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The Avoidance of Double Non-Taxation in Double Tax Treaty Law – A Critical Analysis of the Subject-To-Tax Clause Recommended by the European Commission

Christoph Marchgraber[*]

Countries around the world have traditionally treated tax planning as a legitimate practice, unless the ambiguous borders to abusive behavior have been crossed. However, over time, business structures have become more sophisticated and tax authorities have become involved in keeping pace with the continuous improvement of international tax planning. By exploiting the inconsistencies between domestic tax rules and bilateral double taxation conventions it is even possible that certain income remains completely untaxed. In order to properly address this issue of double non-taxation, the European Commission – alongside the work of the OECD on Base Erosion and Profit Shifting (BEPS) – issued a recommendation on aggressive tax planning. The EU Member States are, inter alia, being encouraged to revise their tax treaty policies. The European Commission recommends the incorporation of a general subject-to-tax clause in the Member States' bilateral double taxation conventions. This article analyses whether the Member States are well advised to follow this recommendation.

1. Subject-To-Tax Clauses: The "Philosopher's Stone" of Double Tax Treaty Law?

States can levy taxes by virtue of their sovereignty. Therefore, the same event may be taxed in two or even more states. Cross-border economic relations would be threatened considerably, though, if two or more states were to subject the same income to taxation.[1] In order to overcome the obstacle of double taxation, states have entered into bilateral double taxation conventions since as early as the end of the nineteenth century.[2] Thereby, the contracting states commit themselves to relinquishing, completely or partially, the imposition of taxes in specific situations. However, the interaction of these rules adopted in accordance with international standards to relieve double taxation and the un-coordinated domestic tax systems can also lead to situations in which certain income remains untaxed in both contracting states. There are manifold reasons for this kind of double non-taxation.[3, 4] Contracting states partially even

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[1] See, for example, Opinion of Advocate General Colomer, 26. 10. 2004, C-376/03, *D*, [2005] ECR I-5821, m.no. 85 ('[T]he fact that a taxable event might be taxed twice is the most serious obstacle there can be to people and their capital crossing … borders.').

[2] See K. Vogel, *Klaus Vogel on Double Taxation Conventions*, Introduction, m.nos. 17 et seq. (K. Vogel (ed.), 3rd edition, Kluwer Law International 1997).

[3] Despite some attempts to develop a plausible definition of double non-taxation, there is no internationally accepted description of this phenomenon. See, for example, H. Hahn, *Generalthema I des 58. IFA-Kongresses 2004 in Wien: Double-Non-Taxation Überblick über den deutschen Nationalbericht*, 12 Internationales Steuerrecht 13, pp. 446-448 (2003); I. Jankowiak, *Doppelte Nichtbesteuerung im Internationalen Steuerrecht*, pp. 32-33 (C.H. Beck 2009); M. Schilcher, *Subject-to-tax-Klauseln in der österreichischen Abkommenspraxis*, p. 17 (Linde 2004); J.M. Mössner, *Steuerrecht international tätiger Unternehmen*[4], p. 270, m.no. 2.251 (J.M. Mössner et al. (eds.), 4th edition, Dr. Otto Schmidt 2012); U. Wolff, *Generalthema I: Doppelte Nicht-Besteuerung*, 13 Internationales Steuerrecht 16, p. 542 (2004); on the term "low taxation" see, for example, O. Bühler, *Prinzipien des Internationalen Steuerrechts*, pp. 169-170 (Internationales Steuerdokumentationsbüro 1964); H. Meyer, *Die*

seek to achieve or consciously accept double non-taxation resulting from the application of a double taxation convention.[5] In many cases, though, double non-taxation stems from the fact that the contracting states simply bind themselves not to raise any taxes with respect to taxing rights that are given to the other contracting state under the double taxation convention. However, there is no corresponding obligation for the other contracting state to exercise a taxing right domestically.[6] Even if a double taxation convention is perfectly reconciled with the domestic tax systems of both contracting states, it is possible that certain income remains untaxed. The contracting states might, for example, apply different treaty rules due to a varying evaluation of the facts of the case, a diverging interpretation of the rules of the double taxation convention or the disparities between their domestic tax systems.[7] Thus, double non-taxation might occur if both contracting states conclude that the double taxation convention does not allow them to tax (negative qualification conflict).[8]

The phenomenon of double non-taxation resulting from the application of a bilateral double taxation convention has already received particular attention in the past. As a result of the Partnership Report of 1999,[9] the OECD even introduced an explicit provision in the OECD Model Convention with Respect to Taxes on Income and on Capital[10] (Article 23A(4) OECD MC) aiming to avoid double non-taxation resulting from negative qualification conflicts.[11]

Vermeidung internationaler Doppel- und Minderbesteuerung auf der Grundlage des Ursprungsprinzips, Dissertation Georg-August-Universität zu Göttingen, pp. 119-127 (1970); H. Schaumburg, *Internationales Steuerrecht*, p. 491, m.no. 13.8 (3rd edition, Dr. Otto Schmidt 2011).

[4] See I. Jankowiak, *supra* n. 3, pp. 34 et seq.; H. Meyer, *supra* n. 3, pp. 150 et seq.; J.M. Mössner, *supra* n. 3, p. 271, m.no. 2.251; M. Schilcher, *supra* n. 3, pp. 20 et seq.; see also *Avoidance of Double Non-Taxation*, p. 489 (M. Lang (ed.), Linde 2003).

[5] See I. Jankowiak, *supra* n. 3, pp. 69 et seq.; M. Lang, *General Report*, in *Double Non-Taxation*, CDFI 89a, p. 21, at pp. 30-31 (IFA (ed.), IBFD 2004); M. Schilcher, *supra* n. 3, pp. 25 et seq.

[6] See M. Lang, *Die Vermeidung der Doppelbesteuerung und der doppelten Nichtbesteuerung als DBA-Auslegungsmaxime?*, 11 Internationales Steuerrecht 18, p. 609, at pp. 611-612 (2002); M. Lang, *Vermeidung der Doppelbesteuerung und der doppelten Nichtbesteuerung als Auslegungsmaxime für Doppelbesteuerungsabkommen?*, in *Auslegung und Anwendung von Doppelbesteuerungsabkommen*, p. 83, at p. 92 (W. Haarmann (ed.), Dr. Otto Schmidt 2004).

[7] See OECD, *The Application of the OECD Model Tax Convention to Partnerships*, 6 Issues in Intl. Taxn., m.nos. 94 et seq. (OECD Publishing 1999); see also H. Loukota, *Die Vermeidung von Besteuerungskonflikten für das international tätige Unternehmen*, in *Besteuerung und Bilanzierung international tätiger Unternehmen*, 30 Jahre Steuerrecht an der Wirtschaftsuniversität Wien, p. 265, at p. 269 (W. Gassner & M. Lang (eds.), Orac 1998); H. Loukota, *Der Einfluss des österreichischen Ertragsteuerrechtes auf die Auslegung von Doppelbesteuerungsabkommen*, in *Ertragsteuern in Wissenschaft und Praxis*, FS Doralt, p. 263, at pp. 280 et seq. (R. Beiser et al. (eds.), LexisNexis 2007); H. Loukota, *Lösung internationaler Qualifikationskonflikte*, 9 Steuer und Wirtschaft International 2, pp. 70 et seq. (1999); J. Schuch & J. Bauer, *Die Überlegungen des OECD-Steuerausschusses zur Lösung von Qualifikationskonflikten*, in *Personengesellschaften im Recht der Doppelbesteuerungsabkommen*, p. 27, at p. 31 (W. Gassner, M. Lang & E. Lechner (eds.), Linde 2000).

[8] For further references see, for example, I. Jankowiak, *supra* n. 3, pp. 34 et seq.; M. Schilcher, *supra* n. 3, pp. 30 et seq.

[9] OECD, *supra* n. 7, paras 112 et seq.

[10] Hereinafter OECD MC, available at: *http://www.oecd.org/tax/treaties/1914467.pdf* (Accessed March 28, 2014).

[11] See OECD Commentary 2000-2012 on Art. 23A and 23B, paras 56.1-56.3; see also OECD Commentary 2000-2012, Art 23A and 23B, paras. 32.1-32.7; for the changes to the commentary on Article 23A(1) OECD MC see, for example, M. Lang, supra n. 5, pp. 95-96; M. Lang, *Qualifikationskonflikte im Recht der Doppelbesteuerungsabkommen*, in *Staaten und Steuern*, FS Vogel, p. 907, at pp. 915-916 (P. Kirchhof et al. (eds.), C. F. Müller 2000); J. Schuch & J. Bauer, *supra* n. 7, pp. 32-33; H. Weggenmann, *Die Empfehlungen der OECD an den Ansässigkeitsstaat zur Lösung von Einordnungskonflikten in Bezug auf Sondervergütungen*, 11 Internationales Steuerrecht 18, p. 614, at pp. 614-615 (2002).

However, bilateral double taxation conventions – and also the OECD MC[12] – still provide opportunities to eliminate or significantly reduce taxation on income. Moreover, it has to be considered that not all bilateral double taxation conventions include a provision corresponding to Article 23(A) OECD MC. Therefore, double non-taxation resulting from the inconsistencies between domestic tax rules and international standards is still an open issue. At the moment, the question of how to avoid tax loopholes created by double taxation conventions is being intensively discussed both at a national[13] and an international level.[14] Regarding the enhancements of double tax treaty law, one might expect that the lead is taken by the OECD. At present, however, the European Commission is attracting attention by encouraging the Member States of the EU to include a subject-to-tax clause in their bilateral double taxation conventions,[15] according to which the taxing right of a contracting state may be restricted by the double taxation convention only if the other contracting state domestically exercises the taxing right assigned to it:[16] 'Where this Convention provides that an item of income shall be taxable only in one of the contracting States or that it may be taxed in one of the contracting States, the other contracting State shall be precluded from taxing such item only if this item is subject to tax in the first contracting State'.

The idea of subject-to-tax clauses is not new.[17] The commentary on the OECD MC several times mentions the possibility of bilaterally agreeing on a rule according to which the relief to be granted by one contracting state is contingent upon the income being subject to tax in the other contracting state.[18] However, the OECD rarely, and then only concerning very specific situations, provides suggestions on how to draft such a provision.[19] As it is ambiguous under

[12] See C. Marchgraber, *Vermeidung doppelter Nichtbesteuerung im DBA-Recht*, in *Niedrigbesteuerung im Unternehmenssteuerrecht* (M. Lang, J. Schuch & C. Staringer (eds.), forthcoming).

[13] For the German perspective see, for example, X. Ditz & J. Schönfeld, *Deutsche Verhandlungsgrundlage für Doppelbesteuerungsabkommen*, 66 Der Betrieb 26/27, pp. 1437 et seq. (2013); J. Lüdicke, *Anmerkungen zur deutschen Verhandlungsgrundlage für Doppelbesteuerungsabkommen*, insert to 22 Internationales Steuerrecht 10, pp. 26 et seq. (2013); see also dBMF, Anwendung von Subject-to-tax-, Remittance-base- und Switch-over-Klauseln nach den Doppelbesteuerungsabkommen unter Berücksichtigung des Urteils des BFH vom 17. Oktober 2007 - I R 96/06 - (BStBl 2008 II S. 953), 20. 6. 2013, GZ IV B 2 – S 1300/09/10006, Dok 2013/0539717; J. Lüdicke, *Subject-to-tax-Klauseln nach den DBA, Bemerkungen zum BMF-Schreiben vom 20. 6. 2013*, 22 Internationales Steuerrecht 19, pp. 721 et seq. (2013).

[14] See Commission Recommendation of 6. 12. 2012 on aggressive tax planning, C(2012) 8806 final; OECD, *Action Plan on Base Erosion and Profit Shifting*, p. 19 (OECD Publishing 2013) ('Work will also be done to clarify that tax treaties are not intended to be used to generate double non-taxation ...').

[15] C(2012) 8806 final, p. 4.

[16] The intention is, obviously, to close all the gaps giving rise to double non-taxation (see C(2012) 8806 final, p. 4.): 'Where Member States, in double taxation conventions which they have concluded among themselves or with third countries, have committed not to tax a given item of income, Member States should ensure that such commitment only applies where the item is subject to tax in the other party to that convention'.

[17] See OECD, *Hybrid Mismatch Arrangements: Policy and Compliance Issues*, p. 14 (OECD Publishing 2012) ('[R]ules taking into account the tax treatment in another country are not a novelty, as in principle … subject to tax clauses … often do exactly that.').

[18] OECD Commentary 1963-2012 on Art. 10 para. 20; OECD Commentary 1963-2012 on Art. 11 para. 13; OECD Commentary 1963-2012 on Art. 12 para. 6; OECD Commentary 1963-2012 on Art. 13 para. 21 and para. 28.12; OECD Commentary 1963-2012 on Art. 15 para. 9; OECD Commentary 1963-2012 on Art. 17 para. 12; OECD Commentary 2005-2012 on Art. 18 paras 14-15; OECD Commentary 1963-2012 on Art. 21 para. 3; OECD Commentary 1963-2012 on Art. 23A and 23B para. 35.

[19] OECD Commentary 1992-2012 on Art. 1 para. 15; OECD Commentary 1963-2012 on Art. 8 para. 3; OECD Commentary 1963-2012 on Art. 28 para. 3; see also OECD, *Tax Treaty Issues Arising From Cross-Border Pensions*, Discussion Draft, p. 5 (OECD Publishing 2003).

which circumstances an item of income is to be considered to be "subject to tax",[20] this resistance is understandable. In many situations, it might be quite obvious that the subject-to-tax clause will apply; for example, if an item of income is subject to a very specific tax exemption which can be considered to be a harmful tax measure. However, there are also other situations in which different countries might have different views on whether a particularity of the domestic tax system of another contracting state should trigger the subject-to-tax clause or not.[21] The question arises whether the subject-to-tax clause recommended by the European Commission is capable of drawing a clear borderline between "harmful" and "harmless" non-taxation in order to prevent the contracting states of a double taxation convention from disagreeing on whether the subject-to-tax clause applies or not. Has the European Commission found the "philosopher's stone" of double tax treaty law which consistently and convincingly transforms double non-taxation into single taxation?

2. The Recommendation of the European Commission: A General Subject-To-Tax Clause

The forms and wordings of subject-to-tax clauses contained in the various bilateral double taxation conventions are manifold.[22] According to the literature, one criterion in order to categorize such rules is whether the subject-to-tax clause only applies to a certain distributive rule (specific subject-to-tax clause) or whether it applies to all categories of income covered by the double taxation convention (general subject-to-tax clause).[23] Following this approach, the subject-to-tax clause as recommended by the European Commission can be described as be-

[20] See M. Lang, *supra* n. 5, pp. 109 et seq.; M. Lang, *„Aggressive Steuerplanung" – eine Analyse der Empfehlung der Europäischen Kommission*, 23 Steuer und Wirtschaft International 2, p. 62, at p. 64 (2013).
[21] See also OECD Commentary 1992-2012 on Art. 1 paras 15-16 ('General subject-to-tax provisions provide that treaty benefits in the State of source are granted only if the income in question is subject to tax in the State of residence. This corresponds basically to the aim of tax treaties, namely to avoid double taxation. For a number of reasons, however, the Model Convention does not recommend such a general provision. … The subject-to-tax approach seems to have certain merits. It may be used in the case of States with a well-developed economic structure and a complex tax law. It will, however, be necessary to supplement this provision by inserting bona fide provisions in the treaty to provide for the necessary flexibility (see paragraph 21 below); moreover, such an approach does not offer adequate protection against advanced tax avoidance schemes such as "stepping-stone strategies"'); OECD, *Double Taxation Conventions and the Use of Conduit Companies*, 1 Issues in International Taxation, paras 30 et seq. (OECD Publishing 1987) ('The subject-to-tax approach, although somewhat similar to the exclusion clauses, covers cases in which it is not possible to give a strict definition of the excluded situation. Thus, the "taxation under ordinary rules" test would exclude from treaty benefits companies enjoying: … [1] Specific privileges granted to "base companies", "domiciled companies", etc.; … [2] Waivers of tax under specific arrangements between the conduit company and the tax administration; … [3] Substantial reduction of tax as well as complete exemption. … On the other hand there are advanced techniques of improper use of tax treaties which could not be covered by the subject-to-tax approach. This is especially so with the "stepping-stone strategies", where the company incurs expenses it can offset against income in accordance with normal rules of tax laws. … Moreover, the subject-to-tax approach would exclude from the benefit of tax treaties companies enjoying: … [1] Tax privileges granted to charitable organisations, pension funds or similar institutions; … [2] Tax privileges granted with a view to fostering the economic development of the country of the conduit company ("tax holidays"). In circumstances such as those derogations from such provisions may be envisaged.').
[22] See M. Lang, *supra* n. 5, pp. 105 et seq.
[23] See M. Schilcher, *supra* n. 3, p. 53; see also E. Burgstaller & M. Schilcher, *Subject-to-Tax Clauses in Tax Treaties*, 44 Eur. Taxn. 6, p. 266, at p. 275 (2004); M. Lampe, *General Subject-To-Tax Clauses in Recent Tax Treaties*, 39 Eur. Taxn. 4/5, p. 183, at p. 184 (1999); M. Schilcher, *Die tatsächliche Besteuerung als maßgebendes Kriterium für die Festlegung des Quellenstaates nach den Doppelbesteuerungsabkommen („Subject-to-tax-Klauseln")*, in *Die Verteilung der Besteuerungsrechte zwischen Ansässigkeits- und Quellenstaat im Recht der Doppelbesteuerungsabkommen*, p. 353, at p. 361 (W. Gassner et al. (eds.), Linde 2005).

ing of a general nature. It is interesting to note that the European Commission's recommendation only refers to double non-taxation of income.[24] However, following the OECD MC and the UN Model Double Taxation Convention between Developed and Developing Countries (UN MC),[25] a multitude of bilateral double taxation conventions also apply to taxes on capital. Therefore, Member States might want to extend the scope of the recommended subject-to-tax clause in order to avoid double non-taxation of capital as well.[26] This could be particularly relevant if a contracting state abolishes all taxes on capital covered by the bilateral double taxation convention. A subject-to-tax clause would ensure that the other contracting state is, in such a situation, not restricted by the double taxation convention from levying taxes on capital which would otherwise remain untaxed.

Another distinctive characteristic of a subject-to-tax clause is whether it focusses on double non-taxation resulting from the source state's lack of exercising the taxing right assigned to it by the double taxation convention or whether it aims at preventing double non-taxation caused by the absence of taxation in the residence state.[27] The subject-to-tax clause recommended by the European Commission cannot be classified in either category, because it applies to both contracting states. Depending on the situation, it has to be determined whether it is up to the residence state or the other contracting state to avoid the imminent double non-taxation.

The recommended subject-to-tax clause, on the one hand, applies if 'the Convention provides that an item of income shall be taxable only in one of the contracting States …'. Thereby, the European Commission obviously wants to address those situations in which a contracting state does not exercise an exclusive taxing right assigned to it by the applicable distributive rule of the double taxation convention. This could be either the residence state (Article 7(1), Article 8(1) or (2), Article 12(1), Article 13(3) or (5), Article 15(1) or (2), Article 18, Article 19(1)(b) or (2)(b), Article 21(1) OECD MC) or the other contracting state (Article 19(1)(a) or (2)(a) OECD MC). The addressee of the subject-to-tax clause is, hence, the contracting state which would be precluded from taxation by such a "complete" distributive rule.[28]

On the other hand, the recommended subject-to-tax clause applies if 'this Convention provides that an item of income … may be taxed in one of the contracting States …'. The distributive rules of the OECD MC always provide that at least one of the contracting states has the right to tax a certain item of income. In those situations in which the distributive rules deter-

[24] For the purpose of the European Commission's recommendation the term "income" must be understood as 'all items which are defined as such under the domestic law of the Member State which applies the term and, where applicable, the items defined as capital gains'. See C(2012) 8806 final, p. 3.
[25] Hereinafter UN MC, available at *http://www.un.org/esa/ffd/documents/UN_Model_2011_Update.pdf* (Accessed March 28, 2014).
[26] For example, the subject-to-tax clause included in Art. 22(1)(5)(b) of the German basis for negotiation for agreements for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital (hereinafter German MC; available at *http://www.bundesfinanzministerium.de/Content/DE/Downloads/BMF_Schreiben/Internationales_Steuerrecht/Allgemeine_Informationen/2013-08-22-Verhandlungsgrundlage-DBA-englisch.pdf?__blob=publicationFile&v=5* [Accessed March 28, 2014]) applies both to taxes on income and on capital.
[27] See M. Lang, *supra* n. 5, pp. 105-106.
[28] For this terminology see K. Vogel, *Conflicts of Qualification: The Discussion is not Finished*, 57 Bull. Intl. Taxn. 2, p. 41, at p. 43 (2003).

mine that certain income "may be taxed" in one contracting state but remain silent on the legal situation of the other contracting state ("open" distributive rules), the method article applies. Articles 23A and 23B OECD MC only apply to the residence state, which is, hence, also the addressee of the subject-to-tax clause in such a situation. However, since the recommended subject-to-tax clause will only apply if one of the contracting states is 'precluded from taxing [an] item of income', the application of the exemption method is required in order for the subject-to-tax clause to be potentially applicable.

The subject-to-tax clause recommended by the European Commission applies to each *item of income*. This raises the question whether or not the subject-to-tax clause relates to a certain category of income – such as income from immovable property (Article 6 OECD MC), dividends (Article 10 OECD MC) or income from employment (Article 15 OECD MC)[29] – or rather to each single element thereof, which would mean that, for example, employment income would have to be split up in its individual elements – such as base salary, bonuses, benefits in kind or any other sort of fringe benefits.[30] The developments in German tax treaty policy show that the idea of referring to each single element of income is not far-fetched. According to the subject-to-tax clause incorporated in Article 22(1)(5)(b) of the German MC,[31] it has to be determined whether or not the other contracting state 'may, under the provisions of the Agreement, tax items of income or capital, *or elements thereof*, but does not actually do so'.[32] In the literature, the many difficulties arising due to such an "atomization" of income have already been illustrated.[33] Since the subject-to-tax clause recommended by the European Commission might also be interpreted in a way that allows for such a dissection of income categories, Member States should be aware of the consequences involved. However, the following argument might be raised against such an interpretation: The plural of the term "item of income" can also be found in the Articles 7(4), 21(1) and 23A(2) OECD MC. It is used in order to refer to 'categories of income which are treated separately in other Articles of the Convention, e.g. dividends'.[34] The coinciding terminology speaks in favor of an OECD-uniform understanding, which means that it is not necessary to further split up a certain category of income. However, even in consideration of this reasoning it might be argued that, in the case of Article 7 OECD MC, it is possible to compartmentalize business profits of an enterprise of a contracting state into its individual elements. According to the wording of Arti-

[29] For an analysis of the term "income" as used in the OECD MC see, for example, M. Lang, *Einkünfteermittlung im Internationalen Steuerrecht*, in *Einkünfteermittlung*, DStJG 34, p. 353, at p. 359 (Hey (ed.), Dr. Otto Schmidt 2011); J. Schuch, *Verluste im Recht der Doppelbesteuerungsabkommen*, pp. 51 et seq. (Linde 1998); F. Wassermeyer, *Der abkommensrechtliche Einkünftebegriff*, 19 Internationales Steuerrecht 9, pp. 324 et seq. (2010).
[30] See J. Lüdicke, *subject-to-tax-Klauseln*, *supra* n. 13, pp. 724-725; see also J. Lüdicke, *Exemption and Tax Credit in German Tax Treaties – Policy and Reality*, 64 Bull. Intl. Taxn. 12, p. 609, at p. 618 (2010); J. Lüdicke, *Exemption and Tax Credit in German Tax Treaties – Policy and Reality*, in *Tax Polymath: A life in international taxation*, Essays in honour of John F. Avery-Jones, p. 269, at p. 293 (P. Baker & C. Bobbett (eds.), IBFD 2010); G. Weitbrecht, *Der Einkünftebegriff in Art. 23 DBA-USA – Auswirkungen auf die Besteuerung US-amerikanischer Betriebsstätten*, 19 Internationales Steuerrecht 22, p. 825, at pp. 828-829 (2010).
[31] See *supra* n. 26.
[32] Emphasis added.
[33] For further details see J. Lüdicke, *Anmerkungen*, *supra* n. 13, pp. 38-39; J. Lüdicke, *subject-to-tax-Klauseln*, *supra* n. 13, pp. 728-729.
[34] OECD Commentary 1963-2012 on Art. 7, para. 60; see also OECD Commentary 1963-2012 on Art. 21, para. 1; OECD Commentary 1963-2012 on Art. 23A and 23B, para. 47; K. Vogel, *supra* n. 4, Art.7, m.no. 150 and Art. 21, m.no. 7.

cle 7(4) OECD MC, after all, such profits might consist – at least partly – of 'items of income which are dealt with separately in other Articles of this Convention'.[35]

In addition to technical aspects of interpretation, Member States have to think about how to implement the subject-to-tax clause recommended by the European Commission in the structure of a double taxation convention. It has to be kept in mind that the proposed subject-to-tax clause does not only apply to double non-taxation triggered by the residence state's application of the exemption method. Therefore, it cannot be included in Article 23A OECD MC, because the method article will not apply if double non-taxation is partially due to the application of a "complete" distributive rule. Following the structure of the OECD MC, it seems reasonable to integrate the recommended subject-to-tax clause in Chapter VI, which deals with special provisions. However, it is doubtful whether including such a general subject-to-tax clause in a bilateral double taxation convention is actually recommendable. When it comes to the interpretation of such a provision, the crucial question is how to determine whether or not an item of income is actually "subject to tax" in the other country. The answer to this question, however, can be very different.[36] A consistent application of the potential "philosopher's stone" of double tax treaty law demands clear guidance on how and in which situation to apply the recommended subject-to-tax clause. Given the associated challenge, the European Commission's remarks on this issue seem surprisingly short:[37] '[A]n item of income should be considered to be subject to tax where it is treated as taxable by the jurisdiction concerned and is not exempt from tax, nor benefits from a full tax credit or zero-rate taxation'.

3. The European Commission's Guidance on the Interpretation of the Subject-To-Tax Requirement

3.1. Lack of Taxability

According to the European Commission, an item of income should be considered to be subject to tax only if it was taxable according to the domestic tax law of the contracting state that is not prevented from taxation by the double taxation convention. At first glance, this seems very straightforward. It has to be kept in mind, though, that the recommendation of the European Commission only refers to 'income tax[es], corporation tax[es] and, where applicable, capital gains tax[es], as well as withholding tax[es] of a nature equivalent to any of these taxes'.[38] However, a double taxation convention, generally, does not only apply to one specific tax but rather covers different kind of taxes on income and on capital.[39] Hence, the question arises whether the subject-to-tax clause would apply if an item of income was subject to a tax that is, in fact, covered by the double taxation convention, but which is not comparable to the

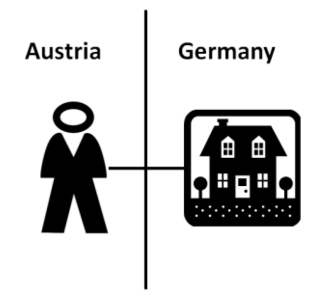
[35] According to the German Federal Fiscal Court ("Bundesfinanzhof"), the subject-to-tax clause included in Article 23(3) of the double taxation convention between Canada and Germany of 1981 (see German Federal Tax Gazette I 1982, pp. 752-763) does not allow dissecting profits into its individual elements (see BFH 27. 8. 1997, I R 127/95). However, the wording of this provision differs from the subject-to-tax clause recommended by the European Commission, because it separately addresses 'profits, income or gains of a resident of a contracting state' instead of generally referring to the term "items of income".
[36] See M. Lang, *supra* n. 5, pp. 109 et seq.
[37] C(2012) 8806 final, p. 4.
[38] C(2012) 8806 final, p. 3.
[39] For an in-depth analysis of Article 2 OECD MC see P. Brandstetter, *"Taxes Covered": A Study of Article 2 of the OECD Model Tax Conventions* (IBFD 2011).

tax potentially imposed by the contracting state that is addressed by the subject-to-tax clause.[40]

A systematic argument against the application of the subject-to-tax clause is that according to Article 23B OECD MC the residence state 'shall allow … as a deduction from the tax on income …, an amount equal to the income tax paid in [the] other state …', irrespective of whether the income tax paid in the other state is fully comparable to the income tax imposed in the residence state.[41] It seems that, from the viewpoint of double tax treaty law, double taxation does not necessarily imply that certain income is subject to comparable taxes in two states. For the purpose of the subject-to-tax clause it can, hence, be concluded that an item of income is to be regarded as subject to tax if the contracting state that is not prevented from taxation by the double taxation convention imposes an income tax covered by the very same treaty. However, even if an item of income is, beyond doubt, not taxable in the contracting state that is not prevented from taxation by the double taxation convention, double non-taxation is not necessarily due to aggressive tax planning (*see* Example 1).

Example 1

Diagram 1: Alienation of Immovable Property



A is a resident of Austria and owns real estate situated in Germany that is held in a private portfolio. In the year X1, the real estate is sold. Under German domestic tax law, the alienation of immovable property held in the private portfolio is taxable, unless the acquisition took place more than ten years ago.[42] In Austria, on the contrary, capital gains derived from the disposal of real estate are subject to a flat tax rate of 25%, irrespective of the holding period.[43] According to Article 13(1) of the double taxation convention between Austria and Germany (DTC Austria-Germany),[44] such capital gains may be taxed in the contracting state where the immovable property is situated. According to Article 23 DTC Austria-Germany, both contracting states apply the exemption method in order to avoid double taxation of such capital gains. If the DTC Austria-Germany, however, included a subject-to-tax clause as recommended by the European Commission, Austria would not be prevented from taxing Austrian residents alienating real estate situated in Germany after the expiration of the holding period of ten

[40] See J. Lüdicke, *Anmerkungen*, *supra* n. 13, at p. 39.
[41] See K. Vogel, *supra* n. 2, Art. 23B, m.no. 153a; see also E. Lechner, *Neuregelung des Anrechnungshöchstbetrages bei der Anrechnung ausländischer Ertragsteuern*, 1 Steuer und Wirtschaft International 3, p. 68, at pp. 71 et seq. (1991); H. Loukota, *Anrechnung ausländischer Steuern*, 1 Steuer und Wirtschaft International 5, p. 139, at p. 141 (1991); H. Loukota, *Anrechnung ausländischer Steuern auf die Gewerbesteuer*, 3 Steuer und Wirtschaft International 1, at pp. 8 et seq. (1993).
[42] See Sections 49(1)(8)(a), 22(2) and 23(1)(1) German Income Tax Act.
[43] See Sections 30, 30a, 30b and 30c Austrian Income Tax Act.
[44] See Austrian Federal Gazette III 182/2002 & III 32/2012 (available at *http://ris.bka.gv.at/Dokumente/BgblPdf/2002_182_3/2002_182_3.pdf* [Accessed March 28, 2014])

years.[45] The result would, on the one hand, be consistent insofar as double non-taxation of capital gains derived from the disposal of immovable property situated in Germany was avoided. On the other hand, it clearly contradicts the situs principle underlying Article 6 and Article 13(1) OECD MC. From a political point of view, it might be justified to deviate from basic principles of double tax treaty law in order to avoid aggressive tax planning. However, in such a situation double non-taxation is not wilfully caused by the taxpayer. The subject-to-tax clause would only apply because of the tax policy decision taken by the Austrian legislator in 2012.[46] Before 2012, capital gains derived from the alienation of real estate held in the private portfolio was – to a large extent comparable to the legislation applicable in Germany – not taxable, unless realized as a speculative capital gain within a period of ten years after acquisition.[47]

Member States should be aware that the subject-to-tax clause recommended by the European Commission does not exclusively apply to double non-taxation caused by aggressive tax planning. It might rather have an impact on all situations in which the tax policy of the contracting states – at present or in the future – differ. Therefore, Member States would have to put even more emphasis on the impact that the envisaged changes to the domestic tax system have on double tax treaty law. Moreover, the developments of another contracting state's domestic tax system have to be monitored more closely as well in order to be able to evaluate the possible ramifications on the taxation of cross-border situations.

3.2. Tax Exemptions

The European Commission considers an item of income not to be subject to tax if it is exempt from tax. The subject-to-tax clause would be triggered if an item of income was tax exempt according to the domestic tax law of the contracting state that is not prevented from taxation by the double taxation convention. It is unclear, though, whether the subject-to-tax clause would also be applicable if both contracting states consider themselves to be prevented from taxation by the double taxation convention (negative qualification conflict). In the end, this could also be regarded as a tax exemption, although due to a bilateral double taxation convention.

According to the OECD, a negative qualification conflict is solved by Article 23A(1) and Article 23A(4) OECD MC. Thus, the residence state would not have to apply the exemption method and double non-taxation would be avoided.[48] However, the OECD's interpretation of Article 23A(1) OECD MC is heavily disputed[49] and not all bilateral double taxation conven-

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[45] See also R. Gebhardt & M. Reppel, *Die neuen Subject-to-tax-Klauseln in deutschen DBA – Praxisfälle und Zweifelsfragen im Kontext des BMF-Schreibens vom 20. 6. 2013*, 22 Internationales Steuerrecht 20, p. 760, at p. 764 (2013).

[46] For more details see, for example, C. Hammerl & G. Mayr, *StabG 2012: Die neue Grundstücksbesteuerung*, Recht der Wirtschaft 3, p. 167, at pp. 168 et seq. (2012); O. Herzog, *Die neue Immobilienbesteuerung ab 1. 4. 2012*, 87 Steuer- und Wirtschaftskartei 11, pp. 563 et seq. (2012); C. Urtz (ed.) *Die neue Immobiliensteuer nach dem 1. StabG 2012* (LexisNexis 2012); J. Perthold & C. Plott (eds.) *Stabilitätsgesetz 2012*, SWK-Spezial (Linde 2012).

[47] See, for example, J. Adametz et al., *Taxation of Investment Income in Austria*, 58 Bull. Intl. Taxn 8, p. 426, at p. 428 (2004).

[48] OECD Commentary 2000-2012 on Art. 23A and 23B para. 32.6; see also M. Lang, *2008 OECD Model: Conflicts of Qualification and Double Non-Taxation*, 63 Bull. Intl. Taxn. 5, pp. 204 et seq. (2009); R. Russo, *The 2008 OECD Model: An Overview*, 48 Eur. Taxn. 9, p. 459, pp. 464 et seq. (2008).

[49] See, for example, W. Gassner & M. Lang, *Double Non-Taxation of a Belgian Tax Law Professor Lecturing in Vienna*, in *Liber Amicorum Luc Hinnekens*, p. 219, pp. 225 et seq. (Bruylant 2002); M. Lang, *supra* n. 11, at p. 917; M. Lang, *Irrwege der DBA-Auslegung am Beispiel der Besteuerung von Lehrbeauftragten*, 8 Steuer und Wirtschaft International 11, p. 508, at p. 512 (1998); M. Lang, *Introduction to the Law of Double Taxation Con-*

tions include a provision corresponding to Article 23A(4) OECD MC.[50] Furthermore, if the residence state, by applying a "complete" distributive rule – such as Article 19(1)(a) or Article 19(2)(a) OECD MC – concludes that the other contracting state has the exclusive taxing right, double non-taxation would remain, irrespective of the interpretation of Article 23A(1) and of Article 23A(4) OECD MC.[51] Assuming that the subject-to-tax clause is also applicable if double non-taxation is caused by a negative qualification conflict, the outcome would be ambiguous. Both contracting states would consider themselves to be precluded from taxation only if the item of income concerned is subject to tax in the other contracting state. There are three possible solutions to this situation of circular cross references: (1) double non-taxation remains, because both contracting states take the position that the other contracting state may tax, or (2) the result is double taxation, because both contracting states conclude that the subject-to-tax clause lift the limits otherwise imposed by the double taxation convention, or (3) the negative qualification conflict is settled by way of a mutual agreement procedure. Either way, it appears that the subject-to-tax clause recommended by the European Commission is not capable of solving negative qualification conflicts in such a manner that both double non-taxation and double taxation are consistently avoided.

The recommendation of the European Commission only addresses tax exemptions relating to an item of income. However, whether a specific tax exemption directly applies to a certain item of income or it remains untaxed because the taxpayer realizing it is individually exempt from tax is simply a matter of legal technique. Hence, an individual exemption applicable to the taxpayer would also trigger the subject-to-tax clause recommended by the European Commission. However, this is one of the reasons why the OECD is skeptical concerning the inclusion of a general subject-to-tax clause.[52] In order to maintain certain tax privileges stipulated in the domestic tax law of a contracting state – such as personal tax exemptions –, the OECD suggests accompanying subject-to-tax clauses with a safeguarding clause.[53] Similar exceptions could also be provided for other situations of double non-taxation that are not caused by aggressive tax planning. Since domestic tax systems tend to be changed much more frequently than double taxation conventions, this can only provide a temporary solution, though. At the time of the double tax treaty negotiations it seems hardly possible to predict all future developments of the domestic tax systems. An alternative to first implementing a very general subject-to-tax clause and then providing specific exceptions for all cases which are not considered to be aggressive tax planning would be to identify and specifically address –

ventions, m.no. 124 (2nd edition, Linde 2013); M. Lang & U. Zieseritsch, *Der Begriff der unselbständigen Arbeit nach Art 15 OECD-MA*, in *Arbeitnehmer im Recht der Doppelbesteuerungsabkommen*, p. 31, at pp. 38-40 (Gassner et al. (eds.), Linde 2003); M. Lang, *supra* n. 48, pp. 205-206; J. Schuch & J. Bauer, *supra* n. 7, pp. 35-39.

[50] See M. Lang, *supra* n. 5, p. 100, whereupon 'Article 23A(4) of the OECD model convention […] has not yet gained wide acceptance in bilateral treaty practice even within the scope of application of the exemption method'.

[51] See A. Rust, *The New Approach to Qualification Conflicts has its Limits*, 57 Bull. Intl. Taxn. 2, p. 45, at p. 49 (2003); see also J.F. Avery Jones, *Conflicts of Qualification: Comment on Prof. Vogel's and Alexander Rust's Articles*, 57 Bull. Intl. Taxn. 5, p. 184, at p. 185 (2003).

[52] See *supra* n. 21.

[53] See OECD Commentary 1992-2012 on Art. 1, para. 19 and para. 21.

by a specific subject-to-tax clause – those situations of double non-taxation that are considered to be undesirable. After all, this also seems to be the current position of the OECD.[54]

3.3. Full Tax Credits

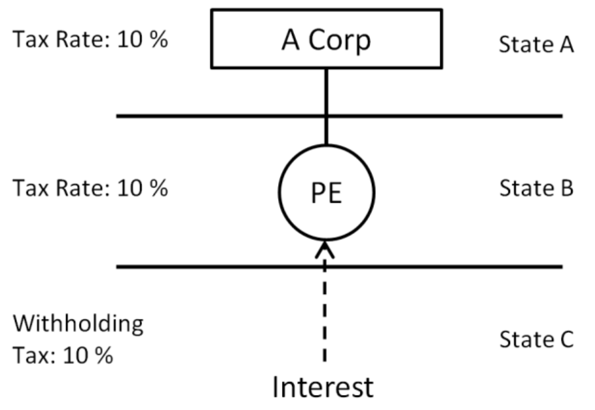
An item of income should also not be considered to be subject to tax if it benefits from a full tax credit. It is unclear which situations the European Commission has in mind when referring to the concept of a full tax credit. Such a system can, for example, be found in the area of dividend taxation. In order to avoid economic double taxation "full imputation systems" allow the recipient of a dividend to credit against the personal dividend tax the corporate income tax paid by the distributing corporation on the distributed profits.[55] Unless the tax rate applied at the level of the shareholder is higher than the tax rate applied at the level of the distributing corporation, the effect of a full imputation system is equivalent to a full tax exemption of the dividends received. However, double taxation conventions, in general, do not deal with economic double taxation of cross-border profit distributions.[56] Therefore, the taxation of the profits earned by the distributing corporation in the source state of the dividend is not affected by the double taxation convention applicable upon distribution. Double tax treaty law would be relevant, though, if the holding in respect of which the dividends are paid was effectively connected with a permanent establishment (PE) situated in the source state. According to Article 10(4) OECD MC, the provisions of Article 7 OECD MC apply in such a case. Since the profit distributions would be attributable to the PE, the source state may tax the dividends in the hands of the receiving person. The residence state would, typically, apply the exemption method. However, if the domestic tax law of the source state provided for a full imputation at the level of the PE, it would be possible to consider the dividends as benefitting from a full tax credit. Dividends attributable to a PE in the other contracting state are covered as part of the business profits attributable to the PE, but since the subject-to-tax clause recommended by the European Commission refers to each "item of income", it might be argued that the profit distributions have to be treated separately within the scope of the subject-to-tax clause. Following these considerations, it is possible that the subject-to-tax clause recommended by the European Commission applies due to the application of a full imputation system.

Beside domestic imputation systems, a full tax credit can also be due to the application of a double taxation convention with a third state (*see* Example 2).

[54] See *supra* n. 18 and n. 19.
[55] See, for example, B.J.M. Terra & P.J. Wattel, *European Tax Law*, pp. 227 et seq. (6th edition, Kluwer Law International 2012).
[56] See OECD Commentary 1977-2012 on Art. 23A and 23B paras 49 et seq.

Example 2

Diagram 2: Business Profits in a Triangular Situation



A Corp is a resident of State A and has a PE in State B. The profits attributable to the PE only consist of interest payments arising in State C. Whereas State A and State B as well as State B and State C have concluded double taxation conventions that follow the OECD MC, State A and State C have not agreed upon a respective treaty. According to the jurisprudence of the supreme court of State B, the double taxation convention with State C also applies to PEs of foreign companies due to the provision corresponding to Article 24(3) OECD MC. The interest payments received by A Corp and attributable to the PE in State B are subject to a 10% withholding tax in State C. According to the bilateral tax treaty rule following Article 23B OEDC MC, this tax can be credited in State B. Since the tax rate in State B is also 10%, the tax credit fully compensates the tax that would have to be paid in State B. If the double taxation convention between State A and State B included a subject-to-tax clause as recommended by the European Commission, it is possible that State A would consider the business profits to not be subject to tax due to the full tax credit available in State B as a result of the double taxation convention between State B and State C. Thus, the subject-to-tax clause would enable State A to fully tax the interest payments attributable to A Corp's PE in State B.

This example shows that the subject-to-tax clause recommended by the European Commission might not only affect domestic tax policy, but also double tax treaty policy. Keeping in mind that a subject-to-tax clause is triggered if the tax policy decisions of the contracting states differ – for example, if an item of income was subject to a tax exemption according to the domestic tax law of the source state whereas the residence state's domestic tax system does not contain a similar form of tax relief – this is not surprising. To conclude a double taxation convention with another country is also a tax policy decision to be taken individually by each country. If a contracting state decided not to conclude a double taxation convention with another country, double taxation would not be avoided in a bilateral cross-border situation. Therefore, such a state could use a subject-to-tax clause in order to ensure that its tax policy decision – not to conclude a double taxation convention with a third country – would not be circumvented in a triangular situation. The Member States should consider the consequences possibly involved before following the recommendation of the European Commission. It is questionable, though, whether it is, in fact, possible to assess the potential aftermath in its entirety.

3.4. Zero-Rate Taxation

The subject-to-tax clause recommended by the European Commission will also apply if 'an item of income … benefits from a … zero-rate taxation'. This seems reasonable since it should not make any difference whether an item of income is not taxable, is exempt from taxation or whether a tax rate of 0% is applied. However, in a progressive income tax system the tax rate is linked to the amount of income earned by the taxpayer. In order to ensure that a taxpayer does not fall below the subsistence minimum due to taxation, many domestic tax systems provide for a zero-rate taxation, unless the income exceeds a certain threshold.[57] The reason for a zero-rate taxation can be very simple. For example, the total amount of income is reduced by the possibility of loss compensation. If this leads to the application of a zero-rate taxation, the subject-to-tax clause will be triggered.[58] However, it is questionable whether the set-off of losses has to be considered to lead to double non-taxation automatically. In the literature, it is argued that even in a loss situation foreign income should be considered to be indirectly taxed in the residence state if it reduces the loss carry-forward and, thus, leads to a temporary deferral of the tax base to the future.[59] From a broader perspective, this argument could also be raised if the disparities of the domestic tax systems of the contracting states result only in temporary differences of taxation (*see* Example 3).[60]

Example 3

A Corp is a resident of State A and has a PE in State B. According to State A's domestic tax law, the profits attributable to the PE amount to 100. If State A applied the exemption method, these profits would have to be exempted. However, unlike State A, the domestic tax system of State B allows for provisions for contingent losses. From the perspective of State B, hence, the PE has suffered a loss of 100 due to a contingent loss in the amount of 200 resulting from a pending transaction attributable to the PE. If the State A-State B double taxation convention included a subject-to-tax clause as recommended by the European Commission, State A could argue that the business profits attributable to the PE are not subject to tax in State B. However, if an actual loss of 100 was realized in the following year, the PE would suffer a loss of 100 from State A's perspective, whereas a profit of 100 would be attributable to the PE according to State B's domestic tax law due to the overvalued provision made in the year X1. From an overall perspective, both contracting states would agree that the total amount of profits attributable to the PE in both years is 0. Still, a profit of 100 would be taxed in the year X1 in State A and in the year X2 in State B.

According to the German Ministry of Finance, even disparities between the domestic tax systems of the contracting states resulting in permanent differences of taxation do not in any event trigger the subject-to-tax clause.[61] This means that, for example, the subject-to-tax

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[57] See German Ministry of Finance, *Die wichtigsten Steuern im internationalen Vergleich 2012*, pp. 28-30, available at *http://www.bundesfinanzministerium.de/Content/DE/Downloads/Broschueren_Bestellservice/2013-04-15-wichtigste-steuern-vergleich-2012.pdf?__blob=publicationFile&v=7* (Accessed March 28, 2014).
[58] See OECD Commentary 1963-2012 on Art. 23A and 23B para. 35; for critical remarks see M. Schilcher, *supra* n. 5, pp. 41 et seq.; A. Steichen & J-P. Winandy, National Report Luxembourg, in in *Double Non-Taxation*, CDFI 89a, p. 513, at p. 527 (IFA (ed.), IBFD 2004); see also A. Rust, *Avoidance of Double Non-Taxation in Germany*, in *Avoidance of Double Non-Taxation*, p. 109, at p. 132 (Lang (ed.), Linde 2003).
[59] See V. Daurer & N. Tüchler, *Foreign Tax Credit – Is a Carry-Forward Obligatory?*, 66 Bull. Intl. Taxn. 10, p. 563, at p. 569 (2012); J. Schuch, *Die Zeit im Recht der Doppelbesteuerungsabkommen*, p. 256 (Linde 2002); see also A. Philipp, *Befreiungssystem mit Progressionsvorbehalt und Anrechnungsverfahren*, p. 115 (Orac 1971).
[60] See German Ministry of Finance, *supra* n. 13, p. 5.
[61] Ibid.

clause included in the German MC will not be triggered if the zero-rate taxation in another country is due to the deduction of business expenses which are not deductible according to German domestic tax law. It is doubtful whether the subject-to-tax clause recommended by the European Commission can be interpreted in such a narrow way.[62] After all, a tax exemption granted by only one of the contracting states also results in a permanent difference.

4. Conclusions

The global fight against aggressive tax planning will have a deep impact on double tax treaty law. The interaction of non-harmonized domestic tax systems and bilateral double taxation conventions provides, after all, an opportunity to withdraw certain items of income from taxation. This is one of the reasons why the OECD started to focus on the issue of double non-taxation resulting from aggressive tax planning by initiating the BEPS project.[63] It remains to be seen what the final outcome of this initiative will be. However, the OECD is not the only international organization dealing with this issue. The European Commission has been active as well and launched a public consultation on double non-taxation on February 29, 2012.[64] A summary report of the responses was published on July 5, 2012[65] followed by a recommendation on aggressive tax planning. Therein, the Member States are, inter alia, encouraged to include a general subject-to-tax clause in their double taxation conventions. However, the Member States should not be too optimistic about this recommendation.

The necessity for subject-to-tax clauses stems from the fact that the tax policy considerations of states differ. Double non-taxation results, inter alia, from the interaction of disparities between the various domestic tax systems and bilateral double taxation conventions. The idea of making the relief to be granted by one contracting state contingent upon the income being subject to tax in the other contracting state in order to avoid tax loopholes has already been discussed in the past. However, although subject-to-tax clauses can be found in various bilateral double taxation conventions around the world, no internationally agreed standard has evolved yet. It is doubtful whether the European Commission's recommendation will lead to a turning point now. Those who expect that the European Commission has found the "philosopher's stone" of double tax treaty law which consistently transforms double non-taxation into single taxation will be disappointed. The proposed subject-to-tax clause would, indeed, avoid double non-taxation resulting from aggressive tax planning. However, since the interpretation of the subject-to-tax requirement is rather ambiguous, it might also cover situations where it makes perfect sense, from a tax policy point of view of one or maybe even both contracting states, that a certain item of income remains untaxed. Neither the wording of the subject-to-tax clause nor the explanatory notes included in the recommendation of the European Commission contain adequate guidance on the question of how to distinguish between "good" and "bad" disparities. The subject-to-tax clause recommended by the European Commission,

[62] In fact, it is even questionable whether the German proposal supports such an interpretation.
[63] OECD, *Addressing Base Erosion and Profit Shifting* (OECD 2013); OECD, *supra* n. 14.
[64] Staff working paper, The internal market: factual examples of double non-taxation cases, Consultation document, TAXUD D1 D(2012).
[65] European Commission, *Summary report of the responses received on the public consultation on factual examples and possible ways to tackle double non-taxation cases*, TAXUD D1 D(2012); see also the comments by M. Nouwen, H&I 4, pp. 22 et seq. (2012).

hence, cannot be designated as the “philosopher’s stone” of double tax treaty law. It rather reminds one of King Midas, who – according to the Greek mythology – made Dionysos confer on him the ability to turn everything he touched into gold. At first sight, the subject-to-tax clause recommended by the European Commission seems similarly tempting, since it allows double non-taxation to be transformed into single taxation. However, it has to be kept in mind that King Midas was not able to anticipate the whole extent of his “gift” which, in the end, even led to his death by starvation.[66] Member States should think twice before equipping their bilateral double taxation conventions with the “Midas touch”, since it might also cover situations where neither of the contracting states expects the subject-to-tax clause to apply.

Although the recommendation of the European Commission can be viewed critically, the idea of subject-to-tax clauses should not necessarily be completely abandoned. If a certain situation can be identified in which taxpayers exploit the interaction between the un-coordinated domestic tax systems of the contracting states and the double taxation convention, a specific subject-to-tax clause might be a useful tool in order to avoid double non-taxation. Thereby, undesired tax loopholes can be closed in a systematic way. A general subject-to-tax clause, on the other hand, seems to be much more difficult to handle in practice. Such a provision, certainly, is very flexible, since it would also avoid double non-taxation resulting from future changes of a contracting state’s domestic tax law. However, contracting states would have to ensure that the general subject-to-tax clause is not triggered unintentionally.

[66] See Aristotle, *Politics*, Book 1, Chapter 9, para. 1257b.