 'a most undesirable precedent' because Australia had not made any concessions on interest in its previous treaties. The recommendation was that Australia reject the Japanese draft interest article. On royalties, despite the similarity of the Japanese request to the royalty provisions in the 1946 UK Treaty and the OECD Model, and the Japanese argument that it was difficult to relate expenses to royalties and the unfairness of taxation of gross royalties at normal rates, Japan/Australia – The Main Issues recommended: 'I do not think we should be prepared to ... concede to them very nearly as much as we have to the UK. We should ... continue to impose tax at normal rates on net royalties derived in Australia.'

6.22 Taxes covered was one of the contentious issues in the Japanese draft. Consistent with its previous treaties, Australia wanted local and state taxes to be excluded from the scope of the treaty on the basis that it was not 'desirable from the legal or practical viewpoint' to cover the possibility of income taxes being reintroduced by the Australian States.

6.23 The final contentious issue was the inclusion of a non-discrimination article in the Japanese draft. Both Japan/Australia – The Main Issues and the draft submission recommended outright rejection of the non-discrimination article. Reservations were expressed about Australia binding itself in any way by a non-discrimination article, and its conflict with (unspecified) provisions in Australian law was pointed out.

6.24 As early as March 1965, Australia was aware that the UK might introduce changes to the manner in which it taxed companies, and this might mean that the UK would request renegotiation of the 1946 UK Treaty, which Australia was no longer satisfied with. Following correspondence and negotiations between Australian and UK officials, it was eventually agreed that the 1946 Treaty would be renegotiated in Canberra in March or April 1967. As Australian resources for negotiating taxation treaties were limited, and as Australia considered that any request for formal negotiations should come from Japan as the initiator of the previous discussions, the decision was made to negotiate a new taxation treaty with the UK first. This decision had significant consequences for the taxation treaty that Australia and Japan eventually entered into in 1969. In the 1967 UK Treaty, Australia agreed to a uniform
withholding tax rate of 15% on dividends, and to withholding tax rates of 10% on interest and royalties. Australia had also agreed to residence taxation of shipping and aircraft profits.\(^{11}\) When negotiations with Japan were resumed in 1968, the concessions Australia made in the 1967 UK Treaty meant that it was difficult for Australia to maintain the hard line adopted in the draft submission of November 1965. At the same time, by removing the exemption for dividends paid by wholly owned Australian subsidiaries of UK companies, and by not including capital gains, other income or non-discrimination articles, the 1967 UK Treaty provided the basis for an Australian argument that Japan could not expect any greater concessions than Australia had granted to the UK.

**6.25** A further Japanese request for a taxation treaty was made during a visit by the Japanese Prime Minister in early 1968. As a consequence, the then Treasurer\(^ {12}\) made a Cabinet submission that Australia should enter into tax treaty negotiations with Japan.\(^ {13}\) Treasury advice indicated that, of all the countries that were seeking to enter into taxation treaties at the time, Japan was chosen because of its importance in Australia’s trade. The Japanese had felt discriminated against by Australia not having a taxation treaty with them, and the Treasury view was that not to conclude a taxation treaty with Japan would be regarded by Japan as a discriminatory and unfriendly act.\(^ {14}\)

**6.26** McMahon’s submission to Cabinet in January 1968 indicated that Australian negotiations with Japan would be based on the ‘source’ principle. Australia expected that the Japanese would look to the 1967 UK Treaty as a guide to the sort of agreement that they could negotiate with Australia. The 1967 UK Treaty was now seen as a sound basis for the negotiation of agreements with other countries.

**6.27** The key features of the 1967 UK Treaty relevant to the negotiations with the Japanese were seen as: (a) taxation at source with a credit being given by the residence country; (b) credit for underlying tax where a corporate shareholder held a more than 10% interest in the paying company resident in the other country; (c)

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\(^ {11}\) See the discussion at 5.140.


\(^ {13}\) William McMahon (Treasurer), Cabinet Taxation Committee, Submission No. 9 ‘Double Taxation Agreement With Japan’, 25\(^ {th}\) January 1968 (hereafter ‘McMahon, 1968’), p1. A copy of the submission is contained in NAA, Prime Minister’s file.

\(^ {14}\) The Treasury advice is set out in Memorandum by the Economic Policy Branch, Prime Minister’s Department, to The Secretary, Prime Minister’s Department, ‘Double Taxation Agreement with Japan Benefits for Australia’, 1 July 1968. NAA, Prime Minister’s file, Document 52.
dividend taxation at source normally being limited to 15% except for some transactions through Permanent Establishments; (d) shipping profits from international operations to be exempted by the source country; (e) international airline profits to be exempted by the source country; (f) interest taxation at source to be limited to 10%; (g) source taxation of royalties (except mineral royalties) to be limited to 10% of the gross royalties;15 and (h) a suitable definition of PE to ensure that the source country had ample right to tax profits originating in it.16

6.28 Given the preliminary discussions, Australia expected Japan to request, as had Britain, the inclusion of a non-discrimination article in the treaty. McMahon’s submission recommended rejecting the non-discrimination article as limiting Australia’s freedom of action regarding the relative taxation treatment of residents and non-residents.17

6.29 Difficulties were anticipated in relation to the treatment of dividends and shipping profits where it was anticipated that the Japanese would adhere to the views they had expressed in the preliminary negotiations.18 Australia could not but agree to a reduction in dividend withholding tax to 15% under the proposed treaty, as this was the rate in its existing treaties. Lowering the level of ownership at which a credit for underlying tax was available would reduce the benefit to the Japanese Treasury from reductions in withholding tax. Given the imbalance of investment flows between Australia and Japan, the reduction in withholding taxes would result in a loss of revenue to Australia, although the submission anticipated that this might be offset by increased revenues resulting from increased Japanese investment in Australia. Australia anticipated that the Japanese would seek a higher level of participation as the trigger for the underlying foreign tax credit, because 25% ownership was the trigger under Japanese domestic law.

6.30 On shipping profits, the submission recognised that the Japanese would be reluctant to agree to a provision that was out of line with international practice and discriminated against them as compared with the UK and the USA. Australia would seek to retain its full taxing rights over coastal shipping.19

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15 Significant changes in the Australian taxation of royalties were contemplated, and the submission recognised that the Japanese would need to be advised of these.
18 See the discussion at 6.8 and 6.9.
When Cabinet was considering the Treasurer’s submission, the Australian Minister for Trade and Industry, John McEwen, made a written submission arguing that the treaty would be balanced in favour of Japan. McEwen considered that the treaty would be likely to promote Japanese investment in Australia at a time when investment in, and exports to, Japan were highly regulated. He was particularly concerned about the effects a treaty that favoured Japanese shipping lines would have on Australian aspirations in overseas shipping. Australian companies had seen a market opportunity for the bulk shipping of minerals from Australia to Japan, and if Japanese shipping were to be exempted from Australian tax, this would be seen as discrimination in favour of Japan and against Australian shipping with possibly adverse Australian political ramifications. On access to Japanese markets, McEwen sought a ‘private understanding’ that government to government negotiations would take place as issues arose and that Australian applications would be sympathetically treated. McEwen favoured a time limit being placed on any exemption of Japanese shipping from Australian taxation under the treaty.

Cabinet resolved that ‘it would not be prudent to introduce into the negotiations … the matters proposed by the Minister for Trade and Industry in his submission … the Minister’s proposals on these issues should be considered by Cabinet in the light of general trade and other interests … when any agreement negotiated by officials is before the Government for approval.’ Cabinet authorised the Treasurer to make arrangements for the negotiation of a treaty with Japan, with the Japanese negotiators being advised that any treaty negotiated at the official level was subject to Australian government approval and subsequent ratification by the Parliament, and that the government may wish to consider the agreement in the light of financial, shipping and trade relations between the two countries. The Cabinet Taxation Committee resolved that these conclusions and this proposed approach be subject to confirmation by Prime Minister John Gorton before negotiations commenced.

Gorton did not approve of the issues raised by McEwen being excluded from the negotiations. Rather, in Gorton’s view, the Japanese should be told during the treaty negotiations that the expectation was that Australian business would receive

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equivalent opportunities for investment in Japan as Australia accorded to Japanese business, and that an exchange of letters to this effect would be sought. Gorton’s view was that the Japanese be asked to exclude shipping from the treaty, and that if they refused, a clear indication be given that Australia would regard this as an issue of significance when considering the ratification of the treaty. While being genuinely negotiated for, these points were not to be pressed to the point of preventing agreement in principle at the official level.\textsuperscript{23} The application of this approach was to nearly derail the negotiations several times.

### The 1968 Japanese And Australian Drafts

6.34 Japan sent a draft treaty to Australia in January 1968, and Australia developed a draft treaty dated February 1968. Relevant features of the two drafts will be discussed as they are considered in the negotiations and correspondence between Australian and Japanese officials. Where relevant, the Australian draft as used in these negotiations will be contrasted with the 1965 Australian model discussed in Chapter 4.\textsuperscript{24}

### The Negotiations In Canberra, 5\textsuperscript{th} to 16\textsuperscript{th} February 1968

6.35 Negotiations were held in Canberra from 5\textsuperscript{th} to 16\textsuperscript{th} February 1968. The Australian Commissioner of Taxation, E T Cain, led the Australian delegation, and the Secretary of the Australian Treasury, Sir Richard Randall, attended the initial sessions.\textsuperscript{25} The Japanese delegation was headed by Tateo Suzuki, Counsellor, Embassy of Japan. The Japanese Ambassador to Australia, Kai, attended the initial session.\textsuperscript{26} During the negotiations, drafts prepared by each of the negotiating countries were studied and information was exchanged about each country’s taxation system. A tentative draft treaty was prepared by Australia following the negotiations. The tentative draft

\textsuperscript{23} Gorton to McMahon, 4\textsuperscript{th} February 1968, NAA, Prime Minister’s file, Document 8.

\textsuperscript{24} The Japanese draft did contain an alienation of property Article whereas the Australian draft, the 1967 Australia – UK Tax Treaty and the 1965 Australian model did not. Strangely, the record of negotiations makes no mention of the alienation of property article. Perhaps this was because, as will be seen below, the Australian draft was used as the de facto guide to the sequence of discussion. The final version of the treaty did not contain an alienation of property article.

\textsuperscript{25} Other members of the Australian delegation were: W J O’Reilly (Second Commissioner of Taxation), T P Boucher and W J Hill (from the ATO), P Daniel and A D Ross (from the Australian Treasury), A H Borthwick and P Knight (from the Department of External Affairs) and R B Hutchinson (from the Attorney-General’s Department). Australian record of negotiations (hereafter ‘Record of Negotiations’) for 5\textsuperscript{th} February 1968, p1 and attached list of participants. NAA, ATO file, Pt 1.

\textsuperscript{26} The other members of the Japanese delegation were: Takekoshi, Honda, Comi, Kito, Ikeda and Hakayama. Record of Negotiations for 5\textsuperscript{th} February 1968, p1 and attached list of participants.
reflected the current views of both delegations on the broad form that a treaty between the countries might take. It was agreed that Australia would prepare a ‘more precise’ draft for study by the Japanese delegation. The negotiations did not reach the stage at which a draft treaty could be initialled by the heads of the respective negotiations. It was agreed that further negotiations should take place, probably in Tokyo.

6.36 Eventually the delegations agreed to give parallel consideration to the drafts of both countries, with the Australian draft being the de facto guide to the sequence of discussion, and to work through them on a clause by clause basis rather than concentrating on major issues. The following discussion concentrates on issues of major dispute in the negotiations and on issues of particular relevance to the questions examined in this thesis.

The First Discussion Of Drafts On A Clause By Clause Basis

Definitions Of Australia and Japan

6.37 The definitions of ‘Australia’ in the Australian draft included the following sub-paragraph:

‘(v) any area outside the territorial limits of the Commonwealth and the said Territories in respect of which there is for the time being in force a law of the Commonwealth or of a State or part of the Commonwealth or of a Territory aforesaid dealing with the exploitation of any of the natural resources of the sea-bed and sub-soil of the continental shelf’

The Japanese were concerned that this definition of Australia might weaken Japan’s case in a fisheries dispute with Australia, which might go to the International Court of Justice. Australia was particularly concerned to preserve its taxing rights over profits.

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27 Cain had proposed that the Australian draft be adopted as a working document, but Japan argued that, as its draft was based on the draft OECD Model, and as Japan had adequate translations of the OECD phraseology, at least parallel consideration should be given to the Japanese draft. Cain agreed to refer to the Japanese draft on phraseology as far as possible, but the question of which draft should be used as a working document was not resolved. Record of Negotiations 7th February 1968 p1.

28 Record of Negotiations 4th day reports that the Japanese appeared to be regarding the Australian draft de facto as a guide to the sequence of discussion.

29 Japan proposed working through the drafts on a clause by clause basis while Cain had proposed concentrating on major issues. Record of Negotiations indicates that a clause by clause approach was tentatively agreed on.

30 An identical provision was contained in Article 2(v) of the 1967 Australia – UK Tax Treaty. No equivalent extension to the continental shelf was contained in the 1965 Australian model.
from the exploitation of offshore petroleum and natural gas resources. It was agreed, via an exchange of letters, that the application of the definition would be limited to the taxation of petroleum exploitation products. Subsequently, Ikeda tabled a draft protocol relating to the continental shelf. The Australian record of negotiations indicates that there was some informal criticism of the draft; and the Memorandum of Understanding dated 16th February identified the issue of the continental shelf as a subject of further discussion following completion of the negotiations.

Taxes Covered

6.38 The Australian draft described the Australian taxes covered as: ‘the Commonwealth income tax, including the additional tax upon the undistributed amount of distributable income of a private company’. Takekoshi asked if there were no local taxes in Australia. O’Reilly replied that, for negotiation purposes it could be taken that there was only the Commonwealth income tax. He pointed out that the States had the right to impose income tax, but to do so would break down the then existing financial arrangements between the Commonwealth and the States. The Commonwealth could not contemplate the possibility of the States imposing an income tax or of seeking to bind the States by bringing their income tax under a treaty. O’Reilly stressed the importance to Australia of preserving the right to impose undistributed profits tax, commenting that while it was very unlikely that a Japanese-owned company would ever have to pay the tax, Australia would not yield its right to impose it.

6.39 The Japanese draft had referred to the Japanese taxes covered as being: ‘the income tax and the corporation tax’. There was an exchange of technical information on: (a) the likelihood of ex Australian dividends being caught for Japanese enterprise tax; (b) the degree to which credit for foreign tax could be carried forward in time or from central Japanese taxes to local taxes; and (c) the treatment of capital gains under Japanese and Australian law. The Australian record of negotiations indicates that Japan was considering replacing the enterprise tax with a value added tax. Australia at the time did not regard capital gains as being income under ordinary concepts and usages, but did include gains from undertaking a profit-making scheme...
in assessable income. The Australian record of the negotiations for the 4th day then states: ‘The tax coverage of the Australian draft was agreed; that of the Japanese draft (after amendment) was agreed provisionally.’

Residence

6.40 The definition of ‘resident’ in the Japanese draft was identical to Article 4(1) of the draft OECD Model with the addition of ‘place of head or main office’ after ‘residence’ and before ‘place of management’.

The Japanese draft provided that dual residence of individuals be resolved by mutual agreement between the competent authorities. For corporate dual residence, it proposed, as a tie-breaker, being the place where the company had its head or main office. In the Australian draft, several definitions interacted to determine the residence of individuals and companies. These were:

‘“Australian corporation” means a company which is a resident of Australia and which does not have its head or main office in Japan.’

‘“Australian resident” means a person, other than a company, who is resident of Australia and is not resident in Japan and is an Australian corporation.’

‘“Japanese corporation” means a juridical person having its head or main office in Japan, or any organisation without juridical personality treated for the purposes of Japanese tax as such a juridical person, which is not a resident of Australia.’

‘“Japanese resident” means any individual who is a resident in Japan and is not a resident of Australia and a Japanese corporation.’

‘“resident in Japan” has the meaning which it has under the laws of Japan relating to Japanese tax.’

‘“resident of Australia” has the meaning which it has under the laws of Australia relating to Australian tax.’

The issues raised in discussion were the possibility of dual residence under Japanese and Australian law, the merits and demerits of eliminating dual residence and the possible machinery for resolving it, and the importance to Australia of

36 Record of Negotiations, 8th February 1968, p2.
37 The Australian drafting echoed, but did not replicate, Article 3 of the 1967 Australia – UK Tax Treaty. By contrast, Article III of the 1965 Australian model used an approach more like that taken in the 1946 Australia – UK Tax Treaty.
preserving taxpayers’ rights of access to the courts. Takekoshi suggested that Australia might agree to the residence provisions of the UK – Japan Treaty or those in the 1967 UK Treaty. In defining a ‘Japanese corporation’ and in excluding a company with its ‘head office in Japan’ from the definition of Australian company, the Australian draft adopted the language used in the corporate dual residence tie-breaker in the Japanese draft and would have meant that a company which was otherwise an Australian resident under the definition in ITAA 1936 (Cth) s6(1) would be a Japanese resident for treaty purposes. The Australian record of negotiations indicates that the matter was left unresolved for further negotiation at this stage.\textsuperscript{38}

\textit{Industrial Or Commercial Profits}

\textbf{6.41} When the definitions of ‘industrial or commercial profits’ were discussed, Comi questioned the Australian definition, which, consistent with earlier Australian treaties and the 1965 Australian model,\textsuperscript{39} specifically excluded items from the scope of ‘industrial or commercial profits’. Comi indicated that Japan would prefer the simpler OECD formula. O’Reilly responded by saying that simpler meant looser. Takekoshi commented that there may be some merit in the Australian technique of defining by inclusion and then exclusion, but that the current Australian wording did not properly accommodate the Japanese approach to capital gains. The Australian record of negotiations notes that it was agreed to look at the matter again after drafting changes.\textsuperscript{40}

\textit{Permanent Establishment}

\textbf{6.42} Progress was made towards agreeing provisionally on individual paragraphs of Article 3 dealing with PEs, with minor drafting changes being agreed. The Japanese requested that some provisions, probably those where the Australian definition was broader than the OECD Model,\textsuperscript{41} be removed to an exchange of letters, something

\begin{footnotesize}
\begin{enumerate}
\item Record of Negotiations, 8\textsuperscript{th} February 1968, p3.
\item See the discussions in Chapters 2, 3, 4 and 5.
\item Record of Negotiations, 8\textsuperscript{th} February 1968, p3. The definition was contained in Article 2(1)(k) of the Australian draft but differed from the definitions in Article II(1)(m) of the 1965 Australian model and Article because it did not expressly exclude contracts or obligations to provide the services of public entertainers (or athletes, in the case of the 1967 UK Treaty).
\item The definition of ‘permanent establishment’ in Article 3 of the Australian draft largely followed the definition in Article 4 of the 1967 UK Treaty. The definition differed from the definition in the Japanese draft of January 1968 in several respects. Under the Japanese definition, the minimum time period for a building site, construction, installation or assembly project to be an example of a permanent establishment was 12 months, whereas it was six months in both the Australian draft and the 1967 UK Treaty. The period had been 12 months in the 1965 Australian model. The agency permanent establishment provision in the Japanese draft used the phrase ‘in the name of’, whereas the Australian model and the 1967 Australia – UK Tax
\end{enumerate}
\end{footnotesize}
which the Australians pointed out would not have the force of law in Australia and hence would be ineffective for tax purposes. Immediately after noting this Japanese request, the record of negotiations states: ‘Mr Cain firmly told the Japanese that they could not ask of Australia more or better conditions than it had recently given to the UK. For Australia to do otherwise would cause embarrassment towards the UK and also create difficulties at the political level.’ This is a clear instance of using previous Australian treaty practice and the treaty practice of third countries and the potential sensitivities of third countries as a negotiating tactic.

*Industrial or Commercial Profits And Associated Enterprises*

6.43 Four issues dominated the discussion of the industrial or commercial profits article of the Australian draft. These were: (i) Australian taxation of film businesses controlled abroad; (ii) Australian taxation of insurance with non-residents; (iii) the application of *ITAA 1936* (Cth) s38; and (iv) paragraph 5, which gave the taxation authorities discretion to determine a price where there was insufficient information to ascertain an arm’s length price. Items (i), (ii) and (iv) had their origins in provisions contained in the 1946 UK Treaty, while item (iii) had its origin in the 1953 US Treaty. Equivalent provisions had been included in all Australian taxation treaties after the 1953 US Treaty. The Australian record of the negotiations stated: ‘Explanations were given by the Australian delegation and the possibilities of accommodation through redrafting were examined. Further consideration will be given to these matters.’ Similar Japanese objections were raised in relation to paragraph 5 of Article 5 (Associated Enterprises) to those raised in relation to Article 4(3), and similar solutions were explored.

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42 Record of Negotiations, 9th February 1968, p5.
43 Record of Negotiations, 10th February 1968, p1. Both the 1965 Australian model and the 1967 UK Treaty contained all these features.
44 Record of Negotiations, 10th February 1968, p1.
During discussion of the dividends article, Takekoshi argued that in order to give equivalent treatment to foreign investment through branches and subsidiaries, the rate of withholding tax on dividends paid by a subsidiary should be reduced. Comi argued that, as Australian tax considerably exceeded Japanese tax, Australia should reduce its rate of withholding tax on dividends as much as possible to avoid an overspill of Japanese foreign tax credits. The Australian response was that, alternatively, Japan could allow Australian corporate tax as a credit against Japanese enterprise tax. No conclusion on these issues was reached on the sixth day of negotiations.

When discussion of the dividend and associated articles continued, the Japanese sought to have Japanese close companies exempted from Australian undistributed profits tax. The Australians' response was extremely negative, indicating that they would not so much as initial a draft providing for such an exemption. The Australian record of the negotiations observes that there was considerable discussion of the significance of, and the necessity for, the concept of 'beneficial ownership' in the Australian draft. While the Japanese agreed with the concept in principle, both parties undertook to re-examine the drafting of the expression.

The Japanese draft contained a definition of 'interest' similar to that in the 1963 draft OECD Model, but after the phrase 'debt claims of every kind' and before the phrase 'as well as all other income' inserted the following words: 'and any excess of the amount repaid in respect of such debt-claims over the amount lent'. The Australian draft, by contrast, did not define 'interest'. In discussion of the interest article, the Australians commented that the Japanese definition was 'lengthy and prolix' and that it was better to leave the meaning of interest to the practice in the legal system of each treaty partner country. Then the Australians pointed out that the 'definitional clutter' in the Japanese draft could be dispensed with if the 'other income' article in the Japanese draft were omitted. The Australian thinking here would appear to be that less detailed definitions were required in the absence of an 'other income' article

As noted in Chapter 4, the 1965 Australian model did not include provisions reducing source taxation of dividends. Article 7 of the Australian draft contemplated, but did not specify the extent of, uniform reductions in source taxation of dividends An overall upper limit of source taxation of 15% had been specified in the 1967 UK Treaty.

Record of Negotiations, 10th February 1968, p2.

Record of Negotiations, 12th February 1968, p1.
because, in those circumstances, each country would retain full source country
taxing rights in relation to categories of income not fitting within defined terms. If this
were the argument, it does appear to have great logical force; however, it has to be
seen in the context of a discussion in which the Australians had just referred to
provisions in the Japanese draft as ‘definitional clutter’. Consistent with prior
Australian practice, the Australians then indicated that Australia was opposed to the
‘other income’ article because it was inconsistent with the Australian view that the
source country, as a matter of principle, had the initial right to tax.48

6.47 The Australian draft did not contain a source rule in relation to interest.49 The source
rule in the Japanese draft corresponded with paragraph 5 of Article 11 of the 1963
draft OECD Model. The Japanese questioned the absence of a source rule from the
Australian draft. The Australian record of negotiations notes that the Australians
argued that it was best to leave the determination of source to domestic law, pointing
to the possible static effect of including a rule in the treaty and arguing that each side
should be free to vary its source rules in accordance with general policy
considerations. The Japanese then pointed out the desirability of freezing source
rules in order to limit the liability of the residence country to give credit. The
Australians then indicated that Australia might be willing to agree to limit credit
obligations to the source rules at the time, provided the government was made aware
that if domestic source rules changed, it would be complicating the situation and
risking the imposition of double taxation.50

Royalties

6.48 When Article 9 dealing with royalties was discussed, the delegations agreed that
there was no substantial difference between the definitions of royalty proposed by
each side. Australia at the time still taxed royalties paid to non-residents on an
assessment basis.51 O'Reilly explained contemplated changes to Australian taxation
of royalties paid to non-residents, which would nonetheless continue to be taxed on a
net basis. Comi suggested that a 10% rate was the ideal. The Australian draft set the

48 Record of Negotiations, 12th February 1968, p1. The 1967 UK Treaty had been the first to
contain an interest article. Article 8 in the Australian draft (dealing with interest) was identical
to paragraphs (1), (2), (3) and (6) of Article 9 of the 1967 UK Treaty.
49 The 1965 Australian model did not contain a source rule for interest. As discussed at 5.128,
source rules for interest were inserted in the 1967 UK Treaty to resolve conflicts between the
UK and Australian law on the source of interest and royalties to enable credit to be given for
tax deducted from ‘criss-cross’ dividends paid by dual resident companies. It appears that
Australia considered that providing a source rule for interest was only necessary where
specific conflicts and problems were identified.
50 Record of Negotiations, 12th February 1968, pp2–3.
51 See the discussion at 2.17.
maximum rate of source country tax on royalties at 20%.\textsuperscript{52} Notwithstanding that McMahon’s Cabinet submission of January 1968 had indicated that the government would agree to a 10% rate on interest,\textsuperscript{53} O’Reilly replied by noting that 20% was the rate in Japanese domestic law and indicating that this would seem to be an appropriate level; he pointed out that Japan would not be giving anything away and that Australia would be reducing from as high a level as 42.5%. The difficulty for Australia at this point was that in the 1967 UK Treaty, it had agreed to a 10% rate on royalties.\textsuperscript{54} O’Reilly explained that this had represented an increase in source basis taxation, because under the 1946 UK Treaty, royalties had been taxed on a residence basis. This was somewhat misleading, because under the 1946 UK Treaty, Australia taxed mineral royalties on a source basis.\textsuperscript{55} Takekoshi, referring to the question of precedents, then commented that if the rate of tax on royalties were not reduced, his government might be unwilling to continue with the agreement. At this point, the Australian record of negotiations notes that the question of rates was left for further discussion.\textsuperscript{56}

\textit{Other Income}

6.49 The Australians reiterated their objections to the ‘other income’ article in the Japanese draft, and suggested that it would be inappropriate to discuss the article further until the other articles had been settled.\textsuperscript{57}

\textit{Credits}

6.50 When the credit article was discussed, the Japanese questioned why the article did not refer to Australia providing exemption. The Australians explained that it was not necessary to refer to the exemption in the credit article where income was exempt under Australian domestic law.\textsuperscript{58} The Japanese commented on the absence of a credit for Japanese underlying tax. The record of negotiations notes that ‘the lack of

\textsuperscript{52} Paragraphs 1 and 2 of Article 9 of the Australian draft. The 1965 Australian model did not contain provisions setting a maximum rate for source taxation of royalties, and the 1967 Australia – UK Tax Treaty had set a maximum source country rate on royalties of 10%.
\textsuperscript{53} See the discussion at 6.27.
\textsuperscript{54} See the discussion at 5.100 and 5.113.
\textsuperscript{55} See the discussion at 2.90.
\textsuperscript{56} Record of Negotiations, 12\textsuperscript{th} February 1968, pp4–5.
\textsuperscript{57} Record of Negotiations, 13\textsuperscript{th} February 1968, p3. Neither the Australian draft nor the 1965 Australian model contained an ‘other income’ article. As discussed at 5.121 to 5.123, Australia had successfully argued for it to be modified so that it only applied to tax on third country income and became Article 18 of that treaty. No equivalent to Article 18 of the 1967 Australia – UK Tax Treaty was contained in the Australian draft.
\textsuperscript{58} The Australian domestic law treatment of foreign source income was as described at 5.7.
need for this was also explained. Presumably, the Australian reasoning here corresponded to the explanation that Australia had provided in negotiating the 1967 UK Treaty.

6.51 Comi then disputed the 10% holding test for Japan allowing credit for Australian underlying tax, and pointed out that Japan had never agreed to this in any of its previous agreements. Cain responded by saying that he had ‘very firm’ instructions for a 10% test and that for Australia this had equivalent significance as the shipping issue had for Japan. The 10% holding test would encourage Japanese investment in Australia, but on a scale that would not require effective control of the Australian enterprise in question and would ensure that the benefit of reducing Australia’s withholding tax on dividends was received by Japanese investors rather than the Japanese Treasury. Takekoshi indicated that Australia’s views had been noted and that he would come back to the issue after consulting his colleagues.

Identification Of Areas Of Dispute

6.52 Following the initial discussion, and a comparison of differences between the Australian and Japanese positions, the delegations considered that there was agreement, in principle, on all but the following:

- dual residence;
- industrial or commercial profits;
- shipping profits;
- the rate of withholding tax on dividends paid by a subsidiary;
- the rate of withholding tax on royalties;
- credit for underlying tax; and
- non-discrimination.

Further discussion of the disputed points then took place.

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59 Record of Negotiations, 13th February 1968, pp3.
60 See the discussion at 5.37, 5.73 and 5.124 to 5.128.
61 Record of Negotiations, 13th February 1968, pp3–4. The 1965 Australian model did not provide for credits for underlying corporate tax. As discussed at 5.125 to 5.129, in negotiating the 1967 Australia – UK Tax Treaty Australia had initially argued for a minimum shareholding percentage of 5% for credits for underlying corporate tax, but had agreed to a 10% minimum shareholding in accordance with the UK draft of September 1966.
62 Record of Negotiations, 14th February 1968, pp1–2.
Further Discussion Of Disputed Issues

Non-Discrimination

6.53 On 14th February 1968, O'Reilly explained why Australia did not want a non-discrimination clause. (O'Reilly's reasons are not stated, but presumably they corresponded with those raised in Canavan's report, in Japan/Australia – The Main Issues and the draft submission, and in McMahon’s Cabinet submission.) O'Reilly pointed out the inconsistencies of the clause as drafted, but the record of negotiations does not specify what the inconsistencies were thought to be. Cain referred to the failure of the UK to have a non-discrimination clause included in its 1967 UK Treaty. O'Reilly said that from Australia's viewpoint, the clause was not negotiable and could not even be weighed in the overall balance of concession and counter concession. Takekoshi then said that he would return to the point subsequently.

Shipping

6.54 The shipping article was a major point of disagreement between the two delegations. Australian domestic law taxed shipping on an arbitrary basis while Japan, consistently with international practice, wanted shipping taxed on an entirely residence basis. The Australians at this point in the negotiations saw conceding a residence basis on shipping as a means of obtaining concessions on other articles. The issue was complicated by the intervention of the Department of Trade and its Minister, John McEwen, and the Prime Minister, John Gorton, seeking separate discussions on allowing greater Australian investment in Japan and shipping to Japan.

6.55 The record of negotiations for 14th February 1968 shows Cain trying to distinguish the concession of shipping on a residence basis in the 1967 UK Treaty, but does not state the basis on which the distinction was made. Cain stated that for Australia to make a concession on shipping, the price in the tax treaty talks (as distinct from the separate ‘political talks’) must be very high because Australia regarded a concession.

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63 See the discussion at 6.13.
64 See the discussion at 6.23.
65 See the discussion at 6.28.
66 As discussed at 5.129 to 5.140, after prolonged negotiations and in response to offsetting concessions the UK had agreed to exclude a non-discrimination article from the 1967 Australia – UK Tax Treaty.
67 Record of Negotiations, 14th February 1968, p2.
68 See the discussion at 5.26 and at 2.14.
69 See the discussion at 6.31 to 6.33.
on shipping as 'tipping the scale of comparative advantages against it in a way which could not be redressed'. When asked what Australia wanted in exchange for a shipping concession, Cain replied that Australia would be prepared to talk on royalties and dual residence but would want a 10% test for underlying tax credit and a uniform flat rate for withholding tax on dividends. The absence of a non-discrimination article would not be acceptable as a balancing item.

6.56 Takekoshi replied that Japan regarded the separate 'political talks' on Australia's shipping and investment interests as being the price for a shipping exemption in the taxation treaty. He described the political issues as 'hanging like a spectre' over the tax treaty talks. As long as this was the case, Japan would insist on full exemption on shipping. But for the political issues, Japan considered that there could be scope for discussion on the shipping exemption. Takekoshi indicated that he would like to have the shipping article set aside from the rest of the agreement and not taken into account in balancing other provisions in the agreement. If Japan did not meet Australia's wishes on the political issues, then the situation would change and the shipping article could be reintroduced into the tax treaty negotiations.

6.57 Cain's reaction was that following Takekoshi's proposition would effectively mean the end of the talks. Both sides wanted to have an in principle document produced by 16th February for consideration by ministers, who might then wish to take other factors into account. In Cain's view, extraneous (clearly a reference to the 'political issues') matters should be looked at after completion of the agreement, not during its negotiation. Cain indicated that Australia wanted an agreement to emerge from the discussions which approximated, as far as possible, its agreement with the UK.

6.58 Cain suggested a compromise under which a shipping exemption would be put in the draft as part of what Japan required and that consideration could then be given to clauses that might be put in as part of what Australia required. Takekoshi agreed, but opened up wider issues for discussion by pointing out that the Japanese had already made concessions on the basis that the shipping question would be decided in Japan's favour. Cain questioned whether any of Japan's concessions were of any substance. When Comi pointed to changes in the definition of PE, Cain replied that Australia already had the definition in its amended form in the 1967 UK Treaty and, as the initiator of the talks, Japan could not seek to obtain more from its treaty with

70 Record of Negotiations, 14th February 1968.
71 Record of Negotiations, 14th February 1968.
72 Record of Negotiations, 14th February 1968.
73 Although not explicitly stated, it appears from the context that Mr Takekoshi was referring to the shipping profits article in the treaty being decided in Japan's favour.
Australia than the UK had. O’Reilly added that the present state of Australian law had not prevented Japanese investment into Australia, and that there were radically divided views in Australian politics as to the extent to which foreign investment should be encouraged.74

**Final Offsetting Concessions In The Negotiations**

6.59 Cain summarised the result of this tortuous discussion of 14th February 1968, stating that: (a) a shipping clause based on the Japanese model would be inserted in the draft; (b) Australia would ask Japan to change its attitude on levels of ownership for foreign underlying tax credits and on the rate of withholding tax on dividends paid to a subsidiary; (c) Australia would agree to talk on dual residence and royalties; and (d) if agreement was possible on these, a draft might be produced. Otherwise Australia would not agree to the Japanese clause on shipping, and that and associated issues of disagreement would have to be the subject of a joint memorandum of understanding setting out the points of difference. Takekoshi concurred with this summary and plan for further discussions.75

6.60 Both sides used the dispute over shipping as a bargaining point in relation to other aspects of the treaty. The session on the ninth day of negotiations closed with Takekoshi indicating that he was inclined to adopt the Australian position on dual residence but required clarification of technicalities. O’Reilly indicated that, in view of the inclusion of the Japanese version of the shipping article, Australia would tentatively propose a uniform rate of 15% on dividend withholding tax and would continue to propose a 20% rate on royalties.76

6.61 Australia tabled a redraft on 15th February which took into account all points agreed on the previous day.77 Discussions continued on 15th and 16th February, with agreement eventually being reached on 16th February through a series of matching concessions. On 15th February, Takekoshi indicated acceptance of Australia’s
position on dual residence and the residence of a payer of a dividend. Cain then observed that this meant that the areas of disagreement were shipping, dividends, credits for underlying tax, and royalties, with shipping outweighing all the other points at issue. For Australia to agree to a shipping exemption, it would be necessary for Japan to agree with Australia’s position on the other points.\(^{78}\)

6.62 Cain, clearly keen to obtain agreement on a draft treaty, pointed out that if Japan as a result of the ‘political talks’ found itself with an over-burdensome commitment, it would be free to withdraw its conditional concurrence from the various provisions of the draft treaty.\(^{79}\)

6.63 Discussion then shifted to the threshold for credits for underlying tax. Comi reiterated that Japan had never used a threshold as low as the 10% threshold that Australia sought. He then offered a ‘tax sparing’ or ‘matching credit’ system for withholding tax on dividends. Under this approach, if Australian tax on dividends were reduced to 15%, Japan would continue to give a foreign tax credit (applying to all shareholders, not just corporate shareholders) for Australian tax of 30%. In addition, full credit for Australian underlying corporate tax would be given to corporate shareholders meeting the 25% ownership test in Japanese domestic law. The Australians rejected this offer, concluding that some of the benefit from Australia reducing its rate of withholding tax would flow to the Japanese Treasury and that there would still be some incentive for Japanese firms to acquire controlling interests in Australian enterprises. It is not entirely clear that these points were made to the Japanese at this time.\(^{80}\)

6.64 When source taxation of royalties was discussed, Comi indicated that Japan would extend the ‘tax sparing’ or ‘matching credit’ offer to royalties if Australia reduced its rate of source country tax on royalties to 10%. The Australians indicated that this was unacceptable. They indicated that if Japan would agree to Australia’s proposals for underlying tax credits, Australia would reduce its source country tax on royalties to 10%,\(^{81}\) but that if Japan did not agree to those proposals, Australia would revert to 20% on royalties.\(^{82}\)

6.65 The Australian position on royalties appears to have been a critical negotiating tactic, as Takekoshi then indicated his delegation’s in principle agreement to the Australian

\(^{78}\) Record of Negotiations, 15th February 1968, p1.
\(^{79}\) Record of Negotiations, 15th February 1968, p2.
\(^{80}\) Record of Negotiations, 15th February 1968, pp2–3.
\(^{81}\) The initial offer was 15%, but Record of Negotiations indicates that ‘this was later dropped to 10%’.\(^{82}\)
\(^{82}\) Record of Negotiations, 15th February 1968, p3.
proposal on credits for foreign underlying tax. As this would be the first time Japan had agreed to a 10% threshold, he wished to obtain confirmation from Tokyo; he noted that if approval were not forthcoming, the whole position would be thrown open again. O'Reilly then invited Takekoshi to point out to his government that in the draft, Australia would be making 'notable concessions' on shipping and on the rate of withholding on royalties and dividends.83

6.66 The shipping and aircraft profits article was considered on 15th February, and substantial redrafting was done.84 O'Reilly was concerned that the absence of a definition of coastal shipping in the 1967 UK Treaty made that agreement deficient in a way that he did not want to see repeated in the treaty with Japan.85 The definition of coastal shipping was discussed subsequently, but the issue was not resolved by the end of the negotiations and was left pending86 on the basis that: the principles of the draft Australian agreement Article 6(1) and (4) were accepted by Japan; that Japan would consider the exemption of Australian shipping from Japanese enterprise tax;87 and that Australia would give further consideration to the treatment of bare boat charter monies.88

6.67 On 16th February, Takekoshi indicated that he had received advice from Tokyo that the Japanese government had agreed to a 10% level for the ownership test for indirect credits for Australian corporate tax, provided Australia gave a full exemption

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83 Record of Negotiations, 15th February 1968, p3. As noted at 6.27, agreeing to source taxation of royalties at a rate of 10% had previously been contemplated in McMahon’s Cabinet submission. Hence, agreeing to a 10% rate was hardly a significant concession, but originally asking for a 20% rate clearly appears to have been a negotiating tactic.

84 Record of Negotiations, 15th February 1968, p3.

85 The relevant definition in the 1967 Australia – UK Tax Treaty was in Article 6(1), which read: (1) A resident of one of the territories shall be exempt from tax in the other territory on profits from the operation of ships or aircraft, other than profits from voyages or operations of ships or aircraft confined solely to places in the other territory, voyages of ships or aircraft between a place in Australia and a place in the Territory of Papua or the Territory of New Guinea being treated as voyages between places within Australia. A draft version of the Australia – Japan Tax Treaty dated 16th February includes a handwritten note indicating that the definition of 'coastal shipping is to be removed to the Protocol'.

86 Record of Negotiations, 16th February 1968, p2.

87 O'Reilly had raised the question of whether Japanese enterprise tax would be levied on Australian shipping engaged in international traffic through Japan. The Japanese reply was that this would only occur if the Australian shipper had a permanent establishment in Japan. O'Reilly pressed for exemption in these circumstances on the basis of adverse political reaction if Japanese enterprise tax were to apply to Australian ships. Record of Negotiations, 16th February 1968, pp1–2.

88 The Japanese had indicated that they would agree to Article 6(4) if Australia would agree to treat a charter fee paid by an Australian skipper to a Japanese company under a bare boat charter either as income from international operations or as a royalty. Record of Negotiations, 16th February, 1968, p1.
of Japanese shipping from Australian tax. The delegations then drafted a press statement and a memorandum of understanding, which was initialled.\footnote{Record of Negotiations, 16\textsuperscript{th} February 1968, pp2–3. The Record of Negotiations actually refers to ‘withholding tax’; however, as it appears that the final rate of dividend withholding tax of 15\% had been previously agreed, and as the minimum shareholding for an indirect credit at 10\% was an offsetting concession against Australia agreeing to a residence basis for shipping, it is likely that the Record of Negotiations here meant to refer to the minimum shareholding requirement for the credit for underlying tax. The memorandum is contained in NAA, ATO file, Pt 2.}

\textbf{The 16\textsuperscript{th} February 1968 Memorandum Of Understanding}

6.68 A memorandum of understanding\footnote{The memorandum is contained in NAA, ATO file, Pt 2.} indicated that the tentative draft prepared on 16\textsuperscript{th} February 1968 was intended to reflect the present views of the delegations as to the broad form that a treaty between Australia and Japan might take. Both sides agreed that further discussions should take place at a time to be arranged and probably in Tokyo. The stage at which a draft treaty could be initialled by the heads of the delegations had not been reached. Both sides appreciated that the preliminary draft was subject, in all respects, to the consideration of their respective governments, and that either government might wish to alter, add to or delete any item in the draft after taking into account any matter which it considered relevant or appropriate. It was agreed that Australia would prepare a more precise draft, still on a tentative basis, as soon as possible and would forward it to Japan for study by the Japanese.

6.69 The memorandum commented that:

- The provisions of Article 6 of the draft were agreed in principle on the understanding that: (a) Japan would give favourable consideration to exempting Australian ships from Japanese enterprise tax; and (b) Australia would give consideration to either exempting from Australian tax consideration received by a Japanese shipowner for a bare boat charter of a Japanese ship to an Australian interest for use in operations on the Australian coast, or treating that consideration as a royalty payment.

- The question was discussed of whether the definition of ‘Australia’ for the purposes of the treaty could be extended so that it included the areas of continental shelf specified in Australian legislation relating to exploitation of petroleum. Australia sought a provision similar to the one contained in its 1967 UK Treaty as applied to activities (including shipping) concerned with petroleum search and extraction.\footnote{Article 2(1)(c) of the 1967 Australia – UK Tax Treaty defined ‘Australia’ as including: ‘any area outside the territorial limits of the Commonwealth and the said Territories in respect of which there is for the time being in force a law of the Commonwealth or of a State or part of the}
of this kind was not appropriate given present Japanese policy on the continental shelf. The Japanese indicated, however, that, once the Australian taxation policy on the continental shelf was clarified, an appropriate protocol could be entered into on the exploitation of petroleum from the continental shelf.

The Commissioner Of Taxation's Report To The Treasurer On The Negotiations In Canberra

6.70 Cain wrote to McMahon on 23rd February 1968, reporting on the stage reached in the negotiations with Japan and seeking approval to resume discussions aimed at producing a final draft treaty for government.92 Randall had kept McMahon informed on the parallel discussions with the Japanese on ‘non-taxation’ matters raised by McEwen. Cain commented that ‘something like three full days’ of negotiations had been lost while the Japanese considered their position on the ‘non-taxation’ matters and the parallel discussions were arranged. Despite these setbacks, Cain reported that substantial agreement in principle had been reached by the final day of negotiations and that the Australian side had produced a preliminary draft reflecting the extent of the agreement.93

6.71 Cain considered that the preliminary draft accorded in all respects with the objectives set by Cabinet, and was quite satisfactory from the Australian viewpoint.94 The articles in the draft dealing with permanent establishment, dividends, interest and royalties corresponded with those in the 1967 UK Treaty. In the negotiations, the Japanese had abandoned their request that a lower rate of withholding tax be applied to dividends paid to a company owning 25% or more of the paying company. The Japanese had agreed to recognise the new Australian source rules for interest and royalties and ‘to resolve to our advantage other difficulties of a substantial kind we would have otherwise encountered as to source of income’. The credit article had involved the important matter of ensuring that reductions in tax under the treaty went to Japanese companies rather than to the Japanese Treasury, and that no particular
Incentive was given to Japanese companies to obtain 25% or more of the shares in an Australian company. This would be achieved with Japan allowing a credit for Australian underlying tax where the Japanese investor held 10% or more of any Australian company. Japan had not agreed to this in any of its other 16 treaties, where it had always used 25% ownership as the threshold for indirect credits. Australia had also succeeded in persuading Japan to delete the non-discrimination article.  

6.72 The area where Australia had not achieved its initial negotiating objective, but one in which Cabinet gave the officials the option to make concessions, was the treatment of shipping profits. Cain reported that the Australian case for retaining its present taxing rights on Japanese shipping was ‘put most forcefully’. In Cain’s view, the principal difficulty Australia faced in retaining its rights in a diminished scale (namely, a reduction of Australian tax by one half) was that there would be ‘obvious and substantial discrimination by Australia against their (Japanese) shipowners as compared with competing shipowners in the UK or the US’.  

6.73 Cain explicitly states that it was decided on Australia’s part to ‘bargain the exemption of Japanese international shipping against other matters important to Australia’, and specifically mentions the concession by the Japanese of allowing a credit for underlying tax on more generous terms. Cain points out that Japan ‘made it quite clear that its eventual concession on credit for “underlying tax” followed from the Australian acceptance of exclusive residence based taxation of shipping profits’. Cain considered that other Japanese concessions were no doubt influenced by this concession.  

6.74 On taxation of shipping between Australian ports, Australia had held out strongly for the right to tax such shipping even in the course of an international voyage, which would mean that Australia had wider rights than under the 1967 UK Treaty. While the Japanese had accepted the Australian proposal in principle, they had also put forward for Australia’s consideration a proposal on bare boat charters. Cain indicated that he had commissioned research to see if Australia could meet this request without foregoing revenue it might otherwise receive.  

95 Cain to McMahon, 23/2/68, pp1–2, para 4.  
96 Cain to McMahon, 23/2/68, p3, para 6.  
97 Cain to McMahon, 23/2/68, p3, para 7.  
98 This variation is not made clear in the Notes of Meetings discussed earlier in this chapter. The changes are reflected in the draft of the treaty dated 10th May 1968 discussed at 6.87.  
99 Cain to McMahon, 23/2/68, p3, para 8.
6.75 Cain concluded by advising that the preliminary draft would need revision on both sides as to technical adequacy, and that shipping and some other issues were not fully resolved. There would be a need for further discussions, and Cain suggested that they take place in late April in Tokyo. While Cain was confident that further discussions would ‘quickly result in a final document being ready for governmental consideration’, he considered that until the issues raised by McEwen were resolved, he could not produce anything other than a document which represented agreement at an official level on the form that a taxation treaty between the countries might take. Japan, in Cain’s view, would want to weigh any concessions they made in the taxation treaty against those they made outside it. Despite this, Cain advised that, in view of Gorton’s direction that agreement in principle on a taxation treaty should be reached, a document of the type he had just described should be produced as soon as possible. Cain sought approval to resume discussions at the earliest time convenient to both sides.

6.76 After receiving Cain’s letter, McMahon evidently asked what the issues were that were not fully resolved, and also raised questions in relation to the continental shelf. O’Reilly replied on 17th February 1968 explaining that, apart from the shipping questions and the continental shelf, the other matters were mainly drafting problems. O’Reilly further explained that as Australian policy on the continental shelf had not been finalised, Japan was reluctant to go so far as recognising the continental shelf as part of Australia for purposes of the treaty. It had been agreed that once Australian policy on the issue was settled, it would be dealt with in an appropriate protocol to the treaty that would recognise Australia’s taxing rights to income through exploitation of the continental shelf. As no reciprocity from Australia was involved, O’Reilly considered that a protocol was the appropriate technical means of dealing with the issue.

6.77 McMahon then wrote to Gorton (with copies to McEwen and to the Minister for External Affairs) on 11th March advising of the progress of discussions. McMahon’s letter largely repeats the points made in Cain’s letter to McMahon. McMahon recommended that there be further discussions in Tokyo but that before these took place, that the matter go to Cabinet to consider the preliminary draft and the

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100 Cain to McMahon, 23/2/68, p4, para 10.
101 See the discussion at 6.33.
102 Cain to McMahon, 23/2/68, p4, para 11.
104 The Minister for External Affairs at the time was Paul Hasluck.
105 Discussed at 6.70 to 6.75.
discussions on the 'non-taxation' matters so that Australian officials could proceed to complete the draft for submission to, and ratification by, governments.\footnote{An undated copy of the letter McMahon to Gorton is in NAA, Treasury file, Pt 9. This same file also contains Ainsley Gatto, Private Secretary to the Prime Minister to Private Secretary to the Treasurer, 13th March 1968, which confirms that the date of McMahon’s letter was 11th March 1968. Documents in the Treasury file indicate that McMahon’s letter was drafted by Treasury on 8th March 1968.}

The Australian Draft Of 10th May 1968 And The Australian Commentary On The Draft

6.78 Australia produced a revised draft and protocol dated 10th May 1968, and forwarded it and a commentary on it to the Japanese.\footnote{Both the draft of 10th May 1968 and the Australian commentary (hereafter referred to as ‘Commentary’) on the draft are contained in NAA, ATO file, Pt 2.} The following paragraphs will discuss the more significant changes made in the Australian draft and protocol, and the Australian commentary on them. The Australian commentary refers to changes suggested by Japanese authorities. The author has not been able definitively to identify a document in the National Archives of Australia that sets out the changes suggested by the Japanese delegation.

Industrial Or Commercial Profits

6.79 Several changes were made to Article 4 dealing with industrial or commercial profits. Two changes were made to Article 4(3) to make it clear that only expenses of the particular enterprise qualified for deduction in calculating the industrial or commercial profits of the enterprise.\footnote{Commentary on Article 4(3).}

6.80 A further change was the deletion of Article 4(5) of the 14th February 1965 draft. That paragraph was aimed at allowing Australia to continue to apply \textit{ITAA 1936} (Cth) ss38–43 in calculating the profits of a permanent establishment where goods were manufactured out of Australia and subsequently imported into Australia and sold by the manufacturer in Australia either before or after importation. The Australian commentary stated that Australia agreed to the deletion of the paragraph and an appropriate provision would be inserted in the protocol.\footnote{Commentary on Article 4(5) previously paragraph (4), p2.}

6.81 A significant change was that the word ‘profits’ was substituted for the phrase ‘income (other than capital gains)’ in Article 4(7). The Australian commentary indicates that the clear basis for this substitution was to avoid the implication that capital gains would otherwise be considered income. This is clear from the following statement in the Australian commentary:
‘Australia is not happy with the expression “income (other than capital gains)”. It carries the implication – embarrassing in the Australian political arena – that income either includes, or could come in the future to include, capital gains. We would be content merely to substitute the word “income”. However, we understand that that word alone would, from your standpoint, include capital gains and you do not wish capital gains to fall under the business profits provisions. We have accordingly substituted the word “profits” in the hope it will prove acceptable to you. It presents no problems for us.”

6.82 Alterations were made to Article 4 in relation to royalties in a way that was intended to be consistent with the then Australian view of source country taxing rights in relation to items not specifically dealt with in a taxation treaty. The draft of 14th February 1965 had simply excluded ‘royalties’. The alteration excluded ‘royalties (including those payments which come within the meaning of ‘royalties’ for the purposes of Article 9)’. The definition of ‘royalties’ in Article 9 of the draft of 10th May 1965 excluded ‘royalties and other payments in respect of the operation of mines or quarries or of the exploitation of any natural resource’. The Australian commentary made the following comments on this alteration to Article 4(7):

‘Royalties are defined in Article 9 expressly to exclude “natural resource” royalties. The intention is that the country of source may levy its full tax on such royalties. However, the effect of the paragraph (7) of the 14.2.68 draft is that, if a natural resource royalty is a profit of a trade or business, the country of source is obliged to find a permanent establishment to which it is attributable to be able to tax it. This is because it is by definition a commercial or industrial profit and is not removed from the scope of that definition by the exclusion of royalties as defined in Article 9. It is not a royalty as defined in Article 9.’

The commentary went on to concede that, having regard to Article 3(2)(f) of the definition of ‘permanent establishment’, the source country would probably be able to find a PE when natural resource royalties were the product of a trade or business. The commentary, however, then goes on to make the following statement:

‘Nevertheless, it is considered that it should be made clear that a natural resource royalty is not a commercial or industrial profit unless effectively connected with a trade or business carried on through a permanent

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110 Commentary on Article 4(5) previously paragraph (7), p2.
111 Commentary on Article 4(5) previously paragraph (7), p3.
establishment. The insertion of the words "(including those payments which come within the meaning of "royalties" for the purposes of Article 9)" is designed to achieve this."

It is difficult to see how the proposed change achieved the effect stated in the Australian commentary. The exclusion of payments which came within the definition of ‘royalty’ for the purposes of Article 9 did not exclude royalty payments for natural resources, as these were not within the definition of ‘royalty’ in Article 9. The final version of Article 4(7) of the treaty included these amendments. A better solution to achieve the desired objective would have been to exclude natural resource royalties from the definition of ‘industrial or commercial profits’.

6.83 The draft also amended Article 4(7) to exclude ‘income from operating ships or aircraft’ from the definition of ‘industrial or commercial profits’ and deleted former Article 4(8), which had stated that Article 4 did not apply to profits from the operation of ships or aircraft which were either exempt from tax under Article 6(1) or to which Article 6(2) applied. Articles 6(2) and (3) of the draft of 14th February 1968 were also deleted from the amended draft. Article 6(2) had given the source state a right to tax 5% of the revenues from coastal shipping, while Article 6(3) excluded ships operated by a Japanese enterprise with a principal place of business in Australia from the operation of Article 6(2). The effect of this exclusion in combination with Article 6(1) of the treaty was that the profits of such an enterprise would be taxed at normal rates for non-residents, but that profits from amounts taxed in the territory of Papua New Guinea were excluded from those on which such an enterprise was taxed in Australia. The Australian commentary pointed out that Australia agreed that, following the deletion of Articles 6(2) and 6(3), paragraph (8) of Article (4) could not remain unchanged. Apparently, the Japanese had suggested an amendment which would have meant that the profits of coastal shipping could be taxed in the source country only if the shipowner operated in the source country through a PE. This was not acceptable to Australia, because Australia intended to tax Japanese shipowners trading on the Australian coast on the basis that 5% of the freight and passage monies were taxable income. This, the commentary explained, was the reason why Article 4(5) had been amended to exclude ‘income from operating ships and aircraft’

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112 Commentary on Article 4(5) previously paragraph (7), p3.
113 This became Article 4(5) in the amended draft.
from the definition of ‘industrial or commercial profits’ and as a consequence Article 4(8) had been deleted as unnecessary.\textsuperscript{114}

\textbf{Associated Enterprises}

6.84 A small but significant change, highlighting Australian anxieties, was made to the associated enterprises article. The words ‘profits which might be expected to accrue to the enterprise of one of the Contracting States’ were changed to ‘profits which might be expected to accrue to one of the enterprises’. The Australian commentary indicated that the article in the draft of 14\textsuperscript{th} February 1968 had been at best ambiguous and could have been read as meaning that a contracting state was entitled to reconstruct the accounts of a parent company only. The amendment was designed, according to the Australian commentary, to make it clear that a contracting state could reconstruct the accounts of any of the enterprises referred to in Article 5(1)(a) so long as it was a resident of the contracting state.\textsuperscript{115}

\textbf{Shipping And Aircraft Profits}

6.85 The amendments made in the draft to Article 6 (shipping and aircraft profits) involved the deletion of Article 6(2) dealing with shipping between Australia and Papua New Guinea. The Australian commentary explained that Australia had agreed to place the references to voyages between Australia and Papua New Guinea in the protocol.\textsuperscript{116} The draft added a new Article 6(2), which made it clear that the exemption from source basis taxation for shipping and aircraft profits extended to profits through participation in a pool service, a joint transport operating organisation or an international operating agency except in so far as the share of profits was attributable to voyages or operations confined solely to places in the source state. The Australian commentary merely noted that the paragraph provided for a pooling clause ‘along the lines sought by the Japanese side’.\textsuperscript{117} Further amendments to Article 6 were intended to make it clear that paragraph 6(3) in the draft referred only to coastal voyages.

\textsuperscript{114} Commentary on Article 4(5) previously paragraph (7), p3.
\textsuperscript{115} Commentary on Article 5.
\textsuperscript{116} Paragraph 5 of the protocol in the draft of 10\textsuperscript{th} May 1968 provided: ‘For the purposes of Articles 6 and 17 profits derived from the carriage by ships or aircraft of passengers, livestock, mails or goods shipped in a place in Australia for discharge in the Territory of Papua or in the Trust Territory of New Guinea shall be treated as profits from a voyage of a ship or aircraft confined solely to places within Australia.’ Note that this is a significantly more specific provision dealing with coastal shipping than the equivalent provision in the 1967 Australia – UK Tax Treaty quoted at note 134 above.
\textsuperscript{117} Commentary on Article 6(1) and 6(2), pp2–3.
Dividends And Interest

6.86 Article 7(1) was amended in the draft by substituting ‘derived by a Japanese resident who is beneficially entitled to the dividends’ for ‘to which a Japanese resident is beneficially entitled’. The Australian commentary indicated that the change was made to ‘give expression to our view that the concessional rate should only apply where the person who is beneficially entitled to the dividends derives the dividends’.\(^{118}\) This reflects a view that, under Article 7(1) in the draft of 14\(^{th}\) February 1968, the concessional rate on dividends might have applied where an Australian company paid a dividend to a person other than the person who was beneficially entitled, because the language of the draft of 14\(^{th}\) February required that a Japanese resident be beneficially entitled to the dividends but did not in terms require that the dividend be either paid to or derived by that Japanese resident. Equivalent changes were made to Article 7(2) and to Articles 9(1) and 9(2) dealing with royalties.

6.87 Other changes to Article 7 dealt with the situation where dividends were paid to dual residents. Under Article 7(4) of the 14\(^{th}\) February 1968 draft, dividends paid by a company of one of the contracting states to a person beneficially entitled to them who was not a resident of the other contracting state were exempt from tax in that other contracting state. In the Australian view, Article 7(4) of the 14\(^{th}\) February 1968 draft would have meant that Japan would have been obliged to exempt from its tax a dividend paid by a single Australian resident company to a dual resident of Australia and Japan, and the converse would also have been true.\(^{119}\) This was a consequence of the Australian drafting that attempted to deal with the issue of dual residence. A ‘resident of one of the Contracting States’ and a ‘resident of the other Contracting State’ meant either an ‘Australian resident’ or a ‘Japanese resident’ as the context required. An ‘Australian resident’ and a ‘Japanese resident’ were defined in a manner which meant that a dual resident could be neither an Australian resident nor a Japanese resident.\(^{120}\) The draft of 10\(^{th}\) May 1968 substituted the following paragraphs for Article 7(4):

\[(4) \quad \text{Dividends paid by a company which is a Japanese resident and to which a person who is not a resident of Australia is beneficially entitled shall be exempt from Australian tax.}\]

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\(^{118}\) Commentary on Article 7(1) and (2).

\(^{119}\) Commentary on Article 7(4) of 14/2/68 draft.

\(^{120}\) See the discussion at 6.40.
(5) Dividends paid by a company which is an Australian resident and to which a person who is not resident in Japan is beneficially entitled shall be exempt from Japanese tax.’

As ‘resident of Australia’ and ‘resident in Japan’ were defined as having the meanings that they had under the laws of the respective countries relating to tax and did not exclude dual residents, the effect of new Articles 7(4) and (5) was that dividends paid by a company resident in one contracting state to a dual resident was not exempt from tax in the other contracting state. Hence, the Australian commentary on the redrafted provisions observed:

‘It seems to Australia that the logical procedure in such a case is for both countries to tax the dividend and for it to be treated as having a source in the country in which the paying country is resident so that the other country will give credit for the tax of the country of source. The new paragraphs are, in association with paragraph 3(a) of Article 17 (the credit Article), designed to give effect to this view.’

Royalties

6.88 The definition of ‘royalties’ had been redrafted in response to an earlier Japanese draft, and, as requested by Japan, had been relocated to Article 9. The Australian commentary regarded the redraft, so far as it referred to natural resources royalties, as being more precise. In response to a request from Japan during the Canberra negotiations, the draft included consideration for the bare boat charter of a ship within the definition of royalties; however, the Australian commentary indicated that the insertion was ‘without commitment on Australia’s part’.

6.89 The definition of ‘royalties’ in the amended draft, which was unchanged in the final version of the treaty, apart from matters of layout, substantially followed the definition in the 1967 UK Treaty but specifically included ‘the bare boat charter of a ship’.

The final portion of the definition in the draft of 16th February 1968 had read, ‘but does not include royalties or other payments in respect of the exploitation of mines, quarries or natural resources’. This was replaced in the amended draft with the following language (corresponding to that used in the 1967 UK Treaty): ‘but does not include royalties or other payments in respect of the operation of mines or quarries or

121 Commentary on Article 7(4) of 14/2/68 draft.
122 See the discussion at 6.65.
123 Commentary on Article 9(2).
of the exploitation of any natural resource'. The amendment was clearly based on the notion that mines and quarries are better described as being 'operated' than as being 'exploited'.

**Public Entertainers**

6.90 Article 12 in the draft was a hybrid of the public entertainers articles in the Japanese draft of January 1968 and the Australian draft of February 1968, but it is possible that a further draft was developed between the drafts of January 1968 and February 1968 and the draft of 10th May 1968. Paragraph 1 differed from paragraph 1 of the Japanese draft and corresponded to the Australian draft of February 1968 in that it contained the words 'shall be deemed to have a source in'. These words applied the deemed source rule that had been included in the public entertainers article in the 1967 Australia – UK Treaty.\(^{124}\)

6.91 Paragraph 2 of Article 12 of the amended draft contained elements from both paragraph 2 of Article 12 of the Japanese draft of January 1968 and the definition of ‘permanent establishment’ in the Australian draft of February 1968. Paragraph 2 of Article 12 of the amended draft read as follows:

> ‘An enterprise of one of the Contracting States shall be deemed to have a permanent establishment in the other Contracting State if in the course of carrying on business it provides the services of public entertainers or athletes referred to in paragraph (1) of this Article in that other Contracting State and the public entertainer or athlete controls, directly or indirectly, such enterprise.’

The words underlined and struck through represent changes made in the amended draft from what appears to have been an earlier draft developed between the drafts of January and February 1968 and the amended draft. The portion (which was deleted from the definition of ‘permanent establishment’ in the amended draft) of paragraph 2 of Article 12 deeming there to be a PE appears to derive from the Australian draft of February 1968, while the reference to the enterprise providing the services of public entertainers or athletes and to the public entertainer or athlete controlling the enterprise appear to derive from the Japanese draft of January 1968. The Australian commentary on the changes in the amended draft stated that the change ‘is designed to eliminate any suggestion that the paragraph is applicable only

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\(^{124}\) See the discussion at 5.90 to 5.91.
to a company the sole business of which is providing the services of entertainers, etc. in the other State. 125 The final version of Article 12 in the treaty was identical to the version in the amended draft.

Credits

6.92 The Australian commentary indicates that Japanese revision to paragraph 1 of the credit article, Article 17, was not acceptable to Australia. A draft of 16th February 1968 had deleted paragraph 1 of the credit article of the draft of 14th February 1968 and of the Australian draft of February 1968, and included a handwritten marginal note requiring a more detailed definition relating to foreign tax credits and tax exemption. The amended draft reinserted paragraph 1 of the draft of 14th February 1968. The Australian commentary explained the methods for relieving international double taxation under domestic law and treaties, and pointed out that Australia had never undertaken to apply the exemption method in tax treaties although, as a feature of domestic law, Australia considered itself bound to use it when it applied. The reason given for not referring to the exemption system in tax treaties was that Australia might at some future time wish to change to a credit system. Australia did not wish to foreshadow such a change in its tax treaties and did not wish to bind itself, even temporarily, to exemption if a change to a credit system was made. 126

6.93 The amended draft made changes, from the draft of 16th February 1968, to the source rule for dividends in Article 17(3)(a). In the draft of 16th February 1968, Article 16(3)(a) and (b) read as follows:

‘(3) For the purposes of this Article –

(a) dividends paid by a company that is a resident of Australia shall be treated in Japan as having a source in Australia;

(b) dividends paid by a company which is a resident of Japan shall be treated in Australia as having a source in Japan.’

In the amended draft, the source rule for dividends was confined to Article 17(3)(a), which read as follows:

125 Australian Commentary, Commentary on Article 12.
126 Commentary on Article 17(1) previously Article 16. The commentary also made a similar point in relation to paragraph 4 of Article 17, which required a giving of credit for additional tax imposed because of adjustments under the associated enterprises article. This paragraph needed to be retained to deal with the possibility that Australia might in future alter their existing policy of exempting profits accruing to the other country as a result of these adjustments. Commentary on Article 17(4) previously Article 16(4).
'(3) For the purposes of this Article –

(a) dividends paid by a company which is a resident of one of the Contracting States shall be treated as having a source in that Contracting State.'

The Australian commentary on the amended draft pointed out that paragraphs (a) and (b) of Article 16 of the draft of 16th February 1968 could have had ‘undesirable results’. The commentary gave an example of a dual resident shareholder receiving a dividend from a dual resident company. In this situation, both Australia and Japan would be obliged to give credit for each other’s tax on the dividend. The commentary observed that there was ‘thus a circular effect and the result could be that the shareholder would bear tax on the dividend only to the extent of the difference between the Australian and Japanese rates of tax’. The commentary considered that the redrafted sub-paragraph ‘might be thought to provide a solution’ to this problem, and noted that it only provided a source for dividends paid by single resident companies and that in unusual situations like the example given, ‘the two taxing authorities could come to some agreement as to which country would allow credit’.127

In fact, the deemed source rule was narrower still because it only applied where a single resident company paid a dividend to a single resident shareholder. The commentary also noted that the source rules in Article 17(3)(b) of the amended draft similarly meant that the deemed source was confined to situations where the interest or royalty was received by a single resident.128

6.94 The source rule for royalties in the credit article was changed in the amended draft by adding ‘(including those payments which come within the meaning of ‘royalties’ for the purposes of Article 9)’ after ‘royalties’. The Australian commentary pointed out that the change was designed to ensure ‘that there is a source rule for natural resource royalties not included in the definition of “royalties” in Article 9’.129 The comment is confusing given that the definition of ‘royalties’ in Article 9 excludes natural resource royalties.130 Hence, including payments within the definition of ‘royalties’ for the purposes of Article 9 in the source rule in Article 16 would not appear to extend that rule to natural resource royalties. Other changes in the source rules for interest and royalties were designed to align them with Australian domestic source rules. The Australian commentary conceded that there would need to be

127 Commentary on Article 17(3) previously Article 16(3).
128 Commentary on Article 17(3)(b) previously Article 16(3)(b), p7.
129 Commentary on Article 17(3)(b) previously Article 16(3)(b), p8.
130 See the discussion at 6.82.
further discussions on whether the redraft adequately covered Japanese source rules.\textsuperscript{131}

6.95 Australia commented that the source rule for profits from ships or aircraft\textsuperscript{132} remained necessary from Australia’s perspective notwithstanding the deletion of Article 6(2).\textsuperscript{133} Australia wanted a specific source rule for amounts that were to be taxed in either country as a result of coastal shipping operations.\textsuperscript{134} A subsequent draft of 10th September 1968 \textsuperscript{135} added the words ‘or aircraft’ following ‘ships’ and amended the sub-paragraph after the word ‘profits’ so that the source rule was confined to ‘profits from voyages or operations confined solely to places in the other Contracting State’.

\textit{The Protocol}\textsuperscript{136}

6.96 Paragraph 1 was a saving provision in relation to the provisions in Divisions 14 and 15 of \textit{ITAA} 1936 (Cth) dealing with film business controlled abroad and insurance. The Australian commentary pointed out that ‘Provisions on the lines of the second sentence of paragraph (1) of the Protocol are incorporated in each of Australia’s other agreements.’ The commentary also noted that Australia’s other agreements contained a deemed source rule in relation to income that Australia taxed under Divisions 14 and 15, and commented that ‘the second sentence of paragraph (1) of the Protocol will ensure that this is also the situation in the Convention between Australia and Japan’.\textsuperscript{137}

6.97 Paragraph 2 preserved Australia’s right to determine profits via s38 of \textit{ITAA} 1936 (Cth). The Australian commentary pointed out that while an effort had been made to redraft the provision\textsuperscript{138} in a ‘less precise way’, Australia had found it necessary to ‘stick fairly closely to the expressions used in section 38’. The paragraph did refer to a method of apportionment of the total profit to its various parts, as requested by the Japanese, although the Australian commentary pointed out that this had no relevance for Australian income tax law.\textsuperscript{139}

6.98 Paragraph 3, from the Australian perspective, preserved the right to use \textit{ITAA} 1936 (Cth) s136 in instances where adequate information for determining the profits of a

\textsuperscript{131} Commentary on Article 17(3)(b) previously Article 16(3)(b), p8.

\textsuperscript{132} Article 17(3)(d) of the amended draft.

\textsuperscript{133} Article 6(2) dealt with source taxation of shipping based on a 5% of gross freights.

\textsuperscript{134} Commentary on Article 17(3)(d) previously Article 16(3)(d).

\textsuperscript{135} The draft of 10\textsuperscript{th} September 1968 is contained in NAA, ATO file, Pt 2.

\textsuperscript{136} Paragraph 5 of the protocol, dealing with the definition of ‘coastal shipping’, was discussed at note 165 above.

\textsuperscript{137} Commentary on paragraph 1 of the protocol.

\textsuperscript{138} The provision had been paragraph 4 of Article 4 of the draft of 14\textsuperscript{th} February 1968.

\textsuperscript{139} Commentary on paragraph 2 of the protocol.
permanent establishment was not available to the relevant competent authority. Similar provisions had been in every Australian taxation treaty since the 1946 UK Treaty, and equivalent provisions had been included in the 1965 Australian model discussed in Chapter 4. No comment was made about paragraph 3 in the Australian commentary on the amended draft.

The Draft Cabinet Submission, June 1968

6.99 On 11th June 1968, Cain forwarded to Randall a draft Cabinet submission, prepared by the ATO, on the negotiations with Japan. Cain stated that the submission had been prepared 'as a basis for bringing the matter before Cabinet at the appropriate time'.

6.100 The draft submission commented that the negotiations had been conducted consistently with the directions of Cabinet and the Prime Minister’s Decision No. 10 (Tax) of 31 January 1968, and that the preliminary draft was in all material respects ‘in line’ with the 1967 UK Treaty. The Japanese had been advised that any draft agreement between officials would be subject to consideration in full by the Australian government as to its acceptability and that, in particular, the government would wish to take into account the result of the separate talks on Australian investment in Japan and on the operation of Australian ships in the bulk cargo trade between Australia and Japan.

6.101 The draft submission summarised the effect of the preliminary draft and of the drafting changes since the negotiations in Canberra, and noted several respects in which the Australian negotiators had been successful in achieving their objectives. This aspect of the submission largely reiterated the points made in Cain’s letter to McMahon. The draft submission noted that Japan had agreed to omit the non-discrimination article. Handwritten corrections on the draft indicate that the omission could be important if Australia ever decided to impose additional tax on the Australian branch profits of non-resident companies.

6.102 The draft submission noted that, consistent with Australia’s other treaties, the draft conceded a residence basis for the taxation of shipping and aircraft profits, and went on to reiterate the points made in Cain’s letter to McMahon.

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140 The draft submission is contained in NAA, ATO file, Pt 2.
141 Decision No. 10 (Tax) of 31 January 1968 discussed at 6.32 to 6.33.
142 See the discussion at 6.70 to 6.75.
143 See the discussion at 6.72 to 6.74.
6.103 Outside of technical drafting and language issues, the draft submission pointed out that there were some matters that required further negotiation. These were: (a) issues relating to the continental shelf (here the draft submission largely reiterated the points made in O’Reilly’s letter to McMahon);¹⁴⁴ and (b) shipping profits (here the draft submission reiterated the points made in Cain’s letter to McMahon¹⁴⁵ concerning Japanese enterprise tax and bare boat charters).

6.104 The draft submission then referred to the two non-taxation issues¹⁴⁶ that McEwen had raised, noting that these were the subject of separate negotiations on which McEwen would be reporting to Cabinet. The submission indicated that McMahon understood that a satisfactory solution on the investment problem was in sight, but that reaching accord on the shipping issue would be more difficult.

6.105 The draft submission concluded by arguing that the parallel non-taxation discussions should not delay settlement of a final draft of the taxation treaty by officials. McMahon recommended that the Australian negotiators be authorised to reach a final draft treaty with the Japanese, making it clear that it would still be subject to approval by the Australian government.

The Australian Cabinet Decision(s) Of July 1968

6.106 O’Reilly wrote to McMahon on 29th July 1968, enclosing a note on the stage reached in the taxation treaty negotiations with Japan.¹⁴⁷ The note¹⁴⁸ observed that McEwen, as Minister for Trade and Industry, had now obtained assurances from Japan relating to investment opportunities for Australian business in Japan and the carriage of a reasonable share of bulk cargo from Australia to Japan in Australian flag vessels.

6.107 To date, the author has been unable to locate a record of a final submission, based on the draft submission, being made to the Australian Cabinet or of a Cabinet decision to resume negotiations with Japan being made. It is reasonably clear that at least a Cabinet decision to resume negotiations with Japan was made in late July 1968. On 30th July 1968, the Australian Cabinet made a decision without submission which noted that understandings had been reached with Japan to cover an agreed position on Australian investment in Japan and on shipping freights. The Cabinet decision further noted that the understandings would be incorporated in an

¹⁴⁴ See the discussion at 6.76.
¹⁴⁵ See the discussion at 6.70 to 6.75.
¹⁴⁶ See the discussion at 6.31 and 6.33.
¹⁴⁷ W J O’Reilly, Second Commissioner to The Commonwealth Treasurer, 29th July 1968, NAA, ATO file, Pt 1.
¹⁴⁸ ‘Double Taxation Agreement With Japan’, no date, NAA, ATO file, Pt 1.
appropriate instrument for initialling by leaders of the respective delegations on completion of the talks on the taxation treaty, and that the instrument would be subsidiary to the taxation treaty and would not be published.\textsuperscript{149} Subsequently, the Australian Department of Trade and Industry was informed that the leader of the Japanese delegation did not have authority to initial the instrument, and that instead an official of the Japanese Ministry of Foreign Affairs would initial the instrument following completion of the taxation treaty negotiations in Tokyo.\textsuperscript{150}

The 1968 Negotiations In Tokyo

\textbf{6.108} Further negotiations, commencing on 2\textsuperscript{nd} September 1968 and lasting for one week, were held in Tokyo. The Australian delegation was led by W J O'Reilly, Second Commissioner of Taxation.\textsuperscript{151} It appears that originally the Japanese delegation was to be led by Yoshikuni, Director General of Taxation Bureau, and Kitahara, Director of European and Oceanic Affairs Bureau,\textsuperscript{152} but O'Reilly's cable reporting the finalisation of the negotiations indicates that K. Ahara, Director-General of European and Oceanic Affairs Bureau, led the Japanese delegation.\textsuperscript{153}

\textbf{6.109} The author has been unable to locate a record of the 1968 negotiations in Tokyo, but documents in the Australian Department of External Affairs files indicate that the negotiations concluded on 9\textsuperscript{th} September 1968 and that a draft treaty was initialled on that date. O'Reilly reported to Cain that the most substantial difficulties arose in relation to the continental shelf protocol, that enterprise tax and coastal shipping were to be as proposed by Australia, and that bare boat charters were not to be mentioned. Two matters were left pending at the time of initialling. The first concerned interpretation of words in the singular and plural cases so as to ensure

\textsuperscript{149} A copy of Cabinet Minute dated 30\textsuperscript{th} July 1968, Decision No. 404 is contained in NAA, ATO file, Pt 2. Copies of the memoranda of understanding relating to Australian investment in Japan and to shipping are contained in NAA, ATO file, Pt 2. G J Cordell, for The Secretary, Department of External Affairs to Australian Embassy, Tokyo, 20\textsuperscript{th} August 1968, refers to 'recent decisions by Cabinet' as having opened the way for resumption of negotiations. This letter is contained in NAA, External Affairs file, Pt 2.

\textsuperscript{150} G F Johnson, Acting First Assistant Secretary, International Trade Relations Division, Department of Trade and Industry to E T Cain, CBE, Commissioner of Taxation, 28\textsuperscript{th} August 1968. NAA, ATO file, Pt 2.

\textsuperscript{151} G J Cordell to Australian Embassy, Tokyo, above n 198. The other members of the Australian delegation were: T P W Boucher, Assistant Commissioner of Taxation; R N Hutchinson, First Assistant Crown Solicitor; and E X W Visbond, from the Department of the Treasury. An official of the Australian Embassy in Tokyo also attended as translator.

\textsuperscript{152} Cable, Australian Embassy to EA, Treasury, DCO, PM's, dated 28\textsuperscript{th} August 1968, NAA, External Affairs file, Pt 3.

\textsuperscript{153} Cable, O'Reilly to Cain, Commissioner of Taxation, date unclear and Press Release, Tokyo, 9\textsuperscript{th} September 1968. Both documents are in NAA, External Affairs file, Pt 3. The Press Release indicates that O'Reilly and Yoshikuni initialled the treaty.
that the singular included the plural and vice versa.\textsuperscript{154} The second concerned the use of the words ‘directly or indirectly’ in paragraph 5 (dealing with the continental shelf) of the protocol. The Japanese regarded the expression as being too broad, while the Australian delegation considered them necessary to define the activities on the continental shelf which were the subject of the paragraph. O’Reilly reported that, in other respects, the initialled treaty corresponded with the draft developed at the Canberra negotiations.\textsuperscript{155}

\textbf{6.110} Australian records of the resolution of the two issues left pending at the time of initialling are fragmentary. Evidently, a possible formula to deal with the singular and plural cases had been discussed during the Tokyo negotiations. It appears that Australia had developed this formula and continued to press for its inclusion. The author has been unable to locate a draft of the formula discussed during the Tokyo negotiations, but it appears likely that it was implemented in the final form of paragraph 6 of the protocol, which reads:

‘The Government of Japan agrees to the Government of the Commonwealth providing in its legislation giving the force of law to the Agreement that the words in the Agreement in the singular include the plural and words therein in the plural include the singular, unless the context of the Agreement otherwise requires.’

\textbf{6.111} The ATO file contains what appears to be an earlier draft of paragraph 5 of the protocol dealing with the continental shelf, but does not contain any indication of the relationship between this draft and the final version of paragraph 5 of the protocol. The principal differences between the draft in the ATO file and the final version of paragraph 5 in the protocol lay in the geographic scope of the area referred to in the paragraph and the purposes for which the reference was made. The draft deemed the term ‘Australia’ to include for ‘the purposes of the Convention\textsuperscript{156} in relation to all acts, matters, circumstances and things touching, concerning, arising out of or connected with the exploration of the sea bed or sub-soil of sub-marine areas adjacent to Australia for petroleum as defined in the \textit{Petroleum (Submerged Lands) Act} of the Commonwealth and for the exploration of the said petroleum’. By contrast,

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\textsuperscript{154} O’Reilly to The Secretary, Department of External Affairs, Canberra, ACT, 10\textsuperscript{th} October 1968, NAA, External Affairs file, Pt 3 indicates that the problem arose because of the absence from the Japanese language of singular and plural forms of expression.

\textsuperscript{155} O’Reilly to Cain, above n 215 and Memorandum signed by O’Reilly and Yoshikuni dated 9\textsuperscript{th} September 1968 contained in NAA, External Affairs file, Pt 3.

\textsuperscript{156} The reference to ‘the Convention’ appears from the context, and from the fact that the treaty in terms refers to itself as ‘the Agreement’, to be to the Convention on the Continental Shelf signed at Geneva on 29\textsuperscript{th} April 1958.
\end{flushleft}
the final version of paragraph 5 of the protocol merely gave the Commonwealth government the right to levy tax on income of a Japanese resident in connection with the exploration for petroleum or the exploitation of petroleum in accordance with the terms of the treaty as if the area referred to in the paragraph were part of Australia. Also, the area referred to in paragraph 5 of the final version of the protocol was limited to ‘an area adjacent to Australia as specified in the Second Schedule to the Petroleum (Submerged Lands) Act 1967–1968 of the Commonwealth. Moreover, the final version of paragraph 5 of the protocol only applied when Australian law was in force in relation to the relevant area.

6.112 O’Reilly advised the Secretary of the Australian Department of External Affairs on 31 January 1969 that the text of the treaty had now been settled at the official level and would now be translated into Japanese. McMahon had approved the treaty and did not propose to submit it to Cabinet or to the taxation committee of Cabinet. McMahon wished to sign the treaty himself in Australia, and O’Reilly requested that External Affairs enquire if this would be acceptable to the Japanese. The text was then translated into Japanese, approved and modified by the Japanese Cabinet, and then checked by the Australian Embassy in Tokyo. The treaty was also accompanied by an exchange of notes requiring consultation between the two governments in the event of a subsequent introduction of sub-national taxes on the profits of ships and aircraft in international traffic in Australia, and a change in the method of relief from double taxation being adopted by Japan where profits of related enterprises had been adjusted under Article 5. The treaty was signed in Canberra on 20 March 1969 by McMahon as Australian Treasurer and by Kai Fumihiko as Japanese Ambassador to Australia.

The Significance Of The Treaty

6.113 The 1969 Japan Treaty was significantly influenced by the 1967 UK Treaty, and continuity with that treaty is apparent. Consistent with the 1967 UK Treaty, source taxation of dividends, interest and royalties was limited to 15%, 10% and 10% respectively, while a residence basis was largely conceded on shipping and aircraft profits. The precedent of the 1967 UK Treaty, coupled with a hard initial negotiating stance, meant that Australia was able to secure variations that it sought from the

157 W J O’Reilly, Second Commissioner of Taxation to The Secretary, Department of External Affairs, 31 January 1969, NAA, External Affairs file, Pt 3.
158 Cable, Australian Embassy, Tokyo to EA, 10/3/69 and M J Percival (Counsellor) to The Secretary Department of External Affairs, 7th March 1969. NAA, External Affairs File, Part 3.
159 A copy of the Exchange of Notes, dated 20th March 1969, is contained in NAA, External Affairs file, Pt 3.
OECD Model. In particular, Australia used a combination of the precedent of the 1967 UK Treaty and a tough initial negotiating stance on shipping profits and royalties to secure agreement from Japan on a uniform rate of source taxation on dividends and on the threshold for credits for underlying Australian corporate tax. The baby boomer structure of previous Australian tax treaties was preserved, with industrial or commercial profits being defined in exclusionary terms and with there being no ‘other income’ article. Unlike the 1967 UK Treaty, there was no tax on third country income article. The definition of PE continued to be broader than the OECD definition, and there was no capital gains article. The beneficial ownership requirement for dividends, interest and royalties was continued and refined, as was the definition of ‘royalties’. Several other variations in previous Australian tax treaties – the savings provision for ITAA 1936 (Cth) divs 14 and 15, the provision allowing application of domestic law in determining arm’s length in the absence of sufficient information, and the provision that effectively allowed the application of ITAA 1936 (Cth) s38 in determining industrial or commercial profits – were all relegated to the protocol. The negotiations were delayed and complicated by the presence of the parallel ‘political talks’ on shipping and investment opportunities for Australian business in Japan.

6.114 In some respects, however, the 1969 Japan Treaty either reverted to previous Australian idiosyncrasies or extended source basis taxation beyond what had been agreed in the 1967 UK Treaty. Thus, at Australia’s request, the treaty did not contain dual residence tie-breakers while maintaining an approach to defining corporate residence that in other respects bore some similarity to the approach used in the 1967 UK Treaty. The absence of a definition of ‘interest’ was consistent with Australian tax treaties prior to the 1967 UK Treaty, although in that treaty ‘interest’ was largely defined in negative terms. The provisions which included carriage between Australia and Papua New Guinea within the meaning of operations within Australia were refined but were relegated to the protocol. A more refined provision dealing with the continental shelf was also developed and placed in the protocol. Australia also succeeded in having an enterprise that provided the services of public entertainers deemed to be a PE, something it had unsuccessfully attempted in negotiating the 1967 UK Treaty. Source rules for dividends, interest and royalties were more closely aligned with the circumstances under which Australian domestic law taxed outbound payments in these categories. In these respects, the 1969 Japan Treaty can be seen as representing the high-water mark of Australian idiosyncrasies

\[160\] See the discussion at 5.90 to 5.91.
and source basis taxing claims in an actual Australian tax treaty following the publication of the 1963 draft OECD Model and prior to Australia joining the OECD.

6.115 This chapter is the final chapter of the thesis devoted to analysis, based on archival materials, of the negotiation and drafting of Australian tax treaties in the period prior to Australia joining the OECD in 1971. Chapter 7, on the basis of the analysis in this and preceding chapters, will draw conclusions relating to the central questions investigated in the thesis.
CHAPTER SEVEN: CONCLUSIONS

7.1 On the basis of previous chapters, this chapter will draw conclusions relating to the central questions investigated in this thesis.

Question 1: What explanations can be derived from archival materials for variations in Australian treaties from the current OECD Model?

7.2 Question 1 of the central questions at 1.4 asked what explanations for variations in currently operative Australian tax treaties from the OECD Model were provided by archival materials relating to the negotiation and drafting of Australian bilateral tax treaties up to and including the treaty with Japan in 1969. The first point that can be made is that the majority of those variations can be found in tax treaties entered into by Australia in this period. The existence of these variations in Australian tax treaties up to and including the 1969 Japan Treaty does not necessarily explain the occurrence of those variations in subsequent and currently operative Australian tax treaties. However, as will be noted at 7.6, there was a strong tendency in Australian treaty practice in this period to continue a provision in subsequent treaties where it accorded with Australian tax policy objectives. This tendency supports an inference that the existence of these variations in early Australian treaties may explain their continued occurrence in subsequent Australian tax treaties. Second, from this perspective, the two most important treaties in this period were the 1946 UK Treaty and the 1967 UK Treaty, as the majority of variations can be traced to one or other of these treaties. The next most significant treaty in the period was the 1953 US Treaty, but very few variations can be traced to the 1969 Japan Treaty or the 1969 Singapore Treaty and only one variation can be traced to the 1957 Canada Treaty.

7.3 One further conclusion that can be drawn from Chapters 2, 3 and 5 is that many of the variations originating in these tax treaties were initiated by the other party in the

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1 Depending on the degree of similarity and influence, that treaty can be regarded as the origin of up to 22 variations from the 2014 OECD Model in currently operative Australian tax treaties. Details of the variations are set out in Appendices 3 and 4.

2 Twenty-two variations from the 2014 OECD Model in currently operative Australian tax treaties can be regarded as having their origins in the 1967 UK Treaty. A further three variations could possibly be regarded as originating in the 1967 UK Treaty. Details of these variations are set out in Appendix 5.

3 The origins of 8 variations from the 2014 OECD Model can be traced to the 1953 US Treaty. Details of these variations are set out in Appendix 3.

4 Three variations can be traced to the 1969 Japan Treaty; one of these was a refinement of a variation first appearing in the 1967 UK Treaty. Details of these variations are set out in Appendix 3.

5 Four variations can be traced to the 1969 Singapore Treaty, but two of these can be seen as refinements of variations in earlier treaties. Details of these variations are set out in Appendix 3.
negotiations. In the 1946 UK Treaty, approximately 70% of variations from the OECD Model were initiated by the United Kingdom, with around one-third of these being modified by Australia in the drafting process. Of the variations from the current OECD Model in the 1953 Australia – US Tax Treaty, it is likely that only the substantial equipment provision and the 15% rate on all dividends were initiated by Australia. Over 70% of the variations from the current OECD Model in that treaty were initiated by the US. In the 1967 UK Treaty, 54% of variations from the current OECD Model were initiated by the UK. The analysis of these treaties demonstrates that it cannot be assumed that a variation from the OECD Model was originally initiated by Australia simply because it continues to be part of Australian tax treaty practice.

7.4 A third observation relating to variations contained in Australia’s first two tax treaties is that many of them are attributable to following the 1945 UK – US Tax Treaty. The influence of the 1945 UK – US Tax Treaty on the United Kingdom’s 6th May 1946 draft of the 1946 Australia – UK Tax Treaty was discussed at 2.38 and 2.98 to 2.99. The 1945 UK – US Tax Treaty also influenced, to a lesser extent, the subsequent drafts of the 1946 UK Treaty. Over 45% of variations from the OECD Model were attributable to following the 1945 UK – US Tax Treaty. Only 1 of 10 variations from the OECD Model attributable to following the 1945 UK – US Tax Treaty was modified in the drafting process. However, over 70% of variations from the 1945 UK – US Tax Treaty were either initiated or modified by Australia. By contrast, the only explicit references to models developed by the League of Nations in the negotiation of the 1946 UK Treaty were in relation to the shipping profits article and to the use of the arm’s length principle in computing profits of branches and related companies.6 In these instances, the reference was by UK officials and was to a principle adopted by the League of Nations rather than to any specific article in any of the League of Nations models as such.

7.5 Similarly, in the case of the 1967 UK Treaty, 7 of the 21 variations from the current OECD Model that were initiated by the UK are attributable to following the 1963 draft OECD Model in respects in which it differed from the current OECD Model. Only one variation initiated by Australia, the omission of an assistance in collection article, can possibly be characterised as following the 1963 draft OECD Model, but the record of

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6 See the discussion at 2.54 and 2.119.
negotiations shows that the deletion of the article from the UK draft was due to Australian domestic law considerations.\(^7\)

**7.6** Having included a provision in a tax treaty, there was a strong tendency to reproduce or refine it in a subsequent treaty, particularly where the provision accorded with general Australian tax treaty policy objectives; this was especially true in relation to Australia’s emphasis on the primacy of source basis taxation. The most notable examples here were the continued use of the savings provision for domestic legislation in situations where information was inadequate to determine an arm’s length price\(^8\) and the use of a substantial equipment provisions in the definition of ‘permanent establishment’.\(^9\) In accounting for a tendency to follow precedents, however, bureaucratic caution and inertia cannot be discounted, particularly once, as discussed in Chapter 4, Australia started to develop internal model treaties. Even where an existing provision was considered by Australia to be less desirable, there were instances where Australia agreed to a request by the treaty partner to include the provision as a result of an argument calling for equality of treatment to that given to other treaty partners. One notable example is agreeing to a shipping exemption in all these treaties despite the Australian policy of maximising source basis taxation and consequently of initially refusing in negotiations to agree to a shipping exemption.\(^10\) In some instances (most significantly in relation to source taxation of dividends, interest and royalties following the entry into the 1967 UK Treaty), Australia changed its official policy on the basis that a precedent had been set by its previous tax treaties.\(^11\) When Australia’s first internal model tax treaty was developed in 1965, there was a strong tendency to favour the language used in existing Australian tax treaties even where the OECD language arguably produced similar results. This can be seen repeatedly in the comments comparing the Australian model with the 1963 OECD draft where the Australian model is characterised as

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\(^7\) The history of this aspect of the drafts is summarised in Appendix 5 comments on OECD Model Article 27 and AV 111. Space considerations have meant that this aspect of the history of the draft and the negotiations were not able to be discussed in Chapter 5.

\(^8\) See the discussion at 2.115 to 2.126, 3.134, 4.153, 5.21, 5.61, 5.94 and 5.96.

\(^9\) See the discussion at 3.41 to 3.43, 3.84 to 3.85, 3.109, 3.136, 3.140, 3.148, 4.102, 4.153, 5.14, 5.15, 5.57, 5.84, 6.42 and 6.113. Although the final versions of the 1967 UK Treaty and the 1969 Japan Treaty did not include substantial equipment provisions, such provisions were included in the initial Australian drafts in those negotiations.

\(^10\) This approach is most particularly evident in the negotiation of the 1967 UK Treaty and the 1969 Japan Treaty, as discussed in Chapters 5 and 6 respectively.

\(^11\) This can be seen, for example, in the change in Australian attitudes to reductions in source taxation of dividends from the review of treaty policy discussed at 4.49, the 1965 Australian draft model discussed at 5.149 and in the negotiation of the 1969 Japan Treaty discussed at 6.13, 6.14, 6.19 to 6.20, 6.29, 6.44 to 6.45, 6.55, 6.59, 6.61, 6.63, 6.65, 6.71 and 6.113. In the negotiations associated with the 1969 Japan Treaty, the Australian attitude changes after the conclusion of the 1967 UK Treaty.
more concise and specific.\textsuperscript{12} This attitude to both the Australian model and the 1963 OECD draft Model is also evident at various points in the negotiation of the 1969 Japan Treaty.\textsuperscript{13}

\textbf{7.7} \hspace{1em} Many of the variations from the OECD Model that Australia initiated in treaties in the period after the 1946 UK Treaty and then after the 1967 UK Treaty have to be seen against the background of this tendency to follow precedents. Consistency with an overall policy objective of the primacy of source basis taxation, bureaucratic inertia, and linguistic and stylistic chauvinism all contributed to Australia initiating variations, while arguments based on precedents with third countries were used as a means of achieving the variations in question.

\textbf{7.8} \hspace{1em} Another type of variation from the OECD Model was offsetting concessions obtained by Australia for agreeing to a provision sought by the other party to the negotiations. Variations that were the product of this approach by Australia to negotiations are evident in the negotiation of the 1967 UK Treaty where Australia agreed to a shipping exemption in exchange for (among others) deletion of the non-discrimination article\textsuperscript{14} and in the 1969 Japan Treaty where Australia obtained tax and trade concessions using a similar approach.\textsuperscript{15} Given that Australian officials and relevant politicians were clearly aware that residence basis taxation of shipping profits was well established by the time these tax treaties were negotiated, it is remarkable that this negotiating tactic continued to be adopted and even more remarkable that it was successful. Again, in all instances the variation was seen as being consistent with Australia’s general tax treaty policy objectives, particularly its emphasis on the primacy of source basis taxation.

\textbf{Question 2: What factors influenced Australian taxation treaty policy and practice between 1946 and 1971 and how, if at all, did those factors change in that period?}

\textbf{7.9} \hspace{1em} The first of the key questions investigated in this thesis naturally leads into and overlaps with the second, namely: What factors influenced Australian taxation treaty policy and practice between 1946 and 1971 and how, if at all, did those factors change in that period?

\textsuperscript{12} See, for example, the discussion at 4.109, 4.111 and 4.114.
\textsuperscript{13} See, for example, the discussion at 6.41.
\textsuperscript{14} See the discussion at 5.130 to 5.133.
\textsuperscript{15} See the discussion at 6.65 of the Australian position on royalties as a negotiating tactic used in conjunction with the position on shipping profits to obtain concessions such as change to the level of ownership at which Japan would allow a credit for foreign underlying tax.
change in that period? In attempting to answer this question, distinctions can be drawn between factors:

(a) that influenced officials in advising in relation to decisions to enter into tax treaties in general and into particular tax treaties;
(b) that influenced politicians in deciding to enter into tax treaties in general and into particular tax treaties;
(c) that influenced politicians and officials in negotiating the broad content and overall bargain of a particular tax treaty; and
(d) that influenced officials in negotiating and drafting the technical details of particular tax treaties.

Although analysis is aided by drawing these distinctions, it is recognised that one or more factors may be relevant under more than one category. The factors and the categories are interrelated and are not mutually exclusive.¹⁶

**Factors Influencing The Decision To Enter Into Tax Treaties In General And Into Particular Tax Treaties**

**Economic Considerations Relating To Current And Expected Trade And Investment Flows**

7.10 Economic considerations relating to current and expected trade and investment flows between Australia and the treaty partner country influenced both politicians and officials in deciding to enter into tax treaties with potential partners during this period. This was a particularly significant factor influencing the decision to enter into

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¹⁶ The difficulty of distinguishing between factors that officials took into account in advising and factors that politicians took into account in deciding needs to be acknowledged. Cabinet submissions were drafted by officials and usually reached their final form before they were sent to the relevant minister for perusal prior to submission to Cabinet. Cabinet minutes in this period virtually never contain transcripts of Cabinet discussions; they usually just minute the final decision reached by Cabinet. Correspondence between departments is usually at the official level, and in instances where it is at the ministerial level the correspondence typically was drafted by officials and then settled by the minister. Only in rare instances is there evidence of either correspondence or Cabinet submissions being significantly altered when settled by ministers. Some indication of the views of ministers can sometimes be found in correspondence between officials and the relevant minister. A limitation of the research undertaken as part of this thesis is that it has been confined to departmental and Cabinet office files held in relevant national archives and has not considered personal papers of relevant ministers. Given this limitation, it is necessary to attribute the final form of Cabinet submissions and of Cabinet decisions and correspondence between ministers to relevant ministers. In the absence of archival evidence, such as ministerial notes or notations, to the contrary the assumption has been made that these Cabinet submissions and ministerial correspondence also represent the views of relevant officials. In the absence of archival evidence to the contrary, the assumption has also been made that preliminary drafts of Cabinet submissions and correspondence between departments represents the views of relevant officials rather than the views of the relevant minister.
Australia’s first comprehensive taxation treaty with the United Kingdom in 1946\footnote{The economic importance of the United Kingdom to Australia at the time was discussed at 2.5 and 2.6. The influence of this factor on the decision to enter into the 1946 Australia – UK Tax Treaty can be seen in the discussion at 2.30, 2.66, 2.68, 2.73, 2.74 and 2.89.} although, in that instance, this factor was partly a product of the incomplete relief from international juridical double taxation provided under the Dominion Income Tax Relief System. A desire to attract US direct investment into Australia was a factor influencing at least some ministers of the Menzies government and some officials – but notably not the Australian Treasury – in deciding to enter into a tax treaty with the United States.\footnote{The Liberal/Country Party policy prior to the 1949 Federal election was discussed at 3.10, and the general attitude of the Menzies government to direct investment from the United States was discussed at 3.17. The possible influence of the dollar loan from the World Bank on the decision to enter into the treaty was discussed at 3.21. Lobbying from US businesses was discussed at 3.22. The Spooner and Hughes report, discussed at 3.23, concluded that a treaty would encourage US investment in Australia. The negative view held by the Australian Treasury of the likely economic effects of a treaty was discussed at 3.24. The negative attitudes to a tax treaty with the US held by Treasury and Taxation Office officials during the Chifley government were discussed at 3.14 to 3.16.} The possible encouragement of Canadian investment in Australia was a factor that led Australian officials and the Australian Cabinet to favour a tax treaty with Canada.\footnote{This aspect was discussed at 3.145. Note in particular that lobbying by Canadian business (notably the Ford Motor Company of Canada) contributed to this belief.}

\subsection*{7.11} Throughout the first formal revision of Australian tax treaty policy, the Australian Treasury remained highly sceptical of whether economic benefits flowed from tax treaties.\footnote{See in particular the discussion at 4.24, 4.35 and 4.37.} While officials from other departments, including the Australian Taxation Office, held more positive views about the economic effects of tax treaties, it is clear that by the early 1960s Treasury had become the dominant department in advising on the economic effects of tax treaties.\footnote{The dominance of Treasury is evident in the drafting of Cabinet Submission 305 discussed at 4.20 to 4.32. The observation is consistent with the analysis of Jones on the role of the Department of the Treasury in the demise of the Division of Industrial Development in the period from 1949 to 1960. See E Jones, ‘Post World War Two Industry Policy: Opportunities and Constraints’ (2002) 42 Australian Economic History Review 312, particularly at 331–2.}

\subsection*{7.12} The importance of the United Kingdom as a trade and investment partner in the early 1960s influenced both the decision to not negotiate with European countries while the UK’s first attempt to join the European Economic Community was ongoing\footnote{The continued, if declining, economic importance of the UK to Australia up to the early 1960s was discussed at 5.5 to 5.6. Although the importance of the UK as a trading and investment partner is not explicitly mentioned, it provides the best explanation of the 1962 decision (discussed at 4.52) to defer negotiations with European countries pending the outcome of the United Kingdom’s first application to join the European Economic Community.} and in the 1966 decision to enter into a new comprehensive tax treaty with the United
Similarly, the importance of Japan as a trading partner by the 1960s was the major factor leading to a decision to enter into tax treaty negotiations with Japan.24

**Cultural And Political Factors**

7.13 There is clear evidence that cultural and political factors were significant in the decision to enter into the tax treaties with the United States in 195325 and with Canada in 1957.26 There is no explicit mention of cultural and political factors in archival material examined relating to the 1946 UK Treaty, although these are mentioned in Cabinet Submission 305 in July 1962 as factors relevant to the entry into that and later tax treaties.27

7.14 Researchers into the strategic and geopolitical environment of the early to mid 1960s have argued that fear of the United Kingdom withdrawing militarily east of Suez affected Australia’s trade relations with the UK,28 but the author has found no direct evidence of this factor influencing the Australian decision to enter into a second tax treaty with the UK.

**Treaty Practice And Domestic Law Considerations Of Treaty Partner And Third Countries**

7.15 The treaty practice and domestic law of the treaty partner was a factor influencing the decision to enter into tax treaties in this period. In the case of the 1946 UK Treaty, the

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23 Again, paradoxically the significance of the UK as a trading and investment partner can be seen not by it being expressly mentioned but by the fact that, as discussed at 6.24, Australia decided to proceed with renegotiating the 1946 UK Treaty before entering into formal negotiations with Japan notwithstanding that a Cabinet decision had been made to do so and notwithstanding that there had been preliminary talks with Japan.

24 As noted at 4.54, O’Donnell’s assessment in 1962 was that Japan was probably the most important trading partner with which Australia did not have a tax treaty. In 1963, Belcher, as discussed at 4.82, considered Japan the most important of the non-OECD countries with whom Australia might negotiate a tax treaty. The significance of Japan as a trading partner was discussed at 6.2 to 6.3. As noted at 6.25, Treasury advice in 1968 indicated that Japan was chosen as a treaty partner because of its importance to Australia’s trade.

25 The general geopolitical context was discussed at 3.18 to 3.21. At 3.24 it was noted that Fadden’s Cabinet submission made express reference to the political considerations arising out of the relationships between the two countries in the then current circumstances.

26 As noted at 3.145, Fadden’s 1953 submission to Cabinet had stated that it would be difficult and perhaps embarrassing in any treaty to deny broadly comparable terms to Canada to those proposed to be agreed with the United States.

27 As discussed at 4.33 and 4.35, Cabinet Submission 305 noted that Australian tax treaties up to that point had been with countries with which Australian political and economic relationships were especially close. While the closeness of the relationship with the UK was regarded as affecting the concessions made in the 1946 Australia – UK Tax Treaty, as discussed at 4.35, Submission 305 also took the view that the concessions were also influenced by the inadequate relief provided under the previous system of Dominion Income Tax Relief.

28 The literature was discussed at 5.6.
inadequate relief provided under the Dominion Income Tax Relief System\textsuperscript{29} and the existence of a foreign tax credit in the 1945 UK – US Tax Treaty\textsuperscript{30} were significant factors, at both the official and political level, contributing to Australia agreeing to enter into a tax treaty with the UK. In the case of the 1953 US Treaty, the problem of credit overspill due to the combination of Australian rates on corporate income and dividends and limitations in the US foreign tax credit system was a major factor in the decision to enter into the treaty.\textsuperscript{31}

7.16 The incomplete relief from international juridical double taxation provided by some foreign jurisdictions was recognised as a reason for entering into tax treaties in McGovern’s 1959–60 assessment of Australian tax treaties,\textsuperscript{32} but a similar recognition does not appear to have been made by Treasury officials who were the primary drafters of Submission 305 in 1962.

7.17 Changes to the UK system of corporate-shareholder taxation with consequences for the appropriate conditions on which credits for underlying corporate tax could be granted were the major reason why the UK wanted the 1946 Australia – UK Tax Treaty revised and were seen in McMahon’s Cabinet submission prior to the 1946 UK Treaty as something that Australia would have to agree to.\textsuperscript{33}

7.18 The failure to credit Australian corporate tax against Japanese local enterprise tax\textsuperscript{34} and other causes of double taxation, such as conflicts of source rules, were noted, in the context of the proposed negotiations with Japan, as reasons for entering into tax treaties.\textsuperscript{35}

\textit{Revenue Considerations And The Primacy Of Source Basis Taxation}

7.19 Throughout the period under review, Australian policy emphasised source basis taxation and was concerned about possible losses of revenue that would result from entering into tax treaties. In the case of the 1946 UK Treaty, although an emphasis on the primacy of source basis taxation and revenue considerations influenced the overall bargain struck in the treaty and its detailed drafting, Australia wanted a comprehensive tax treaty because of the perceived inadequacy of the relief provided under the system of Dominion Income Tax Relief. Despite views on the primacy of

\textsuperscript{29} This point was made at 2.28 and 2.30 in relation to Dominion Income Tax Relief. See also the discussion at 2.60 and 2.66.
\textsuperscript{30} See the discussion at 2.59 and 2.72.
\textsuperscript{31} This issue was discussed at 3.25 to 3.29.
\textsuperscript{32} See the discussion at 4.5 and 4.7.
\textsuperscript{33} See the discussion at 5.40.
\textsuperscript{34} See the discussion at 6.5 of Canavan’s report to Fadden following the Tokyo talks.
\textsuperscript{35} See the discussion of this aspect of Holt’s Cabinet submission at 6.13.
source basis taxation and of the importance of revenue considerations expressed at various points prior to the ministerial agreement outlined at 2.90\textsuperscript{36} one gets the impression that, in the circumstances, trade and investment flows trumped all other considerations and that some compromise on the primacy of source basis taxation and on revenue considerations to obtain a tax treaty was inevitable.

7.20 In the case of the 1953 US Treaty, revenue considerations had been a dominant factor in the Chifley government’s reluctance to negotiate between 1946 and 1949\textsuperscript{37} and were seen as a negative aspect of a tax treaty in both the Spooner and Hughes report\textsuperscript{38} and in Fadden’s Cabinet submission\textsuperscript{39} due to the need to reduce Australian tax on dividends to avoid credit overspill.

7.21 Loss of revenue was a dominant factor in the Chifley government’s unwillingness to enter into a treaty with Canada\textsuperscript{40} and was regarded as a negative aspect of the proposed treaty when Treasury drafted Fadden’s 1953 Cabinet submission\textsuperscript{41}

7.22 Revenue considerations and the primacy of source basis taxation were paramount as considerations on whether or not to enter into tax treaties in the 1959–62 review of tax treaty policy,\textsuperscript{42} in Belcher’s assessment of the 1963 draft OECD Model\textsuperscript{43} and in the 1965 Australian model.\textsuperscript{44} By 1965, dissatisfaction with the amount of source basis taxation provided for in the 1946 UK Treaty had led Australian officials to request a new treaty instead of an amending Protocol.\textsuperscript{45}

\textsuperscript{36} Although revenue considerations and jurisdictional claims are raised by Australia several times in the negotiations leading to the 1946 UK Treaty, the closest that any of these comments comes to suggesting that Australian jurisdictional claims and revenue considerations meant that a tax treaty should not be entered into was a comment in Jackson’s briefing of Evatt discussed at 2.66. The statement of ‘Australia’s Minimum Position’ in Evatt’s memorandum titled, ‘What Australia Asks For’ outlined at 2.74 does indicate that Australia would have to agree to a tax treaty which provided only for a foreign tax credit on business profits and non-portfolio dividends. If anything, this statement shows the importance to Australia of obtaining a tax treaty in relation to business profits and non-portfolio dividends and hence the importance of economic considerations in the decision to enter into a tax treaty.

\textsuperscript{37} The Chifley government’s reluctance to negotiate was discussed at 3.14 to 3.16.

\textsuperscript{38} The Spooner and Hughes report was discussed at 3.23.

\textsuperscript{39} Fadden’s Cabinet submission was discussed at 3.24.

\textsuperscript{40} The Chifley government’s unwillingness to enter into a tax treaty with Canada was discussed at 3.144.

\textsuperscript{41} See the discussion at 3.146.

\textsuperscript{42} See the discussion of the review at 4.20 to 4.51 and the nine-point summary at 4.49.

\textsuperscript{43} Belcher’s assessment of the 1963 draft OECD Model was discussed at 4.57 to 4.84. Revenue considerations are given significant emphasis in Belcher’s summary conclusion at 4.84.

\textsuperscript{44} The emphasis on source basis taxation in Belcher’s draft is evident in the discussion at 4.93, 4.95, 4.97 to 4.100, 4.102 to 4.106. The emphasis on source basis taxation in the revised draft can be seen in 4.109, 4.112 to 4.113, 4.115 to 4.118 and at 4.121.

\textsuperscript{45} See the discussion at 5.10.
An emphasis on revenue and on source basis taxation can be seen in McMahon’s Cabinet submission prior to the negotiations leading to the 1969 Japan Treaty; Australia would enter into treaties where source country taxing rights were preserved to the extent that they had been in the 1967 UK Treaty. Throughout the period, revenue estimates were commonly made by the ATO of the revenue cost of entering into any particular tax treaty based on information supplied by ATO Deputy Commissioners.

**Australian Domestic Law Considerations**

As Australia provided unilateral relief from international double taxation, the consistent Australian attitude throughout the period was that any international juridical double taxation that did exist was either the result of the inadequacy of the unilateral relief provided by the potential treaty partner (most notably in the case of the UK in 1946) or due to differences in tax rates between Australia and the treaty partner country and limitations on the unilateral relief provided by the proposed treaty partner. This led to a reluctance to enter into tax treaties in the period from 1946 to the early 1960s, which was only overcome in the case of the US, Canada and New Zealand by economic, political, strategic and cultural factors. The reluctance is particularly evident in the first formal review of Australian tax treaty policy.

The view that Australian domestic law meant that a treaty was not necessary to prevent international juridical double taxation of Australian residents is still evident in the ‘no concession without commensurate advantages’ stance in Holt’s 1965 Cabinet submission relating to the preliminary negotiations with Japan. Following the signing of the 1967 UK Treaty, that treaty was regarded as setting the norm for distributive articles in Australian tax treaties, and the view that unilateral relief provisions made tax treaties unnecessary is not evident in McMahon’s 1968 submission prior to negotiating the 1969 Australia – Japan Tax Treaty.

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46 The overall approach recommended in McMahon’s submission was discussed at 6.26.
47 As discussed in note 6 to 4.3, this was done systematically in 1959 at the beginning of the first official review of Australian tax treaty policy.
48 Australia’s unilateral relief measures throughout this period were discussed at 2.7, 2.8, 2.13, 3.11 and 5.7.
49 In the case of the 1953 Australia – US Tax Treaty, see the discussion at 3.17 to 3.24.
50 In the case of the 1957 Australia – Canada Tax Treaty, see the discussion at 3.145.
51 See in particular points (1), (4) and (5) in the nine-point summary in Cabinet Submission 305 outlined at 4.49.
52 See the discussion of this aspect of Holt’s Cabinet submission at 6.13 to 6.21.
53 This point was expressly made in McMahon’s 1968 Cabinet submission as discussed at 6.26.
Factors Affecting The Broad Content Of Tax Treaties

Revenue Considerations And The Primacy Of Source Basis Taxation

7.26 Throughout the period, revenue and an emphasis on source taxation were clearly the dominant factors affecting the overall bargain that Australia sought to achieve in tax treaties. Both were heavily emphasised by Australian politicians and officials in the negotiations leading to the ministerial agreement outlined at 2.90, and the concessions from the UK’s initial position that resulted from that agreement are all explicable as means of preserving source basis taxation and Australian revenue.

7.27 In the case of the 1953 US Treaty, McGovern emphasised that Australia’s position was, in general, to oppose any violation of the priority of source taxing rights and that Australia’s major objective was to obtain a reduction in source taxation which would encourage US direct investment in Australia without producing the ‘Treasury effect’. In this respect, obtaining a uniform rate of 15% on all dividends was regarded as a major achievement.

7.28 An emphasis on revenue considerations and on the primacy of source basis taxation was clearly evident in the 1959–62 review of Australian tax treaty policy culminating in the ‘no concessions’ policy of the Cabinet decision of August 1962. Overall revenue considerations are also evident in Belcher’s assessment of the 1963 draft OECD Model and in the 1965 Australian model which gave effect to the ‘no concessions’ policy.

7.29 An objective of obtaining greater source country taxing rights than had been provided for in the 1966 UK draft is evident in McMahon’s 1967 Cabinet submission.

The references in note 36 above can all be equally well classified as affecting the broad content of the treaty. In addition, the concessions that Coombs obviously argued for at his meeting with Gregg outlined at 2.89 can also be seen as a means of preserving source basis taxation and Australian revenue.

See the discussion at 3.33.

See the discussion at 3.32.

McGovern’s views on the uniform 15% rate on dividends were discussed at 3.52 to 3.56.

Cabinet Submission 305 was discussed at 4.33 to 4.51. The Cabinet decision was discussed at 4.52.

See the discussion of Belcher’s assessment of the impact of the OECD Model on future Australian tax treaties at 4.81 to 4.83.

See the discussion at 4.95, 4.97 to 4.100, 4.102 and 4.104 of the manner in which Belcher’s draft consolidated and extended the emphasis on the primacy of source basis taxation in previous Australian tax treaties.

Although this submission does not expressly state an overall objective of maximising source basis taxation, the effect of all of the objectives mentioned in McMahon’s submission,
Similarly, McMahon’s Cabinet submission prior to the negotiations with Japan sought to rely on the 1967 UK Treaty as a precedent for granting greater source country taxing rights than had been provided for in the 1968 Japanese draft.  

_Australian Domestic Law Considerations_

**7.30** One feature of Australian domestic law of recurring significance throughout this period for the overall bargain struck in particular tax treaties, particularly in negotiations between officials, is the Australian system of corporate-shareholder taxation as compared with the system adopted by the treaty partner. This was particularly evident in the 1946 UK Treaty negotiations where Australia was using a classical system while the UK was using a form of integrated system. The relevance to the broad bargain in Australian eyes was the effect that the differences in systems had on reduced rates of source taxation on dividends.

**7.31** Another significant factor was the Australian desire to preserve the operation of Australian domestic law relating to film business and insurance with non-residents and shipping and air transport.

**7.32** The trends identified at 7.30 and 7.31 continued with the 1953 US Treaty, although clearly the fact that these features had been present in the 1946 UK Treaty affected the overall bargain struck. In the case of shipping and air transport, while Australia always ultimately agreed to adopting a residence basis, it consistently tried to negotiate for the residence basis to be expressed in a restrictive form and always began with a position of source basis taxation of shipping profits. All of these features were incorporated into the 1965 Australian model and were also found in the February 1968 draft sent to Japan.

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62 See the discussion of this aspect of McMahon’s Cabinet submission at 6.26 to 6.27 and 6.29.
63 See the discussion at 2.35, 2.47 and 2.61. Note also McGovern’s comment, discussed at 4.13, that the use of a dividend exemption system and a higher corporate tax rate by New Zealand had prevented Australia and NZ from entering into a tax treaty prior to NZ’s change to a classical system.
64 In relation to the 1946 Australia – UK Tax Treaty, see the discussion at 2.43, 2.48, 2.57, 2.60, 2.76, 2.82 and 2.84.
65 As discussed at 3.31, McGovern reported that the US attitude was that the 1946 Australia – UK Tax Treaty should be regarded as setting the pattern for Australian tax treaties with capital exporting nations.
66 The provisions in relation to films and insurance were discussed at 4.95 and 4.106. The provisions in relation to shipping were discussed at 4.97.
67 The provisions relating to film business and insurance with non-residents were noted at 6.43. The absence of an article on shipping profits was due to the Cabinet decision discussed at 6.30 to 6.31 and to the Prime Minister’s decision discussed at 6.33.
Cultural And Political Considerations

7.33 Cultural and political factors did play a role, albeit relatively minor, in influencing the general bargain struck in tax treaties in the period under review. In the 1946 UK Treaty, domestic political considerations were raised by officials to support arguments rejecting the UK’s proposals on dividends and shipping. In the case of the 1953 US Treaty, political considerations in the US are mentioned as reasons for agreeing to particular provisions. Holt’s 1965 Cabinet submission raised what amounted to issues of economic nationalism as reasons for not agreeing to Japan’s request for a reduced rate of source taxation on non-portfolio dividends.

Model Treaties And Policies Developed By International Organisations

7.34 It is remarkable that, throughout the period, the explicit references to model treaties developed by international organisations (such as the League of Nations, the United Nations and the OECD) are virtually all negative. In the 1946 Australia – UK Tax Treaty negotiations, League of Nations principles (in relation to the taxation of shipping profits) are mentioned by UK officials once prior to the ministerial agreement discussed at 2.90. There is no direct evidence that this influenced Australia’s decision to agree to taxing shipping profits on a residence basis. Recent treaties concluded by the UK and the overall bargain struck as part of the ministerial agreement are likely to have had more influence on that decision.

7.35 The first formal review of the 1963 draft OECD Model by Belcher concluded that its provisions were more favourable to capital exporting and maritime nations and that Australia should be able to obtain more favourable treaties from OECD countries than would be obtained by following the OECD Model. A similar point was made in McMahon’s Cabinet submission prior to negotiating the 1967 Australia – UK Tax

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68 See the discussion at 2.46.
69 See the discussion at 2.64 and also Willis’ views on the Australian attitude to films and shipping at 2.48.
70 As discussed at 3.31, McGovern mentioned this as a general factor and, as discussed at 3.49, specifically mentioned it in relation to shipping profits.
71 See the discussion of this aspect of Holt’s submission at 6.19.
72 See the discussion at 2.54.
73 Belcher’s overall conclusion on the 1963 draft OECD Model was discussed at 4.84.
74 The respects in which Belcher considered more favourable tax treaties could be obtained from OECD countries were discussed at 4.81.
Treaty,\textsuperscript{75} and at the opening of those negotiations the Commissioner of Taxation indicated that the ‘lore’ on double tax treaties did not suit Australia as a capital importing country which was not a maritime nation. The UK delegation interpreted these remarks as an indication that Australia did not regard the OECD Model as entirely suitable to Australian circumstances.\textsuperscript{76}

7.36 In summary, the influence of model treaties developed by international organisations on the broad content of Australian tax treaties in this period can be seen as negative. By the mid 1960s, the fact that the 1963 draft OECD Model allocated taxing rights to particular classes of income differently to prior Australian treaties was, if anything, seen as a reason for continuing with prior Australian practice.

The Australian Policy Development And Negotiating Process Itself

7.37 Early on Australian politicians and officials learnt that hard bargaining, intransigence and reference to precedents could produce favourable results. A recognition of the value of offsetting compromises to achieve what were considered to be more important objectives is evident in the negotiation of the 1946 UK Treaty, although this only really begins when Evatt meets with Dalton.\textsuperscript{77}

7.38 It is unclear from the available records whether the compromises made by both sides\textsuperscript{78} in negotiating the 1953 US Tax Treaty were offset against each other. Those negotiations appear to have been relatively convivial, possibly because of the similarities that then existed between the tax systems of the two countries.\textsuperscript{79}

7.39 Offsetting compromises are more evident in the negotiation of the 1957 Canada Treaty where Australia eventually modified its initial position on undistributed profits tax and conceded a residence basis for taxation of shipping profits.\textsuperscript{80}

7.40 During this period, the Australian Treasury moved from a position of peripheral involvement in 1946 to virtual dominance of advice on tax treaty policy by 1965. Treasury was largely responsible for Cabinet Submission 305, which led to the hard

\begin{itemize}
\item This aspect of McMahon’s Cabinet submission was discussed at 5.41.
\item See the discussion of Cain’s opening address at 5.76.
\item As discussed at 2.71 to 2.76, Evatt’s memorandum given to Dalton emphasised the points of most importance to Australia and for the first time offered compromises on issues perceived to be of lesser importance. Further compromises were foreshadowed at Coombs’ meeting with Gregg (discussed at 2.89) and further offsetting compromises were made at the ministerial meeting discussed at 2.90.
\item For Australia, the major compromise was agreeing to residence basis taxation of shipping and air profits. For the US the major compromise was agreeing to a uniform 15% source country rate on dividends.
\item See the more detailed argument to this effect at 3.138.
\item See the argument to this effect at 3.152.
\end{itemize}
line 'no concessions’ Cabinet decision of August 1962.\footnote{The development of Cabinet Submission 305 was discussed at 4.20 to 4.32.} The policy was internally inconsistent, being based on the one hand on the proposition that concessions were unnecessary in tax treaties\footnote{See in particular paragraphs (4) and (5) in the nine-point summary in Cabinet Submission 305 outlined at 4.49.} and on the other using the initial ‘no concessions’ stance (particularly in relation to shipping and aircraft profits) as a means of obtaining concessions in priority areas.\footnote{This view as expressed in Cabinet Submission 305 was discussed at 4.50.} The inconsistency was compounded by the ATO’s evident lack of faith in the viability of a ‘no concessions’ policy.\footnote{See the argument to this effect at 4.58 and note McGovern’s earlier comments discussed at 4.10.}

7.41 In negotiating both the 1967 UK Treaty and the 1969 Japan Treaty, the still relatively tough opening stance enabled negotiators to achieve what were perceived as significant concessions from the other party which affected the overall bargain of the respective treaties in the technical phase of the negotiations.\footnote{In the case of the 1967 Australia – UK Tax Treaty, as discussed at 5.133 to 5.135 and 5.139 to 5.140, Australia’s condition for agreeing to a shipping exemption was that the UK not insist on the presence of a ‘non-discrimination’ article. In the case of the 1969 Australia – Japan Tax Treaty, as discussed at 6.54 to 6.66 and 6.73, Australia used concessions from a tough initial position on shipping profits and royalties as a means of obtaining an agreed threshold for credits for foreign underlying tax. See the argument to this effect at 2.165.}

Factors Affecting Technical Drafting Considerations

Revenue Considerations and Primacy of Source Basis Taxation

7.42 Revenue considerations and an emphasis on the primacy of source basis taxation were also very significant considerations at the technical drafting stage of Australian tax treaties throughout this period. In the 1946 UK Treaty, the overall structure of the treaty, although present in the initial UK draft, can be seen as giving technical expression to the preservation of source country taxing rights for particular categories of income as agreed in the ministerial meeting as outlined at 2.90.\footnote{See the discussion at 3.42 to 3.43. As noted at 3.84 to 3.86, the Australian second draft attempted to broaden the scope of the substantial equipment provision; however, as noted at 3.109, the only change from the second draft that was incorporated in the final draft was the reference to substantial equipment being ‘installed’.

of source taxation of industrial royalties in this treaty. This treaty also included a ‘force of attraction’ rule which increased source basis taxation. While seen as favouring Australia in the longer term, this provision was clearly introduced at the request of the United States but not opposed by Australia. A force of attraction provision was rarely included in subsequent Australian tax treaties and did not find its way into the 1965 Australian model tax treaty.

7.44 With the exception of the ‘force of attraction’ principle, the extensions of source basis taxation in the 1953 Australia – US Tax Treaty were continued in the 1957 Australia – Canada Tax Treaty and were extended further by a provision in the definition of ‘permanent establishment’ in response to the decision in Case 110 (1955) 5 CTBR (NS) 656.

7.45 Revenue considerations and the primacy of source basis taxation were also clearly dominant factors in Belcher’s review of the 1963 draft OECD Model and in the development of Australia’s 1965 model, which consolidated and extended all the provisions in Australian tax treaties that had enlarged the scope for source basis taxation.

7.46 The pattern continued in the negotiation of the 1967 UK Treaty where Australia consistently argued for, or attempted to extend, technical provisions maximising source basis taxation, particularly the definition of ‘permanent establishment’, that had been in the 1965 Australian model or earlier treaties. Again, in negotiating the 1969 Japan Treaty, Australia consistently preferred and argued for provisions from the Australian draft which provided for greater source basis taxation.

**Australian Domestic Law Considerations**

7.47 Technical issues arising due to the relationship between Australian domestic law and treaty provisions affected the detailed drafting of Australian tax treaties throughout the period. The negotiations relating to undistributed profits tax on wholly owned
subsidiaries of UK companies in the 1946 UK Treaty fit into this category. So too do the negotiations in relation to that treaty concerning Australia’s desire to preserve the operation of *ITAA 1936* s136. The ‘deemed source rule’, which can be traced to the 1946 UK Treaty but which developed in the 1967 UK Treaty and the 1969 Japan Treaty as a means of resolving doubts about Australian source under domestic law, also fits into this category. Commentary on the Australian redraft in the negotiations of the 1969 Japan Treaty raises a justification based on avoiding double crediting, but doubts about source under Australian law both preceded and were concurrent with this justification. The inclusion of a credit article, notwithstanding the broad exemption for taxed foreign source income throughout this period, was justified on the basis that it would apply if and when Australia introduced a general foreign tax credit system. In the interim, the drafting which allowed the credit against Australian tax payable was regarded as ensuring that the credit article only applied to dividends (where a foreign tax credit or an inter-corporate rebate applied) or to items which had not been subject to foreign tax and not to other items of foreign source income which were exempt from Australian tax.

7.48 The Australian desire to preserve its perceived right to tax undistributed Australian source profits of non-resident private companies was the principal cause of the delay in entering into a tax treaty with Canada between 1953 and 1957.

7.49 The features referred to in 7.47 were preserved in the 1965 Australian model and in the draft sent to Japan in February 1968.

7.50 In negotiating the 1967 UK Treaty, Australia argued for the omission of the capital gains article in the UK draft on the basis that Australia did not tax capital gains and

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94 These negotiations were discussed at 2.109 to 2.114.
95 These negotiations were discussed at 2.115 to 2.126.
96 The deemed source rule in Articles III(3) and IV(2) of the 1946 UK Treaty was inserted at Australia’s request as part of the discussions relating to *ITAA 1936* s136 discussed at 2.115 to 2.126. It is arguable that the deeming did not extend beyond what was possible under former *ITAA 1936* s136. See the discussion to this effect in C John Taylor, ‘Some Distinctive Features of Australian Tax Treaty Practice: An Examination of their Origins and Interpretation’ (2011) 9 *E Journal of Tax Research* 294 at 309–11. The inclusion of the deemed source rules in the 1967 UK Treaty was discussed at 5.89 at 5.91. In the case of the 1969 Japan Treaty, the deemed source rules in relation to public entertainers, discussed at 6.90, and *ITAA 1936* Divisions 14 and 15, discussed at 6.96, appear to be motivated by resolving doubts about source under Australian domestic law. The use of a deemed source rule in relation to dividends, discussed at 6.93, appears to be intended to ensure that double crediting did not arise.
97 See the discussion at 2.128 for the rationale given for adopting a credit article notwithstanding the Australian broad exemption for taxed foreign source other than dividends at the time.
98 See the discussion at 3.147.
99 See the discussion at 4.95, 4.106 and 4.118.
100 See the discussion at 6.38, 6.43, 6.45, 6.90, 6.93 and 6.96.
did not want to limit its source taxing rights in relation to capital gains should it introduce a capital gains tax in the future. In negotiating the 1969 Japan Treaty, Australia argued for the substitution of the word 'profits' for the phrase 'income (other than capital gains)' in the industrial or commercial profits article to avoid the politically embarrassing implication that income included capital gains.

**Domestic Law And Treaty Practice Of The Treaty Partner And Of Third Countries**

7.51 At several points there is evidence of technical features of a particular treaty being the result of following the treaty practice of Australia's treaty partner or of being a response to the domestic law of the treaty partner. In the case of the 1946 UK Treaty, it is difficult to distinguish between those features of the initial UK draft that reflected UK tax treaty practice and those that amounted to giving expression to the ministerial agreement discussed at 2.90. Possibly the variations from the 1945 UK-US Tax Treaty that were present in both the initial UK draft and in the initial UK proposals for a tax treaty with Australia reflect UK Tax Treaty practice at the time. The scope of the UK taxes against which Australian corporate and shareholder taxes could be credited was an example of the treaty partner's domestic law influencing Australian negotiation of this treaty.

7.52 The influence of the treaty partner's domestic law and treaty practice is more evident in the 1953 US Treaty. The US practice of taxing on the basis of citizenship affected the way 'resident' was defined, while the imposition of US withholding tax on royalties on a gross basis affected the form of the royalty article. Several provisions were included at the request of the United States because they were US tax treaty practice, with only some of them being carried over into subsequent Australian tax treaties.

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101 In relation to the 1967 Australia – UK Tax Treaty, see 5.34, 5.70, 5.119 to 5.120.
102 See the discussion at 6.81.
103 These would include the absence of a capital gains article and the absence of a non-discrimination article. Defining 'industrial or commercial profits' in exclusionary terms might also reflect UK tax treaty practice of the time, but it can also be analysed as a means of giving effect to the ministerial agreement discussed at 2.90. The initial UK proposals were discussed at 2.37 to 2.39. The absence of a capital gains article and of a non-discrimination article from the 1946 Australia – UK Tax Treaty were discussed at 2.102, 2.105, 2.106 and 2.107.
104 See the discussion at 2.129 to 2.130.
105 See the discussion at 3.31.
106 See the discussion at 3.63.
107 These included: the force of attraction provision (discussed at 3.46); the provisions relating to deductible expenses for calculating business profits (discussed at 3.47 and, as argued at 3.137, it is likely that this was included at the request of the US); residence basis for taxing shipping and aircraft profits (discussed at 3.49 to 3.50 – not a variation from the 1946 Australia – UK Tax Treaty but something that the US insisted was part of its tax treaty
Economic Considerations Relating To Current And Expected Trade And Investment Flows

7.53 This factor was less apparent but not absent at the technical drafting stage. It does explain Australia’s concern about credit overspill in the 1946 UK Treaty\textsuperscript{109} and in relation to the characterisation of Australian undistributed profits tax for US foreign tax credit purposes in the 1953 US Treaty.\textsuperscript{110} Similar concerns are also evident in the negotiation of the 1969 Japan Treaty.\textsuperscript{111}

Model Treaties And Policies Developed By International Organisations

7.54 Prior to the publication of the 1963 draft OECD Model, there is little evidence of models developed by international organisations, such as the League of Nations or the United Nations, influencing the technical drafting of Australian tax treaties. The only explicit reference in the technical drafting stage prior to 1963 is the mention by Willis of the League of Nations arm’s length principle for determining branch profits and the profits of associate enterprises. There is no direct evidence that the Australian negotiators were influenced by this argument, as it was raised in the context of their attempts to preserve the operation of ITAA 1936 s136.\textsuperscript{112} The first official Australian assessment of the 1963 draft OECD Model was generally negative,\textsuperscript{113} and the 1965 Australian model followed the 1963 OECD draft Model’s order of presentation but followed prior Australian tax treaties at a technical level.\textsuperscript{114} O’Reilly’s review of the 1966 UK draft noted several respects in which it followed the 1963 draft OECD Model but, in each case, regarded the 1965 Australian model as preferable.\textsuperscript{115} UK officials, but not Australian officials, did refer to the 1963 draft OECD Model as a reason for adopting particular provisions.\textsuperscript{116} In negotiating the practice); the reciprocal collection of taxes provision (discussed at 3.70); and the mutual agreement provision (discussed at 3.73).

\textsuperscript{108} The ‘force of attraction’ principle was not applied in the 1957 Australia – Canada Tax Treaty, although it had been included in the Australian draft sent to Canada and was applied in the 1960 Australia – NZ Tax Treaty. It was not applied in the 1965 Australian model nor in the 1968 draft sent to Japan. The assistance in collection provision was not included in the draft sent to Canada in 1953 nor in the 1965 Australian model nor in the 1968 draft sent to Japan.

\textsuperscript{109} As discussed at 2.129, Australia was concerned about credit overspill if Australian corporate and shareholder tax was not credited against UK excess profits tax in addition to income tax.

\textsuperscript{110} Australia’s concern was evident in McGovern’s report to Fadden, as discussed at 3.68 to 3.69; however, Australia was unsuccessful with this argument. As noted at 3.97, the drafter of the second draft had listed this as an issue for further discussion with US officials. As noted at 3.116, no changes giving effect to this request were made in the final draft of the treaty.

\textsuperscript{111} See the discussion at 6.44, 6.103 and 6.109.

\textsuperscript{112} See the discussion at 2.115 to 2.126. Willis’ reference the League of Nations principle is at 2.119.

\textsuperscript{113} Belcher’s review of the 1963 draft OECD Model was discussed at 4.57 to 4.84.

\textsuperscript{114} See in particular the discussion at 4.93 and 4.108.

\textsuperscript{115} See O’Reilly’s comments at 5.14 to 5.16, 5.27 and 5.38.

\textsuperscript{116} See the discussion at 5.55, 5.63, 5.68, 5.81, 5.98, 5.119 and 5.132.
1969 Japan Treaty, Australian officials, in instances where Japan argued for the draft OECD Model articles, preferred articles based on prior Australian tax treaty practice over OECD.117 Australia was not yet a member of the OECD, regarded the OECD Model as favouring capital exporting and maritime nations118 and preferred to follow drafting technicalities established in its earlier treaties even when these had been discarded by the other party to those treaties.119

The Development Of An Australian Model Tax Treaty

7.55 Prior to 1965, the 1953 US Treaty formed the basis of the Australian draft sent to Canada,120 and the 1957 Canada Treaty appears to have formed the basis for the 1960 NZ Treaty.

7.56 As discussed in Chapter 4, the first Australian ‘model’ tax treaty was finalised in 1965. That model largely represented a consolidation of prior Australian tax treaty practice but had an even heavier emphasis on source taxation than any prior Australian tax treaty. The 1965 Australian model was referred to by Australian officials in assessing the 1966 UK draft,121 in correspondence with UK officials122 and in negotiating the 1967 UK Treaty.

7.57 An Australian draft, developed in February 1968, was used in negotiating the 1969 Japan Treaty. That model was influenced by both the 1965 Australian model and the 1967 UK Treaty.123 Australian politicians and officials clearly regarded the 1967 UK Treaty as forming the basis for the 1968 Australian draft. They also regarded the 1969 Japan Treaty as conforming to the 1968 Australian draft in important respects,124 although it also refined some provisions in that treaty and, in some

117 See the discussion at 6.41 and 6.42.
118 See the discussion at 7.35 and accompanying notes.
119 An example can be seen in the 1967 UK Treaty where the UK draft of September 1966 was closer to the 1963 draft OECD Model than the final treaty was, and where O'Reilly and the Memorandum in analysing the UK draft compared it with the 1946 UK Treaty, with other earlier Australian treaties and with the 1965 Australian model.
121 See the discussion of this aspect of O'Reilly's letter to Randall and of the Memorandum at 5.14 and 5.30.
122 As discussed at 5.56, Cain's letter to Johnson enclosed the definition of 'permanent establishment' in the Australian model.
123 Respects in which the 1968 Australian draft differed from or followed the 1965 Australian model and/or the 1967 Australia – UK Tax Treaty were discussed in detail at 6.34 to 6.51.
124 Cain's report to McMahon in February 1968, discussed at 6.71, identified the important respects in which the initialled draft for the 1969 Australia – Japan Tax Treaty followed the 1967 Australia – UK Tax Treaty. These were the articles dealing with 'permanent
respects, either reverted to earlier Australian treaty practices or extended source basis taxation beyond what had been agreed to in the 1967 UK Treaty.\textsuperscript{125}

\textit{International Tax Policy Considerations}

\textbf{7.58} Throughout the period, the clearly dominant international tax policy consideration that affected detailed drafting was the primacy of source basis taxation.\textsuperscript{126} While other broad policy considerations can be identified in arguments put by Australian officials, recognisable international tax policy nomenclature is not used for them by Australian officials in this period. Australia’s argument for preserving source country taxing rights in relation to undistributed profits was put in terms of equivalent treatment for different forms of business organisation.\textsuperscript{127} Australia’s arguments in relation to foreign tax credits were, at times, that investing in Australian companies should not be disadvantaged when compared with investing in foreign companies. This was consistent with capital export neutrality but was not expressed in those terms.\textsuperscript{128}

\textit{The Australian Approach To Negotiation And Drafting Of Detailed Provisions}

\textbf{7.59} During the detailed drafting of the 1946 UK Treaty, Australia began an approach to negotiation and drafting of detailed provisions which evolved into a practice of seeking comments from ATO Deputy Commissioners, Parliamentary Draftsmen and the Department of External Affairs.\textsuperscript{129} The involvement of Parliamentary Draftsmen appears to have produced an approach to drafting consistent with the legalistic, detailed and specific approach used for Australian domestic law at the time. ATO Deputy Commissioners typically noted respects in which the interaction of a tax treaty with domestic law was problematic and contributed to the inclusion in Australian

\begin{itemize}
  \item establishment’, ‘interest’, ‘dividends’ and ‘royalties’, the 10% ownership requirement for underlying foreign tax credits, the rates of source taxation on dividends and omitting the ‘non-discrimination’ article.
  \item The respects in which the 1969 Australia – Japan Tax Treaty refined provisions in the 1967 Australia – UK Tax Treaty were summarised at 6.113. The respects in which the 1969 Australia – Japan Tax Treaty reverted to earlier Australian idiosyncrasies or further extended source country taxing rights were summarised at 6.114.
  \item See the discussion at 2.160 to 2.165, 3.130 to 3.137, 3.147 to 3.150, 5.157, 5.160 and 6.113 to 6.114.
  \item See the discussion at 2.63.
  \item See the discussion at 2.133.
  \item The general approach used in negotiating and drafting the 1946 Australia – UK Tax Treaty was described at 2.167. The Commonwealth Crown Solicitor and the Solicitor-General were involved in drafting that treaty, but there is no evidence of direct involvement by Parliamentary Draftsmen. The practice of seeking comments on drafts from Deputy Commissioners was continued in negotiating and drafting the 1953 Australia – US Tax Treaty as described at 3.75 (the involvement of the former Crown Solicitor in the drafting of that treaty was identified at note 135 and the involvement of Parliamentary Draftsmen was discussed at note 136).
\end{itemize}
treaties of provisions aimed at counteracting these problems.\textsuperscript{130} Australian negotiating delegations of the period typically included high-ranking Australian Taxation Office officials and officials from the Crown Solicitor’s office. From the 1967 UK Treaty onwards, Australian Treasury officials were involved in negotiations.\textsuperscript{131}

\textit{Drafting Style And Preference For Clarity, Brevity and Familiarity of Language}

\textbf{7.60} While there is some evidence of the influence of these factors in earlier Australian tax treaties, they were a significant influence in the development of the 1965 Australian model. A consistent theme in Ross’ comments when comparing the revised Australian draft with the 1963 draft OECD Model is that the Australian draft was more specific and concise.\textsuperscript{132} Although familiarity of language probably influenced the 1967 UK Treaty, these factors are not explicitly mentioned either in correspondence or in the record of negotiations. Explicit mention of precision of language does occur, however, in negotiating the 1969 Japan Treaty.\textsuperscript{133}

\textbf{Question 3:} What variations in Australian taxation treaties from the OECD Model should be discontinued in future Australian treaty practice, having regard to the original reason why those variations were introduced and subsequent changes in circumstances relevant to Australian taxation treaty practice and policy?

\textsuperscript{130} A good example of the type of comments by Parliamentary Draftsmen can be seen in the comments on the second draft of the 1953 Australia – US Tax Treaty discussed at 3.79 to 3.103 and in the comments on the second draft of the 1969 Australia – Japan Tax Treaty discussed at 6.79 to 6.98.

\textsuperscript{131} The delegations involved in negotiating and drafting the 1946 Australia – UK Tax Treaty were described at 2.45, 2.81 and 2.96. The Australian delegation for the Canberra negotiations leading to the 1953 Australia – US Tax Treaty was described at 3.30, and the Australian delegation for the Washington negotiations was described at 3.104. The Australian delegation involved in negotiating the 1967 Australia – UK Tax Treaty was described at 5.75. It should be noted that negotiations in relation to that treaty were only held in Australia. The delegation sent to Tokyo for preliminary talks in 1962 was described at 6.4. The Australian delegation for the negotiations in Canberra in 1968 was described at 6.35. The Australian delegation for the negotiations in Tokyo in 1968 was described at 6.108.

\textsuperscript{132} See 4.109 where Ross indicates that he prefers Belcher’s draft as being more specific than the OECD draft and describes the OECD draft as containing ‘a waste of roundabout verbiage’ in many areas. See also Ross’ comments on the residence tie-breakers in the draft OECD Model at 4.110 to 4.111. As discussed at 4.114, Ross also commented that the OECD Draft Article 5(3) took four paragraphs to cover what was dealt with (‘on a verbally more economic and more readily intelligible basis’) by the single Taxation clause.

\textsuperscript{133} As discussed at 6.41, O’Reilly responded to a Japanese suggestion that the simpler OECD definition of ‘industrial or commercial profits’ be adopted by saying that ‘simpler meant looser’. The redraft, discussed at 6.84, of the associated enterprises article was intended to remove a possible ambiguity. A desire for precision in drafting of paragraph 2 of the Protocol was discussed at 6.97.
7.61 Paragraph 1.35 noted Vann’s argument that when Australia joined the OECD in 1971 it carried its previous treaty practices with it, resulting in an Australian tax treaty practice characterised by an extreme source position for an OECD country and language oddities maintained even where the OECD terminology produced similar results. As summarised in this chapter, the examination of archival material relating to the negotiation and drafting of Australian tax treaties in the period 1946 to 1969 is consistent with Vann’s argument.

7.62 Revenue considerations and an emphasis on source basis taxation were invariably found to be the principal factors motivating both the overall balance of the bargain in a tax treaty and the detail of provisions which varied from the OECD Model when those variations were sought by Australia. Even in instances where a variation was not initiated by Australia, revenue considerations and an emphasis on source basis taxation were significant factors influencing its continued adoption by Australia in subsequent tax treaties. While it is conceivable that the maintenance of these variations since 1971 has been due to factors other than these and to bureaucratic inertia, such other factors have not been publicly expressed.

7.63 While less emphasis has been placed on source basis taxation in Australian tax treaties since the 2001 Protocol to the Australia – US Tax Treaty, there are several respects in which Australian tax treaties continue to provide greater scope for source basis taxation than does the OECD Model. This is particularly so in the broader definition of ‘permanent establishment’ typically found in Australian tax treaties. Whether or not variations giving greater scope for source basis taxation should be continued into the future is a policy question that hinges partly on an assessment of the present and likely future balance between inbound and outbound capital flows affecting Australia. Although Australia remains a net capital importer, as Vann has pointed out, when investment flows trend towards balance, a country does not give up revenue by treaty decreases in source taxation as these are counterbalanced by increased revenue from residence taxation.134 A separate but related question is whether any revenue loss from a reduction in source country taxing rights is counterbalanced by increased inbound investment and consequential increased economic growth. Policy evaluation would also need to take into account changes in the Australian and global economies affecting methods of conducting business and the relative significance of industries, particularly the shift from tangibles to intangibles and the provision of services.

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134 This aspect of Vann’s argument was discussed at 1.33.
7.64 Both of the policy questions identified in 7.63 need to be assessed on the basis of economic data and analysis and, in that respect, are beyond the scope of this thesis. The contribution of this thesis to these questions has been to highlight the origins of these variations from the OECD Model and the influence of an emphasis on the primacy of source basis taxation and revenue considerations in their development. Awareness of the probable origins of these provisions and of the influence of these policy objectives in their development should assist policymakers in deciding whether to continue these provisions if an assessment is made that inbound and outbound capital flows are likely to be more balanced in the future and/or if the assessment is made that increased inbound investment and economic activity will offset any revenue losses consequent on a reduction in source country taxing rights. 7.65 While revenue considerations and an emphasis on source basis taxation have arguably been the dominant factors affecting the detail of provisions varying from the OECD Model, familiarity with earlier forms of drafting coupled with a view that those forms were both clearer and more specific has been found to be a factor influencing those variations. As Vann has pointed out, however, the difficulty with exceptionalism of this type is that the OECD Commentary becomes less useful as an aid to interpretation of these aspects of Australian tax treaties. It is submitted that, if an assessment is made to discontinue variations from the OECD Model on the basis of the assessments referred to in 7.64, then continuity with prior Australian drafting style does not, of itself, constitute a sound reason for maintaining that practice and drafting style. On the contrary, harmonising the drafting of Australian treaties with OECD drafting as much as possible, should enable greater use to be made of the OECD Commentary in interpreting Australian tax treaties with the effect that Australian tax treaties are interpreted more consistently with international practice. Interpreting Australian tax treaties consistently with international practice is would produce greater certainty for individuals and businesses engaged in cross border activities and, for that reason alone, should be seen as desirable.

7.66 A third category of variations from the OECD Model is those variations that were originally intended to preserve the operation of provisions in domestic law which have since been either repealed or amended. The variation that most obviously fits into this category is the provisions in the business profits and associated enterprises articles which preserve the operation of domestic law where the information available

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135 Vann’s arguments in relation to this point were discussed at 1.36 and 1.37.
is not adequate to determine an arm’s length price. This variation originated in the negotiation of the 1946 UK Treaty and was inserted to preserve the operation of former *ITAA 1936* s136. As discussed at 2.115, former s136 was a provision which allowed the Commissioner to determine the taxable income of a company controlled by non-residents when the company either produced no taxable income or produced less taxable income than might be expected from the business.

7.67 Former *ITAA 1936* s136 was replaced by transfer pricing provisions in *ITAA 1936* Division 13 in 1982. In 2012, *ITAA 1997* Sub-division 815-A was added, which operated concurrently with Division 13. In 2013, Division 13 was repealed and Sub-division 815-A ceased to have effect.136 Currently, *ITAA 1997* Sub-divisions 815-B (between separate entities) and 815-C (between a permanent establishment and the rest of a single entity) are the relevant transfer pricing provisions in Australian domestic law that apply in both treaty and non-treaty cases.

7.68 Under the current transfer pricing rules for separate entities, arm’s length conditions are substituted for actual conditions where the actual conditions produce a transfer pricing benefit as defined137 and effectively similar results are achieved by for profits of a permanent establishment. *ITAA 1997* s815-135 and s815-235 require that Sub-divisions 815-B and 815-C respectively are to be applied so as to best achieve consistency with the OECD Transfer Pricing Guidelines and the Commentary on the OECD Model. Hence, the negation of a transfer pricing benefit under Australian domestic transfer pricing law where a bilateral tax treaty is applicable is contingent on an assessment that relies on concepts and methodologies set out in the relevant bilateral tax treaty, in the OECD Model and in the OECD Transfer Pricing Guidelines. Unlike the previous law, it does not depend on a determination being made by the Commissioner. In addition, where the operation of Sub-division 815-B or of Sub-division 815-C is inconsistent with a relevant Australian bilateral tax treaty, the treaty rules will prevail.138 Hence, it is considered that the provisions in all current Australian tax treaties which preserve the operation of domestic law in the business profits and associated enterprises articles where information is inadequate to determine an arm’s length price, aimed as they originally were at protecting a discretionary power.

137 The broad effect of the current Australian rules is discussed in *Tax Laws Amendment (Countering Tax Avoidance and Multilateral Profit Shifting) Bill 2013*, Explanatory Memorandum, paras 2.16 to 2.31.
138 This is the effect of s4(2) of the *International Tax Agreements Act 1953*. Because the new transfer pricing rules are closely modelled on the language of tax treaty provisions, there is unlikely to be significant differences in operation and hence any need for a tax treaty to limit the domestic law provisions.
are otiose. It is noted that the 2015 German Treaty, which is not yet in force, does not contain provisions that preserve the operation of domestic law in the business profits and associated enterprises articles where information is inadequate to determine an arm’s length price. If the omission of provisions of this nature is to be Australian policy in the future, then it would be consistent with the analysis in this thesis of the origins of provisions of this nature and of current Australian transfer pricing provisions. More generally, it is submitted that there is little point in continuing in Australian tax treaties with variations from the OECD Model which were intended to protect features of Australian domestic law which are no longer operative and where subsequent developments in Australian law have effectively rendered the tax treaty provision otiose.

7.69 An ongoing oddity in Australian tax treaties is the presence of deemed source rules. While in some instances these apply only to specific categories of income, in no case is the deeming entirely confined to the credit article. In the 2015 German Treaty, a deemed source rule applies for Australian law generally and a separate deeming of Australian source is made in the credit article. The better view is that the effect of the deemed source rule is that the treaty rule interacts with domestic law so that tax is levied under domestic law when it would not be in the absence of the treaty. Part of Australian thinking behind the deemed source rule appears to have been to resolve doubts about the source of particular types of income under domestic law. There is also evidence in the negotiations reviewed in this thesis of deemed source rules being seen as needed to ensure the effective functioning of credit articles.

139 The variations on deemed source rules in Australian tax treaties are summarised in Appendix 7. Note that ‘double deeming’ (for the purposes of Australian or both contracting states’ law and deeming for credit purposes) is common. Arguably, where ‘double deeming’ occurs the intent of the drafting is that the first deeming is for purposes of the particular contracting state’s tax law generally (other than credit purposes) and not for credit purposes, which is specifically dealt with by the second deeming.

140 A deemed source rule is contained in paragraph 1 of the Protocol to the 2015 German Treaty signed on 12th November 2015. The influence of pre 1971 Australian tax treaty practice is still evident in the 2015 German Treaty. As shown in Appendix 3, at least 13 variations in that treaty from the current OECD Model can be found in Australian tax treaties entered into prior to 1971.


142 See, in particular the discussion at 5.25 and 5.90–5.91 dealing with the deemed source rule in the case of public entertainers.

143 For example, as discussed at 3.67, this was the justification for deemed source rules given by McGovern in relation to deemed source rules for services, films and insurance in the 1953 US Treaty.
limit the scope of credit obligations, and to avoid dual crediting. Both the rationale of resolving doubts about source and the rationale of ensuring the appropriate operation of provisions aimed at preventing international double taxation can be seen in one of the rare statements by a relevant Australian minister about Australian tax treaty policy. The former rationale is devoid of any policy justification. If Australia wants to expand its concept of source to match deemed source rules in its tax treaties, then it can do so through domestic legislation. Irrespective of the merits of the latter rationale, it would be better implemented either by systematically confining the operation of the deemed source rule to the credit article or by providing in the treaty that Australia has the right to amend its domestic law to deem particular items dealt with in the treaty to have an Australian source.

Finally, following the release of the OECD/G20 Final Recommendations on BEPS (Base Erosion and Profit Shifting), this is a propitious time for a reassessment of variations in Australian tax treaty practice and policy from the OECD Model. At a minimum, the BEPS Final Recommendations will involve changes in the OECD Commentary, and their non-binding recommendations on treaty practice and

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144 See the discussion at 6.47 of the Japanese argument for freezing source rules so as to limit the liability of the residence country to give credit.

145 Most explicitly in the drafter’s comments on the 1969 Japan Treaty on the deemed source rule for dividends as discussed at 6.93. Earlier, as discussed at 2.146, unrelied double taxation of dividends had been perceived to be a problem where the paying company was a dual resident.

146 In announcing a 2008 review of tax treaty policy, the then Assistant Treasurer and Minister for Competition Policy and Consumer Affairs (Chris Bowen) stated: ‘Deemed source rules are included to ensure that a country can exercise the taxing rights allocated to it under the treaty and to ensure appropriate double tax relief by the other country’. The Hon. Chris Bowen MP, Assistant Treasurer, Minister for Competition Policy and Consumer Affairs, Media Release 25/01/2008 No. 004, ‘Australia’s Tax Treaty Negotiation Policy’, 25th January 2008.

147 As Vann notes, above note 141, this approach was taken under paragraph 3 of the Protocol to the 1972 German Treaty, and the power given by the treaty was exercised by s11(3) of the Income Tax International Agreements Act 1953 (Cth).


149 For example, changes to the Commentary are envisaged in the recommendations on hybrid entities (OECD BEPS Final Report, Action 2 – Neutralising the Effects of Hybrid Mismatch Arrangements, para 438) and in the recommendations on artificial avoidance of PE status (OECD BEPS Final Report, Action 7 – Preventing the Artificial Avoidance of Permanent Establishment Status, pp15–44).

150 For example, the OECD BEPS Final Report, Action 7 includes recommendations for changes to the definition of ‘permanent establishment’ (restricting the ‘preparatory or auxiliary’ exception to the definition of PE and an anti-fragmentation rule) and OECD BEPS Final Report, Action 2 includes recommendations for resolving dual residence on a case-by-case basis rather than through dual residence tie-breakers. These will all need to be considered by tax treaty negotiators. As shown in Appendix 3, some provisions in the 2015 German Treaty appear to anticipate these recommendations. While the broader definition of ‘permanent establishment’ in Australian treaties is in some respects consistent with these recommendations, some particular Australian variations (for example, AV6 and AV10, both of
domestic law will need to be considered by Australian negotiators, policy advisors and legislators respectively. The danger is that any adjustments to Australian tax treaty policy and practice will be confined to those actions directly relevant to BEPS recommendations. If so, the result would be a curious hybrid treaty policy and practice that responds to current recommendations while reproducing, possibly merely through bureaucratic inertia, features that developed to deal with issues of former times. As Bruner has argued, the fundamental insight of the BEPS project has been that ‘international coordination of tax policies is a condition for the success of any substantial reform’, which is, Bruner notes, in stark contrast to the current competition-based international tax regime. In Australia’s case, the contrast is particularly stark between a xenophobic historical policy of maximising revenue through excessive source claims and one of international collaboration and cooperation aimed, at least officially, at increasing global welfare. A comprehensive reassessment of variations in Australian tax treaty policy and practice from OECD norms would produce a treaty policy and practice that is consistent with what should be Australian responses to the BEPS recommendations. It is hoped that this thesis will be a resource that assists in such a review.

LIMITATIONS OF THE RESEARCH

7.71 Several limitations of the research conducted in this thesis should be noted.

7.72 First, as pointed out at 7.2, the existence of variations from the OECD Model in Australian tax treaties up to and including the 1969 Japan Treaty does not necessarily explain the occurrence of those variations in subsequent and currently operative Australian tax treaties. A more definitive explanation based on archival material would require examination of archival materials relating to each currently operative subsequent Australian tax treaty. Considerations of length and of the

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151 For example, the recommendations in OECD BEPS Final Report, Action 3 – Designing Effective Controlled Foreign Company Rules (particularly the recommendation at para 51 – Australian rules do not contain a tax rate exemption as such – and the recommendations at para 111 – Australian rules apply different tests for control and for attribution) and in OECD (particularly the recommendations for a best practice approach at paras 22–31 – Australian rules are not based on limiting interest deductions to a fixed percentage of EBITDA) are inconsistent with current Australian domestic law. Arguably, these domestic law rules should be reconsidered in the light of these recommendations. It should be noted, however, that this view is not shared by the Australian Treasurer at the time of writing. The Hon. Scott Morrison MP, Treasurer of the Commonwealth of Australia, Media Release, 6th October 2015, OECD Report Supports Australian Government Action on Multinational Tax Avoidance.

availability of relevant archival materials have meant that such examination was not possible in this thesis.

7.73 Second the archival materials examined have all been contained in official files of one or more governments. Reference has not been made to personal diaries or written recollections of officials and officials involved in the negotiation of treaties have not been interviewed. It is possible that there may be ‘non-official’ explanations for actions taken in negotiating and drafting Australian tax treaties between 1946 and 1971 which are not disclosed in official records.

7.74 Third none of the archival records in relation to the treaties discussed in the thesis can be said to be entirely complete. Significant records from relevant Australian and United Kingdom departments were examined in relation to the 1946 UK Treaty and the 1967 UK Treaty but even there some files were missing and some parts of files were missing. In the case of the 1953 US Treaty and the 1957 Canada Treaty while significant Australian files were able to be examined only limited US and Canadian files were able to be located and examined. In the case of the 1969 Japan Treaty only Australian files were examined. In addition archival materials, even when available, did not always contain direct comment on the reason for a particular variation from the OECD Model and, in some instances, contained somewhat cryptic comments which had to be interpreted by reference to their context.

7.75 Despite these limitations it is submitted that the analysis of the individual treaties and the conclusions made in this chapter in relation to the central questions investigated in this thesis are based reasonable inferences derived from the archival materials that have been available to me.

AREAS FOR FUTURE RESEARCH

7.76 The methodology used in this thesis could, as archival materials become more available, be adopted for researching subsequent Australian treaty policy and practice and the treaty policy and practices of other countries. Natural successors to the research in this thesis using materials that should now be available would be how Australian tax treaty policy and practice was affected by subsequent events such as: Australia’s 1971 OECD membership; the increased importance of Asia to the Australian economy; and the effect of the fall of the Soviet Union and the Warsaw Pact. The methodology could also be applied to other more confined or thematic approaches such as: how Australian and New Zealand tax treaty policy and practice influenced each other; distinctive characteristics of Australian tax treaties with what were then less developed countries starting with the 1969 Singapore Treaty; and an
examination of subsequent instances where Australian tax treaties contained deemed source rules. One of the distinctive features of Australian treaties continues to be the use of a ‘substantial equipment’ provision. A substantial equipment provision first appears to have been used in a bi-lateral tax treaty in the 1950 Protocol to the 1942 United States – Canada Tax Treaty. Further examination of archival records relating to the negotiation of that Protocol could be undertaken to try to resolve more firmly the question of who initiated the inclusion of the provision and why they did so. Subsequent Australian tax treaties for which archival materials should be available and which would merit further research would be the 1980 Canada Treaty (the first Australian treaty not to include some of the structural features of the ‘colonial’ or ‘baby boomer’ model); and the 1982 US Treaty being a treaty with a major trading and investment partner and the first Australian treaty containing a ‘non-discrimination’ article albeit one which at the time was not given the force of law in Australia.
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### APPENDIX ONE

**CHRONOLOGICAL TABLE OF AUSTRALIAN COMPREHENSIVE TAX TREATIES, AMENDING PROTOCOLS, EXCHANGES OF NOTES, AND EXCHANGES OF LETTERS**

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</tr>
</tbody>
</table>
| 31/08/1989 | 27/12/1989 | Applies from 1/01/1990               | Thailand | *Income Tax (International Agreements) Amendment Bill (No2) 1989*  
|          |            | In force                             |          | *s5 IT(IA) Act 1953*       |
| 16/10/1989 | 16/10/1989 | Exchange of notes                     | Singapore | N/A                        |
|          |            | In force                             |          |                            |
| 18/10/1989 | 5/01/1990  | Amending protocol                    | Singapore | *Income Tax (International Agreements) Amendment Bill (No2) 1989*  
|          |            | In force                             |          | *s7 IT(IA) Act 1953*       |
|          |            | In force                             |          | *s5 IT(IA) Act 1953*       |
| 15/10/1990 | 28/12/1990 | Applies from 1/01/1991               | Fiji     | *Taxation Laws Amendment (International Agreements) Bill 1990*  
<p>|          |            | In force                             |          | <em>s5 IT(IA) Act 1953</em>       |
|          |            | In force                             |          |                            |</p>
<table>
<thead>
<tr>
<th>Date</th>
<th>Date</th>
<th>Applies from</th>
<th>Country</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>7/05/1991</td>
<td>4/03/1992</td>
<td>1/01/1993</td>
<td>Poland</td>
<td><em>Income Tax (International Agreements) Amendment Bill (No2) 1991</em></td>
</tr>
<tr>
<td>Date</td>
<td>In force</td>
<td>Country</td>
<td>Description</td>
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<td>----------------------------------------------------------------------------</td>
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</tbody>
</table>
| 27/01/1995 | 29/03/1995     | New Zealand       | Applied from 1/04/1995
Terminated 19/3/2010 | **Income Tax (International Agreements) Amendment Bill 1995**
Former Schedule 4 to IT(IA) Act 1953 |
In force                                           | **International Tax Agreements Amendment Bill 1995**
s5 **ITA Act 1953** |
| 29/05/1996 | 21/10/1996     | Taipei            | Applies from 1/12/1996
In force                                           | **Taxation Laws (International Tax Agreements) Bill 1996**
s5 and s11ZF **ITA Act 1953** |
In force                                           | s5 and s11ZCA **ITA Act 1953** |
Applies 1/07/2001                                    | **International Tax Agreements Amendment Bill (No1) 2000** |
<table>
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<th>Date</th>
<th>Date</th>
<th>Event</th>
<th>Country</th>
<th>Text</th>
</tr>
</thead>
<tbody>
<tr>
<td>7/08/98</td>
<td>6/09/98</td>
<td>Exchange of notes</td>
<td>Norway</td>
<td>N/A</td>
</tr>
<tr>
<td>1/07/99</td>
<td>21/12/99</td>
<td>Applies from 1/01/2000</td>
<td>South Africa</td>
<td>International Tax Agreements Amendment Bill 1999 s5 ITA Act 1953</td>
</tr>
<tr>
<td>24/08/99</td>
<td>22/12/99</td>
<td>Applies from 1/01/2000</td>
<td>Slovakia</td>
<td>International Tax Agreements Amendment Bill 1999 s5 ITA Act 1953</td>
</tr>
<tr>
<td>20/08/99</td>
<td>27/06/000</td>
<td>Amending protocol N/A</td>
<td>Malaysia</td>
<td>International Tax Agreements Amendment Bill 1999 ss11F and 11FA ITA Act 1953</td>
</tr>
<tr>
<td>29/08/99</td>
<td>30/12/99</td>
<td>Applied from 1/01/2000</td>
<td>Argentina</td>
<td>International Tax Agreements Amendment Bill 1999 s5 and s11ZI ITA Act</td>
</tr>
<tr>
<td>9/11/99</td>
<td>27/06/000</td>
<td>Exchange of letters</td>
<td>Malaysia</td>
<td>International Tax Agreements Amendment Bill 1999</td>
</tr>
<tr>
<td>Date</td>
<td>Date</td>
<td>Applies from</td>
<td>Country</td>
<td>Text</td>
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<tr>
<td>2/02/2000</td>
<td>11/04/2001</td>
<td>1/01/2002</td>
<td>Romania</td>
<td><em>International Tax Agreements Amendment Bill (No1) 2000</em></td>
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<td></td>
<td><em>s5 ITA Act 1953</em></td>
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<td><em>s5 ITA Act 1953</em></td>
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<tr>
<td>27/09/2001</td>
<td>13/05/2003</td>
<td>1/07/2003</td>
<td>United States</td>
<td><em>International Tax Agreements Amendment Bill (No1) 2002</em></td>
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<td></td>
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<td></td>
<td></td>
<td><em>ss6 and 20 ITA Act 1953</em></td>
</tr>
<tr>
<td>23/01/2002</td>
<td>18/12/2002</td>
<td></td>
<td>Canada</td>
<td><em>International Tax Agreements Amendment Bill (No2) 2002</em></td>
</tr>
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<td></td>
<td></td>
<td>Amending Protocol</td>
<td></td>
<td><em>s5 ITA Act 1953</em></td>
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<td></td>
<td></td>
<td>Applies from 1/01/2003</td>
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<td>In force</td>
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<td>2nd Amending Protocol</td>
<td></td>
<td><em>ss11F and 11FB ITA Act 1953</em></td>
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<td></td>
<td></td>
<td>And exchange of letters</td>
<td></td>
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<tr>
<td>Date</td>
<td>Date</td>
<td>Description</td>
<td>Country</td>
<td>Notes</td>
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<tr>
<td>5/08/2002</td>
<td>11/02/2002</td>
<td>Exchange of letters</td>
<td>Vietnam</td>
<td>N/A</td>
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<td></td>
<td></td>
<td>In force</td>
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<tr>
<td>9/09/2002</td>
<td>31/12/2003</td>
<td>Applies from 1/01/2004</td>
<td>Mexico</td>
<td><em>International Tax Agreements Amendment Bill 2003</em></td>
</tr>
<tr>
<td></td>
<td></td>
<td>In force</td>
<td></td>
<td>s5 <em>ITA Act 1953</em></td>
</tr>
<tr>
<td>21/08/2003</td>
<td>17/12/2003</td>
<td>Applies from 1/07/2004</td>
<td>United Kingdom</td>
<td><em>International Tax Agreements Amendment Bill 2003</em></td>
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<td></td>
<td></td>
<td>In force</td>
<td></td>
<td>s5 <em>ITA Act 1953</em></td>
</tr>
<tr>
<td>15/11/2005</td>
<td>22/01/2007</td>
<td>Amending protocol</td>
<td>New Zealand</td>
<td><em>International Tax Agreements Amendment Bill (No1) 2006</em></td>
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<tr>
<td></td>
<td></td>
<td>Terminated 19/3/2010</td>
<td></td>
<td>Schedule 4A to <em>ITA Act 1953</em></td>
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<tr>
<td>20/06/2006</td>
<td>1/6/2009</td>
<td></td>
<td>France</td>
<td><em>International Tax Agreements Amendment Bill (No1) 2007</em></td>
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<td></td>
<td>1/1/2010</td>
<td>In force</td>
<td></td>
<td>s5 <em>ITA Act 1953</em></td>
</tr>
<tr>
<td>Date</td>
<td>Date</td>
<td>In force</td>
<td>Country</td>
<td>Agreement Details</td>
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<tr>
<td>31/01/2008</td>
<td>3/12/2008</td>
<td>Applies from 1/1/2009</td>
<td>Japan</td>
<td>International Tax Agreements Amendment Bill (No1) 2008 &lt;br&gt;s5 ITA Act 1953</td>
</tr>
<tr>
<td>24/06/2009</td>
<td>19/03/2010</td>
<td>Applies from 1/5/2010</td>
<td>New Zealand</td>
<td>International Tax Agreements Amendment Bill (No1) 2010 &lt;br&gt;s5 ITA Act 1953</td>
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<tr>
<td>24/06/2009</td>
<td>12/05/2014</td>
<td>NA</td>
<td>Belgium</td>
<td>Schedule 13B to IT(I)A Act 1953 &lt;br&gt;s5 ITA Act 1953</td>
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<tr>
<td>8/9/2009</td>
<td>22/12/2010</td>
<td>22/12/2010</td>
<td>Singapore</td>
<td>s7 ITA Act 1953</td>
</tr>
<tr>
<td>Date</td>
<td>Date</td>
<td>Life</td>
<td>Country</td>
<td>Agreement/Protocol</td>
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<tr>
<td>24/02/2010</td>
<td>8/8/2011</td>
<td>NA</td>
<td>Malaysia</td>
<td>s11F ITA Act 1953</td>
</tr>
<tr>
<td>10/03/2010</td>
<td>8/2/2013</td>
<td>Applies from</td>
<td>Chile</td>
<td>International Tax Agreements Amendment Bill (No1) 2011</td>
</tr>
<tr>
<td>28/4/2010</td>
<td>5/6/2013</td>
<td>Applies to withholding tax from</td>
<td>Turkey</td>
<td>International Tax Agreements Amendment Bill (No1) 2011</td>
</tr>
<tr>
<td>16/12/2011</td>
<td>2/4/2013</td>
<td>NA</td>
<td>India</td>
<td></td>
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<tr>
<td>30/7/2013</td>
<td>14/10/2014</td>
<td>Applies from</td>
<td>Switzerland</td>
<td>International Tax Agreements Amendment Bill 2014</td>
</tr>
<tr>
<td>Date</td>
<td>In force</td>
<td>In force</td>
<td>Country</td>
<td>Status</td>
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<tr>
<td>12/11/15</td>
<td>Not yet in force</td>
<td>Not yet in force</td>
<td>Germany</td>
<td>NA</td>
</tr>
</tbody>
</table>
APPENDIX 2

CURRENT AUSTRALIAN RESERVATIONS IN RELATION TO THE OECD MODEL TAX CONVENTION

Article 2

Australia reserves its position on that part of paragraph 1 which states that the Convention shall apply to taxes on capital.

Article 5 Paragraph 1

Australia reserves the right to treat an enterprise as having a permanent establishment in a State if it carries on activities relating to natural resources or operates substantial equipment in that State with a certain degree of continuity, or a person – acting in that State on behalf of the enterprise – manufactures or processes in that State goods or merchandise belonging to the enterprise.

Article 5 Paragraph 3

Australia reserves its position on paragraph 3, and considers that any building site or construction or installation project which lasts more than six months should be regarded as a permanent establishment.

Australia reserves the right to treat an enterprise as having a permanent establishment in a State if it carries on in that State supervisory or consultancy activities for more than 183 days in any twelve month period in connection with a building site or construction or installation project in that State.

Article 6

Australia reserves the right to include rights relating to all natural resources under this Article.

Article 7

Australia reserves the right to include a provision that will permit its domestic law to apply in relation to the taxation of profits from any form of insurance.

Australia reserves the right to include a provision clarifying its right to tax a share of business profits to which a resident of the other Contracting State is beneficially entitled where those profits are derived by a trustee of a trust estate (other than certain unit trusts that are treated as companies for Australian tax purposes) from the carrying on of a business in Australia through a permanent establishment.

Australia reserves the right to propose in bilateral negotiations a provision to the effect that, if the information available to a competent authority of a Contracting State is inadequate to determine the profits to be attributed to a permanent establishment of an enterprise, the competent authority may apply to the enterprise for that purpose the provisions of the taxation law of that State, subject to the qualification that such law will be applied, so far as the information available to the competent authority permits, in accordance with the principles of this Article.

Article 8

Australia reserves the right to tax profits from the carriage of passengers or cargo taken on board at one place in Australia for discharge in Australia.
Article 9

Australia reserves the right to propose a provision to the effect that, if the information available to a competent authority of a Contracting State is inadequate to determine the profits to be attributed to a permanent establishment of an enterprise, the competent authority may apply to the enterprise for that purpose the provisions of the taxation law of that State, subject to the qualification that such law will be applied, so far as the information available to the competent authority permits, in accordance with the principles of this Article.

Article 12

Paragraph 1

Australia reserves the right to tax royalties at source.

Paragraph 2

Australia reserves the right to amend the definition of royalties to include payments or credits which are treated as royalties under its domestic law.

Australia reserves the right, in order to fill what it considers to be a gap in the Article, to propose a provision defining the source of royalties by analogy with the provisions of paragraph 5 of Article 11, which deals with the same problem in the case of interest.

Article 21

Australia reserves its position on this Article and would wish to maintain the right to tax income arising from sources in its own country.

Article 24

Australia reserves the right to propose amendments to ensure that Australia can continue to apply certain provisions of its domestic law relating to deductions for R&D and withholding tax collection.
APPENDIX 3: VARIATIONS IN CURRENTLY OPERATIVE AUSTRALIAN TAXATION TREATIES FROM THE OECD MODEL CONVENTION ON INCOME AND CAPITAL

The focus of the thesis is on articles with direct relevance to cross border investment by multinational enterprises. For this reason this Table not consider articles in the current or former OECD Models dealing with: Independent Personal Services (former OECD Art 14); Income From Employment (OECD Art 15); Pensions (OECD Art 18); Government Service (OECD Art 19); Students (OECD Art 20); Members of Diplomatic Missions And Consular Posts (Art 27 then 28); Territorial Extension (OECD Art 28 then 29); Entry into Force (OECD Art 29 then 30); and Termination (OECD Art 30 then 31).

<table>
<thead>
<tr>
<th>OECD Model Article Variation Number</th>
<th>Variation In Australian Treaties</th>
<th>Current Treaties Where Variation Appears</th>
<th>Earliest Instance Of Variation</th>
<th>Most Recent Instance Of Variation</th>
<th>UN Equivalent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 2(1) AV1</td>
<td>Not included in Australian Treaties (23 exceptions)</td>
<td>All Australian treaties with the exception of the 1982 Australia – Italy Tax Treaty, the 2013 Swiss Treaty and the 2015 German Treaty.</td>
<td>Australia – UK Tax Treaty 1946. The Australia – UK 1967 Tax Treaty was the first Australian treaty to contain this variation after the</td>
<td>Tax Treaty with Turkey signed April 2010</td>
<td>Identical to OECD Model</td>
</tr>
<tr>
<td>Art2(2) AV2</td>
<td>Not included in any Australian Treaties except 2013 Swiss Treaty and 2015 German Treaty</td>
<td>All Australian treaties except 2013 Swiss Treaty and 2015 German Treaty.</td>
<td>Australia – UK Tax Treaty 1946. The Australia – UK 1967 Tax Treaty was the first Australian treaty to contain this variation after the publication of the 1963 draft OECD Model</td>
<td>2010 Turkish Treaty</td>
<td>Substantially identical to OECD Model</td>
</tr>
<tr>
<td>Art 3(1) AV3(a)</td>
<td>Treaty with Singapore includes a definition of ‘profits of a Singapore enterprise’ and of ‘profits of an Australian enterprise’ in terms which exclude particular categories of income. This is a legacy of the ‘Colonial Model’ referred to in Chapter 4 as the ‘Baby Boomer’</td>
<td>Treaty with Singapore 1969</td>
<td>Australia – UK Tax Treaty 1946</td>
<td>Treaty with Singapore 1969</td>
<td>Approach not taken in UN Model</td>
</tr>
<tr>
<td>AV3(b) ¹</td>
<td>Model’ where industrial or commercial profits were defined in exclusionary terms.</td>
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<tr>
<td>Art 4(1)</td>
<td>In the case of Australia if the person is a resident of Australia for the purposes of Australian tax.</td>
<td></td>
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</tr>
<tr>
<td>AV4</td>
<td>All Australian treaties except 2013 Swiss and 2015 German treaties. US Treaty and 2010 Turkish Treaty state that an ‘Australian company’ is an Australian resident. An ‘Australian company’ is separately Australia – UK Tax Treaty 1946 although dual residents were not treaty residents under 2010 Turkish Treaty 2015 German Treaty differs from both OECD</td>
<td></td>
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</table>

¹ All Australian treaties contain some variations from the general definitions in OECD Article 3. Some of these of these are additional definitions (for example some treaties contain a definition of ‘stock exchange’). Only the treaty with Romania contains a definition of ‘international traffic’ identical to the OECD definition. Other Australian treaties either do not contain a definition of ‘international traffic’ (for example, the treaty with Austria), or vary the OECD definition by excluding the words ‘that has its place of effective management in the Contacting State’ (for example, the treaty with Argentina). A deletion that is permitted in the OECD commentary where the words ‘resident of the Contracting State’ are substituted. Australian treaties signed before 1995 follow the pre 1995 OECD version of Article 3(2). In general Australian treaties post 1995 follow the 1995 OECD version of Article 3(2). Definitions of ‘enterprise’, ‘business’ and ‘national’ are infrequent in Australian treaties, particularly treaties signed before these definitions were added to the OECD Model but can be excluded from more recent treaties (for example, the 2010 Chilean treaty excludes the definitions of ‘enterprise’ and of ‘business’). The definition of ‘national’ is rarely included and is varied in some treaties (for example the 2015 German treaty). As these variations differ significantly between Australian treaties and as each variation may relate to one particular defined term in the OECD model they have not been included in the total of Australian variations from the OECD Model. It was considered that to do so would have exaggerated the extent of the Australian variations from the OECD Model.
<p>| AV5 | Only 11 of 19 post 1995 tax treaties include 1995 addition ‘any political subdivision or local authority thereof’ defined as which is a resident of Australia under Australian law and which is not a resident of the other contracting state under its law. | Australian post 1995 tax treaties other than: New Zealand 2009; Finland 2006; Norway 2006; Mexico 2003; United Kingdom 2003; France 2006; Japan 2008; Chile 2010; Turkey 2010; Switzerland 2013; Germany 2015. | Post 1995 variation first appears in 1995 Czech Treaty | Model and prior Australian tax treaties. In the case or Australia in this treaty, resident of a Contracting State means any person who ‘is liable to tax as a resident of Australia’. 2000 Russian Treaty | Identical to OECD Model |</p>
<table>
<thead>
<tr>
<th>Art 4(3)</th>
<th>AV5.1</th>
<th>AV5.1(a)</th>
<th>AV 5.1(b)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1982 US and 2010 Chilean and Turkish Treaties do not have corporate residence tiebreakers. Chilean Treaty denies dual corporate residents treaty benefits other than under the credit article.</td>
<td>2015 German Treaty varies tiebreaker for persons other than individuals to some extent reflecting OECD BEPS recommendations. Similar drafting can be found in earlier Australian treaties, for example, New Zealand 2009.</td>
<td>2015 German Treaty includes a deemed residence rule for collective investment vehicles in Art 4(4) and Art 4(5) includes a definition of ‘equivalent beneficiary’ for purposes of Art 4(4). 2009 New Zealand</td>
</tr>
<tr>
<td></td>
<td>2010 Turkish Treaty</td>
<td>2015 German Treaty</td>
<td>No equivalent.</td>
</tr>
<tr>
<td></td>
<td>Identical to OECD Model</td>
<td>Identical to OECD Model</td>
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</tr>
<tr>
<td>Art 5(2)</td>
<td>AV6</td>
<td>Treaty contains a deemed residence rule for managed investment trusts.</td>
<td>Treaty first to mention ‘managed investment trusts’</td>
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<tr>
<td></td>
<td></td>
<td>‘Agricultural, pastoral or forestry property’ included on list of examples</td>
<td>All except 1969 Singapore and 2010 Turkish Treaties. In 2006 Finnish Treaty reference is confined to ‘an agricultural, pastoral or forestry property situated in Australia’.</td>
</tr>
<tr>
<td>In 1946 UK – Australia Tax Treaty</td>
<td></td>
<td>‘agricultural or pastoral property’ was expressly mentioned in the ‘includes’ portion of the</td>
<td>2013 Swiss Treaty 2015 German Treaty</td>
</tr>
<tr>
<td>Examples in 5(2) identical to 1977 OECD Model as amended</td>
<td></td>
<td>Treaty</td>
<td></td>
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</tbody>
</table>
definition. In 1953 US–Australia Tax Treaty ‘agricultural or pastoral property’ was expressly mentioned in the ‘includes’ part of the definition. In 1960 Australia–New Zealand Tax Treaty ‘agricultural, pastoral or forestry property’ was expressly mentioned in the ‘includes’ part of the definition.
<table>
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</thead>
<tbody>
<tr>
<td>AV8</td>
<td>Inclusion of ‘connected supervisory activities’</td>
<td>All except Chile</td>
<td><strong>Origins in Australia – United Kingdom Treaty 1967</strong></td>
<td>2013 Swiss Treaty. 2015 German Treaty reference is in Art 5(4)(a) and 9 months requirement applies.</td>
<td>Included in UN Art 5(3)(a)</td>
</tr>
<tr>
<td>AV9(a)</td>
<td>6 month limit for building site, 15 treaties</td>
<td></td>
<td><strong>Australia – 2010 Turkish Treaty</strong></td>
<td></td>
<td>No equivalent.</td>
</tr>
</tbody>
</table>

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<table>
<thead>
<tr>
<th>Art 5(4)</th>
<th>‘Delivery of goods’ not in list of exclusions</th>
<th>Argentina, Indonesia, Norway and Singapore (variation made by 1&lt;sup&gt;st&lt;/sup&gt; Protocol 1989)</th>
<th>1&lt;sup&gt;st&lt;/sup&gt; Singapore Treaty with Norway 2006</th>
<th>‘Delivery of goods’ not in list of exclusions</th>
</tr>
</thead>
<tbody>
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<td>AV11</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>AV12</td>
<td>Examples of preparatory activities given – ‘such as advertising, the supply of information or scientific research’</td>
<td>All except Finland, Hungary, South Africa, Norway, New Zealand, Japan, the UK, and 2015 German Treaty.</td>
<td>2013 Swiss Treaty</td>
<td>No equivalent</td>
</tr>
<tr>
<td>AV12(a)</td>
<td>2015 German Treaty Article 5(7) limits exclusions in Article 5(6) to those of a preparatory or auxiliary character where closely related enterprises with business activities constituting complementary functions as part of a cohesive business operation.</td>
<td>2015 German Treaty reflecting OECD BEPS recommendations.</td>
<td>2015 German Treaty</td>
<td>Cf UN Art 5(4)(f)</td>
</tr>
<tr>
<td>Art 5(5)</td>
<td>Dependant agent without authority to conclude contracts but who habitually maintains a stock of goods</td>
<td>Treaties with Fiji, India, Indonesia, Kiribati, Malaysia, the Philippines, Papua New Guinea, Russia,</td>
<td>Turkish Treaty 2010</td>
<td>Equivalent provision contained in UN</td>
</tr>
<tr>
<td>AV13</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>AV13(a)</td>
<td>2015 German Treaty varies language by referring in Art 5(8) to a person who habitually concludes contracts, or habitually plays the principal role in the conclusion of contracts that are routinely concluded without material</td>
<td>Singapore, Sri Lanka, Thailand and Turkey</td>
<td>United Kingdom Tax Treaty as an exception to the exclusion of agents from being permanent establishments. Positive deeming contained in 1967 Australia-United Kingdom Tax Treaty.</td>
<td>Article 5(5)(b)</td>
</tr>
<tr>
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<p>| AV14 | Person who manufactures or processes in the State for the enterprise goods or merchandise belonging to the enterprise is deemed to be a permanent establishment. | All treaties | Australia – Canada Tax Treaty 1957 | 2015 German Treaty | Equivalent provision not contained in UN Model |
| AV15 | Agent not independent where activities devoted wholly or almost wholly to the relevant enterprise and relations between the agent and the enterprise differ from those that would exist between independent enterprises | Treaties with China, India, Indonesia, Mexico, the Philippines, Thailand and Germany | Treaty with the Philippines 1979 Origin, but not precise terms, can be traced to 1946 Australia – United Kingdom Tax Treaty – appears was agreed to be included in 1967 | 2001 Mexican Treaty. In 2015 German Treaty with some modifications. This reflects OECD BEPS recommendations | Equivalent provision in UN Model Article 5(7). |</p>
<table>
<thead>
<tr>
<th>Art 5(7)</th>
<th>Additional paragraph extends principles in Article 5 to determining whether there is a permanent establishment outside both Contracting States and for determining whether an enterprise not being an enterprise of one of the Contracting States has a permanent establishment in one of the Contracting States.</th>
<th>Appears in thirty five Australian treaties.</th>
<th>Australia – United Kingdom Tax Treaty but this did not happen</th>
<th>1976 Netherlands Treaty</th>
<th>2015 German Treaty</th>
<th>Equivalent provision not in UN Model</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 7(1)</td>
<td>Force of attraction rule applied irrespective of whether there is tax avoidance.</td>
<td>Treaties with India and Indonesia</td>
<td>Australia – USA Treaty 1953</td>
<td>Indian Treaty 1991</td>
<td>1999 Argentina Treaty</td>
<td>Limited force of attraction applied in UN Art 7(1)</td>
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<tr>
<td>AV16</td>
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<tr>
<td>AV17</td>
<td>Force of attraction rule applied only where there is tax avoidance.</td>
<td>Treaties with Argentina, Fiji, Kiribati, Mexico, the Philippines, Papua New Guinea, Sri Lanka and Thailand</td>
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<tr>
<td>Art 7(3)</td>
<td>AV18</td>
<td>Exclusion of certain payments to head office in determining the profit attributable to a permanent establishment.</td>
<td>Treaties with Argentina, China, Indonesia, Mexico and Sri Lanka</td>
<td>1991 China Treaty</td>
<td>2002 Mexican Treaty.</td>
<td>Equivalent provision in UN Art 7(3)</td>
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<td>AV18(a)</td>
<td>Allowance for deductions in determining profits of permanent establishment.</td>
<td>All Australian treaties subsequent to change to OECD Model Article 7</td>
<td>Origins can be traced to 1953 US Treaty</td>
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<td>Art 7(4)</td>
<td>AV19</td>
<td>Old OECD Article 7(4) only appears in three Australian tax treaties</td>
<td>All Australian treaties except those with Denmark, Germany 1972 and Switzerland 1980</td>
<td>Treaty with the UK 1946</td>
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<td>UN Model identical to old OECD Art 7(4)</td>
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<tr>
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<td>AV20</td>
<td>Provision allowing the application of domestic law where information is inadequate (or if there are exceptional difficulties – treaties with India and Korea) to determine profit.</td>
<td>All Australian treaties or protocols to the relevant treaty except 2013 Swiss Treaty and 2015 German Treaty</td>
<td>Australia-UK Treaty 1946</td>
<td>2010 Turkish Treaty.</td>
<td>No equivalent in UN Model</td>
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<td>Art 7(6)</td>
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<td>AV21</td>
<td>Only in 9 Australian treaties</td>
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<td><strong>Australia – UK Treaty 1946</strong></td>
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<td>UN Article 7(5) is identical to OECD Article 7(6)</td>
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<tr>
<td>Art 7</td>
<td><strong>Australian Addition</strong></td>
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<tr>
<td>AV22</td>
<td>Saving clause for domestic law dealing with insurance at time treaty is signed</td>
<td>All Australian treaties or protocols except the treaties with Chile, German Treaty 1972, Korea, 1980 Switzerland, 2013 Switzerland and 2015 Germany. The treaty with Chile has a different provision dealing with insurance premiums. Protocols to the 1972 German, Korean and Swiss treaties stated that Article 7 does not apply to insurance business other than life insurance.</td>
<td><strong>Australia – UK Treaty 1946</strong></td>
<td>2010 Turkish Treaty. Not included in 2013 Swiss Treaty. Included in 2015 German Treaty.</td>
<td>No equivalent provision in UN Model</td>
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<tr>
<td>Art 7</td>
<td><strong>Australian Addition</strong></td>
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<tr>
<td>AV23</td>
<td>Permanent establishment of an enterprise operated through a trust (other than a trust treated as a company for tax purposes) deemed to be a permanent establishment of the beneficiaries of the trust.</td>
<td>All Australian treaties except the treaties with Belgium, Denmark, German Treaty 1972, Italy, Ireland, Korea, Malta, the Netherlands, the Philippines, and Sweden.</td>
<td>Austrian Treaty 1986</td>
<td>2015 Germany Treaty.</td>
<td>No equivalent provision in UN Model</td>
<td></td>
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<tr>
<td>AV24</td>
<td>Australian articles on shipping and air transport differ from the OECD Model. A resident of a Contracting State is taxable on shipping and</td>
<td>This pattern is followed in all Australian tax treaties other than the 2000 Romanian Treaty.</td>
<td>Australia – United Kingdom Tax Treaty 1967. Current</td>
<td>2015 German Treaty.</td>
<td>Article 8(1) is identical to Article 8(1) in the OECD Model</td>
<td></td>
</tr>
<tr>
<td>AV25</td>
<td>aircraft profits only in that State. No reference is made to the place of effective management of the enterprise. This connects back to the definition of ‘resident’ in Art 4(1) or in some treaties to the definition of ‘international traffic’ in Art 3.²</td>
<td>All but five Australian treaties permit source taxation of shipping and aircraft profits of residents of the other Contracting State where the carriage of passengers or goods is confined solely to the source country.³</td>
<td>Australian article virtually identical to original UK draft in 1946 UK treaty.</td>
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<tr>
<td>AV26</td>
<td>Four of Australia’s treaties limit source country taxation in relation to carriage of passengers or goods to</td>
<td>This restriction occurs in all Australian treaties other than the treaties with Italy, Korea, the Philippines, Romania and the US</td>
<td>Australia – United Kingdom Tax Treaty 1967</td>
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<td>2015 German Treaty</td>
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<td>No equivalent in UN Model</td>
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<td></td>
<td>No equivalent in UN Model</td>
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</tbody>
</table>

² The OECD Commentary on Art 8(1) at 2[2] permits this variation.
³ This practice is consistent with the definition of ‘international traffic’ in Article 3 of the OECD Model and with the OECD Commentary on Article 3(1) at 6[6], 6.1[-], 6.2 [-], and 6.3 [-].
<p>| AV27 | All but five Australian treaties contain a paragraph which provides that profits from the carriage of passengers and certain specified cargo shipped in a Contracting State for discharge in that State are deemed to be profits from operations solely with that State. | old treaty) | All Australian treaties other than the treaties with Korea, the Philippines, Russia, 2013 Switzerland and 2015 Germany. | Japanese Treaty 1969 | 2010 Turkish Treaty | No equivalent in UN Model |
| AV28 | Not in any Australian tax treaties but Australian article provides that country may tax shipping where shipping and discharge in the same Contracting State. | All Australian tax treaties |  | Australia – United Kingdom Tax Treaty 1946 | 2015 German Treaty | Alternative A of Art 8(2) identical to OECD Art 8(2) |
| AV29 | Only in two Australian tax treaties | Only in the tax treaties with Italy and Romania. |  | Australia – United Kingdom Tax Treaty 1946 | 2015 German Treaty | Identical to OECD Model in this respect |</p>
<table>
<thead>
<tr>
<th>Art 9(1)</th>
<th>AV30</th>
<th>Addition to treaty with Hungary provides that profit adjustments may be made where a person acting in the Contracting State on behalf of the enterprise manufactures or processes in the State for the enterprise goods or merchandise belonging to the enterprise⁴</th>
<th>1990 Hungarian Treaty</th>
<th>1990 Hungarian Treaty</th>
<th>1990 Hungarian Treaty</th>
<th>Not in UN Model</th>
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</thead>
<tbody>
<tr>
<td>Art 9(2)</td>
<td>AV31</td>
<td>Not included in two of Australia’s post 1977 tax treaties</td>
<td>Not included in treaties with Italy and Switzerland 1980</td>
<td>Australia – United Kingdom Tax Treaty 1946</td>
<td>Italian Treaty 1982</td>
<td>Art 9(2) identical to OECD Art 9(2)</td>
</tr>
<tr>
<td>Art 9(3)</td>
<td>UN Model included</td>
<td>AV32</td>
<td>When provisions in paragraph 2 do not apply</td>
<td>Only appears in treaties with Czech Republic and Mexico</td>
<td>Treaty with Czech Republic 1995</td>
<td>Treaty with Mexico 2003</td>
</tr>
</tbody>
</table>

⁴ Note that, consistent with the OECD Model, Article 5(3)(c) of the Hungary Treaty states that an enterprise shall not be deemed to have a permanent establishment merely by reason of the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise.
<table>
<thead>
<tr>
<th>Australian addition</th>
<th>AV33</th>
<th>All Australian treaties except the Korean, Thai and 2015 German Treaty 2015</th>
<th><strong>Australia – United Kingdom Tax Treaty 1946</strong></th>
<th>2013 Swiss Treaty Not in 2015 German Treaty.</th>
<th>No equivalent in UN Model</th>
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</thead>
<tbody>
<tr>
<td>Art 9 Additional provision</td>
<td>AV34(a)</td>
<td>Korean and Thai treaties</td>
<td><strong>Difference in wording but can be traced to 1946 Australia – United Kingdom Tax Treaty. Provenance is already accounted for in AV33</strong></td>
<td>Thai Treaty 1989</td>
<td>No equivalent in UN Model</td>
</tr>
<tr>
<td>Art 9 Additional</td>
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<tr>
<td>Provision</td>
<td>Description</td>
<td>Korean treaty</td>
<td>Korean Treaty</td>
<td>Korean Treaty 1983</td>
<td>No equivalent in UN Model</td>
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<tr>
<td>AV34(b)</td>
<td>Article 9 only to apply where both Contracting States have a tax interest</td>
<td></td>
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<tr>
<td>AV35(a)</td>
<td>Seven year time limit from date of tax return for adjustment of profits under Article 9. Does not apply in case of fraud, gross negligence, or wilful default or where audit commenced within the seven year period.</td>
<td></td>
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</tr>
<tr>
<td>Art 9</td>
<td>Additional provision</td>
<td>2105 German Treaty</td>
<td>2015 German Treaty</td>
<td>2015 German Treaty</td>
<td>No equivalent in UN Model</td>
</tr>
<tr>
<td>AV35(b)</td>
<td>Ten year time limit from end of tax year when profits accrued for adjustment of profits under Article 9. Does not apply in case of fraud,</td>
<td></td>
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<tr>
<td>Art 10(1)</td>
<td>Inclusion of a requirement in paragraph (1) that dividends be ‘beneficially owned’ by resident of other Contracting State or that the dividends be ‘dividends to which a resident of the other Contracting State is beneficially entitled,’</td>
<td>In all Australian treaties or protocols except the treaty with Chile.</td>
<td><em>Australia – United Kingdom Tax Treaty 1946 first to use phrase ‘beneficially owned’./</em> Phrase does not appear in 1953 Australia–United States Tax Treaty nor in 1957 Australia–Canada Tax Treaty, nor in 1960 Australia–&lt;br/&gt;2010 Turkish Treaty. In paragraph 10(2) of 2013 Swiss Treaty and 2015 German Treaty.</td>
<td>Beneficial ownership requirement in Art 10(2) of UN Model</td>
<td></td>
</tr>
</tbody>
</table>

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5 It should be noted, however, that the beneficial ownership requirement in the 1946 UK Treaty was confined to the situation where a United Kingdom resident owned all the shares in an Australian company.
<p>| AV37 | Rate of 15% for portfolio dividends paid by Australian company but different rate for dividends paid by company resident in other Contracting State |
| | Malaysia (zero per cent); Singapore (zero per cent for dividend by Singapore company or Malaysian company out of Singapore profits); Ireland 15 per cent where Australian resident entitled to tax credit otherwise zero; Malta – may not exceed tax chargeable on the profits |
| | 1969 Singapore Treaty |
| | 1984 Maltese Treaty |
| | UN Model does not specify limits on withholding tax on portfolio dividends but leaves this to be determined by bi-lateral |</p>
<table>
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<tr>
<th>AV38(a)</th>
<th>Less than 15% Australian dividend withholding tax payable if certain conditions are met otherwise 15% withholding tax applies</th>
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<tr>
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<td>Argentina 10% to extent Australian dividend franked and paid to company with minimum of 10% voting power; Czech Republic 5% if to extent Australian dividend franked; Taiwan 10% to extent Australian dividend franked; New Zealand 5% if paid to a New Zealand life insurance company.</td>
</tr>
<tr>
<td>AV38(b)</td>
<td>Higher than 15% dividend withholding tax for portfolio and non-portfolio dividends payable in certain circumstances</td>
</tr>
<tr>
<td></td>
<td>Philippines treaty – rate is 25% where foreign tax credit is not available; Papua New Guinea rate is 15% for dividends paid by Australian company and 25% for dividends paid by Papua New Guinea company; Fiji rate is 20%; Kiribati rate is 20%.</td>
</tr>
<tr>
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<td>Czech Treaty 1995</td>
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<td>New Zealand Treaty 2009</td>
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<td>Philippines Treaty 1979</td>
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<td>Kiribati Treaty 1991</td>
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<td>negotiations</td>
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<tr>
<td>AV38B(c)</td>
<td>Test for application of dividend withholding tax rate of 5% is 10% of voting power not 25% of capital. Test for application of 5% withholding tax has another different requirement from OECD Model.</td>
</tr>
<tr>
<td>AV38(d)</td>
<td>Limit on source country tax only applies where recipient holds at least 25% of the capital of paying company with rates differing from OECD Model.</td>
</tr>
<tr>
<td>AV39</td>
<td>Only six Australian treaties expressly exclude the operation of the 5% rate or 0% rate where the beneficial owner of the dividend is a partnership.</td>
</tr>
<tr>
<td>AV40(a)</td>
<td>Rate of dividend withholding tax on non-portfolio dividends (defined as minimum of 10% voting power) is higher than 5%</td>
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<td>Treaty with Argentina 10% dividend withholding tax; treaty with Austria 15% dividend withholding tax; treaty with Belgium 15% dividend withholding tax; treaty with China 15% dividend withholding tax; treaty with Denmark 15% dividend withholding tax; treaty with Fiji 20% dividend withholding tax; Germany 15% with additional special provision in the Protocol paragraph 6; Hungary</td>
</tr>
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<td>Treaty with Thailand 1989</td>
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</tbody>
</table>
Ireland 15% dividend withholding tax except that zero dividend withholding tax applies where Australian recipient of dividend paid by Irish company does not receive a foreign tax credit; Italy 15% dividend withholding tax; Kiribati 20% dividend withholding tax; Korea 15% dividend withholding tax; Malaysia – 15% dividend withholding tax on unfranked portion of dividend paid by Australian company to Malaysian shareholder with 10% of more voting power; Malta – 15% dividend withholding tax on dividends paid by Australian company; Mexico 15% dividend withholding company where dividend not paid from profits that have borne normal rate of company tax; The Netherlands 15% dividend withholding tax; Papua New Guinea 20% dividend withholding tax on dividends paid by Papua New
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<th>Country</th>
<th>Dividend Withholding Tax Conditions</th>
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<td>Guinea</td>
<td>15% dividend withholding tax on dividends paid by Australian company;</td>
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<td>Philippines – 15% dividend withholding tax where dividend derived by a company</td>
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<td>where credit relief given with 25% dividend withholding tax in other cases;</td>
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<td>Poland 15% dividend withholding tax; Romania 15% dividend withholding tax on</td>
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<td>unfranked portion of dividend paid by Australian company and on portion of</td>
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<td>dividend paid by Romanian company not paid out of profits subject to</td>
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<td></td>
<td>profits tax; Russia 15% dividend withholding tax where not paid from</td>
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<td>profits that have borne normal rate of tax or where recipient’s investment is</td>
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<td>less than AUD700,000 or where dividend is not exempt from</td>
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<tr>
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<td>Australian tax; Singapore 15% dividend withholding tax on dividends paid by Australian company and</td>
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</tbody>
</table>
provision that 15% withholding tax to apply on dividends paid by a Singapore company or a Malaysian company if Singapore reintroduces a tax on dividends; Slovakia 15% dividend withholding tax; Spain 15% dividend withholding tax; Sri Lanka 15% dividend withholding tax; Sweden 15% dividend withholding tax; old Swiss treaty 15% dividend withholding tax; Taipei 15% dividend withholding tax on unfranked portion of dividends paid by an Australian company; Thailand 15% dividend withholding tax where shareholder a company holding at least 25% of the capital and is an industrial undertaking and 20% dividend withholding tax in other cases; Turkey 15% dividend withholding tax where dividend by Turkish company to the extent not paid from profits that have been subjected to the full rate
<table>
<thead>
<tr>
<th>AV40(b)</th>
<th>Rate of dividend withholding tax on non-portfolio dividends (defined as minimum of 10% ownership) is less than 5%.</th>
<th>Treaty with Mexico – zero dividend withholding tax where at least 10% voting power and dividend paid from profits that have borne normal rate of company tax.</th>
<th>2002 Mexican Treaty</th>
<th>2002 Mexican Treaty</th>
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<tbody>
<tr>
<td>Art 10(3)</td>
<td>Treaty with Singapore does not contain a definition of dividend.</td>
<td>Treaty with Singapore</td>
<td>1946</td>
<td>Treaty with Singapore 1969</td>
</tr>
<tr>
<td>AV42</td>
<td>All Australian treaties other than treaty with Singapore contain a definition of dividend but omit ‘jouissance shares or jouissance rights, mining rights, founders shares’.</td>
<td>All Australian treaties other than treaty with Singapore.</td>
<td>1972 German Treaty. Only previous treaty containing a definition of ‘dividends’ was 1967 UK Treaty which simply applied domestic law meaning of each country.</td>
<td>2010 Turkish Treaty. 2015 German Treaty – additional modifications due to German law.</td>
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<tr>
<td>Art 10(5)</td>
<td>Several Australian treaties vary Article 10(5) by adding a proviso that the paragraph does not limit Australia’s taxing rights where the paying company is a dual resident of the two Contracting States</td>
<td>All currently operative pre 2000 Australian treaties with the exception of the treaties with Canada, China, German 1972 Treaty, Hungary, Poland, Singapore, Spain and the USA.</td>
<td>Treaty with the Netherlands March 1976</td>
<td>Treaty with the Slovak Republic, August 1999</td>
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<tr>
<td>AV43</td>
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<td>UN Model does not contain this variation from OECD Model</td>
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<tr>
<td>Art 10</td>
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<td>Australian</td>
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<tr>
<td>omission</td>
<td>1969 Singapore Treaty, 1972 German Treaty do not include an equivalent to Art 10(5)</td>
<td>1969 Singapore Treaty and 1972 German Treaty</td>
<td>Treaty with United Kingdom 1946 did not contain an equivalent of Art 10(5) but contained Article VI(4) expressly permitting levy of undistributed profits tax</td>
<td>1972 German Treaty</td>
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<tr>
<td>AV 44</td>
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<td>Art 10</td>
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<tr>
<td>Australian Addition</td>
<td>2015 German Treaty Art 10(7) State other than State of corporate residence may tax dividend where underlying profit has not been subject to tax at corporate level</td>
<td>2015 German Treaty</td>
<td>2015 German Treaty</td>
<td>2015 German Treaty</td>
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<td>AV 44(a)</td>
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<tr>
<td>Art 10</td>
<td>Australian addition AV45</td>
<td>Zero dividend withholding tax where dividend paid to listed company holding 80% or more of voting power in company paying the dividend.</td>
<td>Treaties with US, UK, Finland, Norway, Japan, 2013 Switzerland, and 2015 Germany</td>
<td>US Protocol 2001 but zero source country tax was payable on dividends paid by a wholly owned subsidiary under 1946 Australia – United Kingdom Tax Treaty</td>
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<tr>
<td>Art 10</td>
<td>AV46</td>
<td>Anti-Abuse rule</td>
<td>Treaties with UK, Finland, Norway, Japan and Turkey.</td>
<td>2003 UK Treaty</td>
</tr>
<tr>
<td>Art 11(1)</td>
<td>AV47</td>
<td>Beneficial ownership requirement included in paragraph 1 rather than in paragraph 2 in all Australian</td>
<td>Treaty with Singapore is structured differently and beneficial ownership requirement appears in both</td>
<td><strong>Beneficial ownership requirement first</strong></td>
</tr>
<tr>
<td></td>
<td>treaties other than the treaty with Singapore, the 2010 Turkish Treaty, the 2013 Swiss Treaty and the 2015 German Treaty.</td>
<td>paragraph 1 and paragraph 2. Beneficial ownership requirement appears in paragraph 2 of treaty with Turkey.</td>
<td>appears in paragraph 1 in 1967 Australia – United Kingdom Tax Treaty</td>
<td>respect</td>
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<tr>
<td>Art 11(2)</td>
<td>Six Australian treaties specific a flat rate of withholding tax higher than 10%(^6)</td>
<td>Argentina treaty specifies 12%, treaties with India, Korea, Malaysia, Malta and the Philippines specify 15%.</td>
<td>Prior to 1967 Australia-United Kingdom Tax Treaty no interest article was included on the basis that full source country taxing rights would be retained in respect of interest. 10% withholding tax first appears in Treaty with Argentina 1999</td>
<td>UN Model does not specify a limit to withholding tax on interest but leaves this to be determined in bilateral negotiations</td>
</tr>
</tbody>
</table>

\(^6\) Australia introduced interest withholding tax in its domestic law in 1967 by *Income Tax Assessment Act (No4) 1967*. 
<p>| AV48(b) | Two treaties specify a rate higher than 10% in certain circumstances | Mexican treaty specifies 10% if person beneficially entitled is a bank or insurance company, or if derived from bonds and securities regularly and substantially traded on a recognised securities market, or paid by banks, or paid by a purchaser of machinery and equipment under a credit sale. In all other cases the Mexican treaty specifies 15%. The Thai treaty specifies 10% for interest to which a financial institution is beneficially entitled and 25% in all other cases. | 1967 Australia – United Kingdom Tax Treaty | Treaty with Thailand 1989 | Treaty with Mexico 2002 |
| AV48(c) | One treaty specifies a positive rate of 5% where the interest is derived by | Treaty with Chile 2010. | Treaty with Chile | Treaty with Chile | Treaty with Chile |</p>
<table>
<thead>
<tr>
<th>Art 11(3)</th>
<th>AV49</th>
<th>2010.</th>
<th>2010.</th>
<th>2015 German Treaty</th>
</tr>
</thead>
<tbody>
<tr>
<td>an unrelated financial institution dealing wholly independently of the payer and 10% in all other cases.</td>
<td>All but ten Australian treaties define ‘interest’ consistently with the definition in the 1963 OECD draft Model. Ten post 1977 treaties contain definitions that differ from the definitions in both the 1963 draft OECD Model and the 1977 OECD Model. Tax treaties with Belgium, the United Kingdom, Norway, Finland, the Netherlands (2nd Protocol), China, France, Hungary, New Zealand, South Africa, Japan, Turkey, Chile, 2013 Switzerland and 2015 Germany all contain definitions that differ from both the 1963 draft OECD Model and the 1977 OECD Model.</td>
<td>1969 Australia – Singapore Tax Treaty first to include a 1963 OECD Model definition of interest. 1967 Australia – United Kingdom Tax Treaty contained a ‘negative’ definition of ‘interest’.</td>
<td>UN Model definition substantially similar to 1977 OECD but also includes: ‘premiums and prizes attaching to such securities, bonds or debentures’</td>
<td></td>
</tr>
</tbody>
</table>

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7 The differences from the 1963 Draft OECD Model largely concern word order rather than matters of substance.
<table>
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</thead>
<tbody>
<tr>
<td>Art 11(5)</td>
<td>AV51</td>
<td>Treaty with Singapore does not include an equivalent to paragraph 5</td>
<td>Treaty with Singapore</td>
<td>Australian treaties prior to the 1972 Australia – Germany Tax Treaty do not</td>
<td>Treaty with Singapore 1969</td>
<td>UN Model includes an equivalent to OECD 11(5)</td>
</tr>
</tbody>
</table>
| AV52 | Paragraph 5 expanded in 34 treaties to include deemed source rule for interest borne by permanent establishment or fixed base in third state. | Treaties with Argentina, Austria, Belgium, Chile, Czech Republic, Denmark, Fiji, Finland, France, 2015 Germany, Hungary, India, Indonesia, Ireland, Italy, Japan, Kiribati, Korea, Malta, Mexico, the Netherlands, New Zealand, Norway, Papua New Guinea, the Philippines, Romania, Russia, Slovakia, South Africa, Spain, Sri Lanka, Switzerland, Turkey, Thailand, the USA and Vietnam. | contain an equivalent to paragraph 5. 1967 UK Treaty is the first with an interest article and hence the first with AV51

Extended deeming has its origins in the 1969 Australia – Singapore Tax Treaty but deemed source rules were contained in a separate article. | Deemed source rule included in Art 11(5) in UN Model but not extended to position where PE or fixed base in third state. | 2015 German Treaty. | Art 11 |
<p>| Australian addition | AV53 | Eighteen treaties provide that no interest withholding tax may be levied in the source country in respect of interest derived by the other State. | Treaties with Argentina, Czech Republic, Finland, France, Hungary, Indonesia, Italy, Japan, Korea, Mexico, Norway, the Philippines, Romania, South Africa, Sweden, Thailand, the UK and the USA. | Treaty with the USA 1982 | 2008 Treaty with Japan | No equivalent |
| Art 11 Australian addition | AV54 | Nine treaties provide that no interest withholding tax may be levied in the source country in respect of interest derived by an unrelated financial institution other than in the case of back to back loans. | Treaties with Finland, France, Japan, Norway, South Africa, the UK, the USA, Switzerland 2013 and the 2015 German Treaty. | Protocol with the USA 2001 | 2015 German Treaty | No equivalent |</p>
<table>
<thead>
<tr>
<th>AV55(a)</th>
<th>Seven treaties deny benefits where there has been either a lack of <em>bona fides</em> or where the indebtedness was created or assigned to take advantage of the article.</th>
<th>Treaties with Finland, Japan, Mexico, New Zealand, Norway, South Africa and the UK.</th>
<th>South African Treaty 1999</th>
<th>2009 New Zealand Treaty</th>
<th>No equivalent</th>
</tr>
</thead>
</table>
| Art 12(1) | All Australian treaties vary paragraph 1 by making taxation by the state of residence permissive rather than exclusive. All Australian treaties permit the source country to levy withholding tax on royalties under paragraph 2 of the article. Rates vary from 5% to 25%. | All Australian treaties. | *Prior to 1967 Australia – United Kingdom Tax Treaties*  
*Australian tax treaties did not set upper limits of source taxation of those royalties where source taxing rights were retained.*  
1967 Australia – United Kingdom Tax Treaty was | 2010 Turkish Treaty. In paragraph 10(2) of 2013 Swiss Treaty. 2015 German Treaty. | UN Model allows taxation by source state at withholding rates to be agreed in bi-lateral negotiations |
<table>
<thead>
<tr>
<th>AV57</th>
<th>Treaties with Turkey and Chile do not require that the resident of the other contracting state be beneficially entitled to the royalties.</th>
<th>Treaties with Turkey and Chile.</th>
<th>2010 Chilean Treaty</th>
<th>2010 Turkish Treaty</th>
<th>Beneficial ownership requirement is included in Art 12(2) of UN Model as a pre-requisite for limiting source country taxation.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 12(2)</td>
<td>Definition of royalties in Australian treaties, other than treaty with Singapore, includes ‘films or tapes</td>
<td>All Australian treaties other than treaty with Singapore.</td>
<td>United Kingdom Tax Treaty 1967 See also Japan</td>
<td>2010 Turkish Treaty and 2013 Swiss Treaty.</td>
<td>Substantially similar language used in Art 12(4)</td>
</tr>
<tr>
<td>AV59</td>
<td>Definition of royalties in Australian treaties up to the 2003 treaty with the UK included ‘for the use of, or the right to use industrial, commercial or scientific equipment’. No Australian treaties between 2003 and 2010 include this aspect of the definition and it was also removed in 2001 by protocol to the USA Treaty and in 2008 by protocol to the South African Treaty. This aspect of the definition was then included in the treaties with Chile and Turkey.</td>
<td>Treaties entered into prior 2003 other than the treaties with the USA and South Africa as amended by 2001 and 2008 protocols respectively. Treaties with Chile and Turkey.</td>
<td><strong>United Kingdom Tax Treaty 1967</strong> More generic terminology is used 2015 German Treaty.</td>
<td><strong>Tax Treaty 1969</strong> Included in Art 12(4) of UN Model</td>
<td></td>
</tr>
<tr>
<td>A60</td>
<td>Definition in ten treaties includes items not within the definitions in either the OECD or UN Models.</td>
<td>Treaties with Argentina, Canada, the Czech Republic, Malaysia, Mexico, New Zealand, Romania, Russia, Slovakia, and Spain.</td>
<td>Treaty with the United Kingdom 1967</td>
<td>Treaty with Germany 2015</td>
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<tr>
<td>Art 12(3)</td>
<td></td>
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</tr>
<tr>
<td>A61</td>
<td>Of Australia’s post 2000 treaties only the treaties with Chile, Mexico and Turkey continue to refer to a ‘fixed base’.</td>
<td>Treaties with Chile, Mexico and Turkey.</td>
<td>2002 Mexican Treaty with</td>
<td>2010 Chilean</td>
<td>Art 12(4) UN Model refers to a ‘fixed base’</td>
</tr>
<tr>
<td>Art 12 Australian addition</td>
<td></td>
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</tr>
<tr>
<td>A62</td>
<td>All of Australia’s treaties, other than the treaty with Singapore, include a rule deeming royalties to have a source where royalties are borne by a permanent establishment or fixed base in one of the Contracting States.</td>
<td>All of Australia’s treaties other than the 1969 Singapore Treaty</td>
<td>1969 Japan Treaty – in the 1967 UK Treaty a different source rule was contained in the credit article</td>
<td>2015 German Treaty</td>
<td>Deemed source rule contained in Art 12(5) of UN Model</td>
</tr>
<tr>
<td>Art 12 Australian addition</td>
<td></td>
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</tbody>
</table>
**AV63**

Thirty five Australian treaties include a deemed source rule where royalties are borne by a permanent establishment or fixed base in a third state.

| Treaties with Argentina, Austria, Belgium, Chile, Czech Republic, Denmark, Fiji, Finland, France, Germany 2015, Hungary, India, Indonesia, Ireland, Italy, Japan, Kiribati, Korea, Malta, Mexico, the Netherlands, New Zealand, Norway, Papua New Guinea, the Philippines, Romania, Russia, Slovakia, South Africa, Spain, Sri Lanka, Switzerland, Turkey, Thailand, the USA, and Vietnam. |
| 1976 Netherlands Treaty |
| 2015 German Treaty |
| No equivalent in UN Model |

**Art 12 Australian addition**

Six Australian treaties deny benefits of the article where there is either a lack of *bona fides* or rights were created or assigned to take advantage of the article.

| Treaties with Finland, Japan, Mexico, Norway, South Africa and the UK. |
| Treaty with Mexico 2002 |
| Treaty with Japan 2008 |
| UN Model Art 12(6) corresponds with OECD Model Art 12(4). |
All but three Australian treaties refer to 'real property' instead of 'immovable property' in the OECD Model.

Malaysian treaty refers to 'land' instead of 'immovable property'.

<table>
<thead>
<tr>
<th>Art 13(1)(^8)</th>
<th>All Australian treaties except the treaties with Malaysia, Mexico, Chile and the 2015 German Treaty.</th>
<th>Treaty with Germany 1972 but only refers to 'income from real property'.</th>
<th>2010 Turkish Treaty</th>
<th>Art 13(1) of UN Model refers to immovable property.</th>
</tr>
</thead>
<tbody>
<tr>
<td>AV65(a)</td>
<td>All Australian treaties except the treaties with Malaysia, Mexico, Chile and the 2015 German Treaty.</td>
<td>Treaty with Netherlands 1976 first to refer to 'income from the alienation of real property'.</td>
<td>Malaysian treaty</td>
<td>Malaysian treaty</td>
</tr>
<tr>
<td>AV65(b)</td>
<td>Malaysian treaty refers to 'land' instead of 'immovable property'.</td>
<td>Malaysian treaty.</td>
<td>Malaysian treaty</td>
<td>Malaysian treaty</td>
</tr>
</tbody>
</table>

\(^8\) The 1976 Netherlands Treaty was the first Australian tax treaty to contain an 'alienation of property' article. At the time Appendix 3 was prepared the 1972 German Treaty was still in force and had not been amended by Protocol. That treaty did not contain an alienation of property or a capital gains article. It was thought that differences between Australian treaty practice and the OECD Model would be overstated if differences due to the omission of Article 13 from the 1972 German Treaty were taken into account.
| AV65(c) | Mexican and Chilean treaties refer to ‘immovable (real) property’. | Treaties with Mexico and Chile. | Treaty with Mexico 2002 | 2010 Chilean Treaty |
| AV65(d) | Twelve Australian treaties refer to ‘income or gains’ instead of ‘gains’ in the OECD Model. | Treaties with China, Hungary, India, Ireland, Malta, Papua New Guinea, Singapore, Sri Lanka, Thailand, the UK, the USA. | Swiss Treaty 1980 | 2003 UK Treaty |
| AV66(a) | Twenty two Australian treaties refer to ‘income, profit or gains’ instead of ‘gains’ in the OECD Model. | Treaties with Argentina, Canada, Chile, Czech Republic, Fiji, Finland, France, Indonesia, Japan, Kiribati, Malaysia, Mexico, New Zealand, Norway, Romania, Slovakia, South Africa, Spain, 2013 Switzerland, Taiwan, Turkey, Vietnam, and 2015 Germany. | Treaty with Fiji 1990 | 2015 German Treaty |
| AV66(b) | Eight Australian treaties refer to ‘income’ instead of ‘gains’ in the | Treaties with Austria, Belgium, Denmark, Italy, Korea, the | 1976 Netherlands Treaty | 1986 Austrian Treaty |

**Treaties with Mexico and Chile:**

- Treaty with Mexico 2002
- Swiss Treaty 1980
- 2010 Chilean Treaty

**Treaties with China, Hungary, India, Ireland, Malta, Papua New Guinea, Singapore, Sri Lanka, Thailand, the UK, the USA:**

- Swiss Treaty 1980
- 2003 UK Treaty

**Treaties with Argentina, Canada, Chile, Czech Republic, Fiji, Finland, France, Indonesia, Japan, Kiribati, Malaysia, Mexico, New Zealand, Norway, Romania, Slovakia, South Africa, Spain, 2013 Switzerland, Taiwan, Turkey, Vietnam, and 2015 Germany:**

- Treaty with Fiji 1990
- 2015 German Treaty

**Treaties with Austria, Belgium, Denmark, Italy, Korea, the:**

- 1976 Netherlands Treaty
- 1986 Austrian Treaty

**UN Model refers to ‘gains’**
<p>| AV66(c) | OECD Model. The treaty with Malaysia refers to ‘profits’ instead of ‘gains’ in the OECD Model. | Netherlands, the Philippines and Sweden. | Treaty with Malaysia. | Treaty with Malaysia | 1972 German Treaty | 1972 German Treaty |
| AV67   | Article 21 in the 1972 German Treaty allows the taxation of ‘capital represented by real property’ and does not refer to gains from the alienation of immovable property. | 1972 German Treaty | Treaty with Malaysia | Treaty with Malaysia | Treaty with Malaysia |
| Art 13(2) | Four Australian treaties do not include paragraph 2. | Treaties with Austria, Italy, Malta and the Netherlands. | Treaty with the Netherlands 1976 | Treaty with Austria 1986 | UN Model includes paragraph 2 but includes gains from movable property of a fixed base for the |
| AV69(b) | Thirty treaties contain a reference to ‘independent personal services’. | Treaties other than treaties with Austria, Belgium, Fiji, France, Germany, Japan, Malaysia, Malta, the Netherlands, Norway, and the UK. | Treaty with the Philippines 1979 | 2013 Swiss Treaty | purpose of performing independent personal services |
| Art 13(3) | Paragraph 3 is not included in nine Australian treaties. | Treaties with Austria, Belgium, Denmark, Italy, Malta, the Netherlands, the Philippines, Sweden and Switzerland (old treaty). | 1976 Netherlands Treaty | 1986 Austrian Treaty | UN Model includes paragraph 3 |
| AV70 | All remaining Australian treaties with an equivalent to Article 13(3) include paragraph 3 but do not refer to ‘boats engaged in inland waterways transport’. | All Australian treaties other than treaties with Austria, Belgium, Denmark, Italy, Malta, the Netherlands, the Philippines, Sweden and Switzerland. | 1976 Netherlands Treaty | 2015 German Treaty |  |</p>
<table>
<thead>
<tr>
<th>Art 13(4)</th>
<th>V72(a)</th>
<th>Thirteen treaties expressly include interests in partnerships, trusts and other entities.</th>
<th>Treaties with Austria, Belgium, Denmark, Italy, Malta, the Netherlands, the Philippines, Sweden and Switzerland (old treaty).</th>
<th>Treaty with the Netherlands 1976</th>
<th>Treaty with Austria 1986</th>
<th>UN Model Art 13(4) refers to interests in partnerships and trusts</th>
</tr>
</thead>
<tbody>
<tr>
<td>AV72(b)</td>
<td>Treaties with Norway and Turkey and 2015 German Treaty refer to ‘shares or comparable interests’.</td>
<td>Treaties with Norway and Turkey and 2015 German Treaty.</td>
<td>2006 Norwegian Treaty</td>
<td>2015 German treaty</td>
<td>UN Model does not refer to ‘shares or comparable interests’</td>
<td></td>
</tr>
<tr>
<td>AV72(c)</td>
<td>Treaty with Chile refers to ‘shares or other rights’.</td>
<td>Treaty with Chile.</td>
<td>Treaty with Chile</td>
<td>Treaty with Chile</td>
<td>UN Model does not refer to ‘shares or other rights’</td>
<td></td>
</tr>
<tr>
<td>AV72(d)</td>
<td>Treaty with Finland refers to ‘shares or comparable interests in an entity’.</td>
<td>Treaty with Finland.</td>
<td>Treaty with Finland</td>
<td>Treaty with Finland</td>
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<tr>
<td>AV72(e)</td>
<td>All remaining Australian treaties refer to 'interests in a company'.</td>
<td></td>
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</tr>
<tr>
<td>AV 72(f)</td>
<td>2015 German Treaty refers back 365 days for determining whether shares met underlying asset test in relation to immovable property. Reflects BEPS recommendations.</td>
<td></td>
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</tr>
<tr>
<td>AV73</td>
<td>All but eight of Australian treaties refer to assets of the company consisting 'principally' of real property instead of specifying that 50% of the assets consist of real property as in the OECD Model.</td>
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</tbody>
</table>

|  | All Australian treaties other than treaties with Austria, Belgium, Chile, Denmark, Germany, Finland, Italy, Malta, the Philippines, Sweden and Switzerland. |
|  | 2015 German Treaty. |
|  | All Australian treaties other than treaties with Chile, Finland, 1972 Germany, Japan, Norway, 2013 Switzerland, 2010 Turkey and 2015 Germany. |
|  | Treaty with the Netherlands 1976 |
|  | 1976 Netherlands Treaty |
| Treaty with Turkey | 2015 German Treaty |
| Treaty with Turkey | 2015 German Treaty |
| Treaty with Turkey | 2015 German Treaty |
| Treaty with Turkey | 2009 New Zealand Treaty |

UN Model does not use this terminology. UN Model does not refer to 'interests in a company'.
<table>
<thead>
<tr>
<th>Art 13(5)</th>
<th>AV74</th>
<th>AV75</th>
<th>AV76</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Four Australian treaties include a paragraph which applies only in respect of 'income from the alienation of capital assets of the enterprise'.</strong></td>
<td>Treaties with Belgium, Denmark, the Philippines, Sweden and .</td>
<td>1979 Belgian Treaty</td>
<td>No equivalent in the UN Model</td>
</tr>
<tr>
<td>Only six Australian treaties include a paragraph identical to OECD 13(5).</td>
<td>Treaties other than treaties with Belgium, Chile, Denmark, Finland, France, Germany 2015, Japan, Norway, the Philippines, Sweden, 2013 Switzerland and Turkey do not include paragraph 13(5) or an equivalent paragraph.</td>
<td>1976 <strong>Netherlands Treaty</strong> and Treaty with New Zealand 2009</td>
<td>Article 13(6) in the UN Model is the equivalent to OECD Article 13(5)</td>
</tr>
<tr>
<td><strong>Provision giving state of residence of the company right to tax gains from shares with a minimum participation</strong></td>
<td>Treaties with Italy, the Netherlands, Turkey, India, Spain, Japan and Chile. Terms of provision vary</td>
<td>1976 Netherlands Treaty</td>
<td>UN Model Article 13(5) is an equivalent</td>
</tr>
<tr>
<td>Art 13 Australian addition</td>
<td>percentage in a company that is a resident of a Contracting State.</td>
<td>considerably between these treaties.</td>
<td>provision</td>
</tr>
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<tr>
<td>AV77(a)</td>
<td>Ten Australian treaties include a definition of ‘real property’ which states that ‘real property’ includes rights to exploit or explore natural resources.</td>
<td>Treaties with Austria, Belgium, Canada, Denmark, Ireland, Italy, Korea, the Netherlands, the Philippines, and Sweden.</td>
<td>1976 Netherlands Treaty</td>
</tr>
<tr>
<td>AV77(b)</td>
<td>The USA treaty contains a definition of ‘real property’ but that definition does not expressly include rights to exploit or explore natural resources.</td>
<td>The 1982 USA treaty.</td>
<td>The 1982 USA treaty</td>
</tr>
<tr>
<td>Art 13 Australian addition</td>
<td>Twenty six Australian treaties include a saving provision for domestic law in relation to the taxation of capital</td>
<td>Treaties with Argentina, Canada, China, Czech Republic, Fiji, Hungary, India, Indonesia, Kiribati,</td>
<td>1988 China Treaty</td>
</tr>
<tr>
<td>AV78</td>
<td></td>
<td></td>
<td>2009 New Zealand Treaty</td>
</tr>
</tbody>
</table>

| | | | No equivalent in UN Model |
|--------------------------|------|-----------------------------------------------------------------|---------------------------------------------------------------------------------|----------------------------|-----------------|----------------|
| Art 17(2)                | AV80 | Does not appear in 1969 Singapore treaty. | 1969 Singapore Treaty | **Did not appear in Australian tax treaties prior to German Treaty 1972. Australia-United Kingdom** | 1969 Singapore Treaty | UN Art 17(2) is the equivalent to OECD Art 17(2) |

- Malaysia, Mexico, New Zealand, Papua New Guinea, Poland, Romania, Russia, Singapore, Slovakia, South Africa, Spain, Sri Lanka, Taiwan, Thailand, the UK, the US, and Vietnam.
<table>
<thead>
<tr>
<th>AV81</th>
<th>Operation of paragraph restricted to cases where public entertainer controls, directly or indirectly the enterprise deriving the profits.</th>
<th>Restriction appears in treaties with Canada, Germany, the Netherlands, old Switzerland, and the US</th>
<th><strong>Tax Treaty 1967</strong>  <em>did not contain Art 17. Was not in 1963 OECD Model</em></th>
<th>1972 <strong>German Treaty</strong></th>
<th>1982 US Treaty</th>
<th>UN Art 17(2) is not so restricted</th>
</tr>
</thead>
<tbody>
<tr>
<td>AV82</td>
<td>Article 21 is not included in seven Australian treaties.</td>
<td>Treaties with Belgium, Germany, Italy, the Netherlands, the Philippines, Singapore and 2013 Switzerland.</td>
<td><strong>Australia – United Kingdom Tax Treaty 1946</strong>  <em>did not contain an equivalent to Art 21</em></td>
<td><strong>2013 Swiss Treaty</strong></td>
<td><strong>UN Model contains equivalents to Arts 21(1) and (2) but adds Art 21 (3). See discussion of AV85 below</strong>*</td>
<td></td>
</tr>
<tr>
<td>AV83</td>
<td>Nineteen post 1977 Australian treaties continue to use the language in the 1963 OECD Article 21(1) rather than the language in the 1977 OECD Article 21(1).</td>
<td>Treaties with Austria, Canada, Denmark, Fiji, India, Indonesia, Ireland, Kiribati, Korea, Malta, Papua New Guinea, Poland, Spain, Sri Lanka, Sweden and Thailand.</td>
<td>1980 Canada Treaty</td>
<td>1992 Indonesia Treaty</td>
<td>UN Art 21(1) is identical to 1977 OECD Art 21(1)</td>
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<tr>
<td>Art 21(2)</td>
<td>Seventeen Australian treaties omit the exclusion of immovable property from Article 21(2).</td>
<td>Treaties with Austria, Canada, Denmark, Fiji, Hungary, India, Indonesia, Ireland, Kiribati, Korea, Malta, Papua New Guinea, Poland, Spain, Sri Lanka, Sweden and Thailand.</td>
<td>1980 Canada Treaty</td>
<td>1992 Indonesia Treaty</td>
<td>UN Model Art 21(2) includes reference to immovable property</td>
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<tr>
<td>AV84</td>
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<tr>
<td>Art 21 Australian addition</td>
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<tr>
<td>AV85</td>
<td>All Australian treaties which include Article 21, other than the treaty with Sweden, contain a provision giving the source country the right to tax</td>
<td>All Australian treaties other than the treaty with Sweden.</td>
<td>1980 Canada Treaty.</td>
<td>2015 German Treaty</td>
<td>UN Model Art 21(3) but reference is to income ‘arising in</td>
<td></td>
</tr>
<tr>
<td>Art 21 Australian addition</td>
<td>Treaty with Sweden gives source country right to tax in paragraph 1 and in paragraph 2 states that the residence country has exclusive right to tax income of its residents from sources in the residence country or a third country</td>
<td>Treaty with Sweden</td>
<td>Cf the ‘tax on third country income’ article in the 1967 Australia – UK treaty.</td>
<td>No equivalent in UN Model</td>
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<tr>
<td>AV86</td>
<td>Treaty with Sweden</td>
<td>Treaty with Sweden</td>
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<tr>
<td>Art 22</td>
<td>Not included in any Australian tax treaties except 2015 German Treaty</td>
<td>All Australian treaties other than 2015 German Treaty</td>
<td>1946 Australia – UK Tax Treaty</td>
<td>UN Model contains an article dealing with Taxation of Capital</td>
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<tr>
<td>AV87</td>
<td></td>
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<tr>
<td>Art 22</td>
<td>2015 German Treaty Art 21 modifies</td>
<td>2015 German Treaty</td>
<td>2015 German</td>
<td>2015 German</td>
<td></td>
<td></td>
</tr>
<tr>
<td>AV87(a)</td>
<td>2015 German Treaty</td>
<td>2015 German Treaty</td>
<td>2015 German</td>
<td>Modification not in</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 23 Australian Variations</td>
<td>OECD Art 22 by only applying to Germany not reciprocally</td>
<td>Treaties</td>
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<tr>
<td>AV88</td>
<td>Australian treaties typically allow a credit for foreign tax paid in the treaty partner country on income in respect of Australian tax payable on the income. The effect is that a credit is not allowed in respect of foreign source income which is exempt from Australian tax.</td>
<td>All Australian treaties</td>
<td></td>
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<tr>
<td>AV89</td>
<td>Twenty one Australian treaties prior to 2003 allowed a credit for foreign underlying corporate tax where the Australian shareholder held 10% or more voting interest in the paying company</td>
<td>Treaties with Canada, China, Czech Republic, Fiji, Hungary, India, Indonesia, Kiribati, Malaysia, Mexico, Papua New Guinea, Poland, Romania, Singapore, Slovakia, South Africa, Spain, Sri Lanka, Treaty with the UK 1967 was the first to have a corresponding provision. Credits for</td>
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</table>

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<thead>
<tr>
<th>Treaty</th>
<th>Treaty</th>
<th>UN Model</th>
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</thead>
<tbody>
<tr>
<td>1946 Australia – UK Tax Treaty</td>
<td>2015 German Treaty</td>
<td>Article 22B of the UN Model differs from Article 23B of the OECD Model but does not have the same structure as Australian tax treaties</td>
</tr>
<tr>
<td>Treaty with Czech Republic signed March 2010</td>
<td>UN Model does not provide for a credit for foreign underlying tax</td>
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</tbody>
</table>
Fourteen Australian tax treaties have provided for tax sparing, however, with the exception of the treaty with the Philippines, these provisions were subject to time limits which have now expired. The tax sparing provision in the Philippines treaty is confined to royalty income.

The treaties in which Australia agreed to tax sparing were those with Argentina, China, Fiji, India, Kiribati, Korea, Malaysia, Malta, Papua New Guinea, the Philippines, Singapore, Sri Lanka, Thailand, and Vietnam.

**Article 22(3) of 2015 German Treaty contains rules dealing with situation**

- **2015 German Treaty**
- **2015 German Treaty**
- **2015 German Treaty**
- No equivalent
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<table>
<thead>
<tr>
<th>Art 24(1)</th>
<th>AV91</th>
</tr>
</thead>
<tbody>
<tr>
<td>where different characterisation in the Contracting States of items of income, profits, gains or elements thereof. Reflects BEPS recommendations.⁹</td>
<td>Only eight Australian treaties include a non-discrimination article. In the case of the treaty with the United States the non-discrimination article was not given the force of law in Australia and remains as an agreement between governments.</td>
</tr>
<tr>
<td>Treaties other than those with Chile, 2015 Germany, Finland, Japan, Norway, South Africa, 2013 Switzerland, Turkey, the UK and the US.</td>
<td>Treaty with the United Kingdom 1946. Treaty with UK 1967 first treaty where treaty partner's draft had contained a non-discrimination article The treaty with the UK in 2003 was the first to give the force of law in Australia to a non-</td>
</tr>
<tr>
<td>2008 Treaty with France most recent new treaty to omit a non-discrimination article. Protocols to Belgian, Singaporean and Malaysian treaties did not insert a non-discrimination article into those treaties.</td>
<td>UN Model Art 24(1) is identical to OECD Model Art 24(1).</td>
</tr>
</tbody>
</table>

⁹ While reflecting BEPS recommendations this variation can be seen as having its origins in the 1999 OECD Partnership Report.
<table>
<thead>
<tr>
<th>Art 24(1)</th>
<th>AV92</th>
<th>Only six Australian treaties include the final sentence in OECD Model Art 24(1).</th>
<th>All Australian treaties except those with Chile, Finland, 2015 Germany, Japan, South Africa and Switzerland.</th>
<th>1982 US Treaty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 24(2)</td>
<td>AV93</td>
<td>OECD Art 24(2) does not appear in any Australian treaties</td>
<td>All Australian treaties.</td>
<td>2010 Turkish Treaty</td>
</tr>
<tr>
<td>Art 24(3)</td>
<td>AV94</td>
<td>Six Australian treaties qualify the first sentence in OECD Art 24(3) by</td>
<td>Treaties with Chile, Finland, Japan, South Africa, Turkey and the UK.</td>
<td>2015 German Treaty</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Treaty with the USA 1982 was the first treaty containing a non – discrimination article that did not contain an equivalent to OECD Art 24(2).</td>
<td>UN Model Art 24(2) is identical to OECD Model Art 24(2).</td>
</tr>
<tr>
<td>AV95</td>
<td>Adding, 'in similar circumstances'. Two Australian treaties qualify the first sentence in OECD Art 24(3) by adding, 'in the same circumstances'. Treaties with Norway and the USA.</td>
<td>Treaty with the USA 1982</td>
<td>Model Modification does not appear in UN Model</td>
<td></td>
</tr>
<tr>
<td>---</td>
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<td>---</td>
<td></td>
</tr>
<tr>
<td>AV96</td>
<td>Second sentence in OECD Art 24(3) is only included in unmodified form in treaty with Japan 2013 treaty with Switzerland and 2015 German Treaty. Treaties with Chile, Norway, Turkey, the UK and the USA. Treaties with Finland and South Africa include the sentence but omit the phrase 'on account of civil status or family responsibilities'.</td>
<td>Treaty with Turkey 2010.</td>
<td>Second sentence of Art 24(3) in UN Model is identical to OECD Model</td>
<td></td>
</tr>
<tr>
<td>AV97</td>
<td>Second sentence in OECD Art 24(3) is included in Finland and South Africa in modified form but is not included in any other Australian treaties other than treaty with Japan. Treaties with Finland and South Africa. All other Australian treaties, which include an equivalent to Art 24, other than the treaties with Japan and the revised Swiss Treaty, do not include the second sentence in OECD Art 24(3).</td>
<td>Treaty with Finland 2007</td>
<td>Treaty South Africa 2008</td>
<td>Second sentence of Art 24(3) in UN Model is identical to OECD Model</td>
</tr>
<tr>
<td>Art 24(5)</td>
<td>AV98</td>
<td>Six Australian treaties modify Art 24(5) by adding the phrase ‘similar enterprises in similar circumstances’.</td>
<td>Treaties with Finland, Japan, Norway, South Africa, Turkey, and the UK.</td>
<td>Treaty with the UK 2003</td>
</tr>
<tr>
<td>---</td>
<td>---</td>
<td>---</td>
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<td>---</td>
</tr>
<tr>
<td>AV98(a)</td>
<td>Treaty with Chile modifies Art 24(5) by adding the phrase ‘similar company in similar circumstances’.</td>
<td>Treaty with Chile.</td>
<td>Treaty with Chile.</td>
<td>Treaty with Chile signed March 2010</td>
</tr>
<tr>
<td>AV98(b)</td>
<td>Treaty with the USA modifies Art 24(5) by adding the phrase ‘similar corporations in similar circumstances’.</td>
<td>Treaty with the USA.</td>
<td>Treaty with the USA.</td>
<td>Treaty with the USA 1982</td>
</tr>
<tr>
<td>Art 24(6)</td>
<td>AV99</td>
<td>Treaties with Norway, South Africa and the USA do not include OECD Art 24(6).</td>
<td>Treaties with Norway, South Africa and the USA 1982.</td>
<td>Treaty with the USA 1982</td>
</tr>
<tr>
<td>AV100</td>
<td>Treaties with Finland, Turkey and the UK modify Art 24(6) by stating that</td>
<td>Treaties with Finland, Turkey and the UK.</td>
<td>Treaties with Finland, Turkey and the UK.</td>
<td>Treaty with the UK 2003</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AV101</td>
<td>Art 24 only applies to taxes subject to the treaty. Treaty with Chile states that Art 24 applies to the taxes subject to the treaty as well as the GST in the case of Australia and the VAT in the case of Chile.</td>
<td>Treaty with Chile.</td>
<td>Treaty with Chile.</td>
<td>2010 Chile Treaty</td>
</tr>
<tr>
<td>-------</td>
<td>--------------------------------------------------------------------------------------------------</td>
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<td>------------------</td>
</tr>
<tr>
<td>AV102(a)</td>
<td>All Australian treaties which include a non-discrimination article exclude provisions designed to prevent the avoidance or evasion of taxes from its operation.</td>
<td>Treaties with Chile, Finland, Germany 2015, Japan, Norway, South Africa, Switzerland 2013, Turkey, the UK and the US. No other Australian treaties include a non-discrimination article.</td>
<td>Treaty with USA 1982.</td>
<td>2015 German Treaty</td>
</tr>
<tr>
<td>AV102(b)</td>
<td>Australia’s treaties with Finland, Japan, Norway, South Africa, Turkey and the UK exclude from the operation of Art 24 provisions which do not permit deferral of tax on transfer of an asset where subsequent transfer would be beyond the tax jurisdiction of the Contacting State.</td>
<td>Treaties with Finland, Japan, Norway, South Africa, Turkey and the UK.</td>
<td>Treaty with the UK 2003.</td>
<td>2010 Turkish Treaty</td>
</tr>
<tr>
<td>AV102(c)</td>
<td>Australia’s treaties with Finland, Japan, Norway, South Africa, Turkey and the UK exclude from the operation of Art 24 provisions which provide for consolidation of groups of entities as a single entity for tax purposes.</td>
<td>Treaties with Finland, Japan, Norway, South Africa, Turkey and the UK.</td>
<td>Treaty with the UK 2003.</td>
<td>2010 Turkish Treaty</td>
</tr>
<tr>
<td>AV102(d)</td>
<td>Australia’s treaties with Finland, Japan, Norway and South Africa exclude from the operation of Art 24 provisions which do not allow tax rebates or credits in relation to dividends.</td>
<td>Australia’s treaties with Finland, Japan, Norway and South Africa.</td>
<td>Treaty with Norway 2006</td>
<td>2006 Norwegian Treaty</td>
</tr>
<tr>
<td>----------------</td>
<td>--------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------</td>
<td>-----------------</td>
<td>-----------------------</td>
</tr>
<tr>
<td>Art 24 Australian addition</td>
<td>All Australian treaties which include Art 24, other than the USA, Swiss 2013 and German 2015 treaties, exclude from the operation of Art 24 provisions which provide for deductions to eligible taxpayers for expenditure on research and development.</td>
<td>Treaties with Chile, Finland, Japan, Norway, South Africa, Turkey, and the UK. No other Australian treaties, other than the treaties with the USA, 2013 Switzerland and 2015 Germany include a non-discrimination article.</td>
<td>Treaty with the UK 2003.</td>
<td>2010 Turkish Treaty</td>
</tr>
<tr>
<td>Art 24 Australian addition</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AV102(f)</td>
<td>All Australian treaties which include Art 24, other than the USA, Swiss 2013 and German 2015 treaties, exclude from the operation of Art 24 provisions which are otherwise agreed to be unaffected by Art 24.</td>
<td>Treaties with Chile, Finland, Japan, Norway, South Africa, Turkey, and the UK. No other Australian treaties, other than the treaties with German 2015, Switzerland 2013 and the USA, include a non-discrimination article.</td>
<td>2003 UK Treaty</td>
<td>2010 Turkish Treaty</td>
</tr>
<tr>
<td>Art 24</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AV102(g)</td>
<td>Treaties with Chile, Norway, Turkey and the UK exclude from the operation of Art 24 provisions that restrict entitlement to personal allowances, reliefs and reductions to residents.(^{10})</td>
<td>Treaties with Chile, Norway, Turkey and the UK</td>
<td>Treaty with the UK 2003.</td>
<td>2010 Turkish Treaty with Turkey signed April 2010</td>
</tr>
<tr>
<td>Art 24 Most favoured nation clauses</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\(^{10}\) It is questionable whether this is a true variation or merely the relocation to a separate paragraph the final sentence in OECD Article 24(3).
<table>
<thead>
<tr>
<th>AV103</th>
<th>Australia's treaties with Korea, Mexico, Romania, Spain and Taipei contain a provision to the effect that if Australia subsequently enters into a treaty with a third state containing a non-discrimination article Australia will enter into negotiations with the treaty partner with a view to providing the same treatment to the treaty partner as is provided in the treaty with the third state.</th>
<th>Treaties with Korea, Mexico, Romania, Spain and Taipei.</th>
<th>1982 Korean Treaty</th>
<th>2003 Mexican Treaty</th>
<th>No equivalent in UN Model.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 25(1)</td>
<td>Art 25(1) AV104(a) Australia’s treaties with Canada, Germany, Singapore and Switzerland (old treaty) do not include a time limit in Article 25(1).</td>
<td>Treaties with Canada, Germany, Singapore and Switzerland (old treaty)</td>
<td>Australia — United States Tax Treaty 1953 contained mutual agreement article with no time limit</td>
<td>Treaty with the United Kingdom 2003.</td>
<td>Treaty with Canada 1980</td>
</tr>
<tr>
<td>AV104(b)</td>
<td>The treaty with the United Kingdom specifies the time limits which apply.</td>
<td>Treaty with the United Kingdom 2003.</td>
<td>Treaty with the United Kingdom</td>
<td>Treaty with the United Kingdom</td>
<td>Variation not in UN Model</td>
</tr>
<tr>
<td>AV104(c)</td>
<td>in domestic law.</td>
<td></td>
<td></td>
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<tr>
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<td></td>
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</tr>
<tr>
<td></td>
<td>The treaties with Italy, Malaysia and the Philippines uses a two year time limit.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>AV104(d)</th>
<th>in domestic law.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The treaties with the Czech Republic and Slovakia use a four year time period.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Art 25(2)</th>
<th>in domestic law.</th>
</tr>
</thead>
<tbody>
<tr>
<td>AV105</td>
<td>Treaty with Singapore does not contain Art 25(2) but includes words having similar effect to Art 25(2) in paragraph (1) of its mutual agreement procedure article.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Treaty with Italy, Malaysia, and the Philippines.</th>
<th>Treaty with Italy, Malaysia, and the Philippines.</th>
<th>Treaty with Italy</th>
<th>Treaty with Italy</th>
</tr>
</thead>
</table>

**Treaty with Singapore 1969**

- **Australia – United States Tax Treaty 1953 also had this form.**
- **Australia – Singapore Tax Treaty 1969 follows Australia-United Kingdom Tax Treaty 1967**

**Treaty with Singapore 1969**

- UN Model Art 25(2) identical to OECD Model Art 25(2).
<table>
<thead>
<tr>
<th>AV106(a)</th>
<th>Treaties with Belgium, Canada, Fiji, Germany, Italy, the Philippines and Switzerland (old treaty) omit the reference to ‘notwithstanding any time limits’ in Art 25(2).</th>
<th>Treaties with Belgium, Canada, Fiji, Germany, Italy, the Philippines, and Switzerland (old treaty).</th>
<th>1990 Fiji Treaty</th>
<th>Variation not in UN Model</th>
</tr>
</thead>
<tbody>
<tr>
<td>AV106(b)</td>
<td>Australia is required to implement agreement ‘notwithstanding any time limits’ in treaties with Mexico, Chile and Turkey but respective treaties set out time limits for relevant treaty partner.</td>
<td>Treaties with Mexico, Chile and Turkey.</td>
<td>2010 Turkish Treaty</td>
<td>Variation not in UN Model</td>
</tr>
<tr>
<td>Art 25(4)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AV107</td>
<td>All Australian treaties omit the phrase 'including through a joint committee consisting of themselves or their representatives.'</td>
<td>All Australian treaties.</td>
<td><em>Australia – United Kingdom Tax Treaty 1967 contained a provision permitting communication between tax authorities which did not refer to a joint committee.</em></td>
<td>2015 German Treaty.</td>
</tr>
<tr>
<td>-------</td>
<td>---------------------------------------------------------------------------------------------------------------------------------</td>
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<td>------------------------------------------------------------------------------------------------------------------------------------------------</td>
<td>-----------------</td>
</tr>
<tr>
<td>AV108</td>
<td>Equivalent provision included in <em>The early mutual</em></td>
<td>All treaties other than treaties with 2010 Turkish</td>
<td>UN Model does</td>
<td></td>
</tr>
<tr>
<td>Art 25 Australian addition</td>
<td>Treaties with Canada, Chile, France, Japan, Malaysia, Mexico, New Zealand, Norway, South Africa, Turkey and the UK contain an alternative dispute resolution mechanism under which a dispute can be taken to the Council for Trade in Services established under GATS.</td>
<td>Treaty with South Africa 1999</td>
<td>2013 Swiss Treaty</td>
<td>No equivalent in UN Model.</td>
</tr>
<tr>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td>AV109</td>
<td>Treaties with Canada, Chile, France, Japan, Malaysia, Mexico, New Zealand, Norway, South Africa and Turkey.</td>
<td>Treaty with South Africa 1999</td>
<td>2013 Swiss Treaty</td>
<td>No equivalent in UN Model.</td>
</tr>
<tr>
<td></td>
<td>Treaty with New Zealand and there it is limited to issues of fact. Equivalent provision is included 2013 Swiss Treaty and in 2015 German Treaty.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 26(1)</td>
<td>Australia’s pre 2005 treaties conform to the pre 2005 OECD Model. Australia’s post 2005 treaties confirm to the 2005 amendment to the OECD Model. In addition, protocols to the treaties with Singapore, Malaysia, and South Africa mean that those treaties now conform to the 2005 amendments to Art 26(1) of the OECD Model. This has not been classified as a variation. The 2015 German treaty contains minor variations from the OECD Article 26(1) in that the obligation to provide information on behalf of political subdivisions or local authorities is confined to Germany. This has not been classified as a variation.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 26(3)</td>
<td>AV110</td>
<td>Paragraph 3 of the Australia-USA Tax Treaty varies from the OECD Model</td>
<td>1982 USA Treaty</td>
<td>1982 USA Treaty</td>
</tr>
<tr>
<td></td>
<td>OECD Art 26(3).</td>
<td></td>
<td></td>
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<td>---</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 26(4)</td>
<td>Australia’s pre 2005 treaties, and the South African treaty as amended by a 2008 Protocol, conform to the pre 2005 OECD Model. Australia’s post 2005 treaties confirm to the 2005 amendment to the OECD Model. This has not been classified as a variation.</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Art 26(5)</td>
<td>Australia’s pre 2005 treaties, and the South African Treaty as amended by a 2008 Protocol, conform to the pre 2005 OECD Model. Australia’s post 2005 treaties confirm to the 2005 amendment to the OECD Model. This has not been classified as a variation.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 27</td>
<td>AV111 Of Australia’s tax treaties coming into force post 2008 only those with Finland, France, New Zealand and Norway, the South African Treaty as</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>All post 2008 tax treaties other than those with Finland, France, New Zealand, Norway, the South African Treaty as amended by the 2008 Treaty with Japan 2008 September 1966 UK draft 2015 German Treaty. UN Model has no equivalent to Art 27.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
amended by a 2008 Protocol, the 2013 Swiss Treaty and the 2015 German Treaty contain an assistance in collection article.

| Art 27(8) | AV112 | All Australian treaties that contain an assistance in collection article include an additional sub-paragraph stating that there is no obligation on a contracting state ‘to provide assistance if that State considers that the taxes with respect to which assistance is requested are imposed contrary to generally accepted taxation principles.’ Paragraph 37 of the OECD Commentary suggests that this subparagraph could be included in the assistance in

Protocol, the 2013 Swiss Treaty and the 2015 German Treaty contained an assistance in collection article but at Australia's request it was excluded from the final version of the treaty.

Treaties with Finland, France, New Zealand, Norway, the South African Treaty as amended by the 2008 Protocol, the 2013 Swiss Treaty and the 2015 German Treaty

Protocol to Treaty with South Africa 2008

2015 German Treaty
<table>
<thead>
<tr>
<th>Additional article</th>
<th>AV113</th>
<th>Article 28 provides for procedural rules for deduction of withholding tax at source at rates set in domestic law and for subsequent refund where rates reduced by treaty.</th>
<th>2015 German Treaty</th>
<th>2015 German Treaty</th>
<th>2015 German Treaty</th>
<th>No equivalent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Additional article</td>
<td>AV114</td>
<td>Article 30 provides for protection of personal information</td>
<td>2015 German Treaty</td>
<td>2015 German Treaty</td>
<td>2015 German Treaty</td>
<td>No equivalent</td>
</tr>
</tbody>
</table>
### APPENDIX 4

**TABLE 2: VARIATIONS FROM CURRENT OECD MODEL HAVING THEIR ORIGINS IN AUSTRALIA – UNITED KINGDOM TAX TREATY 1946 AND VARIATIONS FROM 1945 UNITED KINGDOM – UNITED STATES TAX TREATY**

<table>
<thead>
<tr>
<th>OECD Model Article</th>
<th>Variation From UK – US Treaty 1945</th>
<th>Variation present in first UK draft 6th May 1946</th>
<th>History of amendments between first draft and final treaty</th>
<th>Initiator of variation from UK – US 1945</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 1</td>
<td>No</td>
<td>OECD Art 1 not present in UK draft of 6th May 1946</td>
<td>OECD Art 1 not present in Draft II, Draft III or Final form of Article</td>
<td>UK</td>
</tr>
<tr>
<td>Art 2(1) AV1</td>
<td>No – same basic approach</td>
<td>Yes – but not in the form that appeared in final treaty</td>
<td>Draft II (22nd May 1946 – worked on in Australia) Article I(1) The taxes which are the subject of the present Agreement are: In the Commonwealth of Australia: The Commonwealth income taxes including sur-taxes and undistributed profits taxes (hereinafter referred to as “Australian tax”); In the United Kingdom of Great Britain and Northern Ireland: The income tax (including sur-tax) and the national defence contribution (hereinafter referred to as “United Kingdom tax” [Change from draft of 6th May 1946]</td>
<td>Basic approach UK Precise terms Australia</td>
</tr>
<tr>
<td>Draft II as at 19th July 1946</td>
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</tr>
<tr>
<td>[Unchanged]</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Draft III (Prepared in Australia 8th August 1946)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Article I(1)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The taxes which are the subject of the present Agreement are:

In the Commonwealth of Australia:
The Commonwealth income tax (including super-tax), the social services contribution, the additional tax assessed on the undistributed amount of the distributable income of a private company, the further tax imposed on the portion of the taxable income of a company (other than a private company) which has not been distributed as dividends, and the war-time (company) tax (hereinafter referred to as “Australian tax”);

[Change from Draft II]
In the United Kingdom of Great Britain and Northern Ireland:
The income tax (including sur-tax), the excess profits tax, and the national defence contribution (hereinafter referred to as “United Kingdom tax”)

[No change from Draft II]
Final form of Article I (1) in Treaty

[As per Draft III]
<table>
<thead>
<tr>
<th>Art 2(2) AV2</th>
<th>No</th>
<th>No equivalent in UK draft of 6th May 1946</th>
<th>No equivalent in Draft II, Draft III or Final Form of Article.</th>
<th>UK</th>
</tr>
</thead>
</table>

**Art 2(4)**

Variation not present in any current Australian Tax Treaties

No - Virtually identical to UK – Australia 1946

Equivalent provision in UK draft of 6th May 1946 was Art II(2) which read:

(2) The present Agreement shall also apply to any other taxes of a substantially similar character imposed by either Contracting Government subsequently to the date of signature of the present Agreement or by the Government of any territory of which the present Agreement is extended under Article XIV.

No changes in Draft II, Draft III and Final form of Article

UK

<p>| Art 3(1) AV3 | Yes - no equivalent in UK – US 1945 | UK draft of 6th May 1946 included a definition of 'industrial or commercial profits' as follows: (i) The term &quot;industrial or commercial profits&quot; includes mining and farming profits but does not include income in the form of dividends, interest, rents or royalties, insurance premiums, management charges, or remuneration for personal services. | Draft II (22nd May 1946 – worked on in Australia) (i) The term &quot;industrial or commercial enterprise or undertaking&quot; includes an enterprise or undertaking engaged in mining, agricultural or pastoral activities, or in the business of banking, insurance, life insurance or dealing in investments, and the term &quot;industrial or commercial profits&quot; includes profits from such activities or business but does not include income in the form of dividends, interest, rents, royalties, management charges, or remuneration for personal services. | Basic structure - UK Precise terms- Australia |</p>
<table>
<thead>
<tr>
<th></th>
<th>Draft II as at 19th July 1946</th>
<th>Draft III (8th August 1946)</th>
<th>Final form of Article</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 1946</td>
<td>[no change from Draft II 22nd May 1946]</td>
<td>[no change from Draft II]</td>
<td>[no change from Draft II]</td>
</tr>
</tbody>
</table>

| Art 3(2) | No - Substantially similar but not identical | UK draft of 6th May 1946 was identical to what would later become Art 3(2) of the 1963 Draft OECD Model | [No changes made in Draft II, Draft III, or the Final form of Article.] |

| Art 4(1) AV4 | No – same basic approach but detailed drafting different | Yes, but not in form that appeared in final version of the treaty Article II(f) The terms “resident of the United Kingdom” and “resident of Australia” mean respectively any person who is resident in the United Kingdom for the purposes of United Kingdom tax and not resident of Australia for the purposes of Australian tax and any person who is resident in Australia for the purposes of Australian tax who is not resident in the United Kingdom for the purposes of United Kingdom tax; and a company shall be regarded as resident in the United Kingdom if its business is managed and controlled in the United Kingdom and shall be regarded as resident of Australia if it is incorporated in Australia or if, not being incorporated in Australia, it carries on business in | Draft II (22nd May 1946 – worked on in Australia) Article II(f) The terms “resident of the United Kingdom” and “resident of Australia” mean respectively any person who is resident in the United Kingdom for the purposes of United Kingdom tax and not resident of Australia for the purposes of Australian tax and any person who is resident of Australia for the purposes of Australian tax who is not resident in the United Kingdom for the purposes of United Kingdom tax; and a company shall be regarded as resident in the United Kingdom if its business is managed and controlled in the United Kingdom and shall be regarded as resident of Australia if it is incorporated in Australia or if, not being incorporated in Australia, it carries on business in Basic approach UK Detailed drafting Australia |
Kingdom and shall be regarded as resident in Australia if its business is managed and controlled in Australia.

Australia and has either its central management and control in Australia or its voting power controlled by Australian residents. \[\text{Change from draft of 6\textsuperscript{th} May 1946}\]

Draft II as at 19\textsuperscript{th} July 1946

Article II(f)

The terms “resident of the United Kingdom” and “resident of Australia” mean respectively any person who is resident in the United Kingdom for the purposes of United Kingdom tax and not resident of Australia for the purposes of Australian tax and any person who is resident of Australia for the purposes of Australian tax who is not resident in the United Kingdom for the purposes of United Kingdom tax; \[\text{Change from Draft II as at 22\textsuperscript{nd} May 1946}\]

Draft III (8\textsuperscript{th} August 1946)

\[\text{No change from Draft II as at 19\textsuperscript{th} July 1946}\]

Final form of Article

\[\text{As per Draft II as at 19\textsuperscript{th} July 1946}\]

<table>
<thead>
<tr>
<th>Art 5</th>
<th>Definition of PE</th>
<th>United Kingdom draft of 6\textsuperscript{th} May 1946</th>
<th>Draft II (22\textsuperscript{nd} May 1946 – worked on in Australia)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>‘Agricultural, pastoral or forestry property’ not</td>
<td>Article II(j)</td>
<td>Article II(j)</td>
</tr>
</tbody>
</table>
| AV6 | included in list of examples in UK – US 1945
| AV13 | Dependant agent without authority to conclude contracts but who habitually maintains a stock of goods is deemed to be a permanent establishment was included in UK – US 1945 but 'at prices fixed' not in UK – US 1945
| AV15 | Requirement that broker or commission agent not a PE only if

The term "permanent establishment" when used in respect of an enterprise of one of the territories, means a branch, management, mine, farm, or other fixed place of business, but does not include an agency unless the agent has, and habitually exercises, a general authority to negotiate and conclude contracts on behalf of such enterprise or has a stock of merchandise from which he regularly fills orders on its behalf.

An enterprise of one of the territories shall not be deemed to have a permanent establishment in the other territory merely because it carries on business dealings in that other territory through a bona fide broker or general commission agent acting in the ordinary course of his business as such.

The fact that an enterprise of one of the territories maintains in the other territory a fixed place of business exclusively for the purchase of goods or merchandise shall not of itself constitute that fixed place of business a permanent establishment of the enterprise. [No change from draft of 6th May 1946]

UK used term 'farm'.
Australia substituted:
'agricultural or pastoral property'
Australia added
'at prices fixed etc'

UK included deeming re depliant agent

The term "permanent establishment", when used with respect to an enterprise of one of the territories, means a branch, mine, agricultural or pastoral property, or other fixed place of business, but does not include an agency in the other territory unless the agent has, and habitually exercises, authority to conclude contracts on behalf of such enterprise otherwise than at prices fixed by the enterprise or has a stock of merchandise from which he regularly fills orders on its behalf. [Change from draft of 6th May 1946]

An enterprise of one of the territories shall not be deemed to have a permanent establishment in the other territory merely because it carries on business dealings in that other territory through a bona fide broker or general commission agent acting in the ordinary course of his business as such and receiving remuneration in respect of those dealings at a rate not less than that customary in the class of business in question. [Change from draft of 6th May 1946]

The fact that an enterprise of one of the territories maintains in the other territory a fixed place of business exclusively for the purchase of goods or merchandise shall not of itself constitute that fixed place of business a permanent establishment of the enterprise. [No change from draft of 6th May 1946]

Australia inserted
'rate customary'
remuneration at rate customary – not in UK – US 1945

business a permanent establishment of the enterprise.

The fact that a company which is a resident of one of the territories has a subsidiary company which is a resident of the other territory or which is engaged in trade or business in that other territory (whether through a permanent establishment or otherwise) shall not of itself constitute that subsidiary company a permanent establishment of the parent company.

The fact that a company which is a resident of one of the territories has a subsidiary company which is a resident of the other territory or which is engaged in trade or business in that other territory (whether through a permanent establishment or otherwise) shall not of itself constitute that subsidiary company a permanent establishment of its parent company. [No change from draft of 6th May 1946]

Draft II as at 19th July 1946

Article II(j)

The term "permanent establishment", when used with respect to an enterprise of one of the territories, means a branch or other fixed place of business and includes a management, factory, mine, agricultural or pastoral property, but does not include an agency in the other territory unless the agent has, and habitually exercises, authority to conclude contracts on behalf of such enterprise otherwise than at prices fixed by the enterprise or regularly fills orders on its behalf from a stock of goods or merchandise in that other territory. [Change from Draft of 6th May 1946 and from Draft II as at 22nd May 1946]

Provided that an enterprise of one of the territories shall not be deemed to have a

Australia changed word order
permanent establishment in the other territory merely because it carries on business dealings in that other territory through a bona fide broker or general commission agent acting in the ordinary course of his business as such and receiving remuneration in respect of those dealings at the rate customary in the class of business in question. [Change from Draft of 6th May 1946 and from Draft II as at 22nd May 1946]

Provided that the fact that an enterprise of one of the territories maintains in the other territory a fixed place of business exclusively for the purchase of goods or merchandise shall not of itself constitute that fixed place of business a permanent establishment of the enterprise. [Change from draft of 6th May 1946 or from Draft II as at 22nd May 1946]

The fact that a company which is a resident of one of the territories has a subsidiary company which is a resident of the other territory or which is engaged in trade or business in that other territory (whether through a permanent establishment or otherwise) shall not of itself constitute that subsidiary company a permanent establishment of its parent company. [No change from draft of 6th May 1946 or from Draft II as at 22nd May 1946]

Draft III (8th August 1946)

[Only change from Draft II was that the order of the second and third paragraphs was]
| Art 7 | UK addition | Yes | **UK draft 6\(^{th}\) May 1946**

   - Article III(4)
     Profits derived by an enterprise of one of the territories from sales, under contracts concluded in that territory, of goods stocked in a warehouse in the other territory for convenience of delivery and not for purposes of display shall not be attributed to a permanent establishment of the enterprise in that other territory, notwithstanding that the offers of purchase have been obtained by an agent of the enterprise in the other territory and transmitted by him to the enterprise for acceptance. | **Draft II (22\(^{nd}\) May 1946 – worked on in Australia)**

   - [No change in printed copy. Handwritten note indicates to be omitted.]
   - Draft II as at 19\(^{th}\) July 1946
   - [Omitted]
   - Draft III (1\(^{st}\) August 1946)
   - [As per Draft II 19\(^{th}\) July 1946]
   - Final form of Article
   - [As per Draft II 19\(^{th}\) July 1946] | **Initial UK addition rejected by Australia** |

| Art 7(3) | No | No equivalent to Art 7(3) in UK draft of 6\(^{th}\) May 1946 | **No change in Draft II, Draft III, or Final form of Article** | **UK** |

| Art 7 | Australian Addition | Yes | **Not in original UK draft of 6\(^{th}\) May 1946**

   - Article III(3)
     Where an enterprise of one of the territories | **Draft II (22\(^{nd}\) May 1946 – worked on in Australia)**

   - **[No change from UK draft of 6\(^{th}\) May 1946]** | **Australia**

   - **UK involved in final Drafting** |
<table>
<thead>
<tr>
<th>Draft II as at 19th July 1946</th>
</tr>
</thead>
<tbody>
<tr>
<td>Article III(3)</td>
</tr>
</tbody>
</table>

Where an enterprise of one of the territories is engaged in trade or business in the other territory through a permanent establishment situated therein, there shall be attributed to that permanent establishment the industrial or commercial profits which it might be expected to derive in that other territory if it were an independent enterprise engaged in the same or similar activities under the same or similar conditions and dealing at arm’s length with the enterprise of which it is a permanent establishment.

<table>
<thead>
<tr>
<th>Draft III (1st August 1946)</th>
</tr>
</thead>
</table>

Where an enterprise of one of the territories is engaged in trade or business in the other territory through a permanent establishment situated therein, there shall be attributed to that permanent establishment the industrial or commercial profits which it might be expected to derive in that other territory if it were an independent enterprise engaged in the same or similar activities and its dealings with the enterprise of which it is a permanent establishment were dealings at arm’s length with that enterprise; and the profits so attributed shall be deemed to be income derived from sources in that other territory.
that other territory.

If the information available to the taxation authorities concerned is inadequate to determine the profits to be attributed to the permanent establishment, nothing in this paragraph shall affect the application of the law of either territory in relation to the liability of the permanent establishment to pay tax on an amount determined by the exercise of a discretion or the making of an estimate by the taxation authorities of that territory: Provided that such discretion shall be exercised or such estimate shall be made, so far as the information available to the taxation authority permits, in accordance with the principle stated in this paragraph.

Final form of Article

As per Draft III with ‘authorities’ being changed to ‘authority’ in both instances where it appears in Draft III and with minor punctuation changes.

| Art 7(6) | AV21 | OECD Article 7(6) not in original UK draft of 6th May 1946 | No change in Draft II, Draft III, or Final form of Article | UK |
| Art 7(7) | No | OECD Article 7(7) not in original UK draft of 6th May 1946 | No change in Draft II, Draft III, or Final form of Article | UK |
| Art 7 | Australian | Not in original UK draft of 6th May 1946 Azerbaijan | Draft II (22nd May 1946 – worked on in Australia) Article III | Australia |
(1) The industrial or commercial profits of a United Kingdom enterprise shall not be subject to Australian tax unless the enterprise is engaged in trade or business in Australia through a permanent establishment situated therein. If it is so engaged, tax may be imposed on those profits by Australia, but only on so much of them as is attributable to that permanent establishment:

Provided that nothing in this paragraph shall affect -

(a) the operation of Divisions 14 and 15 of Part III
of the Australian Income Tax Assessment Act 1936-1946 (or that Act as amended from time to time) relating to film business controlled abroad and insurance with non-residents, or the corresponding provisions of any statute substituted for that Act; or

(b) the application of the law of Australia regarding the imposition of war-time (company) tax where a holding company has elected that its subsidiary companies shall be treated as branches.

[Change from Draft II as at 22nd May 1946]

Draft III (1st August 1946)

[As per Draft II as at 19th July 1946]
Final form of Article

[As per Draft II as at 19th July 1946]

<table>
<thead>
<tr>
<th>Art 8 AV24</th>
<th>Final form of UK – Australia 1946 was closer to UK-US 1945 than was original UK draft</th>
<th>Original UK Draft 6th May 1946 Article V</th>
<th>Draft II (22nd May 1946 – worked on in Australia) Article V</th>
<th>Initial UK draft differed from UK – US 1945. Australia initiated amendments bringing draft closer to UK – US 1945.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Notwithstanding the provisions of Articles III and IV, profits which a resident of one of the territories derives from operating ships or aircraft shall be exempt from tax in the other territory.</td>
<td>Notwithstanding the provisions of Articles III and IV, profits which a resident of one of the territories derives from operating ships whose port of registry is in that territory, or aircraft registered in that territory, shall be exempt from tax in the other territory.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AV28</td>
<td>AV29</td>
<td>No equivalents in UK – US 1945 to OECD 8(2) or 8(3)</td>
<td>Language similar to that used in initial UK draft was reverted to in the September 1966 UK draft and can in this sense be seen as the source of AV24</td>
<td>No change in Draft II, Draft III, or Final form of Article</td>
</tr>
<tr>
<td>------</td>
<td>------</td>
<td>-----------------------------------------------</td>
<td>--------------------------------------------------------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Art 9(2)</td>
<td>AV31</td>
<td>No</td>
<td>OECD Article 9(2) not included in United Kingdom draft of 6th May 1946 (not in 1963 Draft OECD Model)</td>
<td>No change in Draft II, Draft III, or Final form of Article</td>
</tr>
<tr>
<td>Art 9 Australian addition</td>
<td>AV33</td>
<td>Yes</td>
<td>Not included in United Kingdom draft of 6th May 1946</td>
<td>Draft II (22nd May 1946 – worked on in Australia) [No change from UK draft of 6th May 1946]</td>
</tr>
</tbody>
</table>

[Handwritten changes consistent with Draft III]
(a) an enterprise of one of the territories participates directly or indirectly in the management, control or capital of an enterprise of the other territory, or

(b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of one of the territories and an enterprise of the other territory, and

(c) in either case conditions are made or imposed between the two enterprises, in their commercial or financial relations, which differ from those which would be made between independent enterprises,

then any profits which would but for those conditions have accrued to one of those enterprises, but by reason of those conditions have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

Draft III (1st August 1946)

Article IV

(1) Where

(a) an enterprise of one of the territories participates directly or indirectly in the management, control or capital of an enterprise of the other territory, or

(b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of one of the territories and an enterprise of the other territory, and

(c) in either case conditions are operative between the two enterprises in their commercial or financial relations which differ from those which might be expected to operate between independent enterprises dealing at arm’s length with one another,

then, if by reason of those conditions profits which might be expected to accrue to one of the enterprises do not accrue to that enterprise, there may be included in the profits of that enterprise the profits which would have accrued to it if it were an independent enterprise and its dealings with the other enterprise were dealings at arm’s length with that enterprise or an independent
(2) Profits included in the profits of an enterprise of one of the territories under paragraph (1) of this Article shall be deemed to be income derived from sources in that territory and shall be taxed accordingly.

(3) If the information available to the taxation authority concerned is inadequate to determine, for the purposes of paragraph (1) of this Article, the profits which might be expected to accrue to an enterprise, nothing in that paragraph shall affect the application of the law of either territory in relation to the liability of that enterprise to pay tax on an amount determined by the exercise of a discretion or the making of an estimate by the taxation authority of that territory: Provided that such discretion shall be exercised or such estimate shall be make, so far as the information available to the taxation authority permits, in accordance with the principle stated in that paragraph.

\[\text{[Changed from UK draft of 6th May 1946 and Draft II]}\]

Final form of Article

\[\text{[As per Draft III]}\]

<p>| Art 10(1) | Yes. no mention of | United Kingdom draft of 6th May 1946 | Draft II (22nd May 1946 – worked on in Australia) | UK |</p>
<table>
<thead>
<tr>
<th>AV36</th>
<th>‘beneficial ownerships’ although note final sentence in Article VI(1) of UK – US 1945</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Article VI</td>
</tr>
<tr>
<td></td>
<td>(1) The rate of Australian tax on dividends derived from sources within Australia by a resident of the United Kingdom who is subject to United Kingdom tax in respect thereof and not engaged in trade or business in Australia through a permanent establishment situated therein shall not exceed half the rate which would be applicable to the dividends but for this paragraph.</td>
</tr>
<tr>
<td></td>
<td>(2) Notwithstanding the provisions of the foregoing paragraph, dividends paid to a company which is a resident of the United Kingdom by a company which is a resident of Australia paid by a company resident in Australia, all of whose shares (less directors’ qualifying shares) which have under all circumstances full voting rights are beneficially owned by the former company shall be exempt from Australian tax: Provided that exemption shall not be allowed if ordinarily more than one quarter of the gross income of the Australian company is derived from interest and dividends other than interest and dividends from any wholly-owned subsidiary company. [Change from UK draft of 6th May 1946]</td>
</tr>
<tr>
<td></td>
<td>(3) Dividends paid to a United Kingdom resident by a company which is a United Kingdom resident shall be exempt from Australian tax. [Change from UK draft of 6th May 1946]</td>
</tr>
<tr>
<td></td>
<td>(4) Dividends paid by a company resident in the United Kingdom to an individual who is an Australian resident subject to Australian tax in respect thereof and is not engaged in trade or business in the United Kingdom through a permanent establishment situated therein shall be exempt from United Kingdom sur-tax. [Change</td>
</tr>
</tbody>
</table>
(4) Dividends derived from sources within the United Kingdom by an individual who is a resident of Australia subject to Australian tax in respect thereof, and not engaged in trade or business in the United Kingdom through a permanent establishment situated therein, shall be exempt from United Kingdom sur-tax.

Draft II as at 19th July 1946

Article VI

(1) Any dividend paid to a United Kingdom resident by a company which is a United Kingdom resident shall be exempt from Australian tax.

[Change from previous drafts by relocating provision from Article VI(3) to Article VI(1)]

(2) Any dividend paid by a company which is a resident of Australia (whether also resident in the United Kingdom or not) to a company which-

(a) is a United Kingdom resident,

(b) is subject to United Kingdom tax in respect thereof, and

(c) beneficially owns all the shares (less directors' qualifying shares) of the former company,

shall be exempt from Australian tax: Provided that the exemption shall not apply if ordinarily more than one-half of the taxable income of that company is derived from interest, dividends and rents other than interest, dividends and rents from any wholly-owned subsidiary company the taxable income of which consists wholly or mainly of industrial or commercial profits. [Change from previous drafts]
(3) Without limiting the exemptions provided by paragraphs (1) and (2) of this article, the amount of Australian tax payable in respect of any dividend paid out of profits derived from sources in Australia to a United Kingdom resident who is subject to United Kingdom tax in respect thereof and is not engaged in trade or business in Australia through a permanent establishment situated therein, shall not exceed half the amount which would be payable in respect of the dividend but for this paragraph. [Change from previous drafts]

(4) Notwithstanding the foregoing provisions of this Article, the amount of the additional tax assessable in respect of the undistributed amount of the distributable income of a company which is a private company for purposes of Australian tax shall be the amount which would have been assessable if those provisions had not been included in this Agreement. [Change from previous drafts]

(5) Any dividend paid by a company resident in the United Kingdom (whether also a resident of Australia or not) to an individual who-

(a) is an Australian resident,

(b) is subject to Australian tax in respect thereof, and

(c) is not engaged in trade or business in the United Kingdom through a permanent
establishment situated therein,

shall be exempt from United Kingdom sur-tax.

[Change from previous drafts]

Draft III (1st August 1946)

[As per draft II as at 19th July 1946]

Final form of Article

Article VI

(1) Any dividend paid to a United Kingdom resident by a company which is a United Kingdom resident shall be exempt from Australian tax.

(2) Any dividend paid by a company which is a resident of Australia (whether or not also resident in the United Kingdom or elsewhere) to a company which-

(a) is a United Kingdom resident,

(b) is subject to United Kingdom tax in respect thereof, and

(c) beneficially owns all the shares (less directors' qualifying shares) of the former company,

shall be exempt from Australian tax: Provided that
the exemption shall not apply if

(i) the total of the directors’ qualifying shares exceeds five percent of the paid-up capital of the company paying the dividend, or

(ii) ordinarily more than one-half of the taxable income of that company is derived from interest, dividends and rents other than interest, dividends and rents from any wholly-owned subsidiary company the taxable income of which consists wholly or mainly of industrial or commercial profits. [Change from previous drafts]

(3) Subject to such provisions as may be enacted in Australia for the purpose of determining the amount of Australian tax payable in respect of any dividend, and without limiting the exemptions provided in paragraphs (1) and (2) of this Article, the amount of Australian tax payable in respect of any dividend the whole or part of which is paid out of profits derived from sources in Australia to a United Kingdom resident who is subject to United Kingdom tax in respect thereof and is not engaged in trade or business in Australia through a permanent establishment situated therein, shall not exceed half the amount which would be payable in respect of the dividend or part thereof but for this paragraph. [Change from previous drafts]

(4) Notwithstanding the foregoing provisions of this Article, the amount of the additional tax assessable in respect of the undistributed amount of the distributable income of a company which is
a private company for purposes of Australian tax shall be the amount which would have been assessable if those provisions had not been included in this Agreement.

(5) Any dividend paid by a company resident in the United Kingdom (whether or not also a resident of Australia or elsewhere) to an individual who-

(a) is an Australian resident,

(b) is subject to Australian tax in respect thereof, and

(c) is not engaged in trade or business in the United Kingdom through a permanent establishment situated therein,

shall be exempt from United Kingdom sur-tax.

Art 10(3) No United Kingdom draft of 6th May 1946 did not contain a definition of 'dividend'

No definition of 'dividend' was contained in: Draft II (22nd May 1946 – 1st draft worked on in Australia); Draft II as at 19th July 1946; Draft III (1st August 1946); or Final form of Article

Art 10 Australian addition relating to Not included in draft of 6th May.

Not included in Draft II as at 22nd May 1946. Included in Draft II as at 19th July 1946. Draft III
<table>
<thead>
<tr>
<th>Article</th>
<th>Description</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 10</td>
<td>Zero dividend withholding tax where dividend paid to listed company holding 80% or more of voting power in company paying the dividend.</td>
<td>UK draft 6th May 1946 no withholding tax on dividends paid by a wholly owned subsidiary. Substantive aspects of provision not altered in subsequent drafts.</td>
</tr>
<tr>
<td>Art 11</td>
<td>Yes, UK-US Article VII was an 'interest' article</td>
<td>UK draft of 6th May 1946 did not contain an 'interest' article. No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</td>
</tr>
<tr>
<td>Art 12(1)</td>
<td>Yes, UK –US 1945 exempted industrial and cultural Royalties derived from sources within one of United Kingdom draft of 6th May 1946 Article VII</td>
<td>Draft II (worked on in Australia) 22nd May 1946. No change from UK draft of 6th May 1946.</td>
</tr>
</tbody>
</table>

Ministerial agreement discussed at 2.90 allowed Australia to continue to levy undistributed profits tax. Form of article drafted by Australia.
<table>
<thead>
<tr>
<th>Art 12(2)</th>
<th>United Kingdom draft 6th May 1946</th>
<th>Draft II (worked on in Australia) 22nd May 1946</th>
<th>UK initial definition but Australian amendments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes, UK-US 1945 merely stated that ‘royalties’ included</td>
<td>In this Article the term “royalty” means any</td>
<td>In this Article the term “royalty” means any royalty</td>
<td></td>
</tr>
<tr>
<td>Draft II as at 19th July 1946</td>
<td>Article VII</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Any royalty derived from sources within one of the territories by a resident of the other territory who is subject to tax in that other territory in respect thereof and not engaged in trade or business in the first mentioned territory through a permanent establishment situated therein, shall be exempt from tax in the first mentioned territory; but no exemption shall be allowed under this Article in respect of any royalty paid by a company to a company which controls, directly or indirectly, more than one-half of the entire voting power in the paying company.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Article VII</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>[Both Draft III and the Final Form of the Article were as per Draft II as at 19th July 1946]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>rentals in respect of motion picture films</td>
<td>royalty or other amount paid as consideration for the use of, or the privilege of using, any copyright, patent, design, secret process or formula, trade-mark, or other like property, but does not include royalties or other amounts paid in respect of the operation of mines or quarries or of other extraction of natural resources or rents or royalties in respect of cinematograph films.</td>
<td>or other amount paid as consideration for the use of, or the privilege of using, any copyright, patent, design, secret process or formula, trade-mark, or other like property, but does not include royalties or other amounts paid in respect of the operation of mines or quarries or of other extraction of natural resources or rents or royalties in respect of motion picture films.</td>
<td></td>
</tr>
</tbody>
</table>

*Draft III 1st August 1946*

*Final Form of the Article*

**Article VII**

(2) In this Article the term “royalty” means any royalty or other amount paid as consideration for the use of, or the privilege of using, any copyright, patent, design, secret process or formula, trade-mark, or other like property, but does not include royalty or other amount paid in respect of the operation of a mine or quarry or of other extraction of natural resources or a rent or royalty in respect of a motion picture film.

*(Change from UK draft of 6th May 1946 and from Draft II as at 22nd May 1946)*

Draft III 1st August 1946

Final Form of the Article

*[Both Draft III and the Final Form of the Article were as per Draft II as at 19th July 1946]*
<table>
<thead>
<tr>
<th>Art 13</th>
<th>Yes, Art XIV of US – UK 1945 exempted UK residents not engaged in US trade or business from US tax on gains from sale or exchange of capital assets</th>
<th>No equivalent in United Kingdom draft of 6th May 1946</th>
<th>No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</th>
<th>UK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 17</td>
<td>No</td>
<td>Not in 6th May 1946 United Kingdom draft</td>
<td>No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</td>
<td>UK</td>
</tr>
<tr>
<td>Art 21(1)</td>
<td>No</td>
<td>Not in UK draft 6th May 1946</td>
<td>No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</td>
<td>UK</td>
</tr>
<tr>
<td>Art 22</td>
<td>No</td>
<td>Not in UK draft 6th May 1946</td>
<td>No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</td>
<td>UK</td>
</tr>
<tr>
<td>Art 23</td>
<td>Australian treaties typically allow a credit for foreign tax paid in the treaty partner country on income in respect of</td>
<td>UK draft 6th May 1946 Article XIII</td>
<td>Draft II (22nd May 1946 – worked on in Australia) Article XIII</td>
<td>Basic provisions UK Australia refined drafting</td>
</tr>
<tr>
<td>Australian Variations</td>
<td>(1) Subject to the provisions of the law of the United Kingdom regarding the allowance as a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom, Australian tax</td>
<td>(1) Subject to the provisions of the law of the United Kingdom regarding the allowance as a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom, Australian tax payable, whether directly or by deduction, in respect of income derived from</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Australian tax payable on the income.</td>
<td>Twenty one Australian treaties prior to 2003 allowed a credit for foreign underlying corporate tax where the Australian shareholder held 10% or more voting interest in the paying company.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>--------------------------------------</td>
<td>---------------------------------------------------------------------------------------------------</td>
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<td></td>
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</tr>
<tr>
<td>Sources in Australia shall be allowed as a credit against any United Kingdom tax payable in respect of that income. Where such income is an ordinary dividend paid by a company resident in Australia, the credit shall take into account the Australian tax payable in respect of its profits by the company paying the dividend, and where it is a dividend paid on participating preference shares and representing both a dividend at a fixed rate to which the shares are entitled and an additional participation in profits, the Australian tax so payable by the company shall likewise be taken into account in so far as the dividend exceeds that fixed rate.</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>(2) Subject to such provisions (which shall not affect the general principle hereof) as may be enacted by Australia, United Kingdom tax payable in respect of income from sources derived from the United Kingdom (including United Kingdom tax deductible from such income) shall be allowed as a credit against any Australian tax payable in respect of that income. Where such income is an ordinary dividend paid by a company resident in the United Kingdom, the credit shall take into account (in addition to any United Kingdom income tax appropriate to</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) Where income is derived from sources in the United Kingdom by a resident of Australia and United Kingdom tax is payable in respect thereof:</td>
<td></td>
<td></td>
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<tr>
<td>(a) the income shall be exempt from Australian tax unless it is a dividend;</td>
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<tr>
<td>(b) if the income is a dividend, the United Kingdom tax payable in respect thereof shall be included in the assessable income for purposes of Australian tax for the person entitled to the dividend and shall be allowed as a credit against any Australian tax payable in respect of the dividend.</td>
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<tr>
<td>For the purposes of this paragraph, a dividend paid by a company resident in the United Kingdom shall be deemed to be income derived from sources in the United Kingdom, and the</td>
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</table>
(2) The dividend shall be treated as an income from the United Kingdom for the purposes of United Kingdom tax payable in respect of any such dividend shall be deemed to be:

- the amount of United Kingdom income tax deductible from the gross amount of the dividend, but not exceeding tax on that gross amount at the net rate of United Kingdom income tax applicable to the dividend for the purposes of United Kingdom tax where, owing to the allowance of double taxation relief in the United Kingdom, that net rate is less than the rate of United Kingdom income tax deductible from the dividend;

- in the case of an ordinary dividend, such part of the United Kingdom national defence contribution payable in respect of its profits by the company paying the dividend as is attributable to the proportion of those profits represented by the dividend; and

- in the case of a dividend paid on participating preference shares and representing both a dividend at the fixed rate to which the shares are entitled and an additional participation in profits, such part of the United Kingdom national defence contribution payable in respect of its profits by the company paying the dividend as would fall to be included under sub-paragraph (ii) if the amount representing that additional participation was an ordinary dividend.

For the purposes of this Article, profits or remuneration for personal (including professional) services performed in one of the territories shall be deemed to be income derived from sources in that territory, and the services of an individual whose services are wholly or mainly performed in

reduction).

(4) For the purposes of this Article, profits or remuneration for personal (including professional) services performed in one of the territories shall be deemed to be income derived from sources within that territory, and the services of an individual whose services are wholly or mainly performed on aircraft operated by a resident of one of the territories shall be deemed to be performed in that territory.

[Change from UK draft of 6th May 1946]

Draft II as at 19th July 1946

Article XII (renumbered from XIII)

Subject to the provisions of the law of the United Kingdom regarding the allowance as a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom, Australian tax payable, whether directly or by deduction, in respect of income derived from sources in Australia shall be allowed as a credit against any United Kingdom tax payable in respect of that income. Where such income is an ordinary dividend paid by a company who is a resident of Australia, the credit shall take into account (in addition to any Australian tax (other than War-time (Company) tax) payable in respect of the dividend) the Australian tax (other than War-time (Company) tax) payable in respect of its profits by the company paying the dividend, and where it is a dividend paid on participating preference shares and representing both a dividend at the fixed rate to which the shares are entitled and an additional participation in profits, the Australian tax so payable by the company shall likewise be taken into account in so far as the dividend exceeds that
fixed rate.

For the purposes of this paragraph, any amount which is included in a person's taxable income under Division 14 of the Australian Income Tax Assessment Act 1936/46 (or that Act as amended from time to time) relating to film businesses controlled abroad or under the corresponding provisions of any statute substituted for that Act, shall be deemed to be derived from sources in Australia.

(2) Where Australian tax is payable in respect of income derived from sources in the United Kingdom by a person who is a resident of Australia, being income in respect of which United Kingdom tax is payable, whether directly or by deduction, the United Kingdom tax so payable reduced by the amount of any relief or repayment attributable to that income to which that person is entitled under the law of the United Kingdom shall, subject to such provisions (which shall not affect the general principle hereof) as may be enacted in Australia, be allowed as a credit against the Australian tax payable in respect of that income: if that person elects to have the amount of the United Kingdom tax (as so reduced) included in his assessable income for purposes of Australian tax.

For the purposes of this paragraph, a dividend paid by a company resident in the United Kingdom shall be deemed to be income derived...
from sources in the United Kingdom, and the United Kingdom tax payable in respect of any such dividend shall be deemed to be:

the amount of United Kingdom income tax deductible from the gross amount of the dividend, but not exceeding tax on that gross amount at the net rate of United Kingdom income tax applicable to the dividend for the purposes of United Kingdom tax where, owing to the allowance of double taxation relief in the United Kingdom, that net rate is less than the rate of United Kingdom income tax deductible from the dividend;
in the case of an ordinary dividend, such part of the United Kingdom national defence contribution payable in respect of its profits by the company paying the dividend as is attributable to the proportion of those profits represented by the dividend; and
in the case of a dividend paid on participating preference shares and representing both a dividend at the fixed rate to which the shares are entitled and an additional participation in profits, such part of the United Kingdom national defence contribution payable in respect of its profits by the company paying the dividend as would fall to be included under sub-paragraph (ii) if the amount representing that additional participation was an ordinary dividend.

(3) Where tax is imposed by both Contracting Governments on income derived from sources outside both Australia and the United Kingdom by a person who is a resident of Australia for purposes of Australian tax and is also resident in
the United Kingdom for purposes of United Kingdom tax, there shall be allowed against the tax imposed by each Contracting Government a credit which bears the same proportion to the amount of that tax (as reduced by any credit allowed in respect of tax payable in the territory from which the income is derived) or to the amount of the tax imposed by the other Contracting Government (reduced as aforesaid), whichever is the less, as the former amount (before any such reduction) bears to the sum of both amounts (before any such reduction).

For the purposes of this Article, profits or remuneration for personal (including professional) services performed in one of the territories shall be deemed to be income derived from sources in that territory.

**[Change from UK draft of 6th May 1946 and from Draft II as at 22nd May 1946]**

Draft III (1st August 1946)

Article XII

Subject to the provisions of the law of the United Kingdom regarding the allowance as a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom, Australian tax payable, whether directly or by deduction, in respect of income derived from sources in Australia shall be allowed as a credit against any United Kingdom tax payable in respect of that income. Where such income is an ordinary
dividend paid by a company which is a resident of Australia, the credit shall take into account, in addition to any Australian tax payable in respect of the dividend, the Australian tax (other than war-time (company) tax) payable in respect of its profits by the company paying the dividend, and where it is a dividend paid on participating preference shares and representing both a dividend at the fixed rate to which the shares are entitled and an additional participation in profits, the Australian tax (other than war-time (company) tax) so payable by the company shall likewise be taken into account in so far as the dividend exceeds that fixed rate.

For the purposes of this paragraph, any amount which is included in a person's taxable income under Division 14 or 15 of Part III of the Australian Income Tax Assessment Act 1936-46 (or that Act as amended from time to time) relating to film business controlled abroad and insurance with non-residents, or under the corresponding provisions of any statute substituted for that Act, shall be deemed to be derived from sources in Australia.

(2) Where Australian tax is payable in respect of income derived from sources in the United Kingdom by a person who is a resident of Australia, being income in respect of which United Kingdom tax is payable the United Kingdom tax so payable (reduced by the amount of any relief or repayment attributable to that income to which that person is entitled under the law of the United Kingdom), shall, subject to such provisions (which
shall not affect the general principle hereof) as may be enacted in Australia, be allowed as a credit against the Australian tax payable in respect of that income: Provided that where the income is a dividend paid by a company resident in the United Kingdom the credit the recipient elects to have the amount of the United Kingdom tax (as so reduced) included in his assessable income for purposes of Australian tax.

For the purposes of this paragraph, a dividend paid by a company resident in the United Kingdom shall be deemed to be income derived from sources in the United Kingdom, and the United Kingdom tax payable in respect of any such dividend before reduction as aforesaid shall be deemed to be the amount of United Kingdom income tax deductible from the gross amount of the dividend but not exceeding tax on that gross amount at the net United Kingdom rate applicable to the dividend for purposes of United Kingdom tax where, owing to the allowance of double taxation relief in the United Kingdom, that net rate is less than the rate of United Kingdom income tax deductible from the dividend.

(3) Where tax is imposed by both Contracting Governments on income derived from sources outside both Australia and the United Kingdom by a person who is a resident of Australia for purposes of Australian tax and is also resident in the United Kingdom for purposes of United Kingdom tax, there shall be allowed against the tax imposed by each Contracting Government a credit which bears the same proportion to the
amount of that tax (as reduced by any credit allowed in respect of tax payable in the territory from which the income is derived) or to the amount of the tax imposed by the other Contracting Government (reduced as aforesaid), whichever is the less, as the former amount (before any such reduction) bears to the sum of both amounts (before any such reduction).

(4) For the purposes of this Article, profits, remuneration or other income in respect of personal (including professional) services performed in one of the territories shall be deemed to be income derived from sources in that territory.

[Change from UK draft of 6th May 1946, from Draft II as at 22nd May 1946 and from Draft II as at 19th July 1946]

Final form of Article

Article XII

(1) Subject to the provisions of the law of the United Kingdom regarding the allowance as a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom, Australian tax payable, whether directly or by deduction, in respect of income derived from sources in Australia shall be allowed as a credit against any United Kingdom tax payable in respect of that income. Where such income is an ordinary dividend paid by a company which is a
resident of Australia, the credit shall take into account, in addition to any Australian tax payable in respect of the dividend, the Australian tax (other than war-time (company) tax) payable in respect of its profits by the company paying the dividend, and where it is a dividend paid on participating preference shares and representing both a dividend at the fixed rate to which the shares are entitled and an additional participation in profits, the Australian tax (other than war-time (company) tax) so payable by the company shall likewise be taken into account in so far as the dividend exceeds that fixed rate.

For the purposes of this paragraph, any amount which is included in a person's taxable income under Division 14 or 15 of Part III of the Australian Income Tax Assessment Act 1936-1946 (or that Act as amended from time to time) relating to film business controlled abroad and insurance with non-residents, or under the corresponding provisions of any statute substituted for that Act, shall be deemed to be derived from sources in Australia.

(2) Where Australian tax is payable in respect of income derived from sources in the United Kingdom by a person who is a resident of Australia, being income in respect of which United Kingdom tax is payable, whether directly or by deduction, the United Kingdom tax so payable (reduced by the amount of any relief or repayment attributable to that income to which that person is entitled under the law of the United Kingdom), shall, subject to such provisions (which shall not
affect the general principle hereof) as may be enacted in Australia, be allowed as a credit against the Australian tax payable in respect of that income: Provided that where the income is a dividend paid by a company resident in the United Kingdom the credit shall be allowed only if the recipient elects to have the amount of the United Kingdom tax (as so reduced) included in his assessable income for purposes of Australian tax.

For the purposes of this paragraph, a dividend paid by a company resident in the United Kingdom shall be deemed to be income derived from sources in the United Kingdom, and the United Kingdom tax payable in respect of any such dividend before reduction as aforesaid shall be deemed to include the amount of United Kingdom income tax deductible from the gross amount of the dividend (but not so much of that income tax as exceeds tax on that gross amount at the net United Kingdom rate applicable to the dividend for purposes of United Kingdom tax where, owing to the allowance of double taxation relief in the United Kingdom, that net rate is less than the rate of United Kingdom income tax deductible from the dividend).

(3) Where tax is imposed by both Contracting Governments on income derived from sources outside both Australia and the United Kingdom by a person who is a resident of Australia for purposes of Australian tax and is also resident in the United Kingdom for purposes of United Kingdom tax, there shall be allowed against the tax imposed by each Contracting Government a
credit which bears the same proportion to the amount of that tax (as reduced by any credit allowed in respect of tax payable in the territory from which the income is derived) or to the amount of the tax imposed by the other Contracting Government (reduced as aforesaid), whichever is the less, as the former amount (before any such reduction) bears to the sum of both amounts (before any such reduction).

(4) For the purposes of this Article, profits, remuneration or other income in respect of personal (including professional) services performed in one of the territories shall be deemed to be income derived from sources in that territory.

**[Changes from all previous drafts]**

<table>
<thead>
<tr>
<th>Art 24 AV91</th>
<th>Yes, Art XXI of US – UK 1945 was a non-discrimination article</th>
<th>Not in UK draft of 6th May 1946</th>
<th>No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</th>
<th>UK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 25(1) AV105</td>
<td>No</td>
<td>Not in UK draft of 6th May 1946</td>
<td>No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article.</td>
<td>UK</td>
</tr>
<tr>
<td>Art 26</td>
<td>Exchange of information</td>
<td>United Kingdom draft of 6th May 1946 Article XIII</td>
<td>Draft II (22nd May 1946 – worked on in Australia) Article XIII</td>
<td></td>
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<td></td>
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<tr>
<td>No.</td>
<td>Art XX of UK – US 1945 was identical to Art XIII in UK draft of 6th May 1946</td>
<td>(1) The taxation authorities of the Contracting Governments shall exchange such information (being information available under the respective taxation laws of the Contracting Governments) as is necessary for carrying out the provisions of the present Agreement or for the prevention of fraud or for the administration of statutory provisions against legal avoidance in relation to the taxes which are the subject of the present Agreement. Any information so exchanged shall be treated as secret and shall not be disclosed to any persons other than persons concerned with the assessment or collection of the taxes which are the subject of the present Agreement. No information shall be exchanged which would disclose any trade secret or trade process.</td>
<td>(1) The taxation authorities of the Contracting Governments shall exchange such information (being information available under the respective taxation laws of the Contracting Governments) as is necessary for carrying out the provisions of the present Agreement or for the prevention of fraud or for the administration of statutory provisions against legal avoidance in relation to the taxes which are the subject of the present Agreement. Any information so exchanged shall be treated as secret and shall not be disclosed to any persons other than persons concerned with the assessment or collection, or the determination of appeals in relation to, the taxes which are the subject of the present Agreement. No information shall be exchanged which would disclose any trade secret or trade process.</td>
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<tr>
<td></td>
<td></td>
<td>(2) As used in this Article, the term &quot;taxation authorities&quot; means, in the case of Australia, the Commissioner of Taxation or his authorised representative; in the case of the United Kingdom, the Commissioners of</td>
<td>(2) As used in this Article, the term &quot;taxation authorities&quot; means, in the case of Australia, the Commissioner of Taxation or his authorised</td>
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</tr>
<tr>
<td></td>
<td></td>
<td>Draft II as at 19th July 1946</td>
<td>representative; in the case of Australia, the Commissioner of Taxation or his authorised</td>
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</tbody>
</table>

Australian drafting changes
Inland Revenue or their authorised representative; and in the case of any territory to which the present Agreement is extended under Article XIV, the competent authority for the administration in such territory of the taxes to which the present Agreement applies.

representative; in the case of the United Kingdom, the Commissioners of Inland Revenue or their authorised representative; and in the case of any territory to which the present Agreement is extended under Article XIV, the competent authority for the administration in such territory of the taxes to which the present Agreement applies.

[Change from UK draft of 6th May 1946 and from Draft II as at 22nd May 1946]

Draft III (1st August 1946)

[Minor change from Draft II as at 19th July 1946 by inserting ‘of’ after ‘collection’ in paragraph 1.

Final form of Article

Identical to Draft III

| Art 27 | No | Not in 6th May 1946 United Kingdom draft | No changes were made to UK draft of 6th May 1946 by Draft II, Draft III or Final Form of Article. | UK |
## APPENDIX 5

### VARIATIONS FROM 1963 DRAFT OECD MODEL IN AUSTRALIA – UNITED KINGDOM TREATY 1967

<table>
<thead>
<tr>
<th>OECD Model Article</th>
<th>Australian Variation Number (AV)</th>
<th>Present In UK Draft Of September 1966? Present in previous Australian Tax Treaties?</th>
<th>Drafting history to Final Draft</th>
<th>Initiator of variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 1</td>
<td>2014 and 1963 identical</td>
<td>No equivalent to Art 1 in earlier Australian tax treaties</td>
<td>No changes</td>
<td>UK</td>
</tr>
<tr>
<td></td>
<td></td>
<td>No equivalent to Art 1 in UK Draft September 1966</td>
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<td></td>
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<tr>
<td>Art 2(1)</td>
<td>AV1</td>
<td>Yes, although the UK draft contemplated that Australia would draft the list of Australian taxes</td>
<td>Final draft identical to draft of 13th April 1967 which read:</td>
<td>Basic approach</td>
</tr>
<tr>
<td></td>
<td>2014 and 1963 identical</td>
<td>AV1 present in earlier Australian tax treaties</td>
<td>(b) In Australia: the Commonwealth income tax, including the additional upon the undistributed amount of the</td>
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<tr>
<td>Art 2(2)</td>
<td>AV2</td>
<td>No equivalent to Art 2(2) included in UK Draft AV2 present in earlier Australian tax treaties</td>
<td>No changes</td>
<td>UK</td>
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<tr>
<td>Art 3(1)</td>
<td>AV3</td>
<td>AV3 present in earlier Australian tax treaties Yes, but UK draft was amended by narrowing the definition during the negotiation and drafting process. UK draft September 1966 Article 6(6) The term &quot;industrial or commercial profits&quot; means income derived by an enterprise from the conduct of a trade or business, including income derived by an enterprise from the furnishing of services of employees or other personnel, but it does not include dividends, interest, royalties (as defined in Articles 9, 10, and 11) or rents other than dividends,</td>
<td>Final Draft (apart from renumbering) corresponded with Draft of Article 5(7) of the draft of 13th April 1967 which read as follows: 5(7) The term &quot;industrial or commercial profits&quot; means income derived by an enterprise from the conduct of a trade or business, including income derived by an enterprise from the furnishing of services of employees or other personnel, but it does not include- (a) dividends, interest, royalties (as defined in Articles 8, 9 and 10) or rents other than dividends, interest, royalties or rents effectively connected with a trade or business carried on through a permanent establishment which an enterprise of one of Basic approach UK but definition narrowed at Australia's request.</td>
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</tbody>
</table>
interest, royalties or rents effectively connected with a trade or business carried on through a permanent establishment which an enterprise of one of the territories has in the other territory; nor does the term include remuneration for personal (including professional) services.

(b) remuneration for personal (including professional) services; or

c) income arising from, or in relation to, contracts or obligations to provide the services of public entertainers or athletes referred to in Article 13.

Art 4(1) AV4

1963 differed from 2014 with Art 4(1) being identical to UK draft September 1966 Art 3(1)

AV4 Present in earlier Australian Treaties No. UK draft Art 3(1) identical to Art 4(1) OECD 1963 Draft except for use of ‘territory’ or ‘territories’ instead of ‘Contracting State’ or ‘Contracting States’

UK draft September 1966

(1) For the purposes of this Agreement the terms ‘resident of the United Kingdom’ and ‘resident of Australia’ mean respectively any person who, under the law of the United Kingdom, is liable to tax therein by reason of his domicile, residence, place management or any other criterion of a similar nature and any person who, under the law of Australia, is liable to tax therein by reason of his domicile, the territories has in the other territory; or

Draft of 13th April 1967 read as follows:

Article 3(1)

(1) For the purposes of this Agreement -

(a) the term ‘Australian company’ means any company which

(i) is incorporated in Australia and which has its centre of administrative or practical management in Australia (whether or not any person outside Australia exercises or is capable of exercising any overriding control or discretion of the company or of its

Australia
Australian draft 16th June 1967
residence, place of or any other criterion of a similar nature.

Art 3(2) and Art 3(3) of the UK draft were identical to Art 4(2) and Art 4(3) of the 1963 OECD Draft with the words ‘territory’ or ‘territories’ being substituted for ‘Contracting State’ or ‘Contracting States’ respectively.

(2) Where by reason of the provisions of paragraph (1) above an individual is a resident of both territories, then his status shall be determined in accordance with the following rules:

(a) he shall be deemed to be a resident of the territory in which he has a permanent home available to him. If he has a permanent home in both territories, he shall be deemed to be a resident of the territory with which his personal and economic relations are closest (hereinafter referred to as his “centre of vital policy or affairs in any way whatsoever; or

(ii) is managed and controlled in Australia;

(b) the term ‘United Kingdom company’ means any company which is managed and controlled in the United Kingdom and which is not an Australian company;

(c) the term "United Kingdom resident" means any United Kingdom company and any person (other than a company) who is resident in the United Kingdom for the purposes of United Kingdom tax but the term does not include any individual, not being ordinarily resident in the United Kingdom, who is liable to tax in the United Kingdom only if he derives income from sources therein; and

(d) the term "Australian resident" means any Australian company and any other person
interests”;
(b) if the territory in which he has his centre of vital interests cannot be determined or if he has not a permanent home available to him in either territory, he shall be deemed to be a resident of the territory in which he has an habitual abode;
(c) if he has an habitual abode in both territories or in neither of them, he shall be deemed to be a resident of the territory in which he is a national;
(d) if he is a national of both territories or of neither of them, the taxation authorities of the territories shall determine the question by mutual agreement.

(3) Where by reason of the provisions of paragraph (1) a person other than an individual is a resident of both territories, then it shall be deemed to be a resident of the territory in which its place of effective (other than a United Kingdom company) who is a resident of Australia for the purposes of Australian tax but the term does not include any individual, not being ordinarily resident in Australia, who is liable to tax in Australia only if he derives income from sources therein.

(2) Where by reason of the provisions of paragraph (1) of this Article an individual is both a United Kingdom resident and an Australian resident-
(a) he shall be treated solely as a United Kingdom resident-

(i) if he has a permanent home available to him in the United Kingdom and has not a permanent home available to him in Australia;

(ii) if sub-paragraph (a)(i) is not applicable but he has an habitual abode in the United Kingdom and has not an habitual abode in Australia;

(iii) if neither sub-paragraph (a)(i) nor sub-paragraph (a)(ii) of this paragraph is applicable but the territory with which his personal and economic relations are closest is the United Kingdom;
| Management is situated. | Article 3(4) in UK draft had no equivalent in OECD Draft 1963  
(4) The terms “resident of one of the territories” and “resident of the other territory” mean a person who is a resident of the United Kingdom or a person who is a resident of Australia as the context requires.  
(5) The terms ‘United Kingdom enterprise’ and ‘Australian enterprise’ mean respectively an industrial or commercial enterprise or undertaking carried on by a United Kingdom resident and an industrial or commercial enterprise or undertaking carried on by an Australian resident, and the terms ‘enterprise of one of the territories’ and ‘enterprise of the other territory’ mean a United Kingdom enterprise or an Australian enterprise, as the context requires. | (b) he shall be treated solely as an Australian resident-  
(i) if he has a permanent home available to him in Australia and has not a permanent home available to him in the United Kingdom;  
(ii) if sub-paragraph (b)(i) is not applicable but he has an habitual abode in Australia and has not an habitual abode in the United Kingdom;  
(iii) if neither sub-paragraph (b)(i) nor sub-paragraph (b)(ii) is applicable but the territory with which his personal and economic relations are closest is Australia. | (3) Where by reason of the provisions of paragraph (1) of this Article a person other than an individual is both a United Kingdom resident and an Australian resident-  
(a) it shall be treated solely as a United Kingdom resident if it is managed and controlled in the United Kingdom;  
(b) it shall be treated solely as an Australian resident if it is managed and controlled in Australia. | (4) Identical to United Kingdom draft of September 1966  
(5) Identical to United Kingdom draft of |
September 1966.

Final Draft was as per Australian draft 16th June 1967

Article 3(1)

(1) For the purposes of this Agreement -

(a) the term ‘Australian company’ means any company which being a resident of Australia – remainder of 1(a) was identical with draft of 13th April 1967.

(b) identical with draft of 13th April 1967.

(c) the term "United Kingdom resident" means any United Kingdom company and any person (other than a company) who is resident in the United Kingdom for the purposes of United Kingdom tax but the term does not include any individual, not being ordinarily resident in the United Kingdom, who is liable to tax in the United Kingdom.
only if he derives income from sources therein; and

(d) the term "Australian resident" means any Australian company and any other person (other than a United Kingdom company) who is a resident of Australia for the purposes of Australian tax but the term does not include any individual, not being ordinarily resident in Australia, who is liable to tax in Australia only if he derives income from sources therein.

(2) Where by reason of the provisions of paragraph (1) of this Article an individual is both a United Kingdom resident and an Australian resident-

(a) he shall be treated solely as a United Kingdom resident-

(i) if he has a permanent home available to him in the United Kingdom and has not a permanent home available to him in Australia;

(ii) if sub-paragraph (a)(i) of this paragraph is not applicable but he has an habitual abode in the United Kingdom and has not an
habitatual abode in Australia;

(iii) if neither sub-paragraph (a)(i) nor sub-paragraph (a)(ii) of this paragraph is applicable but the territory with which his personal and economic relations are closest is the United Kingdom;

(b) he shall be treated solely as an Australian resident—

(i) if he has a permanent home available to him in Australia and has not a permanent home available to him in the United Kingdom;

(ii) if sub-paragraph (b)(i) of this paragraph is not applicable but he has an habitual abode in Australia and has not an habitual abode in the United Kingdom;

(iii) if neither sub-paragraph (b)(i) nor sub-paragraph (b)(ii) of this paragraph is applicable but the territory with which his personal and economic relations are closest is Australia.

(3) Identical to draft of 13th April 1967.

(4) Identical to draft of 13th April 1967.

(5) Identical to draft of 13th April 1967.

| Art 5(2)- | AV6 | AV6 present in earlier Australian tax treaties |
| 5(3) | AV7 | Yes, assembly project included in UK Draft September 1966 but here followed OECD Draft 1963  
**AV7 not present in earlier Australian tax treaties** |
|  | AV8 | No, connected supervisory activities not included in UK Draft September 1966  
**AV8 not present in earlier Australian tax treaties** |
|  | AV9 |  |

Final draft was as per draft of 16<sup>th</sup> June 1967 which, apart from the insertion of commas was identical to Article 4(4) in the draft of 13<sup>th</sup> April 1967. Article 4(4) in draft of 16<sup>th</sup> June 1967 read:

‘An enterprise of one of the territories shall be deemed to have a permanent establishment in the other territory if it carries on supervisory activities in that other territory for more than six months in connection with a building site, or a construction, installation or

UK initiated AV7 but this was not a variation from 1963 OECD Draft

Australia initiated ‘connected supervisory activities’
| Art 5(4) | AV12 1963 and 2014 | AV12 not present in earlier Australian tax treaties | Final draft corresponded with draft of 13\textsuperscript{th} April 1967 which added ‘such as advertising’ | Australia initiated 6 months |

UK Draft September 1966 required 12 months for building site

**AV9 not present in earlier Australian tax treaties**

UK draft September 1966

Article 4(2)

(2) The term “permanent establishment” shall include especially:

(g) a building site, construction or assembly project which exists for more than twelve months.

assembly project which is being undertaken in the other territory'.

Final draft was as per draft of 13\textsuperscript{th} April 1967 which required 6 months for building sites, construction or installation projects.

Australia initiated 6 months
<table>
<thead>
<tr>
<th>Art 5(5)</th>
<th>AV13 not present as a deeming in earlier Australian tax treaties</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>No, UK draft followed OECD Draft 1963 or scientific research' to the end of Article 4(3)(e).</td>
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496
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AV13 not present as a deeming in earlier Australian tax treaties

Not applicable

Australia initiated
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<table>
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<tr>
<th>Art 6</th>
<th>1967 Australia – UK Tax Treaty did not contain an income from immovable property article</th>
<th>UK Draft of September 1966 contained an immovable property article</th>
<th>Final Draft corresponded with draft of 13th April 1967 which did not contain an immovable property article</th>
<th>Australia initiated omission of immovable property article</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>AV14 originated in 1957 Australia – Canada Tax Treaty but refined in 1967 Australia – United Kingdom Tax Treaty</td>
<td>AV14 originated in 1957 Australia – Canada Tax Treaty but refined in 1967 Australia – United Kingdom Tax Treaty</td>
<td>Final draft corresponded with draft of 13th April 1967 which added paragraph (c) to Article 4(5). Paragraph (c) read as follows:</td>
<td>Australia initiated omission of immovable property article</td>
</tr>
<tr>
<td></td>
<td>No, no equivalent in UK draft of September 1966</td>
<td>No, no equivalent in UK draft of September 1966</td>
<td>‘If in so acting he manufactures or processes in that first-mentioned territory any goods for the enterprise.</td>
<td>Australia initiated omission of immovable property article</td>
</tr>
<tr>
<td></td>
<td>activities of the agent are limited to those mentioned in paragraph 4.</td>
<td>activities of the agent are limited to those mentioned in paragraph 4.</td>
<td>Final Draft corresponded with draft of 13th April 1967 which did not contain an immovable property article</td>
<td>Not reflected in Australian Tax Treaties currently in force</td>
</tr>
</tbody>
</table>
term “immovable property” shall in any case include property accessory to immovable property, livestock and equipment of agricultural and forestry enterprises, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixes payments for the working of, or right to work, mineral deposits, sources and other natural resources; ships and aircraft shall not be regarded as immovable property.

(3) The provisions of paragraph (1) shall apply to income derived from the direct use of, letting, or use in any other form of immovable property.

(4) The provisions of paragraphs (1) to (3) of this Article shall also apply to income from immovable property of an enterprise and to income from immovable property used for the performance of professional services.

<table>
<thead>
<tr>
<th>Art 7(4)</th>
<th>AV19</th>
<th>Not present in UK draft September 1966</th>
<th>No change</th>
<th>UK initiated</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1963 OECD Draft</td>
<td>AV19 present in earlier Australian Tax Treaties</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Art 7(4) not present in 2014 Model</td>
<td></td>
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<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Art 7 Australian addition</th>
<th>Not present in 1963 OECD Draft or in 2014 Model</th>
<th>Not present in UK draft September 1966</th>
<th>Art 5(4) Final Version corresponded with draft of 13th April 1967 which read as follows: Art 6(4)</th>
<th>No longer reflected in Australian Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>UK Draft September 1966</td>
<td>In determining the industrial or commercial profits of an enterprise of one of the territories which are taxable in the other territory in</td>
<td></td>
</tr>
</tbody>
</table>
In determining the industrial or commercial profits of an enterprise of one of the territories which are taxable in the other territory in accordance with the previous paragraphs of this Article, there shall be allowed as deductions all expenses of the enterprise (including executive and general administrative expenses) which would be deductible if the permanent establishment were an independent enterprise and which are reasonably connected with the profits so taxable, whether incurred in the territory in which the permanent establishment is situated or elsewhere.

Variation not present in earlier Australian Tax Treaties and not reflected in Australian Tax Treaties currently in force

| Art 7 | AV20 | No present in UK Draft September 1966 | Art 5(5) Final Version corresponded with draft of 13th April 1967 which read as follows: If the information available to the taxation
| Australian addition | OECD Draft or in AV20 present in earlier Australian Tax | No present in UK Draft September 1966 | Australia initiated variation |

Treaties currently in force
- UK initiated words underlined
- Australia initiated words in italics
<table>
<thead>
<tr>
<th>Art 7</th>
<th>Australian addition</th>
<th>2014 Model</th>
<th>Treaties</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>AV22</td>
<td>OECD Draft or in 2014 Model</td>
<td>UK Draft September 1966 contained Article 6(7) preserving certain aspects of UK law relating to insurance</td>
</tr>
<tr>
<td></td>
<td>Not present in 1963</td>
<td></td>
<td>Art 6(7) UK Draft September 1966</td>
</tr>
</tbody>
</table>

Nothing in the foregoing provisions of this Article shall affect any of the provisions of the law of the United Kingdom relating to the liability to tax of a life assurance company not having its head office in the United Kingdom in respect of income from the investment of its life assurance fund, being provisions which (except so far as they were rendered authority concerned is inadequate to determine the profits to be attributed to the permanent establishment, nothing in this Article shall affect the application of the law of either territory in relation to the liability of the permanent establishment to pay tax on an amount determined by the exercise of a discretion or the making of an estimate by the taxation authority of that territory. Provided that such discretion shall be exercised or such estimate shall be made, so far as the information available to the taxation authority permits, in accordance with the principle stated in this Article.

Article 5(8) in draft of 13th April 1967 read as follows:

Nothing in paragraphs (1) and (2) of this Article shall affect any provisions of the law of either territory relating specifically to any person who carries on a business of any form of insurance or who derives income from a film business controlled abroad. Provided that if the law in force in either territory at the date of signature of this Agreement relating to the taxation of such persons is varied (otherwise than in minor respects so as not to affect its general character, or by this

UK introduced saving provision relating to certain UK insurance provisions. Australia initiated extension to insurance with non-residents generally and to film business controlled abroad.
ineffective by virtue of Article III of the Agreement between Australia and the United Kingdom with respect to taxes on income signed at London on 29 October, 1946) were in force on the date of signature of this Agreement, or which, if they have been modified since that date, have been modified only in minor respects so as not to affect their general character.

Previous Australian treaties had contained a form of AV22

Agreement), the Contracting Governments shall consult with each other with a view to agreeing to such amendment of this paragraph as may be necessary.

Final Version Art 5(8) corresponded with Art 5(8) in draft of 16th June 1967 which read as follows:

Nothing in this Article shall apply to either territory to prevent the operation in the territory of any provisions of its law relating specifically to the taxation of any person who carries on a business of any form of insurance or to the taxation of a non-resident who derives income under any contract or agreement with any person in relation to the carrying on in the territory by that person of any form of film business controlled abroad. Provided that if the law in force in either territory at the date of signature of this Agreement relating to the taxation of such persons is varied (otherwise than in minor respects so as not to affect its general character, or by this Agreement), the Contracting Governments shall consult with each other with a view to agreeing to such amendment of this paragraph as may be necessary.
<table>
<thead>
<tr>
<th>Art 8</th>
<th>AV24</th>
<th>Art 8(1) identical in 1963 and 2014</th>
<th>UK draft of September 1966 based exclusion on residence. UK Draft September 1966</th>
<th>Art 7</th>
<th>This aspect unchanged in Final Draft</th>
<th>UK initiated AV24</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>A resident of one of the territories shall be exempt from tax in the other territory on profits from the operation of ships or aircraft in international traffic</td>
<td></td>
<td>Art 7</td>
<td></td>
</tr>
<tr>
<td></td>
<td>AV25</td>
<td>No equivalent in 1963 Draft or in 2014 Model</td>
<td>Not present in UK Draft September 1966</td>
<td>Article 7 in UK Draft September 1966</td>
<td>A resident of one of the territories shall be exempt from tax in the other territory on</td>
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<td></td>
<td></td>
<td></td>
<td>A version of AV24 present in previous Australian Tax Treaties but form of current AV24 dates from 1967 UK Treaty</td>
<td></td>
<td>Article 6 in draft of 13th April 1967 read as follows: (1) A resident of one of the territories shall be exempt from tax in the other territory on profits from the operation of ships or aircraft other than profits from voyages or flights confined solely to places in the other territory, voyages of ships or aircraft between a</td>
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<td></td>
<td>Article 7 in UK Draft September 1966</td>
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<td>A resident of one of the territories shall be exempt from tax in the other territory on</td>
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<tr>
<td>AV26</td>
<td>No equivalent in 1963 Draft or in 2014 Model</td>
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<tr>
<td></td>
<td>profits from the operation of ships or aircraft in international traffic.</td>
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<tr>
<td></td>
<td>AV25 not present in earlier Australian Tax Treaties</td>
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<tr>
<td></td>
<td>Not present in UK Draft September 1966</td>
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<td></td>
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<tr>
<td></td>
<td>AV26 not present in earlier Australian Tax Treaties</td>
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<tr>
<td></td>
<td>place in Australia and a place in the Territory of Papua or the Territory of New Guinea being treated as voyages between places within Australia.</td>
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<td></td>
<td>(2) Subject to paragraph (3) of this Article, where, in accordance with paragraph (1) of this Article, a resident of one of the territories is charged to tax in the other territory on profits from the operation of ships the amount of the profits so charged shall not exceed five per cent, of the amounts paid (net of any rebates) for the carriage of passengers, mails or cargoes shipped in the other territory.</td>
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<tr>
<td></td>
<td>(3) Paragraph (2) of this Article shall not apply to the profits derived from the operation of ships by a United Kingdom enterprise whose principal place of business is in Australia, but there shall be excluded from the profits on which any such enterprise is charged to Australian tax any amounts of profits taxed in the Territory of Papua or the territory of New Guinea.</td>
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<tr>
<td></td>
<td>Article 6 in draft of 16th June 1967 read as follows:</td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(1) Identical to draft of 13th April 1967</td>
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<tr>
<td></td>
<td>(2) Where a resident of one of the territories is not exempted under</td>
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<tr>
<td></td>
<td>Australia initiated AV26</td>
<td></td>
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</tbody>
</table>
paragraph (1) of this Article from tax in the other territory on profits from the operation of ships the amount of such profits that shall be charged to tax in that other territory shall not exceed five per cent of the amounts paid or payable (net of rebates) for the carriage of passengers, livestock, mails or goods shipped in the other territory.

(3) Identical to draft of 13th April 1967.

Johnson’s letter to Cain dated 4th September 1967 suggested substituting ‘of ships or aircraft’ for ‘or flights’ in paragraph (1). Johnson also suggested an amendment to paragraph (2) which was substantially reflected in the draft of 11th October 1967 which read as follows:

(2) The amount which shall be charged to tax in one of the territories as profits from voyages of ships in respect of which a resident of the other territory is not exempt from tax in the first-mentioned territory under paragraph (1) of this Article shall not exceed 5 per cent of the amounts paid or payable
(net of rebates) in respect of such voyages for the carriage of passengers, livestock, mails or goods shipped in the first-mentioned territory.

Article 6 in the Final Version of the Treaty corresponded with the draft of 16th June 1967.

<table>
<thead>
<tr>
<th>Art 8(2)</th>
<th>AV28</th>
<th>Yes, Art 8(2) omitted from UK Draft September 1966</th>
<th>No change</th>
<th>UK initiated AV28</th>
</tr>
</thead>
<tbody>
<tr>
<td>Both 1963 Draft and 2014 Model contain Art 8(2)</td>
<td>AV28 present in previous Australian Tax Treaties</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Art 8(3)</th>
<th>AV29</th>
<th>Yes, Art 8(3) omitted from UK Draft September 1966</th>
<th>No change</th>
<th>UK initiated AV29</th>
</tr>
</thead>
<tbody>
<tr>
<td>Both 1963 Draft and 2014 Model contain Art 8(3)</td>
<td>AV29 present in previous Australian Tax Treaties</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<p>| Art 9(2) | AV31 | Yes, UK Draft September 1966 did not contain Art 9(2) | No change | UK initiated AV31 but this was not a variation from |</p>
<table>
<thead>
<tr>
<th>Art 9Australian addition</th>
<th>AV33</th>
<th>Not present in UK Draft September 1966</th>
<th>Final Draft Art 7(3) corresponded with Art 7(3) of draft of 13th April 1967 which read as follows:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>AV33 present in previous Australian Tax Treaties</td>
<td>If the information available to the taxation authority concerned is inadequate to determine, for the purposes of paragraph (1) of this Article, the profits which might be expected to accrue to an enterprise, nothing in this Article shall affect the application of the law of either territory in relation to the liability of that enterprise to pay tax on an amount determined by the exercise of a discretion or the making of an estimate by the taxation authority of that territory. Provided that such discretion shall be exercised or such estimate shall be made, so far as the information available to the taxation authority permits, in accordance with the principle stated in that paragraph.</td>
</tr>
<tr>
<td>Art 10(1)</td>
<td>AV36</td>
<td>Requirement present in UK Draft September 1966</td>
<td>This aspect not changed in subsequent drafts</td>
</tr>
<tr>
<td></td>
<td></td>
<td>AV36 appeared in 1946 Australia – UK Tax</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Phrase does not appear in 1963 Draft</td>
<td></td>
</tr>
</tbody>
</table>

1963 OECD Draft

Australia initiated AV33

UK initiated AV36
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 10(2) AV40(a) 1963 Draft and 2014 substantially the same</td>
<td>UK Draft September 1966 contemplated differential rates on portfolio and non-portfolio dividends.</td>
</tr>
<tr>
<td></td>
<td>UK Draft September 1966 Art 9(1)</td>
</tr>
<tr>
<td>1) United Kingdom tax on dividends beneficially owned by a resident of Australia which are derived by such a resident from a company which is a resident of the United Kingdom shall not exceed</td>
<td></td>
</tr>
<tr>
<td>(a) per cent of the gross amount of the dividends if the recipient is a company which controls directly or indirectly at least 25 per cent of the voting power in the company paying the dividend;</td>
<td></td>
</tr>
<tr>
<td>(b) In all other cases per cent of the gross amount of the dividend.</td>
<td></td>
</tr>
<tr>
<td>2) Australian resident shall not exceed 15 per cent of the gross amount of the dividend.</td>
<td></td>
</tr>
<tr>
<td>Final Draft Arts 8(1) &amp; (2) was identical with draft of 13\textsuperscript{th} April 1967 which read as follows:</td>
<td></td>
</tr>
<tr>
<td>(1) The United Kingdom tax on dividends derived and beneficially owned by an Australian resident shall not exceed 15 per cent of the gross amount of the dividends.</td>
<td></td>
</tr>
<tr>
<td>(2) The Australian tax on dividends derived and beneficially owned by a United Kingdom resident shall not exceed 15 per cent of the gross amount of the dividends.</td>
<td></td>
</tr>
<tr>
<td>Australia initiated AV40(a)</td>
<td></td>
</tr>
</tbody>
</table>
AV 40(a) (in the sense of a standard limit on source country tax of both portfolio and non-portfolio dividends) originated in 1953 Australia – United States Tax Treaty and is also found in the 1957 Australia – Canada Tax Treaty and in the 1960 Australia – New Zealand Tax Treaty.

<table>
<thead>
<tr>
<th>Art 10(3)</th>
<th>AV42</th>
<th>Yes, but amended to final form in negotiation and drafting process.</th>
<th>Article 8(3) in draft of 13th April 1967 read as follows: (3) The term &quot;dividends&quot; includes any item (other than interest or royalties relieved from tax under Article 9 or Article 10 of this Agreement) which-</th>
<th>UK initiated AV42</th>
</tr>
</thead>
<tbody>
<tr>
<td>1963 Draft and 2014 Model differ but not a a respect which is relevant to AV42</td>
<td></td>
<td>UK Draft September 1966</td>
<td>Article 9(3)</td>
<td></td>
</tr>
</tbody>
</table>
(a) The term "dividends" in the case of the United Kingdom includes any item (other than interest or royalties relieved from United Kingdom tax under Article 9 or Article 10 of this Agreement) which, under the law of the United Kingdom is treated as a distribution of a company;

(b) the term “dividends” in the case of Australia includes — [to be drafted by Australia]

No previous Australian Tax Treaty had contained a definition of ‘dividend’

Final Draft Article 8(3) was identical with draft of 16th June 1967 which read as follows:

(3) The term "dividends" includes any item (other than interest or royalties relieved from tax under Article 9 or Article 10 of this Agreement) which—

(a) in the case of the United Kingdom is, under the law of the United Kingdom, a distribution of a company;

(b) in the case of Australia is, or is deemed to be, under the law of the Commonwealth of Australia.

Art 10 | There were other variations in the UK draft
<table>
<thead>
<tr>
<th>Other variations</th>
<th>and others developed in negotiations (due to New Broken Hill situation). The variations were particular to the context and none of them affect currently operative treaties</th>
</tr>
</thead>
</table>
| Art 11(1) AV47 (variant) Beneficial ownership requirement appears in both Art 9(1) and (2) as in 1969 Australia – Singapore Tax Treaty. | Yes, UK draft of September 1966 contained ‘beneficial ownership’ requirement in both Arts 10(1) and (2)  

**Previous Australian Tax Treaties do not contain an interest article and hence do not contain a variant on AV47** |
| 1963 Draft Art 11(2) did not contain a beneficial ownership requirement | This aspect not changed in final draft |
| Art 11(3) AV49 (variant) 1963 Draft definition of ‘interest’ differed from 2014 Model definition of ‘interest’ | UK initiated variation |
| | UK draft of September 1966 did not contain a definition of ‘interest’  

**Previous Australian Tax Treaties do not contain an interest article and hence do** |
<p>| | This aspect not changed in final draft |</p>
<table>
<thead>
<tr>
<th>Art 11(5)</th>
<th>AV51</th>
<th>Differences exist between 1963 Draft Art 11(5) and 2014 Model 11(5) but these are not relevant to the omission of Art 11(5) that is AV51</th>
<th>UK draft of September 1966 did not include an equivalent to Art 11(5) Previous Australian Tax Treaties do not contain an interest article and hence do not contain AV51</th>
<th>This aspect not changed in final draft</th>
<th>UK initiated variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 11</td>
<td></td>
<td>There were other variations which were particular to the context and are not reflected in currently operative treaties</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 12(1)</td>
<td>AV56</td>
<td>2014 Model differs from 1963 Draft by adding a beneficial ownership requirement but this difference is not relevant for AV56</td>
<td>No. UK Draft September 1966 Articles 11(1) and (2) 1. Royalties derived and beneficially owned by a resident of the United Kingdom shall be exempt from tax in Australia; 2. Royalties derived and beneficially owned by a resident of Australia shall be exempt from tax in the United Kingdom.</td>
<td>Final Draft Articles 10(1) and (2) was identical with draft of 13th April 1967 which read as follows: 1. The United Kingdom tax on royalties derived and beneficially owned by an Australian resident shall not exceed 10 per cent of the gross amount of the royalties. 2. The Australian tax on royalties derived and beneficially owned by a United Kingdom resident shall not exceed 10 per cent of the gross amount of the royalties.</td>
<td>AV56 initiated by Australia</td>
</tr>
</tbody>
</table>
Previous Australian Tax Treaties gave exclusive residence basis taxation to some royalties and did not set upper limits on source taxation of other royalties. 1967 UK – Australia Tax Treaty is first exact instance of AV56.

<table>
<thead>
<tr>
<th>Art 12(2)</th>
<th>AV 58</th>
</tr>
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<tbody>
<tr>
<td>Art 12(2)</td>
<td>AV 58</td>
</tr>
</tbody>
</table>

No reference in either 1963 Draft or in 2014 Model to ‘films or tapes used for radio or television broadcasting’

UK Draft September 1966 included reference to films or tapes for radio or television broadcasting but exact phraseology was developed during negotiations and drafting.

UK Draft September 1966

Article 11(4)

The term "royalties" as used in this Article means any royalties, rentals or other amounts paid as considerations for the use of, or the right to use, copyrights of literary, artistic or scientific works (including motion picture films* or films or tapes for radio or television broadcasting), patents, designs or

Article 10(5) in draft of 13th April 1967 read as follows:

(5) In this Article the term "royalties" means payments of any kind to the extent to which they are paid as consideration for the use of, or the right to use, any copyright, patent, design or model, plan, secret formula or process, trademark, or other like property or right, or industrial, commercial or scientific equipment, or for the supply of scientific, technical, industrial or commercial knowledge, information or assistance but does not include royalties or other amounts paid in respect of the operation of mines or

UK initiated AV58 but Australia settled exact phraseology
models, plans, secret processes or formulae, trade-marks or other like property or rights, or for industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience, but does not include royalties or other amounts paid in respect of the operation of mines or quarries or of the extraction or removal of natural resources.

No previous Australian treaties had included AV58

AV59

AV 59 was included in UK Draft of September 1966 but this was not a variation from 1963 OECD Draft

No previous Australian Tax Treaties had included AV59

AV60

Portions in italics in 1966 UK Draft above were not included in 1963 OECD Draft

quarries or of the extraction or removal of natural resources.

Final Draft Article 10(5) was identical with draft of 16th June 1967 which read as follows:

(5) In this Article the term "royalties" means payments of any kind to the extent to which they are paid as consideration for the use of, or the right to use, any copyright, patent, design or model, plan, secret formula or process, trademark, or other like property or right, or industrial, commercial or scientific equipment, or for the supply of scientific, technical, industrial or commercial knowledge, information or assistance, and includes any payments of any kind to the extent to which they are paid as consideration for the use of, or the right to use, motion picture films, films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but does not include royalties or other amounts paid in respect of the operation of

UK initiated AV59 but this was consistent with 1963 OECD Draft
<table>
<thead>
<tr>
<th>Art 12 Australian addition</th>
<th>AV62</th>
<th>AV60</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>No equivalent to Article 13 in Final Draft of 1967</td>
<td>September 1966 UK Draft contained a capital gains article</td>
<td>Definition. The portion underlined in the 1966 UK Draft above was an exclusion not in the 1963 OECD Draft. <em>The OECD Draft referred to ‘cinematograph films’ whereas the United Kingdom draft of September 1966 referred to ‘motion picture films’.</em> Portions in italics in the draft of 16th June 1967 were initiated by Australia.</td>
<td>Mines or quarries or of the extraction or removal of natural resources. No change in this respect in subsequent drafting. See extract from draft of 16th June 1967 quoted in relation to AV 58.</td>
</tr>
<tr>
<td>September 1966 UK Draft contained a capital gains article</td>
<td>A different source rule for royalties was contained in the credit article</td>
<td>A different source rule for royalties was contained in the credit article</td>
<td>See discussion of credit article</td>
</tr>
</tbody>
</table>

Variation from 1963 OECD Model and from September 1966 UK Draft initiated by Australia

(1) Gains from the alienation of property forming part of the business property of a permanent establishment which an enterprise of one of the territories has in the other territory or of any property pertaining to a fixed base.
Model but September 1966 UK Draft differed from 1963 OECD Draft

available to a resident of one of the territories for the purpose of performing professional services, including such gains from the alienation of such a permanent establishment (either alone or together with the whole enterprise) or of such a fixed base, may be taxed in the other territory.

(2) Notwithstanding paragraph (1) of this Article, gains derived by a resident of one of the territories from the alienation of ships or aircraft operated in international traffic and movable property pertaining to the operation of such ships and aircraft shall be exempt from tax in the other territory.

(3) Gains from the alienation of property other than those mentioned in paragraph (1) shall be taxable only in the territory of which the alienator is a resident.

<table>
<thead>
<tr>
<th>Art 17</th>
<th>1963 Draft</th>
<th>1966 Draft</th>
<th>Australian variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australian variation</td>
<td>1963 Draft Art 17(1) differed in phraseology from 2014 Model and did not include Art 17(2) of 2014 Model</td>
<td>UK September 1966 Draft Article 15 corresponded to Article 17 of 1963 OECD Draft</td>
<td>As discussed at 5.87 the inclusion of a source rule had been agreed on 6th April 1967 but the inclusion is not mentioned as a change in the draft of 16th June 1967. The Final Draft is identical with the draft of 13th April 1967 which reads as follows: Article 13</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Australian initiated deemed source rule and removal of equivalent to OECD 1963 Art 17</td>
</tr>
</tbody>
</table>
Notwithstanding anything contained in Articles 11 and 12, income derived by public entertainers, such as theatre, motion picture, radio or television artistes, and musicians, and by athletes, from their personal activities as such shall be deemed to have a source in, and may be taxed in, the territory in which these activities are exercised.

<table>
<thead>
<tr>
<th>Art 17(2)</th>
<th>AV80</th>
<th>UK draft September 1966 did not contain an equivalent to Article 17(2). Previous Australian treaties had not contained an equivalent to Article 17(2)</th>
<th>No change</th>
<th>UK initiated</th>
</tr>
</thead>
<tbody>
<tr>
<td>OECD 1963 did not contain an equivalent to Article 17(2)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Art 21</th>
<th>AV82</th>
<th>AV82</th>
<th>Final version of 1967 Australia – UK Tax Treaty did not contain an ‘other income’ article.</th>
<th>Australia initiated AV82</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paragraph 2 of 2014 did not appear in 1964 Draft</td>
<td>No, UK Draft September 1966 included an ‘other income’ article</td>
<td>Previous Australian Tax Treaties had not contained ‘other income’ articles but 1967 Australia – UK Tax Treaty was first where treaty partner's draft had included an ‘other income’ article</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Art 21 Australian addition</td>
<td>Cf AV86</td>
<td>UK Draft September 1966 contained an ‘other income’ article which read: Items of income of a resident of one of the territories who is subject to tax there in respect thereof being income of a class or from sources not expressly mentioned in the foregoing Articles of this Agreement shall be taxable only in that territory.</td>
<td>Article 18 in the draft of 13th April 1967 read as follows: Income derived from sources outside both the United Kingdom and Australia by a resident of one of the territories who is subject to tax there in respect thereof shall be taxed only in that territory. Article 18 in draft of 16th June 1967 read as follows: (1) This article shall apply to a person who is resident of Australia and is also resident in the United Kingdom; (2) Where income is derived from sources outside both the United Kingdom and Australia by such a person and that person is treated as a resident of one of the territories and is subject to tax in that territory in respect of that income, the income so derived shall be taxed only in that territory. By letter to Cain dated 4th September 1967 Johnson suggested that paragraph (2) be Australia initiated change. Not reflected in any currently operative Australian tax treaties.</td>
<td></td>
</tr>
</tbody>
</table>
amended to read as follows:

(3) Where such a person is treated for the purposes of this Agreement solely as a resident of one of the territories he shall be exempt in the other territory from tax on any income in respect of which he is subject to tax in the first-mentioned territory if that income is derived:

(a) from sources in the first mentioned territory; or
(b) from sources outside both territories.

Johnson’s amendment was incorporated in the draft of 11th October 1967. Article 18 in the final version of the treaty corresponded with Article 18 in the draft of 11th October 1967.

<table>
<thead>
<tr>
<th>Art 22</th>
<th>AV87</th>
<th>AV87</th>
<th>No change</th>
<th>UK initiated.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>No equivalent to Art 22 was included in UK Draft September 1966</td>
<td></td>
</tr>
</tbody>
</table>
Previous Australian Tax Treaties had not contained an equivalent to Art 22

<table>
<thead>
<tr>
<th>Art 23 Australian Variations</th>
<th>AV 89</th>
<th>UK Draft September 1966 Article 21</th>
<th>Draft dated 13th April 1967</th>
<th>Australia initiated variations but further variations were initiated by the United Kingdom.</th>
</tr>
</thead>
</table>
|                             |       | (1) Subject to the provisions of the law of the United Kingdom regarding the allowance of a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom (which does not affect the general principle hereof) –  
(1) Australian tax payable under the laws of Australia and in accordance with this Agreement whether directly or by deduction, on profits, income or chargeable gains from sources within Australia, (excluding in the case of a dividend tax payable in respect of the profits out of which the dividend is paid) shall be allowed as a credit against any United Kingdom tax computed by reference to the same profits, income or chargeable gains by reference to which Australian tax is computed; and  
(2) In the case of a dividend paid by a company which is a resident of Australia to a company which is resident in the United Kingdom and which controls directly or indirectly at least 10 per cent of the voting power in the Australian company, the credit will take into account (in addition to any Australian tax creditable under (a) the Australian tax payable by the company in respect of the profits out of which such dividend is paid. |
|                             |       | (a) unchanged                      |                             |                                                                                               |
|                             |       | (b) In the case of a dividend paid by a company which is a resident of Australia to a company which is resident in the United Kingdom and which controls directly or indirectly at least 10 per cent of the voting power in the Australian company, the credit will take into account (in addition to any Australian tax creditable under (a) the Australian tax payable by the company in respect of the profits out of which such dividend is paid. |
indirectly at least 10 per cent of the voting power in the Australian company, the credit will take into account (in addition to any Australian tax creditable under (a)) the Australian tax payable by the company in respect of the profits out of which such dividend is paid.

(2) [To be drafted by Australia]

(3) For the purposes of this Article profits or remuneration for personal (including professional) services performed in one of the territories shall be deemed to be income from sources within that territory, and the services of an individual whose activities are wholly or mainly performed in ships or aircraft operated in international traffic by a resident of one of the territories shall be deemed to be performed in that territory.

(4) Where profits on which an enterprise of one of the territories has been charged to tax in that territory are also included in the profits of an enterprise of the other territory and the profits so included are profits which would have accrued to that enterprise in the other territory if the conditions made between each of the enterprises had been those which would have been made between independent enterprises dealing at arm’s length, the amount of such profits included in the profits of both enterprises shall be payable in a country outside Australia (which shall not affect the general principle hereof), the United Kingdom tax payable under the laws of the United Kingdom and in accordance with this Agreement, whether directly or indirectly or by deduction, on income derived by a resident of Australia from sources in the United Kingdom shall be allowed as a credit against the Australian tax assessed by reference to the same income by reference to which the United Kingdom tax is payable.

(b) In the event that Australia should cease to allow a company which is a resident of Australia a rebate at the average rate of tax payable by the company in respect of dividends derived from sources in the United Kingdom and included in the taxable income of the company, the
treated for the purposes of this Article as income from a source in the other territory of the enterprise of the first-mentioned territory and credit shall be given accordingly in respect of the extra tax chargeable in the other territory as a result of the inclusion of the said amount.

**Credits for underlying tax were allowed irrespective of the level of shareholding in the 1946 Australia – UK Tax Treaty**

Contracting Governments will enter into negotiations in order to establish new provisions concerning the credit to be allowed by Australia against its tax on the dividends.

(3) For the purposes of this Article –

(a) dividends (as defined in Article 8) paid by a company under the law of one of the territories is a resident, or is resident in that territory, for the purposes of that territory’s tax shall be treated in the other territory as being income from sources in the first-mentioned territory;

(b) interest and royalties (as defined in Articles 9 and 10) which under the law of one of the territories are derived from sources within that territory shall be treated in the other territory as having a source in the first-mentioned territory;

(c) remuneration in respect of an employment exercised aboard a ship or aircraft in international traffic shall be treated as having a source in the territory in which the place of effective management of the enterprise is situated;

(d) any amount which is included, for the purposes of tax in one of the territories, in the chargeable
<table>
<thead>
<tr>
<th></th>
<th></th>
<th>profits or taxable income of a person who is a resident of the other territory, and which is so included under any provision of the law of the first-mentioned territory for the time being in force regarding taxation of income of a business or any form of insurance or of a film business controlled abroad shall be treated as having a source in the first-mentioned territory.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(4)</td>
<td>As per UK Draft of September 1966.</td>
<td>Draft of 16th June 1967</td>
</tr>
<tr>
<td>(1)</td>
<td>(a) unchanged</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(b) In the case of a dividend paid by a company which is a resident of Australian to a company which is resident in the United Kingdom and which controls directly or indirectly at least 10 per cent of the voting power in the first mentioned company, the credit will take into account (in addition to any Australian tax creditable under (a) the Australian tax</td>
<td></td>
</tr>
</tbody>
</table>
payable by the company in respect of the profits out of which such dividend is paid.

For the purpose of allowing relief from United Kingdom tax in accordance with this paragraph, where a distribution is made by a company which is a resident of Australia and which is also a resident in the United Kingdom, the amount of the United Kingdom income tax for which the company is liable to account in respect of the distribution shall be computed by reference to the gross amount of the distribution charged to Australian tax and credit for the Australian tax so charged shall be allowed against the said amount of income tax.

(2)

(a) Subject to the provisions of the law of Australia from time to time in force and which relate to the allowance of a credit against Australian tax of tax payable in a country outside Australia
(which shall not affect the general principle hereof), the United Kingdom tax payable under the laws of the United Kingdom and in accordance with this Agreement (reduced by the amount of any relief or repayment attributable to that income under the law of the United Kingdom), whether directly or indirectly or by deduction, on income derived by a resident of Australia from sources in the United Kingdom (excluding in the case of dividends tax payable in respect of the profits out of which the dividend is paid) shall be allowed as a credit against the Australian tax assessed by reference to the same income by reference to which the United Kingdom tax is payable.

(b) In the event that Australia should cease to allow a company which is a resident of Australia a rebate in its
assessment at the average rate of tax payable by the company in respect of dividends derived from sources in the United Kingdom and included in the taxable income of the company, the Contracting Governments will enter into negotiations in order to establish new provisions concerning the credit to be allowed by Australia against its tax on the dividends.

(3) For the purposes of this Article –
(a) dividends (as defined in Article 8) paid by a company under the law of one of the territories is a resident, or is resident in that territory, for the purposes of that territory’s tax shall be treated in the other territory as being income from sources in the first-mentioned territory;
(b) interest and royalties (as defined in Articles 9 and 10), which under the law of one of the territories –
(i) are derived from sources within that territory; or

(iii) being derived by a non-resident are subject to withholding tax, shall be treated in the other territory as having a source in the first-mentioned territory;

(c) unchanged from draft of 13th April 1967;

(d) any amount which is included, for the purposes of tax in one of the territories, in the chargeable profits or taxable income of a person who is a resident of the other territory, and which is so included under any provision of the law of the first-mentioned territory for the time being in force regarding taxation of income of a business or any form of insurance or of income derived under a contract or agreement with a person who carries on in the first-mentioned territory any form of film business controlled abroad shall be treated as having a source in the first-mentioned territory.

(e) profits to which paragraph (2) of Article 6 applies derived by a
(5) Where profits, on which an enterprise of one of the territories has been charged to tax in that territory, are also included, by virtue of this Agreement, in the profits which, because of the circumstances existing between the two enterprises, might have been expected to accrue to the enterprise of the other territory, the profits so included shall be treated for the purposes of this Article as profits of the enterprise of the first-mentioned territory from a source in the other territory and relief shall be given in accordance with this Article in respect of the extra tax chargeable in the other territory as a result of the inclusion of such profits.

Final draft was identical with draft of 11th October 1967 which read as follows:

(1) Unchanged from draft of 16th June 1967.
(2) Unchanged from draft of 16th June 1967.
(3) For the purposes of this Article:
(a) (i) Australian tax borne by a
United Kingdom resident in
respect of dividends (as defined in
Article 8) paid by a company
which is a resident of Australia
shall be treated as tax on income
from sources in Australia;
(ii) United Kingdom tax borne by
an Australian resident in respect
of dividends (as defined in Article
8) paid by a company which is
resident in the United Kingdom
shall be treated as tax on income
from sources in the United
Kingdom;
(b) Unchanged from draft of 16th June
1967.
(c) Unchanged from draft of 16th June
1967.
(d) Unchanged from draft of 16th June
1967.
(e) Unchanged from draft of 16th June
1967.
(4) Unchanged from draft of 16th June
1967.
<table>
<thead>
<tr>
<th>Art 24(1)</th>
<th>AV91</th>
<th>AV91</th>
<th>Final version of 1967 Australia – UK Tax Treaty did not contain a 'non-discrimination' article.</th>
<th>Australia initiated AV91</th>
</tr>
</thead>
<tbody>
<tr>
<td>1963 Draft did not contain words 'in particular with respect to residence' in paragraph 1. 1963 Draft contained a definition of 'nationals' in paragraph 2. 1963 Draft did not contain 2014 paragraph 4.</td>
<td>UK Draft September 1966 contained a 'non-discrimination article'.</td>
<td>Previous Australian Tax Treaties had not contained a 'non-discrimination' article but 1967 Australia – UK Tax Treaty was first where treaty partner’s draft had included a 'non-discrimination' article</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Art 25(1)</th>
<th>AV104(a)</th>
<th>AV104(a)</th>
<th>Final Draft was identical with draft of 13th April 1967 which read as follows:</th>
</tr>
</thead>
<tbody>
<tr>
<td>1963 OECD Draft Art 25(1) did not contain a time limit. Significant differences in phraseology existed between 1963 OECD Draft and 2014 Model</td>
<td>UK Draft September 1966 differed from 1963 OECD Draft but both drafts did not contain time limits. 1953 US Treaty contained a mutual agreement procedure with no time limits</td>
<td>Article 23</td>
<td></td>
</tr>
<tr>
<td></td>
<td>UK Draft September 1966</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Article 23

Where a taxpayer considers that the action of the taxation authority of either territory has resulted or will result in taxation contrary to the provisions of this Agreement, he shall be entitled to present his case to either taxation authority. Should the taxpayer’s claim be deemed worthy of consideration, the taxation authority to which the claim is made shall endeavour to come to an agreement with the other taxation authority.

### Article 20

(1) Where a taxpayer considers that the action of the taxation authority of either territory has resulted or will result in taxation contrary to the provisions of this Agreement, he shall be entitled to present his case to either taxation authority. Should the taxpayer’s claim be deemed worthy of consideration, the taxation authority to which the claim is made shall endeavour to come to an agreement with the other taxation authority.

### Article 20

(1) Where a taxpayer considers that the action of the taxation authority of either territory has resulted or will result in taxation contrary to the provisions of this Agreement, he shall be entitled to present his case to either taxation authority. Should the taxpayer’s claim be deemed worthy of consideration, the taxation authority to which the claim is made shall endeavour to come to an agreement with the other taxation authority.
<table>
<thead>
<tr>
<th>AV05</th>
</tr>
</thead>
<tbody>
<tr>
<td>1963 OECD Draft Art 25 did not contain an equivalent to 2014 Art 25(2)</td>
</tr>
<tr>
<td>AV06</td>
</tr>
<tr>
<td>1963 OECD Draft Art 25 did not contain 2014 Art 25(2) and hence AV06 is not a variation from 1963 OECD Draft</td>
</tr>
<tr>
<td>AV07</td>
</tr>
<tr>
<td>Equivalent phrase was included in 1963 OECD Draft Art 25(4)</td>
</tr>
<tr>
<td>AV08</td>
</tr>
<tr>
<td>1963 OECD Draft</td>
</tr>
</tbody>
</table>

**Article 20**

1. Where a taxpayer considers that the action of the taxation authorities of the Contracting Government has resulted or will result in taxation contrary to the provisions of this Agreement, he shall be entitled to present his case to the Government of the territory of which he is a national or resident. Should the taxpayer's claim be deemed worthy of consideration, the taxation authority of the Government to which the claim is made shall endeavour to come to an agreement with the other taxation authority of the other Government with a view to a satisfactory adjustment.

2. The taxation authorities of the Contracting Governments may communicate with each other directly to implement the provisions of this Agreement and to assure its consistent interpretation and application. In particular, the taxation authorities may consult together to endeavour to resolve disputes arising out of the application of paragraph (3) of Article 6.
<table>
<thead>
<tr>
<th>Art 25(5)</th>
<th>Art 26(1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Art 25 did not contain an equivalent to 2014 Model Art 26(2) or Art 26(4). Phraseology of Art 26(1) of 1963 Draft differed from phraseology of 2014 Model Art 26(2) or Art 26(4).</td>
<td>1963 OECD Draft did not contain an equivalent to 2014 Model Art 26(2) or Art 26(4). Phraseology of Art 26(1) of 1963 Draft differed from phraseology of 2014 Model Art 26(2) or Art 26(4).</td>
</tr>
<tr>
<td>or Article 8, or the determination of the source of particular items of income.</td>
<td>Exchange of information article in UK Draft September 1966 differed from 1963 OECD Draft.</td>
</tr>
<tr>
<td><strong>1953 US Treaty had contained a mutual agreement procedure with no time limit. The mutual agreement procedure article in 1969 Singapore Treaty follows 1967 UK Treaty form.</strong></td>
<td>UK Draft September 1966</td>
</tr>
<tr>
<td>AV107 was a variation from 1963 OECD Draft Art 25(4)</td>
<td>Article 24</td>
</tr>
<tr>
<td>AV108 was not a variation from 1963 OECD Draft Art 25</td>
<td>The taxation authorities of the Contracting Governments shall exchange such information (being information which is at their disposal under their respective taxation laws in the normal course of administration) as is necessary for carrying out the provisions of this Agreement or for the prevention of fraud or for the administration of</td>
</tr>
<tr>
<td>Final Draft was identical with draft of 13th April 1967 which read as follows:</td>
<td></td>
</tr>
<tr>
<td><strong>Article 21</strong></td>
<td><strong>UK initiated variation. Only minor drafting change between UK Draft September 1966 and Final Draft. Form of article not reflected in</strong></td>
</tr>
</tbody>
</table>
as is necessary for carrying out the provisions of this Agreement or for the prevention of fraud or for the administration of statutory provisions against legal avoidance in relation to the taxes which are the subject of this Agreement. Any information so exchanged shall be treated as secret but may be disclosed to persons (including a court or tribunal) concerned with the assessment, collection, enforcement or prosecution in respect of the taxes which are the subject of this Agreement. No information as aforesaid shall be exchanged which would disclose any trade, business, industrial or professional secret or trade process.

| Model. | as is necessary for carrying out the provisions of this Agreement or for the prevention of fraud or for the administration of statutory provisions against legal avoidance in relation to the taxes which are the subject of this Agreement. Any information so exchanged shall be treated as secret but may be disclosed to persons (including a court or tribunal) concerned with the assessment, collection, enforcement or prosecution in respect of the taxes which are the subject of this Agreement. No information as aforesaid shall be exchanged which would disclose any trade, business, industrial or professional secret or trade process. |
| Model. | statutory provisions against legal avoidance in relation to the taxes which are the subject of this Agreement. Any information so exchanged shall be treated as secret but may be disclosed to persons (including a court or tribunal) concerned with the assessment, collection, enforcement or prosecution in respect of the taxes which are the subject of this Agreement. No information as aforesaid shall be exchanged which would disclose any trade, business, industrial or professional secret or trade process. |
| currently operative Australian Tax Treaties | |

| Art 27 | 1963 OECD Draft did not contain an ‘assistance in collection article’ |
| AV111 | AV111 UK Draft of September 1966 did contain an ‘assistance in collection’ article. |
| AV111 | UK Draft September 1966 Article 25 (1) Each of the Contracting Governments will endeavour to collect on behalf of the other Contracting Government, such amounts as may be necessary to ensure that relief granted by this Agreement from taxation imposed by such other Contracting Government |
| AV111 | Article did not appear in Final Version or in subsequent drafts. United Kingdom ‘Notes of Meetings’ for 31 March 1967 records that ‘The Australians might have constitutional difficulties in giving the article legal effect and it might be better to drop it.’ |
| AV111 | Australia initiated what is a variation from current OECD Model but this was not a variation from 1963 OECD Draft. |
Paragraph (1) of this Article shall not impose upon either of the Contracting Governments the obligation to carry out administrative measures which are of a different nature from those used in the collection of its own tax or which would be contrary to its sovereignty, security or public policy. In determining the administrative measures to be carried out each Contracting Government may take into account the administrative measures and practices of the Contracting Government in recovering taxes on behalf of the first-mentioned Contracting Government. 

Only the 1953 Australia – United Kingdom Tax Treaty had contained an 'assistance in collection' article.

| Total number of variations from 2014 OECD Model in currently operative Australian tax treaties | 40 |
| Number of variations that had their origins in 1946 UK Treaty or other earlier Australian treaties | 5 |
Number of variations originating in 1967 UK Treaty 35
Number of variations initiated by the UK 22 (5 were modified by Australia in drafting)
Number initiated by the UK that followed 1946 UK Treaty 3
Number initiated by the UK that followed 1963 OECD 7
Number initiated by Australia 17 (1 was modified by UK in drafting)
Number initiated by Australia that followed earlier Australian treaties 2
Number initiated by Australia that followed 1963 OECD 1 (although this was variation from UK 1966 draft)
APPENDIX 6: FEATURES OF AUSTRALIAN TAX TREATY PRACTICE LISTED BY KT ALLEN IN 1988-1990

(1) the definition of ‘Australia’ (where Allen emphasised the need to include the continental shelf in order to continue to tax offshore exploration and exploitation of natural resources)\(^1\);

(2) the extended definition of income from real property to include royalty and other payments for the exploration and exploitation of natural resources and income from leasing contracts\(^2\);

(3) the definition of permanent establishment (here Allen highlighted the Australian inclusions of ‘agricultural, pastoral or forestry property’, the deemed carrying on of business by an enterprise through a permanent establishment where substantial equipment was used by or under contract with the enterprise, provisions which applied a six month rule to building sites, construction, installation or assembly projects and associated supervisory activities and specifically mentioned the deemed services permanent establishment provision in the Australia – China Tax Treaty\(^3\));

(4) the provision limiting expenses that can be deducted in calculating business profits to those that would be allowable if the permanent establishment were an independent entity paying the expenses (Allen comments that this provision was intended to exclude from deductibility expenses which were not deductible under the domestic law of the country where the permanent establishment was located)\(^4\);

(5) the provisions authorising the application of domestic law consistently with the general principles of the business profits article in instances where the information available is inadequate to determine profits to be attributed to a permanent establishment (Allen saw this provision as permitting a reference back to the then transfer pricing provisions in ITAA 1936 Div13)\(^5\);

(6) provisions in some treaties, such as the 1988 Australia – China Tax Treaty) clarifying Australia’s right to tax business profits from the carrying on of a business in Australia through a permanent establishment indirectly through an interposed trust\(^6\);

(7) the use of the expression ‘might be expected to operate’ in place of ‘would be made between’ in the associated enterprises article.

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\(^1\) K T Allen Assistant Commissioner (International Branch) Policy and Legislation Group, ATO, Canberra, ‘The relevant considerations, factors and criteria involved in negotiating Australia’s double tax agreements’, Thomson Reuters, Checkpoint, Commentary, International Agreements at [1860].

\(^2\) Allen, supra note 1 at [1865].

\(^3\) Allen, supra note 1 at [1870].

\(^4\) Allen, supra note 1 at [1885].

\(^5\) Allen, supra note 1 at [1885]. At [1895] Allen makes the same point in relation to Australia’s variations on the associated enterprises article.

\(^6\) Allen, supra note 1 at [1890].
change which Allen regarded as recognising that independent firms did not always deal independently with one another\(^7\);

(8) the rates of withholding tax on dividends, interest and royalties then usually sought by Australia in tax treaties (namely, 15% on dividends, 10% on interest and 10% on royalties) noting that since the introduction of dividend imputation the withholding tax on dividends only applied to unfranked dividends and pointing out that, in addition, Australia, as an aid to source taxation, sought the widest definition of ‘royalty’ for tax treaty purposes\(^8\);

(9) the then recent change of policy on articles dealing with capital gains which, subject to certain exceptions, was to require capital gains to be taxed in accordance with the domestic law of each country\(^9\);

(10) the practice of giving the source country the right to tax ‘anything that is otherwise left out’ that is derived by a resident of one country from a source in the other country\(^10\);

(11) the Australian practice of including source rules in tax treaties which can have the effect of giving greater taxing rights than are specified in Australian domestic law\(^11\);

(12) the practice of not construing credit provisions in Australian tax treaties in a manner which limits the scope of relief from international double taxation provided by Australian domestic law\(^12\);

(13) the then current policy, notwithstanding proposed changes to overall government policy on the tax treatment of foreign source income, to provide tax sparing relief for specified development incentives of appropriate treaty partner countries in otherwise satisfactory agreements\(^13\);

(14) not agreeing to the non-discrimination which Allen characterised as: being outside the proper scope of a tax treaty; possibly preventing a country from taking appropriate steps to ensure a proper distribution of taxing rights between them; and possibly preventing a government

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\(^7\) Allen, supra note 1 at [1895].

\(^8\) Allen, supra note 1 at [1900].

\(^9\) Allen, supra note 1 at [1905]. Allen also commented that previously Australia’s tax treaties did not deal comprehensively with capital gains as the fact that Australia did not tax them meant that there could be no double taxation. Allen noted that Australia’s approach had been to ensure that income from the alienation of real property could be taxed in the source country. Allen’s view was that, subject to a few limited exceptions, Australia’s existing tax treaties did not prevent Australia from taxing ‘as ordinary income’ under its domestic law, capital gains from the disposal of a ‘taxable Australian asset’ as defined in ITAA 1936 former s160T.

\(^10\) Allen, supra note 1 at [1915].

\(^11\) Allen, supra note 1 at [1910]. Allen justified this practice as resolving any conflict in domestic law source rules and as obviating any question of income not having, by domestic law rules, a source in the country to which the treaty gave taxing rights.

\(^12\) Allen, supra note 1 at [1920].

\(^13\) Allen, supra note 1 at [1925].
from using taxation measures for the purposes of desirable economic regulation.\textsuperscript{14}
APPENDIX 7

ANALYSIS OF DEEMED SOURCE RULES IN CURRENTLY OPERATIVE AUSTRALIAN TAX TREATIES

Treaties where deeming is for the purposes of Australian law generally and separate deeming of Australian source is made in the credit article

2015 Treaty with Germany

Treaties where deeming is for the purposes of Australian tax generally and separate deeming for credit purposes for both Contracting States is made in the credit article.

Treaty with the United Kingdom

Treaties where deeming is for the purposes of the law of both Contracting States and no other deeming is made

Treaty with Chile (also contains specific source rules for interest and royalties)
Treaty with Denmark
Treaty with New Zealand
Treaty with Slovakia
Treaty with Sri Lanka
Treaty with Switzerland

Treaties where deeming is for the purposes of Australian tax generally and a separate deeming of source in the other Contracting State is made for credit purposes

Treaty with Austria (also contains specific source rules for interest and royalties)
Treaty with the Czech Republic
Treaty with Belgium (also contains specific source rules for interest)
Treaty with The Netherlands (in Protocol only)
Treaty with Sweden (deemed Swedish source for credit purposes is only for the purposes of Australian law)

Treaties where deeming is made for purposes of Australian tax generally and a separate deeming is made for credit purposes for both Contracting States

Treaty with Argentina (also contains specific source rules for interest and royalties)
Treaty with Canada (also contains specific source rules for interest and royalties)

Treaties where deeming is made for the purposes of the law of both Contracting States generally and a separate deeming is made for credit purposes for both Contracting States

Treaty with Fiji
Treaty with Finland

Treaty with France (also contains separate deeming relating to business profits and deeming for credit purposes does not extend to business profits. Also contains separate deeming provisions in relation to partnership profits)
Treaty with India
Treaty with Japan
Treaty with Kiribati
Treaty with Papua New Guinea (provision states that deeming will not apply to interest to which Article 11 applies until the law of Papua New Guinea includes source rules)
Treaty with Romania
Treaty with South Africa
Treaty with Turkey
Treaty with Vietnam

Treaties where deeming is made for credit purposes only for both Contracting States

Treaty with China (also contains specific source rules for interest and royalties)

Treaties where deeming is made for credit purposes for both Contracting States and same paragraph also extends deeming to the law of both Contracting States generally

Treaty with Hungary
Treaty with Indonesia
Treaty with Italy
Treaty with Korea
Treaty with Malaysia
Treaty with Mexico
Treaty with Norway
Treaty with The Philippines
Treaty with Poland
Treaty with Russia
Treaty with Spain

Treaties where deeming is confined to business profits and associated enterprises articles

Treaty with Singapore

Treaties where deeming is confined to interest and royalties articles

Treaty with the United States (but basically applies domestic source rules of the two states although there are some deeming provisions)

Treaties where no deeming is made

Treaty with Taipei