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HOUSE OF REPRESENTATIVES

INTERNATIONAL TAX AGREEMENTS AMENDMENT BILL (No. 1) 2007

EXPLANATORY MEMORANDUM

(Circulated by authority of the
Treasurer, the Hon Peter Costello MP)

Table of contents

Glossary 1

General outline and financial impact 3

Chapter 1 2006 Australia-France tax Convention 11

Chapter 2 2006 Australia-Norway tax Convention 81

Chapter 3 Regulation impact statement for the 2006 France Convention 153

Chapter 4 Regulation impact statement for the 2006 Norway Convention 169

Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

Abbreviation	***Definition***
ATO	Australian Taxation Office
CGT	capital gains tax
Commissioner	Commissioner of Taxation
FBT	fringe benefits tax
GATS	General Agreement on Trade in Services
GST	goods and services tax
GST Act	*A New Tax System (Goods and Services Tax) Act 1999*
ITAA 1936	*Income Tax Assessment Act 1936*
ITAA 1997	*Income Tax Assessment Act 1997*
MEC group	multiple entry consolidated group
MFN	most favoured nation
OECD	Organisation for Economic Co-operation and Development
OECD Model	OECD *Model Tax Convention on Income and on Capital*
the Airline Profits Agreement	the *Agreement between the Government of the Commonwealth of Australia and the Government of the French Republic for the Avoidance of Double Taxation of Income Derived from International Air Transport* (signed 27 March 1969)
the existing France treaty	the *Agreement between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* (signed on 13 April 1976)

Abbreviation	***Definition***
the existing Norway treaty	the *Convention between Australia and the Kingdom of Norway for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital,* and its associated Protocol (signed in 1982)
the France Convention	the *Convention between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation with Respect to Taxes on Income and the Prevention of Fiscal Evasion* and its associated Protocol
the Norway Convention	the *Convention between Australia and the Kingdom of Norway for the Avoidance of Double Taxation with respect to Taxes on Income and the Prevention of Fiscal Evasion*
the Protocol	the *Protocol to the Convention between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income*
UK	United Kingdom of Great Britain and Northern Ireland
US	United States of America

General outline and financial impact

What will this Bill do?

This Bill amends the *International Tax Agreements Act 1953* to give the force of law in Australia to the following tax treaties:

- The *Convention between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation with Respect to Taxes on Income and the Prevention of Fiscal Evasion*, and its associated Protocol, (together referred to as 'the France Convention' for the purposes of this general outline) which was signed in Paris on 20 June 2006.

- The *Convention between Australia and the Kingdom of Norway for the Avoidance of Double Taxation with respect to Taxes on Income and the Prevention of Fiscal Evasion* (referred to as 'the Norway Convention' for the purposes of this general outline) which was signed in Canberra on 8 August 2006.

The 2006 France Convention is Australia's second comprehensive tax treaty with France. The existing tax treaty, which was concluded in 1976 and partially revised by an amending Protocol in 1989, is not well aligned with modern business practices, the respective tax systems and modern tax treaty practice. The France Convention will also cover airline profits which are currently covered by the *Agreement between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation of Income Derived from International Air Transport* (the Airline Profits Agreement) signed in 1969. The new France tax treaty will modernise the tax relationship between the two countries and will serve to facilitate trade and investment between Australia and France.

The 2006 Norway Convention is Australia's second comprehensive tax treaty with Norway. The existing tax treaty, which was concluded in 1982 is, like the existing tax treaty with France, and reflecting its age, not well aligned with modern business practices, the respective tax systems and modern tax treaty practice. The new Norway tax treaty will modernise the tax relationship between the two countries and will serve to facilitate trade and investment between Australia and Norway. Both the existing France and Norway treaties contained most favoured nation (MFN) obligations around providing similar taxation treatment in respect

of dividends, interest and royalties to that provided by Australia to other countries. The obligation to negotiate was triggered by the entry into effect in 2003 of amendments to the treaty with the United States (US) and the renegotiated United Kingdom (UK) treaty.

Who will be affected by this Bill?

Persons who are residents of Australia and/or France or Norway and who derive income, profits or gains from Australia or France or Norway will be affected by this Bill.

How is the legislation structured?

The *International Tax Agreements Act 1953* gives the force of law in Australia to Australia's tax treaties which appear as Schedules to that Act. The provisions of the *Income Tax Assessment Act 1936* (ITAA 1936), the *Income Tax Assessment Act 1997* (ITAA 1997) and the *Fringe Benefits Tax Assessment Act 1986* are incorporated into and read as one with the *International Tax Agreements Act 1953*. The provisions of this Act (including the terms of the tax treaties) take precedence over provisions of the:

- ITAA 1936 (other than section 160AO which determines maximum foreign tax credits and the general anti-avoidance rules under Part IVA);
- ITAA 1997; and
- *Fringe Benefits Tax Assessment Act 1986* (other than section 67 which is an anti-avoidance rule).

In what way does this Bill change the *International Tax Agreements Act 1953*?

The *International Tax Agreements Act 1953* is amended to insert the text of the France Convention and the Norway Convention as Schedules to that Act. Australia's tax treaties (with the exception of the Timor Sea Treaty which incorporates provisions for the avoidance of double taxation between Australia and Timor Leste) appear as Schedules to the above Act, which gives them the force of law.

When will these changes take place?

From the date of Royal Assent.

When will the Conventions enter into force, and from what date will the Conventions have effect?

The 2006 France Convention

The France Convention will enter into force on the first day of the second month following the date of last notification by diplomatic notes that the domestic processes to give the Convention the force of law in the respective countries has been completed. In Australia, enactment of this Bill giving the force of law to the Convention is the prerequisite to such notification.

Once it enters into force the Convention will apply as follows

Application in Australia

For withholding taxes on income derived:

- on or after 1 January next following the date on which the treaty enters into force.

For other Australian taxes on income, profits or gains:

- the Australian year of income beginning on or after 1 July in the calendar year next following the date on which the treaty enters into force.

Application in France

For taxes on income withheld at source:

- the calendar year following the calendar year in which the treaty enters into force.

For taxes on income not withheld at source:

- any calendar year or accounting period beginning after the calendar year in which the treaty enters into force.

For other taxes, for taxation where the taxable event occurs:

- after the calendar year in which the treaty enters into force.

Exchange of information application date

From the date of entry into force of the treaty.

Assistance in recovery date of application

From the date agreed in an exchange of notes between Australia and France.

The 2006 Norway Convention

The Norway Convention will enter into force on the last date of notification by diplomatic notes that the domestic processes to give the Convention the force of law in the respective countries has been completed.

Once it enters into force the Convention will apply as follows

Application in Australia

For withholding taxes on income derived:

- on or after 1 January next following the date on which the treaty enters into force.

For other Australian taxes on income, profits or gains:

- the Australian year of income beginning on or after 1 July in the calendar year next following the date on which the treaty enters into force.

Application in Norway

For taxes on income withheld at source:

- the calendar year following the calendar year in which the treaty enters into force.

Exchange of information application date

From the date of entry into force of the treaty.

Assistance in collection of taxes date of application

From the date agreed in an exchange of notes between Australia and France.

The financial impact of this Bill

The France Convention

The direct cost to revenue from the proposed tax treaty is estimated to be approximately A$10 million per annum. The estimated distribution of this first round cost in future years is shown in the table below:

2007-08	***2008-09***	***2009-10***	***2010-11***
–A$5m	–A$10m	–A$10m	–A$10m

Treasury has not estimated the second round impact of the proposed tax treaty as Treasury does not quantify the second round impact of minor policy proposals as the benefits are generally too small to measure with any degree of certainty. However, it is expected that the Convention could lead to an increase in foreign investment in Australia and an increase in economic activity. The increase in economic activity is likely to lead to increases in other forms of tax collection. The second round effects could offset the direct costs to revenue.

The Norway Convention

Treasury has estimated the impact of the first round effects on forward estimates as unquantifiable but probably negligible.

Compliance costs

No significant compliance costs will result from the entry into force of the two Conventions.

Summary of regulation impact statements

The France Convention

Impact: Medium.

Main points:

- The France Convention is expected to have an impact on Australian residents doing business with France and includes Australian investors, banks, suppliers of technology, consultants, exporters, Australian employees working in France, and Australian residents receiving pensions from France. The treaty will also impact on the Australian Government and the Australian Taxation Office (ATO).

- While source country tax on interest will continue to be limited to 10 per cent, there will be no withholding tax charged on interest derived by a financial institution resident in the other country, or on interest derived by a government body of the other country. No tax is payable on dividends in the source country where the dividend is paid out of profits that have borne the normal rate of company tax (in Australia, where the dividend is franked). A 5 per cent rate limit applies to other dividends where, in the case of Australia, the dividend recipient is a company that holds directly at least 10 per cent of the voting power of the company paying the dividend, or, in the case of France, 10 per cent of the capital of the company paying the dividend. A 15 per cent limitation applies to other dividends. The 5 per cent and 15 per cent limits apply to both franked and unfranked dividends. The general limit for royalties will be reduced from 10 per cent to 5 per cent.

- The revised tax treaty will assist the bilateral relationship by updating an important treaty in the network of commercial treaties between the countries, and by providing for greater cooperation between tax authorities to prevent fiscal evasion and tax avoidance.

- The direct annual cost to revenue of the proposed treaty is estimated to be around A$10 million, which is likely to be offset by estimated second round revenue gains from increased investment, gross domestic product, and growth. No material costs to taxpayers have been identified as likely to arise from the proposed treaty but there is likely to be a

small, unquantifiable administration cost. It is expected that overall, the new treaty will produce a positive economic outcome for Australia.

The Norway Convention

Impact: Medium.

Main points:

- The Norway convention is expected to have an impact on Australian residents doing business with Norway and includes Australian investors, banks, suppliers of technology, consultants, exporters, Australian employees working in Norway, and Australian residents receiving pensions from Norway. The treaty will also impact on the Australian Government and the ATO.

- While source country tax on interest will continue to be limited to 10 per cent, there will be no withholding tax charged on interest derived by a financial institution resident in the other country, or on interest derived by a government body of the other country. No tax is payable on dividends in the source country where the dividend recipient is a company that holds directly at least 80 per cent of the voting power of the company paying the dividend, subject to certain conditions. A 5 per cent rate limit applies to other dividends where the dividend recipient is a company that holds directly at least 10 per cent of the voting power of the company paying the dividend. A 15 per cent limitation applies to other dividends. These limits apply to both franked and unfranked dividends. The general limit for royalties will be reduced from 10 per cent to 5 per cent.

- The revised tax treaty will assist the bilateral relationship by updating an important treaty in the network of commercial treaties between the countries and provides for greater cooperation between tax authorities to prevent fiscal evasion and tax avoidance.

- Treasury has estimated the impact of the first round effects on forward estimates as unquantifiable but probably negligible. No material costs to taxpayers have been identified as likely to arise from the proposed treaty but there is likely to be a small, unquantifiable administration cost. It

is expected that overall, the new treaty will produce a positive economic outcome for Australia.

Chapter 1
2006 Australia-France tax Convention

Outline of chapter

1.1 Schedule 1 amends the *International Tax Agreements Act 1953*. This chapter explains the rules that apply in the 2006 Australia-France tax Convention.

Context of amendments

1.2 The *Convention between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation with Respect to Taxes on Income and the Prevention of Fiscal Evasion*, and its associated Protocol, (together referred to as 'the Convention', however for the remainder of this chapter, referred to as the France Convention) was signed in Paris on 20 June 2006.

1.3 Once in force, the France Convention will replace:

- the *Agreement between the Government of Australia and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* signed on 13 April 1976 (the existing France treaty);
- the Protocol to the existing France treaty as signed on 19 June 1989 (the 1989 Protocol); and
- the *Agreement between the Government of the Commonwealth of Australia and the Government of the French Republic for the Avoidance of Double Taxation of Income Derived from International Air Transport* (the Airline Profits Agreement) signed on 27 March 1969.

Summary of new law

Main features of the new Convention

1.4 The main features of the France Convention are as follows:

- Income from real property may be taxed in full by the country in which the property is situated. Income from real property for these purposes includes natural resource royalties ***[Article 6].***

- Business profits (including income derived from professional services or other activities of an independent nature) are generally to be taxed only in the country of residence of the recipient unless they are derived by a resident of one country through a branch or other prescribed permanent establishment in the other country, in which case that other country may tax the profits. These rules also apply to:

  - business trusts; and

  - payments for spectrum licences ***[Article 7; Protocol, item 3].***

- Profits derived from the operation of ships and aircraft in international traffic are generally to be taxed only in the country of residence of the operator ***[Article 8].***

- Profits of associated enterprises may be taxed on the basis of dealings at arm's length ***[Articles 9 and 22].***

- Dividends, interest and royalties may generally be taxed in both countries, but there are limits on the tax that the country in which the dividend, interest, or royalty is sourced may charge on such income flowing to residents of the other country who are the beneficial owners of the income ***[Articles 10 to 12].***

- In the case of dividends:

  - no source country tax is payable on intercorporate dividends where the dividend recipient is a company that holds directly at least per 10 per cent of the voting power of the Australian company paying the dividend (or at least 10 per cent of the capital of the company in the case of France), and the dividend is paid out profits

  that have borne the normal rate of company tax ***[Article 10, subparagraph 2(a)]***;

  – a 5 per cent rate limit applies to other intercorporate dividends where the dividend recipient is a company that holds directly at least 10 per cent of the voting power of the Australian company paying the dividend (or at least 10 per cent of the capital of the company in the case of France) ***[Article 10, subparagraph 2(b)]***; and

  – a 15 per cent limitation applies to all other dividends ***[Article 10, subparagraph 2(c)].***

- Source country taxation on interest is limited to 10 per cent ***[Article 11, paragraph 2].*** However, exemptions from source country taxation have been provided for certain interest paid to:

  – certain government bodies ***[Article 11, subparagraph 3(a)]***; and

  – financial institutions ***[Article 11, subparagraph 3(b)].***

- The rate limit on source country taxation of royalties is 5 per cent ***[Article 12, paragraph 2].***

- Income, profits or gains from the alienation of real property may be taxed in full by the country in which the property is situated. Subject to that rule and other specific rules in relation to business assets and shares or other interests in land rich entities (which may be taxed in full by the country in which the property is situated), all other capital gains will be taxable only in the country of residence. A specific provision deals with the alienation of property by departing residents ***[Article 13].***

- Income from employment, that is, employees' remuneration, will generally be taxable in the country where the services are performed. However, where the services are performed during certain short visits to one country by a resident of the other country, the income will be exempt in the country visited ***[Article 14].***

- Directors' remuneration may be taxed in the country in which the company of which the person is a director is resident for tax purposes ***[Article 15].***

- Income derived by entertainers and sportspersons may be taxed by the country in which the activities are performed ***[Article 16]***.

- Pensions and annuities will generally be taxed only in the country of residence of the recipient. Some public service pensions may be taxed only by the paying country ***[Articles 17 and 18]***.

- Income from government service (including government service pensions) will generally be taxed only in the country that pays the remuneration. However, the remuneration shall only be taxed in the other country where the services are rendered in that other country by a resident who is a national or citizen of that other country, provided that the resident is not a dual national or citizen ***[Article 18]***.

- Payments made from abroad to visiting students for the purposes of their maintenance or education will be exempt from tax in the country visited ***[Article 19]***.

- Other income (ie, income not dealt with by other Articles) derived by a resident of one country from sources in the other country may generally be taxed in both countries, with the country of residence of the recipient providing double tax relief ***[Article 20]***.

- Source rules in the France Convention prescribe, for domestic law and treaty purposes, the source of income or profits derived by a resident of one country which may be taxed in the other country ***[Article 21]***.

- Double taxation relief for income which, under the France Convention, may be taxed by both countries, is required to be provided by the country of which the taxpayer is a resident under the terms of the Convention as follows:

  – in Australia, by allowing a credit for the French tax against Australian tax payable on income derived by a resident of Australia from sources in France ***[Article 23, paragraph 1]***; and

  – in France, by allowing either a credit for the Australian tax against French tax payable in some circumstances, or for an amount equal to the French tax attributable to certain types of income provided the income has been

taxed in Australia. The method applied will depend on the type of income ***[Article 23, paragraph 2]***.

- In the case of Australia, effect will be given to the double tax relief obligations arising under the France Convention by application of the general foreign tax credit provisions of Australia's domestic law, or the relevant exemption provisions of that law where applicable.

- Consultation and exchange of information between the two taxation authorities is authorised by the France Convention. The Convention authorises and requires Australia to exchange information where the information relates to taxes administered by the Commissioner of Taxation (Commissioner) ***[Articles 24 and 25]***.

- The France Convention ensures the integrity of the tax system by providing for the mutual assistance in the collection of tax debts. This will allow the Australian Taxation Office, in certain circumstances, to seek assistance from the French tax administration to collect Australian taxation debts ***[Article 26]***.

- Australian expatriates who are temporarily resident in France are protected from paying French capital tax on non-French property ***[Article 28]***.

- Australian and French partnership taxation is asymmetric. The France Convention therefore includes a *Partnerships* Article to provide Australian partners of French partnerships greater access to treaty benefits ***[Article 29]***.

Comparison of key features of new law and current law

New law	***Current law***
Updates all Articles, having regard to Australian, French and the Organisation for Economic Co-operation and Development (OECD) tax treaty developments since the existing France treaty arrangements were entered into.	Not applicable.
Extends the coverage of the France Convention to Australian tax on capital gains and updates the list of taxes to which the new treaty arrangements apply. In the case of Australia, these taxes are: • the income tax; • the resource rent tax; and • any identical or substantially similar taxes imposed under the federal law of Australia. However, a broader range of taxes apply in the case of Articles 25 (*Exchange of Information*) and 26 (*Assistance in Recovery*). In the case of Australia the taxes covered are all federal taxes administered by the Commissioner.	In the case of Australia, the taxes to which all Articles of the existing France treaty apply are: • the income tax; and • any identical or substantially similar taxes imposed under the federal law of Australia.
Updates the meaning of 'permanent establishment' in Article 5. In particular, under the new Convention an enterprise is deemed to have a ***permanent establishment*** if: • it has a building site etc which lasts more than 12 months or connected supervisory activities which last more than six months; or • it maintains substantial equipment for rental or other purposes for more than six months.	A building site constitutes a permanent establishment only where the project lasts for more than 12 months. In addition, an enterprise is deemed to have a ***permanent establishment*** if: • it carries on supervisory activities for more than six months in connection with a building site; or • substantial equipment is being used in that country for more than six months by, for, or under contract.

New law	***Current law***
Broadens the meaning of 'real property' in Article 6 to include exploration and mining rights over natural resources.	No equivalent.
Aligns the treatment of income from independent personal services to the OECD standard under Article 7 (*Business Profits*). It also clarifies the application of this Article to business trusts.	Income from independent personal services is treated under the previous international standard in Article 13 (*Independent Personal Services*).
Reduces the rate of dividend withholding tax to: • zero for dividends on non-portfolio holdings of more that 10 per cent, where the income out of which the dividend is paid has borne the full rate of company tax; and • 5 per cent for other non-portfolio holdings.	The rate of dividend withholding tax is limited to 15 per cent.
No equivalent.	An additional branch profits tax is permitted, but the rate is limited to 10 per cent of the after-tax amount in the case of Australia, and 15 per cent in the case of France.
Reduces the rate of interest withholding tax from 10 per cent to zero where certain interest is derived: • from investment of official reserve assets; or • by a financial institution.	No equivalent.
Reduces the rate of royalty withholding tax from a maximum of 10 per cent to 5 per cent of the gross royalty payment.	The rate of royalty withholding tax is limited to 10 per cent of the gross payment.
Updates the definition of 'royalties' and excludes payments for use of equipment.	Definition of 'royalties' includes payments for use of industrial, commercial and scientific equipment.
Includes a comprehensive *Alienation of Property* Article which allocates taxing rights over capital gains.	Coverage limited to income from alienation of real property and interests in land-rich companies.

New law	***Current law***
No equivalent.	Exemption of remuneration of teachers and professors from visits of less than two years.
Allocates taxing rights over income not dealt with elsewhere in the treaty.	Deals only with 'other income' of a dual resident.
Closely aligns Article 25 (*Exchange of Information*) to the 2005 OECD standard. The effect of the changes is to expand the range of taxes to which the Article applies and to clarify that bank secrecy laws do not limit the exchange of information.	The existing rules apply to a narrower range of taxes.
Includes a new Article 26 (*Assistance in Recovery*) which authorises and requires Australia and France to provide assistance to each other in collection of cross-border tax debts.	No equivalent.
Provides that Australian expatriates temporarily resident in France are protected from paying capital tax on non-French property.	No equivalent.
Provides for flow-through treatment of Australian partnerships and provides Australian partners in French partnerships with greater access to treaty benefits.	No equivalent.

Detailed explanation of new law

Article 1 — Persons Covered

Scope

1.5 This Article establishes the scope of the application of the France Convention by providing for it to apply to persons (defined to include individuals, companies and any other body of persons) who are residents of one or both of the countries. It generally precludes extra-territorial application of the treaty. ***[Article 1]***

1.6 The application of the France Convention to persons who are dual residents (ie, residents of both countries) is dealt with in Article 4 (*Residence*).

1.7 The Protocol clarifies that the competent authorities of each country may settle, jointly or separately, the mode of application of the treaty. ***[Protocol, item 1]***

Article 2 — Taxes Covered

Taxes covered

1.8 Article 2 specifies the existing taxes of each country to which the France Convention applies. These are, in the case of Australia:

- the Australian income tax (including that imposed on capital gains); and
- the resource rent tax in respect of offshore petroleum projects.

1.9 The new treaty extends the operation of the treaty to Australian tax on capital gains, which are not covered in the existing France treaty. ***[Article 2, subparagraph 1(a)]***

1.10 Although Australia considers the resource rent tax to be encompassed by the term 'income tax', a specific reference to this has been included in the France Convention to put beyond doubt that it is a tax covered. ***[Article 2, subparagraph 1(a)]***

1.11 As with the existing France treaty, the France Convention generally does not cover Australia's goods and services tax (GST), wool tax and levies, customs duties, state taxes and duties and estate tax and duties. However, federal taxes administered by the Commissioner are covered for the purposes of the *Exchange of Information* and *Assistance in Recovery* Articles. ***[Article 2, subparagraph 3(a)]***

1.12 It is specifically stated that the France Convention applies only to taxes imposed under the federal law of Australia. This is to ensure that the Convention does not bind Australian states and territories and applies only to federal taxes. ***[Article 2, subparagraph 1(a)]***

1.13 For France, the France Convention applies to:

- the income tax;
- the corporation tax;
- the additional taxes on corporations; and

- the widespread social security contributions and contributions for the reimbursement of the social debt.

[Article 2, subparagraph 1(b)]

Identical or substantially similar taxes

1.14 The application of the France Convention will be automatically extended to any identical or substantially similar taxes which are subsequently imposed by either country in addition to, or in place of, the existing taxes. The competent authorities (ie, the Commissioner in Australia and the Minister in charge of the budget in France, or their authorised representatives) are required to notify each other in the event of a significant change in the taxation law of the respective countries. ***[Article 2, paragraph 2]***

Taxes covered for the purposes of information exchange and assistance in the collection of tax debts

1.15 Paragraph 3 specifies the taxes to which Article 25 (*Exchange of Information*) and Article 26 (*Assistance in Recovery*) will apply. The taxes to which these Articles apply are, in the case of Australia, all federal taxes administered by the Commissioner, and in the case of France, all taxes. ***[Article 2, paragraph 3]***

Article 3 — General Definitions

Definition of Australia

1.16 As with Australia's other recent tax treaties, 'Australia' is defined to include certain external territories and areas of the continental shelf. By reason of this definition, Australia preserves its taxing rights, for example, over mineral exploration and mining activities carried on by non-residents on the seabed and subsoil of the relevant continental shelf areas (under section 6AA of the *Income Tax Assessment Act 1936* (ITAA 1936), certain sea installations and offshore areas are to be treated as part of Australia). ***[Article 3, subparagraph 1(a)]***

Definition of France

1.17 The defined term 'France' covers France and the European and Overseas departments of the French Republic (including areas of the continental shelf). The Overseas departments of the French Republic are: French Guiana, Guadeloupe, Martinique and Réunion. France does not cover other dependent areas of France, such as French Polynesia and New Caledonia. ***[Article 3, subparagraph 1(b)]***

Definition of person

1.18 The definition of 'person' includes individuals, companies and any other body of persons. This includes a partnership (as a body of persons). ***[Article 3, subparagraph 1(d)]***

Definition of company

1.19 The definition of 'company' in the France Convention accords with Australia's tax treaty practice.

1.20 The Australian tax law treats certain trusts (public unit trusts and public trading trusts) and corporate limited partnerships (limited liability partnerships) as companies for income tax purposes. These trusts and partnerships are included as companies for the purposes of the France Convention. ***[Article 3, subparagraph 1(e)]***

Definition of international traffic

1.21 In this Convention, this term is of relevance for taxation of profits from shipping and air transport operations (Article 8 (*Ships and Aircraft*)), income, profits or gains from the alienation of ships and aircraft (paragraph 3 of Article 13 (*Alienation of Property*) and wages of crew (paragraph 3 of Article 14 (*Income from Employment*)).

1.22 The definition of 'international traffic' covers international transport by a ship or aircraft operated by an enterprise of one country, as well as domestic transport within that country. However, it does not include transport where the ship or aircraft is operated solely between places in the other country, that is, where the place of departure and the place of arrival of the ship or aircraft are both in that other country, irrespective of whether any part of the transport occurs in international waters. For example, a 'voyage to nowhere' which begins and ends in Sydney on a ship operated by a French enterprise would not come within the definition of international traffic, even if the ship travels through international waters in the course of the cruise. ***[Article 3, subparagraph 1(l)]***

Definition of tax

1.23 For the purposes of the France Convention, the terms 'Australian tax' and 'French tax' do not include any amount of penalty or interest imposed under the respective domestic tax law of the two countries. This is important in determining a taxpayer's entitlement to a foreign tax credit under the double tax relief provisions of Article 23 (*Elimination of Double Taxation*) of the Convention.

1.24 In the case of a resident of Australia, any penalty or interest component of a liability determined under the domestic taxation law of France with respect to income that France is entitled to tax under the France Convention, would not be a creditable 'French tax' for the purposes of paragraph 1 of Article 23 (*Elimination of Double Taxation*). This is in keeping with the meaning of 'foreign tax' in subsection 6AB(2) of the ITAA 1936. Accordingly, such a penalty or interest liability would be excluded from calculations when determining the Australian resident taxpayer's foreign tax credit entitlement under paragraph 1 of Article 23 (pursuant to Division 18 of Part III of the ITAA 1936 — Credits in respect of foreign tax). ***[Article 3, paragraph 2]***

Terms not specifically defined

1.25 Where a term is not specifically defined within this Convention or clarified in the Protocol, that term (unless used in a context that requires otherwise) is to be taken to have the same interpretative meaning as it has under the domestic taxation law of the country applying the France Convention at the time of its application. In that case, the term's meaning under the taxation law of the country will have precedence over the meaning it may have under other domestic laws.

1.26 The same term may have a different meaning and a varied scope within different Acts relating to specific taxation measures. For example, GST definitions are sometimes broader than income tax definitions. The definition more specific to the type of tax should be applied in such cases. For example, where the matter subject to interpretation is an income tax matter, but definitions exist in either the ITAA 1936 or the *Income Tax Assessment Act 1997* (ITAA 1997) and *A New Tax System* (*Goods and Services Tax*) *Act 1999*, the income tax definition would be the relevant definition to be applied.

1.27 If a term is not defined in the France Convention, but has an internationally understood meaning in tax treaties and a meaning under the domestic law, the context would normally require that the international meaning be applied. ***[Article 3, paragraph 3]***

Article 4 — Residence

Residential status

1.28 This Article sets out the basis by which the residential status of a person is to be determined for the purposes of the France Convention. Residential status is one of the criteria for determining each country's taxing rights and is a necessary condition for the provision of relief under the Convention. The concept of who is a resident according to Australian

taxation law, or domiciled in France for purposes of French taxation law, provides the basic test. ***[Article 4, paragraph 1]***

Residency of Governments

1.29 The Article specifically provides that a country, a political subdivision or statutory body or a local authority of the country are residents for the purposes of the treaty. The Australian Federal Government, the State Governments and local councils will be residents for the purpose of the Convention. Public authorities and other entities created for public purposes under an Australian law will also be residents. This does not necessarily mean that income, profits or gains derived by these bodies from sources in France will be subject to tax in France as sovereign immunity principles may apply. ***[Article 4, paragraph 1]***

1.30 The OECD *Model Tax Convention on Income and on Capital* (OECD Model) Commentary makes it clear that it has always been the understanding of member countries that the OECD Model applied to treat governments as residents even in the absence of an express reference to that effect.

Special residency rules

1.31 Paragraph 2 specifies that a person is not a resident of a country (for purposes of the France Convention) if that person is liable to tax in that State in respect only of income from sources in that State.

1.32 This paragraph deals with a person who may be considered to be a resident of a State according to its domestic laws but is only subject to taxation on income from sources in that State, such as, foreign diplomatic and consular staff. In the Australian context, this also means that Norfolk Island residents who are generally subject to Australian tax on Australian source income only, will not be residents of Australia for the purposes of the France Convention. Accordingly, France will not have to forgo tax in accordance with the France Convention on income derived by residents of Norfolk Island from sources in France (which will not be subject to Australian tax). ***[Article 4, paragraph 2]***

Dual residents

1.33 This Article also includes a set of tie-breaker rules for determining how residency is to be allocated to one or other of the countries for the purposes of the France Convention if a taxpayer, whether an individual, a company or other taxable unit, qualifies as a dual resident, that is, a resident of both countries in accordance with paragraph 1 of the Article.

1.34 The tie-breaker rules for individuals apply certain tests, in a descending hierarchy, for determining the residential status (for the purposes of the France Convention) of an individual who is a resident of both countries under their respective domestic laws.

1.35 These rules, in order of application, are:

- If the individual has a permanent home available to them in only one of the countries, the person is deemed to be a resident solely of that country for the purposes of the France Convention.

- If the individual has a permanent home available in both countries or in neither, then the person's residential status takes into account the person's personal or economic relations with Australia and France, and the person is deemed for the purposes of the France Convention to be a resident only of the country with which the person has the closer personal and economic relations.

- Residency will be determined on the basis of an individual's citizenship or nationality where the foregoing test is not determinative.

[Article 4, paragraph 3]

1.36 A dual resident remains, however, in relation to Australia, a resident for the purposes of Australian domestic law. Accordingly, that person remains liable to tax in Australia as a resident, insofar as the France Convention allows.

1.37 Where a non-individual (such as a body corporate) is a resident of both countries in accordance with paragraph 1, the entity will be deemed, for purposes of the France Convention, to be a resident of the country in which its place of effective management is situated. ***[Article 4, paragraph 4]***

French partnerships

1.38 A partnership or group of persons that has its place of effective management in France is a resident of France provided that all its partners, shareholders or other members are personally liable to French tax on their share of the partnership or group's profits. This provision is necessary to address the asymmetric taxation treatment of partnerships by Australia and France. A partnership or group that is a resident of France under this paragraph is entitled to the benefits of the France Convention,

notwithstanding that it may be fiscally transparent for purposes of Australian tax law. ***[Article 4, paragraph 5]***

1.39 However, where a member of such a partnership or group is a resident of a third country (ie, is not a resident of either Australia or France) and the partnership or group is not subject to corporation tax in France, then Australia may tax that member on their share of income, profits or gains in accordance with domestic law and any tax treaty with the country of which the member is a resident. The Protocol makes clear that Australia reserves the right to treat such partnership or group as fiscally transparent for the purposes of determining entitlement to tax benefits under any treaty with the member's country of residence. ***[Protocol, item 2]***

Article 5 — Permanent Establishment

Role and definition

1.40 The application of various provisions of the France Convention (principally Article 7 (*Business Profits*)) is dependent upon whether a person who is a resident of one country carries on business through a permanent establishment in the other country, and if so, whether income derived by that person is attributable to, or assets of that person are effectively connected with, that permanent establishment.

1.41 The definition of the term 'permanent establishment' in this Article corresponds generally with definitions of the term in Australia's more recent tax treaties. The term also fully encompasses the concept of 'fixed base', which is used in the existing France treaty in a separate Article dealing with independent personal services. As such services will now be dealt with under Article 7 (*Business Profits*), it is intended that places that constitute a fixed base for purposes of the existing France treaty would come within the meaning of permanent establishment for purposes of the France Convention.

Meaning of permanent establishment

1.42 The primary meaning of ***permanent establishment*** is expressed as being a fixed place of business through which the business of an enterprise is wholly or partly carried on. To be a permanent establishment within the primary meaning of that term, the following requirements must be met:

- there must be a place of business;

- the place of business must be fixed (both in terms of physical location and in terms of time); and
- the business of the enterprise must be carried on through this fixed place.

[Article 5, paragraph 1]

1.43 Other paragraphs of this Article elaborate on the meaning of the term by giving examples (by no means intended to be exhaustive) of what may constitute a permanent establishment — for example:

- an office;
- a factory;
- a mine or quarry; or
- an agricultural property.

1.44 As paragraph 2 of this Article is subordinate to paragraph 1, the examples listed will only constitute a permanent establishment if the primary definition in paragraph 1 is satisfied. ***[Article 5, paragraph 2]***

Agricultural, pastoral or forestry activities

1.45 Most of Australia's tax treaties include as a permanent establishment an agricultural, pastoral or forestry property. This reflects Australia's policy of retaining taxing rights over exploitation of Australian land for the purposes of primary production. This approach ensures that the arm's length profits test provided for in Article 7 (*Business Profits*) applies to the determination of profits derived from these activities. This position is also reflected in this Convention. ***[Article 5, subparagraph 2(g)]***

Preparatory and auxiliary activities

1.46 Certain activities do not generally give rise to a permanent establishment (eg, the use of facilities solely for storage, display or delivery).

1.47 Generally these activities are of a preparatory or auxiliary character and are unlikely to give rise to substantial profits. The necessary economic link between the activities of the enterprise and the country in which the activities are carried on does not exist in these circumstances.

1.48 Unlike the OECD Model, which provides that the listed activities are deemed not to constitute a permanent establishment, the France Convention provides that an enterprise will not be deemed to have a permanent establishment merely by reason of such activities. This is to prevent the situation where enterprises structure their business so that most of their activities fall within the exceptions when, viewed as a whole, the activities ought to be regarded as a permanent establishment.

1.49 Another feature consistent with Australia's tax treaty practice is that subparagraph 4(f) of Article 5 (*Permanent Establishment*) of the OECD Model — dealing with combinations of the activities of the kind referred to in subparagraphs 3(a) to 3(e) of this treaty — is not included. Australia does not consider that an enterprise undertaking multiple functions of the kind indicated in subparagraphs 3(a) to 3(e) would generally be engaged only in preparatory or auxiliary activities. ***[Article 5, paragraph 3]***

Deemed permanent establishment

Building site or construction or installation project

1.50 Under paragraph 4, an enterprise is deemed to have a permanent establishment and to be carrying on business through that permanent establishment in a country if it has a building site or construction, installation or assembly project in that country which exists for more than 12 months. ***[Article 5, subparagraph 4(a)]***

Supervisory and consultancy activities

1.51 Supervisory activities carried on for more than six months in connection with a building site or construction, installation or assembly project are deemed to constitute a permanent establishment. This provision broadly aligns with Australia's reservation to Article 5 (*Permanent Establishment*) of the OECD Model.

1.52 The term 'building site or construction, installation or assembly project' includes not only the construction of buildings but also the construction of roads, bridges or canals, the renovation (involving more than mere maintenance or redecoration) of buildings, roads, bridges or canals, the laying of pipelines and excavating and dredging. Planning and supervision are considered part of the building site if carried out by the construction contractor. However, planning and supervision carried out by another unassociated enterprise will not be taken into account in determining whether the construction contractor has a permanent establishment in Australia. ***[Article 5, subparagraph 4(b)]***

Substantial equipment

1.53 Under subparagraph 4(c), an enterprise shall be deemed to have a permanent establishment if it has substantial equipment in a country for rental or other purposes for longer than six months, unless the equipment is leased under a 'hire-purchase' agreement. Under Australian law, the lessee under a 'hire-purchase' agreement (a lease accompanied by certain lessee purchase options or rights) is broadly treated for tax purposes as the owner of the leased property.

1.54 This provision reflects Australia's reservation to the OECD Model concerning the use of substantial equipment. Australia's experience is that the permanent establishment provision in the OECD Model may be inadequate to deal with high value activities involved in the development of natural resources, particularly in offshore regions.

1.55 The meaning of the term 'substantial' depends on the relevant facts and circumstances of each individual case. However, some examples of substantial equipment would include:

- large industrial earthmoving equipment or construction equipment used in road building, dam building or powerhouse construction;
- manufacturing or processing equipment used in a factory;
- oil and drilling rigs, platforms and other structures used in the petroleum/mining industry; and
- grain harvesters and other large agricultural machinery.

1.56 For the purposes of the France Convention the enterprise is deemed to carry on business through the substantial equipment permanent establishment. ***[Article 5, subparagraph 4(c)]***

Anti-avoidance provision

1.57 Given that this Article contains certain timeframes, an anti-avoidance rule is included to ensure that where associated enterprises carry on connected activities the periods will be aggregated in determining whether the enterprises have a permanent establishment in the country in which the activities are being carried on. Activities will be regarded as connected where, for example, different stages of a single project are carried out by different subsidiaries within a group of companies.

1.58 Paragraph 5 is an anti-avoidance measure aimed at counteracting contract splitting for the purposes of avoiding the application of the permanent establishment rules.

1.59 Subparagraph 5(c) provides that an enterprise shall be deemed to be associated with another enterprise if one enterprise is controlled directly or indirectly by the other or if both are controlled directly or indirectly by the same third person or persons. Subparagraph 5(b) also provides that a period of concurrent activities by such associated enterprises is only counted as one period for aggregation purposes. ***[Article 5, paragraph 5]***

Dependent agents

1.60 Subparagraph 6(a) reflects Australia's tax treaty practice in relation to a person who acts on behalf of an enterprise of another country of deeming that person to constitute a permanent establishment if that person has and habitually exercises an authority to conclude contracts on behalf of the enterprise.

1.61 A person who substantially negotiates all essential parts of a contract on behalf of an enterprise will be regarded as exercising an authority to conclude contracts on behalf of that enterprise within the meaning of this provision, even if the contract is subject to final approval or formal signature by another person.

1.62 Activities of a dependent agent, however, will not give rise to a permanent establishment where that agent's activities are limited to the purchase of goods or merchandise for the enterprise. ***[Article 5, subparagraph 6(a)]***

Manufacturing or processing on behalf of others

1.63 Subparagraph 6(b) is consistent with another of Australia's reservations to the OECD Model. It deals with situations where a person acts on behalf of another in manufacturing or processing that other person's goods. An example is the situation where a mineral plant refines minerals at cost, so that the plant operations produce no Australian profits. Title to the refined product remains with the mining consortium and profits on sale are realised mainly outside of Australia.

1.64 Subparagraph 6(b) deems such a plant to be a permanent establishment because the manufacturing or processing activity (which gives the processed minerals their real value) is conducted in Australia, and therefore Australia should have taxing rights over the business profits arising from the sale of the processed minerals to the extent that they are attributable to the processing activity carried on in Australia. This

subparagraph prevents an enterprise which carries on substantial manufacturing or processing activities in a country through an intermediary from claiming that it does not have a permanent establishment in that country.

1.65 This subparagraph is in the existing France treaty. The inclusion of this subparagraph is insisted upon by Australia in its tax treaties and is consistent with Australia's policy of retaining taxing rights over profits from manufacturing or processing on behalf of others including, importantly, in the exploitation of Australia's mineral resources. ***[Article 5, subparagraph 6(b)]***

Independent agents

1.66 Business carried on through an independent agent will not, of itself, give rise to a permanent establishment, provided that the independent agent is acting in the ordinary course of that agent's business as such an agent. ***[Article 5, paragraph 7]***

Subsidiary companies

1.67 Generally, a subsidiary company will not be a permanent establishment of its parent company. A subsidiary, being a separate legal entity, would not usually be carrying on the business of the parent company but rather its own business activities. However, a subsidiary company gives rise to a permanent establishment if the subsidiary permits the parent company to operate from its premises such that the tests in paragraph 1 of Article 5 are met, or acts as an agent of the parent company such that a dependent agent permanent establishment is constituted. ***[Article 5, paragraph 8]***

Other Articles

1.68 The principles set down in this Article are also to be applied in determining whether a permanent establishment exists in a third country, or whether an enterprise of a third country has a permanent establishment in Australia (or France), when applying the source rule contained in:

- paragraph 7 of Article 11 (*Interest*); and
- paragraph 5 of Article 12 (*Royalties*).

[Article 5, paragraph 9]

Article 6 — Income from Real Property

Where income from real property is taxable

1.69 This Article provides that the income of a resident of France or Australia from real property may be taxed by the country in which the real property is situated. Thus, income from real property in Australia will be subject to Australian tax laws. ***[Article 6, paragraph 1]***

1.70 As in the existing France treaty, paragraph 1 provides that income derived from agricultural, pastoral or forestry property will be treated as income from real property. Income from agricultural, pastoral or forestry property is also dealt with under Article 5 (*Permanent Establishment*) and the related 'business profits' provisions of Article 7 (*Business Profits*) of the treaty. ***[Article 5, subparagraph 2(g)]***

1.71 The inclusion of income from agricultural, pastoral or forestry property in both Articles 6 and 7 ensures that such income will receive the same treatment regardless of which Article is considered to apply.

Definition

1.72 Income from 'real property' (which is primarily defined as having the meaning which it has under the domestic law of the country where the property is situated) also extends, in the case of Australia, to income from:

- the direct use, letting or use of any form of real property, a lease of land and any other interest in or over land (including exploration and mining rights); and
- royalties and other payments relating to the exploration for or exploitation of mines or quarries or other natural resources or rights in relation thereto.

[Article 6, subparagraph 2(a)]

1.73 This Article makes allowance for the fact that French law recognises a concept of immovable property in place of the Australian law concept of real property. As in the existing France treaty, 'real property' is defined separately for France and Australia to reflect this difference.

1.74 In the case of France, the definition follows the OECD Model definition of immovable property and includes:

- property accessory to real property;

- livestock and equipment used in agriculture and forestry;
- rights to which the provisions of the general law respecting landed property apply;
- usufruct of immovable property (generally, a right to use property without degrading it and to retain any profits derived from it); and
- rights to variable or fixed payments as consideration for the working of or right to work mineral deposits, mineral sources and other natural resources.

[Article 6, paragraph 2(b)]

1.75 Ships and aircraft are excluded from the definition of real property. Therefore, this Article does not cover income from their use. ***[Article 6, paragraph 2]***

Shares or other rights to enjoyment of real property

1.76 In accordance with French treaty practice, paragraph 4 of this Article provides that income arising from the direct use, letting or use in any other form from shares or other rights in a company, trust or comparable institution that provide a right to enjoy real property situated in a country may be taxed in that country.

1.77 Paragraph 4 would apply, for example, if a French resident owns a share in a company, where that share gives rise to an entitlement to stay in an apartment in Australia, often referred to as a time share arrangement. In such a situation, Australia would have a taxing right over the income the French resident received from letting the Australian apartment to another person to occupy. This paragraph applies notwithstanding that the French resident may not be carrying on business in Australia through a permanent establishment, as required by Article 7 (*Business Profits*). ***[Article 6, paragraph 4]***

Form of exploitation of real property

1.78 Paragraphs 3 and 6 make it clear that the general rule in paragraph 1 and the additional rule in paragraph 4 apply irrespective of the form of exploitation of the real property. ***[Article 6, paragraphs 3 and 6]***

Real property of an enterprise

1.79 Paragraph 5 extends the application of this Article to income derived from the use or exploitation of real property of an enterprise.

1.80 Accordingly, this Article (when read with Article 7 (*Business Profits*)) ensures that the country in which the real property is situated may impose tax on the income derived from that property by an enterprise of the other country, irrespective of whether or not that income is attributable to a permanent establishment of such an enterprise situated in the first-mentioned country. ***[Article 6, paragraph 5]***

Deemed situs

1.81 Under Australian law the place where an interest in land, such as a lease, is situated (situs) is not necessarily where the underlying property is situated. This paragraph puts the situation of the interest or right beyond doubt by deeming the situs to be where the underlying real property over which the lease or right is granted is situated or where any exploration may take place. ***[Article 6, paragraph 7]***

Article 7 — Business Profits

1.82 Article 7 is concerned with the taxation by one country of business profits derived by an enterprise that is a resident of the other country.

1.83 The taxing of these profits depends on whether they are attributable to the carrying on of a business through a permanent establishment in that country. If a resident of one country carries on business through a permanent establishment (as defined in Article 5 (*Permanent Establishment*)) in the other country, the country in which the permanent establishment is situated may tax the profits of the enterprise that are attributable to that permanent establishment. ***[Article 7, paragraph 1]***

1.84 If an enterprise which is a resident of one country derives business profits in the other country other than profits attributable to a permanent establishment in that other country, the general principle of this Article is that the enterprise will not be liable to tax in the other country on such business profits (except where paragraph 6 of this Article applies — see the explanation in paragraphs 1.88 and 1.89).

Determination of business profits

1.85 Profits of a permanent establishment are to be determined for the purposes of this Article on the basis of arm's length dealings. The provisions in the France Convention correspond to international practice and the comparable provisions in Australia's other tax treaties. ***[Article 7, paragraphs 2 and 3]***

1.86 No profits are to be attributed to a permanent establishment merely because it purchases goods or merchandise for the enterprise.

Accordingly, profits of a permanent establishment will not be increased by adding to them any profits attributable to the purchasing activities undertaken for the head office. It follows, of course, that any expenses incurred by the permanent establishment in respect of those purchasing activities will not be deductible in determining the taxable profits of the permanent establishment. ***[Article 7, paragraph 5]***

Inadequate information

1.87 The domestic law of the country in which the permanent establishment is situated (eg, Australia's Division 13 of Part III of the ITAA 1936) may be applied to determine the tax liability of a person, consistently with the principles of the Article. This is of particular relevance where, due to inadequate information, the correct amount of profits attributable on the arm's length principle basis to a permanent establishment cannot be determined, or can only be ascertained with extreme difficulty. Paragraph 4 explicitly recognises the right of each country to apply its domestic law in these circumstances. This is consistent with Australia's reservation to Article 7 (*Business Profits*) of the OECD Model. ***[Article 7, paragraph 4]***

Profits dealt with under other Articles

1.88 Where income is specifically dealt with under other Articles of the France Convention, the effect of those particular Articles is not overridden by this Article.

1.89 Paragraph 6 of this Article lays down the general rule of interpretation that categories of income which are the subject of other Articles of the France Convention (eg, Article 8 (*Ships and Aircraft*), Article 10 (*Dividends*), Article 11 (*Interest*), Article 12 (*Royalties*) and Article 13 (*Alienation of Property*)) are to be treated in accordance with the terms of those Articles (except where otherwise provided, for example, by paragraph 4 of Article 10 (*Dividends*) where the asset in respect of which the income is paid is effectively connected with a permanent establishment). ***[Article 7, paragraph 6]***

Insurance with non-residents

1.90 Each country has the right to continue to apply any provisions in its domestic law relating to the taxation of income from any form of insurance, other than life insurance. However, if the relevant law in force in either country at the date of signature of the treaty is subsequently varied (otherwise than in minor respects so as not to affect its general character), the countries must consult with each other with a view to agreeing to any amendment of this paragraph that may be appropriate. An effect of this paragraph is to preserve, in the case of Australia, the

application of Division 15 of Part III of the ITAA 1936 (Insurance with Non-residents). This is consistent with Australia's reservation to Article 7 (*Business Profits*) of the OECD Model. ***[Article 7, paragraph 7]***

Trust beneficiaries

1.91 The principles of Article 7 will apply to business profits which under the France Convention fall to be taxed under this Article and which are derived by a resident of one of the countries (directly or through one or more interposed trust estates) as a beneficiary of a trust estate other than a trust estate which is treated as a company for tax purposes.

1.92 In accordance with this provision, Australia has the right to tax a share of business profits, originally derived by a trustee of a trust estate (other than a trust estate that is treated as a company for tax purposes) from the carrying on of a business through a permanent establishment in Australia, to which a resident of France is beneficially entitled under the trust estate. This ensures that such business profits will be subject to tax in Australia where, in accordance with the principles set out in Article 5 (*Permanent Establishment*), the trustee of the relevant trust estate has a permanent establishment in Australia in relation to that business. The principles of this paragraph will also apply where relevant to other Articles of the France Convention, such as Article 13 (*Alienation of Property*) in its application to income, profits or gains arising from the alienation of the assets of a permanent establishment or the permanent establishment itself. ***[Article 7, paragraph 8]***

Spectrum licenses

1.93 Payments made for use of, or the right to use, the radiofrequency spectrum under a spectrum licence will fall under this Article. Accordingly, profits of a non-resident licence holder from operating radiocommunications devices under the licence, or authorising others to use the rights under the spectrum licence will be taxable in Australia to the extent that those profits are attributable to a permanent establishment of the non-resident licence holder in Australia. ***[Protocol, item 3]***

1.94 Where the person receiving payments for the use of a spectrum licence (within the meaning of the *Radiocommunications Act 1992*) does not have a permanent establishment in Australia, subsection 3(11A) of the *International Tax Agreements Act 1953* will operate so that the person is taken to carry on business through a permanent establishment and the payments will be taken to be attributable to a permanent establishment.

Article 8 — Ships and Aircraft

1.95 The main effect of this Article is that the right to tax profits from the operation of ships or aircraft in international traffic, including a share of profits attributable to participation in a pool service or other profit sharing arrangement, is generally reserved to the country in which the operator is a resident for tax purposes. ***[Article 8, paragraphs 1 and 5]***

1.96 The profits covered consist in the first place of the profits directly obtained by the enterprise from the transportation of passengers or cargo by ships or aircraft (whether owned, leased or otherwise at the disposal of the enterprise) that it operates in international traffic. However, as international transport has evolved, shipping and air transport enterprise invariably carry on a large variety of activities to facilitate, or support their international operations. Consistent with the 2005 OECD Model Commentary on Article 8, paragraph 1 also covers profits from activities which are not directly connected with the operation of the enterprise's ships or aircraft in international traffic but which are ancillary to such operation.

1.97 Paragraph 2 reflects Australian treaty policy of reserving to the source country the right to tax profits from internal traffic and profits from other coastal and continental shelf activities, including non-transport shipping and aircraft activities, within its own waters and airspace. Profits derived directly or indirectly by a French enterprise from the operation of ships or aircraft, to the extent that they relate to operations confined solely to places in Australia, may thus be taxed in Australia. ***[Article 8, paragraph 2]***

1.98 As in the existing France treaty, the amount which will be charged to tax in the source country from internal transport operations of ships is limited to 5 per cent of the amount paid or payable (net of rebates) in respect of carriage. ***[Article 8, paragraph 3]***

1.99 However, the limit on the amount to be charged to tax will not apply where such profits are attributable to a permanent establishment of an enterprise situated in the source country. In these circumstances, the profits may be taxed in the source country at ordinary rates under paragraph 2. ***[Article 8, paragraph 4]***

1.100 Australia's taxing rights are specifically preserved over profits from the carriage by ships or aircraft of passengers or cargo (including mail) where the passenger or cargo is shipped and discharged in Australia. ***[Article 8, paragraph 6]***

Example 1.1

A ship operated by a French enterprise, in the course of an international voyage from Marseilles to Melbourne, makes a stop in Perth to pick up cargo. Profits derived from the transport of the goods loaded in Perth and discharged in Melbourne would be profits from operations confined solely to places in Australia. Australia would therefore have the right to tax the profits relating to such transport. Five per cent of the amount paid in respect of the transport of those goods would be deemed to be taxable income of the operator for Australian tax purposes pursuant to Division 12 of Part III of the ITAA 1936, and may be taxed in Australia in accordance with the Article.

Example 1.2

A French enterprise operates sightseeing flights to observe whales in the Southern Ocean. Passengers board the aircraft in Hobart and disembark at the same airport later on the same day. These operations would be regarded as operations confined solely to places in Australia, notwithstanding that the aircraft passes through international airspace. Australia would therefore have the right to tax the profits relating to the carriage of these passengers.

1.101 Operations involving the use of ships or aircraft, such as haulage, survey or dredging activities, or other activities relating to exploration or extraction of natural resources that are undertaken in Australia (including coastal waters, the continental shelf areas and external territories) are also regarded as operations confined solely to places in Australia.

Article 9 — Associated Enterprises

Reallocation of profits

1.102 This Article deals with associated enterprises (such as parent and subsidiary companies and companies under common control). It authorises the reallocation of profits between related enterprises in Australia and France on an arm's length basis where the commercial or financial arrangements between the enterprises differ from those that might be expected to operate between unrelated enterprises dealing wholly independently with one another.

1.103 This Article would not generally authorise the rewriting of accounts of associated enterprises where it can be satisfactorily demonstrated that the transactions between such enterprises have taken place on normal, open market commercial terms. Consistent with Australia's recent treaty practice, the inclusion of the expression 'dealing

wholly independently with one another' in paragraph 1 recognises dealings on a truly independent basis as the appropriate benchmark for determining whether the transactions have taken place on normal, open market commercial terms. ***[Article 9, paragraph 1]***

1.104 The broad scheme of Australia's domestic law provisions relating to international profit shifting arrangements under which profits are shifted out of Australia, whether by transfer pricing or other means, is to impose arm's length standards in relation to international dealings. Where the Commissioner cannot ascertain the arm's length consideration, it is deemed to be such an amount as the Commissioner determines.

1.105 Paragraph 2 of this Article specifically recognises the right of each country to apply its domestic law relating to the determination of the tax liability of a person (eg, Australia's Division 13 of the ITAA 1936) to its own enterprises in cases where the available information is inadequate, provided that such provisions are applied, so far as the information available to the competent authority permits, consistently with the principles of the Article. This reflects Australia's reservation to Article 9 (*Associated Enterprises*) of the OECD Model. ***[Article 9, paragraph 2]***

Correlative adjustments

1.106 Where a reallocation of profits is made (either under this Article or, by virtue of paragraph 2, under domestic law) so that the profits of an enterprise of one country are adjusted upwards, a form of double taxation would arise if the profits so reallocated continued to be subject to tax in the hands of an associated enterprise in the other country. To avoid this result, the other country — if it considers the primary adjustment justified — will make an appropriate compensatory adjustment to the amount of tax charged on the profits involved to relieve any such double taxation.

1.107 It would generally be necessary for the affected enterprise to apply to the competent authority of the country not initiating the reallocation of profits for an appropriate compensatory adjustment to reflect the reallocation of profits made by the other treaty partner country. If necessary, the competent authorities of Australia and France will consult with each other to determine the appropriate adjustment. ***[Article 9, paragraph 3]***

Article 10 — Dividends

1.108 This Article allocates taxing rights in respect of dividends flowing between Australia and France. The Article provides that:

- certain cross-border intercorporate dividends will be either exempt or subject to a maximum 5 per cent rate of source country tax;
- a maximum 15 per cent rate of source country tax may be applied on all other dividends;
- dividends paid in respect of a holding which is effectively connected with a permanent establishment are dealt with under Article 7 (*Business Profits*); and
- extra-territorial application by either country of taxing rights over dividend income is not permitted.

Permissible rate of source country taxation

Exemption for certain cross-border intercorporate dividends

1.109 No tax will be payable in the source country on dividends paid to a company that is resident in the other country where:

- the recipient company holds directly at least 10 per cent of the voting power of the company paying the dividends, or in the case of France, the company holds directly at least 10 per cent of the capital of the company paying the dividends; and
- the dividends are paid out of profits that have borne the normal rate of company tax.

[Article 10, subparagraph 2(a)]

1.110 This Article allows both countries to tax other dividends flowing between them but limits the rate of tax that the source country may impose on dividends paid by companies that are residents of that country under its domestic law to residents in the other country who are the beneficial owners of the dividends. ***[Article 10, paragraphs 1 and 2]***

Five per cent rate limit for certain cross-border intercorporate dividends

1.111 A rate limit of 5 per cent will apply for dividends paid in respect of company shareholdings that do not qualify for the intercorporate

dividend exemption under subparagraph 2(a) of this Article, but constitute a direct interest (ie, voting interest in the case of Australia and capital interest in the case of France) of at least 10 per cent in the company that paid the dividends. This rate will apply to non-portfolio dividends that are paid out of profits that have not borne the normal rate of company tax. ***[Article 10, subparagraph 2(b)]***

Fifteen per cent rate limit for all other dividends

1.112 In all other cases, the treaty provides that the source country will generally limit its tax to 15 per cent of the gross amount of the dividend. In the case of Australia, this will mean that the domestic rate of withholding tax imposed on unfranked dividends will be reduced from 30 per cent to 15 per cent. ***[Article 10, subparagraph 2(c)]***

1.113 Despite the provisions described above, the dividend withholding tax exemption provided by Australia under its domestic law for franked dividends paid to non-residents will continue to apply.

Profits that have borne the normal rate of company tax and Australia's franking system

1.114 In the case of Australia, dividends paid out of profits that have borne the normal rate of company tax will be dividends, or part of a dividend, that is franked in accordance with Australia's franking (imputation) credit rules. This will also be the case where a dividend is paid by a member of a multiple entry consolidated (MEC) group to a French company and the dividend is franked with imputation credits from the MEC group consolidated franking account.

Future changes to either country's domestic tax treatment of dividend

1.115 If there is a material change to either country's general approach to taxing dividends (eg, a change to Australia's domestic law arrangements for franked dividends flowing overseas), the two countries are obliged to consult with each other to consider whether any amendment to paragraph 2 of Article 10 would be appropriate as a consequence of the change to domestic law. ***[Article 10, paragraph 2]***

Dividends effectively treated as business profits

1.116 The limitation on the tax of the country in which the dividend is sourced does not apply to dividends derived by a resident of the other country who has a permanent establishment in the source country from which the dividends are derived, if the holding giving rise to the dividends is effectively connected with that permanent establishment.

1.117 Where the holding is so effectively connected, the dividends are to be treated as business profits and therefore subject to the full rate of tax applicable in the country in which the dividend is sourced in accordance with Article 7 (*Business Profits*). ***[Article 10, paragraph 4]***

1.118 Franked and unfranked dividends paid by an Australian company will be included in the assessable income of a non-resident company or individual where the dividends are attributable to a permanent establishment situated in Australia. Expenses incurred in deriving the dividend income are allowable as a deduction from that income when calculating the taxable income of the non-resident. Further, a non-resident company or individual may be entitled to tax offsets in respect of any franked dividends under Australia's domestic law.

Extra-territorial application precluded

1.119 The extra-territorial application by either country of taxing rights over both dividend income and undistributed profits is precluded. Broadly, one country (the first country) will not tax dividends paid by a company resident solely in the other country, unless:

- the person deriving the dividends is a resident of the first country; or
- the shareholding giving rise to the dividends is effectively connected with a permanent establishment in the first country.

1.120 For example, Australia may not tax dividends paid by a French company to a resident of France out of profits derived from Australian sources, unless the French shareholder has a permanent establishment in Australia with which the holding is effectively connected. Similarly, a country is precluded from imposing an undistributed profits tax on a company which is a resident of the other country, even if those undistributed profits arose in the first country. Australia does not impose an undistributed profits tax.

1.121 These restrictions do not apply when the company is, for tax purposes, a resident of both Australia and France under the respective laws of the two countries. ***[Article 10, paragraph 5]***

Definition of dividends

1.122 The term ***dividends*** in this Article means income from:

- shares or other rights which participate in profits and are not debt-claims; and

- other amounts that are subject to the same tax treatment as a distribution or dividend by the laws of the country of which the paying company is a resident.

1.123 The inclusion of 'other amounts which are subjected to the same taxation treatment as a distribution or dividend' within the definition is consistent with the reservation lodged by France to Article 10 (*Dividends*) of the OECD Model, which expands the definition to cover all income subjected to the taxation treatment of distributions. This may include certain interest payments that are treated as distributions under its domestic law and are therefore subject to the *Dividends* Article in preference to the *Interest* Article. This part of the definition also provides that income from equity interests as determined under Australia's debt-equity rules is included in the definition. ***[Article 10, paragraph 3]***

Article 11 — Interest

1.124 This Article allocates taxing rights in respect of interest flows between Australia and France. The Article provides that:

- an exemption from source country tax generally applies to certain cross-border interest flows to:
  - the government, its monetary institutions or central banks; or
  - financial institutions;
- a maximum 10 per cent rate of source country tax may be applied on all other interest income;
- interest paid on an indebtedness which is effectively connected with a permanent establishment shall be subject to Article 7 (*Business Profits*);
- interest payments are deemed to have an Australian source (and may therefore be taxed in Australia) where:
  - the interest is paid by an Australian resident to a French resident; or
  - the interest is paid by a non-resident to a French resident and it is an expense of the payer in carrying on business in Australia through a permanent establishment; and

- relief will be restricted to the gross amount of interest which would be expected to be paid on an arm's length dealing between independent parties.

Permissible rate of source country taxation

Ten per cent rate limit

1.125 This Article provides for interest income to be taxed by both countries but requires the country in which the interest arises to generally limit its tax to 10 per cent of the gross amount of the interest where a resident of the other country is the beneficial owner of the interest. ***[Article 11, paragraphs 1 and 2]***

Exemptions for interest paid to government bodies

1.126 The exemption for interest paid to government bodies reflects the principle of sovereign immunity and will apply to interest derived from the investment of the Government's official reserve assets. Similar exemptions apply in a number of Australia's tax treaties. ***[Article 11, subparagraph 3(a)]***

Exemptions for interest paid to financial institutions

1.127 The exemption for interest paid to financial institutions recognises that the agreed 10 per cent withholding tax rate on gross interest can be excessive given their cost of funds. The exemption will also broadly align the treatment of interest paid to French financial institutions with the Australian domestic law exemption for interest paid on widely distributed arm's length corporate debenture issues (section 128F of the ITAA 1936). ***[Article 11, subparagraph 3(b)]***

1.128 The term ***financial institution*** means a bank or other enterprise substantially raising debt finance in the financial markets or by taking deposits at interest and using those funds in carrying on the business of providing finance. It does not include a corporate treasury or a member of a group that performs the financing services of the group. ***[Article 11, subparagraph 3(b)]***

1.129 The exemption will not be available for interest paid as part of an arrangement involving back-to-back loans or other arrangement that is economically equivalent and structured to have a similar effect. The denial of the exemption for these back-to-back loan type arrangements is directed at preventing related party and other debt from being structured through financial institutions to gain access to a withholding tax exemption. The exemption will only be denied for interest paid on the

component of a loan that is considered to be back-to-back. ***[Article 11, paragraph 4]***

1.130 A back-to-back arrangement would include, for instance, a transaction or series of transactions structured in such a way that:

- a French financial institution receives or is credited with an item of interest arising in Australia; and
- the financial institution pays or credits, directly or indirectly, all or substantially all of that interest (at any time or in any form, including commensurate benefits) to another person who, if it received the interest directly from Australia, would not be entitled to similar benefits with respect to that interest.

1.131 However, a back-to-back arrangement would generally not include a loan guarantee provided by a related party to a French financial institution.

Definition of interest

1.132 The term ***interest*** is defined for the purposes of this Article to include interest from:

- government securities;
- bonds and debentures;
- other forms of indebtedness; and
- income which is subjected to the same taxation treatment as income from money lent by the law of the Contracting State in which the income arises.

1.133 Penalty charges for late payment are specifically excluded from definition of interest, consistent with the OECD Model. This provision is unnecessary for Australian purposes because Australia's domestic law does not treat penalty charges for late payments as interest. ***[Article 11, paragraph 5]***

Interest effectively treated as business profits

1.134 Interest derived by a resident of one country which is paid in respect of an indebtedness which is effectively connected with a permanent establishment of that person in the other country, will form part of the business profits of that permanent establishment and be subject to the provisions of Article 7 (*Business Profits*). Accordingly, the rate

limitation of 10 per cent and the exemption for financial institutions do not apply to such interest in the country in which the interest is sourced. ***[Article 11, paragraph 6]***

Deemed source rules

1.135 The source rules which determine where interest arises for purposes of the Article are set out in paragraph 7. They operate to allow Australia to tax interest paid by a resident of Australia to a resident of France that is the beneficial owner of that interest. Australia may also tax interest paid by a non-resident, being interest which is beneficially owned by a French resident, if it is an expense incurred by the payer of the interest in carrying on a business in Australia through a permanent establishment.

1.136 However, consistent with Australia's interest withholding tax provisions, an Australian source is not deemed in respect of interest that is an expense incurred by an Australian resident in carrying on a business through a permanent establishment in France or outside both Australia and France (ie, the permanent establishment is in a third country). In that case, the interest is deemed to arise in the country in which the permanent establishment is situated. ***[Article 11, paragraph 7]***

1.137 In determining whether a permanent establishment exists in a third country, the principles set out in Article 5 (*Permanent Establishment*) apply.

Related persons

1.138 This Article includes a general safeguard against payments or credits of excessive interest where a special relationship exists between the persons associated with a loan transaction — by restricting the amount on which the 10 per cent source country tax rate limitation applies to an amount of interest which might have been expected to have been agreed upon if the parties to the loan agreement were dealing with one another at arm's length. Any excess part of the interest remains taxable according to the domestic law of each country but subject to the other Articles of the tax Convention. ***[Article 11, paragraph 8]***

1.139 Examples of cases where a special relationship might exist include payments to a person (either individual or legal):

- who controls the payer (whether directly or indirectly);
- who is controlled by the payer; or

- who is subordinate to a group having common interests with the payer.

1.140 It also covers relationships of blood or marriage and, in general, any community of interests.

Article 12 — Royalties

1.141 This Article allocates taxing rights in respect of royalties paid or credited between Australia and France. The Article provides that:

- a maximum 5 per cent rate of source country tax may be levied on the gross amount of the royalties;
- royalties paid in respect of a right or property which is effectively connected with a permanent establishment are subject to Article 7 (*Business Profits*);
- equipment royalties are not included within the definition of royalties and will be taxed in accordance with either Article 7 (*Business Profits*) or Article 8 (*Ships and Aircraft*);
- payments for spectrum licences are subject to Article 7 (*Business Profits*);
- royalties are deemed to have an Australian source (and may therefore be taxed in Australia) where:
  - the royalties are paid by an Australian resident to a French resident; or
  - the royalties are paid by a non-resident to a French resident and are an expense of the payer in carrying on business in Australia through a permanent establishment; and
- relief will be restricted to the gross amount of royalties which would be expected to be paid on an arm's length dealing between independent parties.

Permissible rate of source country taxation

1.142 This Article in general allows both countries to tax royalty flows but limits the tax of the country of source to 5 per cent of the gross amount of royalties beneficially owned by residents of the other country. ***[Article 12, paragraphs 1 and 2]***

1.143 In the absence of a tax treaty, Australia taxes royalties paid to non-residents at 30 per cent of the gross royalty.

1.144 The 5 per cent rate limitation does not apply to natural resource royalties, which, in accordance with Article 6 (*Income from Real Property*), remain taxable in the country of source without limitation of the tax that may be imposed.

Definition of royalties

1.145 The definition of 'royalties' in the France Convention reflects most elements of the definition in Australia's domestic income tax law. It includes payments for the supply of scientific, technical, industrial or commercial know-how but not payments for services rendered, except as provided for in subparagraph 3(c). The definition also includes payments for the use of intellectual property stored on various mediums and used in connection with television, radio or other broadcasting (eg, satellite, cable and Internet broadcasting). ***[Article 12, paragraph 3]***

1.146 Payments for the use of, or the right to use industrial, commercial or scientific equipment, which are included in the definition of royalties in the existing France treaty, are not included in the definition under the France Convention. Such payments for equipment leasing will either be treated as business profits under Article 7 (*Business Profits*) or as profits from international transport operations (for certain leases of ships and aircraft) under Article 8 (*Ships and Aircraft*). The exclusion of payments for the use of equipment from the *Royalties* Article reflects common international tax treaty practice and recognises that source country taxation on a gross basis may be excessive given low profit margins.

1.147 The definition does not include payments made for the use of spectrum licences. Rather, Article 7 (*Business Profits*) applies to such payments. ***[Protocol, item 3]***

Payments for the supply of know-how versus payments for services rendered

1.148 The OECD Model Commentary deals with the need to distinguish these two types of payments in paragraph 11.3 of the Commentary on Article 12. The Commentary cites the following criteria as relevant for the purpose of making the distinction:

- Contracts for the supply of know-how concern information of the kind described in paragraph 11 (of the Commentary) that already exists or concern the supply of that type of information after its development or creation and include

specific provisions concerning the confidentiality of that information.

- In the case of contracts for the provision of services, the supplier undertakes to perform services which may require the use, by that supplier, of special knowledge, skill and expertise but not the transfer of such special knowledge, skill or expertise to the other party.

- In most cases involving the supply of know-how, there would generally be very little more which needs to be done by the supplier under the contract other than to supply existing information or reproduce existing material. On the other hand, a contract for the performance of services would, in the majority of cases, involve a very much greater level of expenditure by the supplier in order to perform his contractual obligations. For instance, the supplier, depending on the nature of the services to be rendered, may have to incur salaries and wages for employees engaged in researching, designing, testing, drawing and other associated activities or payments to sub-contractors for the performance of similar services.

1.149 Payments for design, engineering or construction of plant or building, feasibility studies, component design and engineering services may generally be regarded as being in respect of a contract for services, unless there is some provision in the contract for imparting techniques and skills to the buyer.

1.150 In cases where both know-how and services are supplied under the same contract, if the contract does not separately provide for payments in respect of know-how and services, an apportionment of the two elements of the contract may be appropriate.

1.151 Payments for services rendered are to be treated under Article 7 (*Business Profits*).

Image or sound reproduction or transmission

1.152 The royalty definition includes payments made for the use of, or the right to use, motion picture films. It also covers payments for the use of, or the right to use images or sounds, however reproduced or transmitted, for use in connection with broadcasting. Such images or sounds may be reproduced on any form of media, such as film, tape, CD or DVD, or transmitted electronically, such as by satellite, cable or Internet. Where the images or sounds are for use in connection with any

form of broadcasting, such as television, radio or web-casting, the payments will constitute a royalty. ***[Article 12, subparagraph 3(d)]***

Forbearance

1.153 Consistent with the existing France treaty and Australian tax treaty practice, subparagraph 3(e) expressly treats as a royalty, amounts paid or credited in respect of forbearance to grant to third persons, rights to use property covered by this Article. This is designed to address arrangements along the lines of those contained in *Aktiebolaget Volvo v Federal Commissioner of Taxation* (*1978*) 8 ATR 747; 78 ATC 4316, where instead of amounts being payable for the exclusive right to use the property they were made for the undertaking that the right to use the property will not be granted to anyone else. This provision ensures that such payments are subject to tax as a royalty payment under the terms of the *Royalties* Article. ***[Article 12, subparagraph 3(e)]***

Other royalties effectively treated as business profits

1.154 As in the case of interest income, the withholding tax rate limitation does not apply to royalties paid in respect of property or rights which are effectively connected with a permanent establishment in the country in which the income is sourced. Such income is subject to full taxation under Article 7 (*Business Profits*). ***[Article 12, paragraph 4]***

Deemed source rules

1.155 The source rules which determine where royalties arise for purposes of this Article effectively correspond, in the case of Australia, with the deemed source rule contained in section 6C (Source of royalty income derived by a non-resident) of the ITAA 1936 for royalties paid to non-residents of Australia. They broadly mirror the source rule for interest income contained in paragraph 7 of Article 11 (*Interest*).

1.156 Consistent with Australia's royalty withholding tax provisions, royalty payments that are an expense incurred by an Australian resident in carrying on a business through a permanent establishment outside both Australia and France (ie, the permanent establishment is in a third country) will not be subject to tax in Australia. Those royalties are deemed to be sourced in the country in which the permanent establishment is situated. ***[Article 12, paragraph 5]***

1.157 In determining whether a permanent establishment exists in a third country, the principles set out in Article 5 (*Permanent Establishment*) apply.

Related persons

1.158 Where a special relationship exists between the payer and the beneficial owner of the royalties, the 5 per cent source country tax rate limitation will apply only to the extent that the royalties are not excessive. Any excess part of the royalty remains taxable according to the domestic law of each country but subject to the other Articles of this Convention.

1.159 Examples of special relationships have been provided in respect of the corresponding paragraph in Article 11. ***[Article 12, paragraph 6]***

Article 13 — Alienation of Property

Taxing rights

1.160 This Article allocates between the respective countries taxing rights in relation to income, profits or gains arising from the alienation of real property and other items of property.

1.161 The reference to 'income, profits or gains' in this Article is designed to put beyond doubt that a gain from the alienation of property which in Australia is income or a profit under ordinary concepts, will also be taxed in accordance with this Article, rather than Article 7 (*Business Profits*), together with relevant capital gains.

Real property

1.162 Income, profits or gains from the alienation of real property may be taxed by the country in which the property is situated. For the purpose of this Article, the term 'real property' has the same meaning as it has under paragraph 2 of Article 6. Where the property is situated is determined in accordance with paragraph 7 of Article 6 (*Income from Real Property*). ***[Article 13, paragraphs 1, 7 and 8]***

Permanent establishment

1.163 Paragraph 2 deals with income, profits or gains arising from the alienation of property (other than real property covered by paragraph 1) forming part of the business assets of a permanent establishment of an enterprise. It also applies where the permanent establishment itself (alone or with the whole enterprise) is alienated. Such income, profits or gains may be taxed in the country in which the permanent establishment is situated. This corresponds to the rules for taxation of business profits contained in Article 7 (*Business Profits*). ***[Article 13, paragraph 2]***

Disposal of ships or aircraft

1.164 Income, profits or gains derived by a resident of a country from the disposal of ships or aircraft operated by that resident in international traffic, or of associated property (other than real property covered by paragraph 1), are taxable only in that country. This rule corresponds to the operation of Article 8 (*Ships and Aircraft*) in relation to profits from the international operation of ships or aircraft. ***[Article 13, paragraph 3]***

1.165 For the purposes of this Article, the term 'international traffic' does not include any transportation which commences at a place in a country and returns to that place or another place in that country, after travelling through international airspace or waters (eg, so-called 'voyages to nowhere' by cruise ships). ***[Article 3, subparagraph 1(l)]***

Shares and other interests in land-rich entities

1.166 Paragraph 4 applies to situations involving the alienation of shares or other interests in companies, and other entities, where the value of the assets is principally attributable to the real property situated in the other country. Income, profits or gains from alienation of such shares or interests may be taxed by the country in which the real property is situated. This paragraph complements paragraph 1 of this Article and is designed to cover arrangements involving the effective alienation of incorporated real property, or like arrangements.

1.167 This provision is in line with international practice and ensures that capital gains on a non-resident's indirect, as well as direct, interests in certain targeted assets are taxable in Australia. (Such treatment applies whether the real property is held directly or indirectly through a chain of interposed entities.) While not limited to chains of companies, or even chains of entities, only some of which are companies, the example of chains of companies is used to make clear that the corporate veil should be lifted in examining direct or indirect ownership.

1.168 This provision responds to the tax planning opportunities exposed by the decision of the Full Federal Court in the *Commissioner of Taxation v Lamesa Holdings BV* (1997) 77 FCR 597. It is designed to protect Australian taxing rights over income or gains on the alienation or effective alienation of Australian real property (as defined) despite the presence of interposed bodies corporate or other entities. ***[Article 13, paragraph 4]***

Preventing double taxation of departing residents

1.169 The purpose of paragraph 5 is to prevent double taxation of capital gains of departing residents. A person who ceases to be a resident

of Australia will generally trigger a tax liability on unrealised gains from assets held, other than taxable Australian assets (gains from real property and the sale of a permanent establishment in Australia or the assets of such a permanent establishment). The departing Australian resident may elect to either pay the Australian tax at the time of departure or to defer tax on the unrealised gain until the actual disposal of the asset. A former Australian resident who has been taxed on the unrealised gains upon departure from Australia, and who becomes a French resident, may elect to be treated for French taxation purposes as having, immediately before ceasing to be a resident of Australia, alienated and reacquired the property for an amount equal to its fair market value at that time. ***[Article 13, paragraph 5]***

Example 1.3

> An Australian resident, Alison, owns a house in New Zealand which was purchased in the year 2002 for $200,000 (this is the cost base of the asset as Alison has not incurred any further expenditure which should be taken into account in determining the cost base of the asset). At the time Alison ceases to be an Australian resident, the market value of the house is $300,000. Alison will therefore have an Australian capital gains tax liability of $100,000 from the unrealised gain. Alison pays the tax on this unrealised gain rather than defers payment of the tax.
>
> Alison later sells the house for $400,000, while a resident of France. Paragraph 5 will allow Alison to elect to treat the original purchase price as $300,000 and the time of acquisition as the time immediately preceding the change of residence for French tax purposes. This will mean that Alison will not be taxed in France on the gain that accrued on the house during the period of Alison's residence in Australia. ***[Article 13, paragraph 5]***

Capital gains

1.170 This Article contains a sweep up provision which reserves the right to tax any capital gains from the alienation of other types of property to the country in which the person deriving the gains is a resident. These would include, for example, gains from the disposal of shares or other interests in an entity (other than a land-rich entity). Such gains derived by Australian residents will be taxable only in Australia, regardless of where the property is situated, and will not be taxed in France. The liability of the Australian resident to taxation on such gains will be determined in accordance with Australia's domestic law. ***[Article 13, paragraph 6]***

Article 14 — Income from Employment

Basis of taxation

1.171 This Article generally provides the basis upon which the remuneration of visiting employees is to be taxed. However this Article does not apply in respect of income that is dealt with separately in:

- Article 15 (*Directors' Fees*);
- Article 16 (*Entertainers and Sportspersons*);
- Article 17 (*Pensions and Annuities*); and
- Article 18 (*Government Service*).

1.172 Generally, remuneration derived by a resident of one country from employment exercised in the other country may be taxed in that other country. However, subject to specified conditions, there is a conventional provision for exemption from tax in the country being visited where visits of only a short-term nature are involved. ***[Article 14, paragraphs 1 and 2]***

Short-term visit exemption

1.173 The conditions for this exemption are that:

- the period of the visit or visits does not exceed, in the aggregate, 183 days in any 12-month period commencing or ending in the fiscal year of the visited country;
- the remuneration is paid by, or on behalf of, an employer who is a resident of the same country as the employee; and
- the remuneration is not borne by a permanent establishment which the employer has in the country being visited.

1.174 Where all of these conditions are met, the remuneration so derived will be liable to tax only in the country of residence of the recipient. ***[Article 14, paragraph 2]***

1.175 Where a short-term visit exemption is not applicable, remuneration derived by a resident of Australia from employment in France may be taxed in France. However, this Article does not allocate sole taxing rights to France in that situation. ***[Article 14, paragraph 1]***

1.176 Accordingly, Australia would also be entitled to tax that remuneration in accordance with the general rule of the ITAA 1997 that a resident of Australia remains subject to tax on worldwide income. However, in accordance with Article 23 (*Elimination of Double Taxation*) Australia would in this situation be required to relieve the double taxation.

1.177 Although Article 23 provides for the double tax relief to be provided by Australia to be in the form of the grant of a credit against the Australian tax for the French tax paid, the 'exemption with progression' method of providing double tax relief in relation to employment income derived in the situation described would normally be applicable in practice pursuant to the foreign service income provisions of section 23AG of the ITAA 1936. This method exempts the income from foreign employment from tax in Australia, but takes into account the foreign earnings when calculating the Australian tax on other assessable income the person has derived.

Employment on a ship or aircraft

1.178 Income from an employment exercised aboard a ship or aircraft operated in international traffic may be taxed in the country of which the enterprise operating the ship or aircraft is a resident. ***[Article 14, paragraph 3]***

1.179 For the purposes of this Article, the term 'international traffic' does not include any transportation which commences at a place in a country and returns to that place or another place in that country, notwithstanding that the vessel travels through international waters (eg, so-called 'voyages to nowhere' by cruise ships). ***[Article 3, subparagraph 1(l)]***

Article 15 — Directors' Fees

1.180 This Article relates to remuneration received by a resident of one country in the person's capacity as a director of a company which is a resident of the other country. To avoid potential practical difficulties in such cases of ascertaining in which country a director's services are performed, and consequently where the remuneration is to be taxed, the Article provides that directors' fees and similar payments may be taxed in the country of residence of the company. ***[Article 15]***

Article 16 — Entertainers and Sportspersons

Personal activities

1.181 Under this Article, income derived by visiting entertainers and sportspersons from their personal activities as such may be taxed in the

country in which the activities are exercised, irrespective of the duration of the visit. The term 'entertainer' is intended to have a broad meaning and would include, for example, actors and musicians as well as other performers whose activities have an entertainment character, such as comedians, talk-show hosts, participants in chess tournaments or racing drivers. The application of this Article extends to income generated from promotional and associated kinds of activities engaged in by the entertainer or sportsperson while present in the visited country. ***[Article 16, paragraph 1]***

Safeguard

1.182 Paragraph 2 is designed to ensure that income in respect of personal activities exercised by an entertainer or sportsperson, where derived by another person (eg, a separate enterprise which formally provides the entertainer's or sportsperson's services), may be taxed in the country in which the entertainer or sportsperson performs, whether or not that other person has a permanent establishment in that country. ***[Article 16, paragraph 2]***

Article 17 — Pensions and Annuities

1.183 Pensions (not including government pensions) and annuities (the term 'annuity' as used in this Article is defined in paragraph 2) are taxable only by the country of which the recipient is a resident. The application of this Article extends to pensions and annuity payments made to dependants, for example, a widow, widower or children of the person in respect of whom the pension or annuity entitlement accrued where, upon that person's death, such entitlement has passed to that person's dependants. ***[Article 17, paragraphs 1 and 2]***

War service pensions

1.184 Paragraph 3 reflects the intended operation of paragraph 3 of Article 17 of the existing France treaty, and ensures that any pension or allowance paid by a country in respect of war service, or in respect of wounds, disabilities or death caused by war, that is exempt from tax in that country will also be exempt in the other country. ***[Article 17, paragraph 3]***

Eligible termination payments

1.185 Lump sum payments on the termination of employment are not considered to be pensions and are not covered by this Article. Article 20 (*Other Income*) applies to such payments.

Contributions to foreign pension schemes

1.186 Paragraph 4 of this Article broadly continues the treatment provided under paragraph 5 of Article 17 of the existing France treaty. It provides that each country is required to treat contributions of a resident employee to a pension scheme in the other country in the same way as contributions made to a recognised pension scheme are treated. However, this provision will only apply where:

- immediately before commencing employment activities in the country, the individual was not a resident of that country, and was participating in the foreign pension scheme; and
- the pension scheme is accepted by the competent authority of that country as generally corresponding to a recognised pension scheme for tax purposes.

[Article 17, subparagraph 4(a)]

1.187 The term 'pension scheme', for the purposes of subparagraph 4(a), means an arrangement in which the individual participates in order to secure retirement benefits payable in respect of the relevant employment services. A pension scheme is recognised for tax purposes in a country if the contributions to the scheme would qualify for tax relief in that country. ***[Article 17, subparagraph 4(b)]***

1.188 Paragraph 4 has little operation in Australia, since employee contributions to pension schemes generally do not qualify for tax relief in Australia. The provision does not extend to contributions on behalf of employees, such as employer contributions, or to contributions by self-employed individuals.

Article 18 — Government Service

Salary and wage income

1.189 Salary and wage type income, other than government service pensions or annuities, paid to an individual for services rendered to a government (including a political subdivision, statutory body or local authority) of one of the countries, is to be taxed only in that country. However, such remuneration will be taxable only in the other country if:

- the services are rendered in that other country; and

- the recipient is a resident of, and a national or citizen of, that other country, and is not also a national or citizen of the paying country.

1.190 The term 'statutory body' is not defined in the France Convention. In Australia, a statutory body would include an entity incorporated for public purposes by a law of Australia, as well as an entity which is entrusted by a law of Australia with functions to be performed in the public interest or for a public purpose. ***[Article 18, paragraph 1]***

Government pensions

1.191 Any pension paid by, or out of funds created by, a government (including a political subdivision, statutory body or local authority) of one of the countries to an individual in respect of services rendered to that government, is to be taxed only in that country. However, such pension will be taxable only in the other country if the individual is a resident of, and a national or citizen of, that other country and is not also a national or citizen of the first mentioned country. ***[Article 18, paragraph 2]***

Business income

1.192 Remuneration or pensions paid in respect of services rendered in connection with a trade or business carried on by any governmental authority referred to in paragraph 1 or 2 of this Article is excluded from the scope of the Article. Such remuneration will remain subject to the provisions of Article 14 (*Income from Employment*), Article 15 (*Directors' Fees*), Article 16 (*Entertainers and Sportspersons*) or Article 17 (*Pensions and Annuities*). ***[Article 18, paragraph 3]***

1.193 Where a statutory body of a country carries on activities that are not primarily supported by public funds of that country (including public funds of its political subdivisions or local authorities), such activities will be regarded as business activities of that body for purposes of this Article. Salaries, wages, pensions etc paid in respect of services rendered in connection with such activities are excluded from the scope of the Article. ***[Protocol, item 4]***

Article 19 — Students

Exemption from tax

1.194 This Article applies to students who are temporarily present in one of the countries solely for the purpose of their education if the students are, or immediately before the visit were, resident in the other country. In these circumstances, payments from abroad received by the

students solely for their maintenance or education will be exempt from tax in the country visited. This will apply even though the student may qualify for tax purposes as a resident of the country visited during the period of their visit.

1.195 The exemption from tax provided by the visited country is treated as extending to payments received by the student for the maintenance of dependent family members who have accompanied the student to the visited country.

Employment income

1.196 Where, however, a student from France who is visiting Australia solely for educational purposes undertakes any employment in Australia, for example:

- undertakes some part-time work with a local employer; or
- during a semester break undertakes work with a local employer,

the income earned by that student as a consequence of that employment may, as provided for in Article 14 (*Income from Employment*), be subject to tax in Australia. In this situation, the payments received from abroad for the student's maintenance or education will not, however, be taken into account in determining the tax payable on the employment income that is subject to tax in Australia. No Australian tax would be payable on the employment income if the student qualifies as a resident of Australia during the visit and the taxable income of the student (excluding maintenance payments received from abroad) does not exceed the tax-free threshold applicable to Australian residents for income tax purposes.

Article 20 — Other Income

Allocation of taxing rights

1.197 This Article provides rules for the allocation between the two countries of taxing rights with respect to items of income not dealt with in the preceding Articles of the France Convention. The scope of the Article is not confined to such items of income arising in one of the countries — it extends also to income from sources in a third country.

1.198 Broadly, such income derived by a resident of one country is to be taxed only in the country of residence unless it is from sources in the other country, in which case the income may also be taxed in the other

country. This is consistent with Australia's reservation to Article 21 (*Other Income*) of the OECD Model. ***[Article 20, paragraphs 1 and 3]***

1.199 Where the income may be taxed in both countries in accordance with this provision, the country of residence of the recipient of the income is obliged by Article 23 (*Elimination of Double Taxation*) to provide double taxation relief.

1.200 This Article does not apply to income (other than income from real property as defined in paragraph 2 of Article 6 (*Income from Real Property*)) where the right or property in respect of which the income is paid is effectively connected with a permanent establishment which a resident of one country has in the other country. In such a case, Article 7 (*Business Profits*) will apply. ***[Article 20, paragraph 2]***

Article 21 — Source of Income

Deemed source

1.201 This Article effectively deems income, profits or gains derived by a resident of a country which, in accordance with the France Convention, may be taxed in the other country, to have a source in that other country. It therefore avoids any difficulties arising under domestic law source rules in respect of the exercise by Australia of the taxing rights allocated to Australia by the France Convention over income or gains derived by residents of France. ***[Article 21, paragraph 1]***

1.202 Paragraph 2 has a broadly similar purpose as that of paragraph 1 of this Article. Like the corresponding provision in the existing France treaty, paragraph 2 deems profits which are included as profits of an enterprise of a country under paragraph 1 of Article 9 (*Associated Enterprises*) to be income of that enterprise derived from sources in that country for the purposes of taxation of the enterprise. ***[Article 21, paragraph 2]***

Source of income — double taxation relief

1.203 Paragraph 3 of this Article deems income, profits or gains of a resident of one country to arise in the other country if those amounts are taxable in the other country under the treaty. The paragraph applies for the purposes of Article 23 (*Elimination of Double Taxation*) and for the purposes of the domestic tax laws of the country in which the recipient of the income is resident. ***[Article 21, paragraph 3]***

1.204 This provision is variously included in a specific *Source of Income* Article, such as Article 21 of this treaty, or in the *Elimination of Double Taxation* Article of Australia's tax treaties. It is intended to

ensure that where an item of income, profit or gain is taxable in both countries, double taxation relief will be given by the recipient's country of residence in accordance with Article 23, regardless of whether the amount may be regarded as having a source in the country of residence under its ordinary source rules. In this way, income, profits or gains derived by a resident of Australia, which is taxable by France under this Convention, will be treated as foreign income for the purposes of the ITAA 1936 and the ITAA 1997, including the foreign tax credit provisions of the ITAA 1936. ***[Article 21, paragraph 3]***

Article 22 — Rules of Taxation

1.205 This Article, like its counterpart in the existing France treaty, is complementary to the provisions of Article 9 (*Associated Enterprises*) of the treaty which apply where related enterprises are not dealing on an arm's length basis. Paragraph 2 of Article 9 allows recourse to relevant domestic laws only if the information available to the competent authority of a Contracting State is inadequate to determine properly attributable profits. This Article permits a wider recourse to the domestic law in other cases of non-arm's length dealings.

1.206 This Article operates so that nothing in the treaty prevents either country from applying its domestic law to tax residents of Australia or France on those profits which might otherwise have been expected to have accrued to the resident had the transaction between the Australian resident and the French resident been conducted at arm's length. ***[Article 22]***

Article 23 — Elimination of Double Taxation

1.207 Double taxation does not arise in respect of income flowing between Australia and France:

- where the terms of the tax treaty provide for the income to be taxed only in one country; or
- where the domestic taxation law of one of the countries exempts the income from its tax.

1.208 It is necessary, however, to prescribe a method for relieving double taxation for other classes of income which, under the terms of the tax treaty, remain subject to tax in both countries. In accordance with international practice, Australia's tax treaties provide for double tax relief to be provided by the country of residence of the taxpayer by way of a credit basis of relief against its tax for the tax of the country of source. This Article also reflects that approach.

Australian method of relief

1.209 This Article requires Australia to provide Australian residents a credit against their Australian tax liability for French tax paid in accordance with the France Convention on income derived from French sources which are taxable in Australia. The term 'income' in this context is intended to have a broad meaning and includes items of profit or gains which are dealt with under the income tax law. ***[Article 23, paragraph 1]***

1.210 Australia's general foreign tax credit system, together with the terms of this Article and of the France Convention generally, will form the basis of Australia's arrangements for relieving a resident of France from double taxation on income or gains arising from sources in France.

1.211 Accordingly, effect is to be given to the tax credit relief obligation imposed on Australia by paragraph 1 of this Article by application of the general foreign tax credit provisions (Division 18 of Part III) of the ITAA 1936.

1.212 Notwithstanding the credit basis of relief provided for by paragraph 1 of this Article in relation to salary and wages and like remuneration derived by a resident of Australia during a continuous period of foreign service (as defined in subsection 23AG(7) of the ITAA 1936) in France, the exemption with progression method of relief will be applicable.

1.213 Dividends and branch profits derived from France by an Australian resident company that are exempt from Australian tax under the foreign source income measures (eg, sections 23AH and 23AJ of the ITAA 1936) will continue to qualify for exemption from Australian tax under those provisions. As double taxation does not arise in these cases, the credit form of relief will not be relevant.

French relief

1.214 In the case of a resident of France who is taxed in France on income which is taxable in Australia under this Convention, this Article requires France to allow the French resident a credit, rather than a deduction, against the French tax.

1.215 The amount of the tax credit will depend on the type of income. In the case of income other than that listed below, the tax credit will be equal to the amount of the French tax attributable to such income. This provision will only apply in relation to income that has been subjected to Australian tax. In effect, no French tax will be payable on such income. ***[Article 23, sub-subparagraph 2(a)(i)]***

1.216 The amount of the tax credit in the case of income listed below will be equal to the amount of tax paid in Australia in accordance with this Convention. However, the amount of the tax credit shall not exceed the amount of French tax attributable to that income. The income to which this tax credit applies is income referred to in the following provisions of this Convention:

- Article 7 (*Business Profits*) and paragraph 2 of Article 13 (*Alienation of Property*), in relation to income that is subject to the corporation tax;
- Article 10 (*Dividends*);
- Article 11 (*Interest*);
- Article 12 (*Royalties*);
- paragraph 1 of Article 13 (*Alienation of Property*);
- paragraph 3 of Article 14 (*Income from Employment*);
- Article 15 (*Directors' Fees*);
- Article 16 (*Entertainers and Sportspersons*); and
- Article 20 (*Other Income*).

[Article 22, sub-subparagraph 2(a)(ii)]

1.217 As France generally operates a territorial tax system corporation tax arises on foreign source profits only in circumstances where a group of French resident companies elect to include in their assessable income the profits from their foreign operations. In these circumstances business profits will be subject to the corporation tax and a credit will only be allowed for the amount of Australian tax paid by the permanent establishment in Australia of a member of the group of companies.

1.218 The term ***the amount of French tax attributable to such income***, as used in paragraph 2 of this Article, means:

- where the tax on that income is calculated by applying a proportional rate, the amount of the net income multiplied by the rate which actually applies to that income; and
- where the tax on that income is calculated by applying a progressive scale, the amount of the net income multiplied by the rate resulting from the ratio of tax actually payable on the

total net income taxable in accordance with French law to the amount of that total net income.

Article 24 — Mutual Agreement Procedure

Consultation on specific cases

1.219 This Article provides for consultation between the competent authorities of the two countries with a view to reaching a solution in cases where a person is able to demonstrate actual or potential imposition of taxation contrary to the provisions of the France Convention. ***[Article 24, paragraph 2]***

1.220 A person wishing to use this procedure may present a case to the competent authority of the country of which the person is a resident. Presentation of a case by a person to a competent authority does not deprive them of access to, or affect their rights in relation to, other legal remedies available under the domestic laws of the countries. ***[Article 24, paragraph 1]***

1.221 If the person's claim seems to the competent authority to which a case has been presented to be justified, and that competent authority is not itself able to solve the problem, then the competent authority is required to seek to resolve the case by mutual agreement with the competent authority of the other country, with a view to avoiding taxation not in accordance with the Convention. ***[Article 24, paragraph 2]***

1.222 If, after consideration by the competent authorities, a solution is reached, it shall be implemented in accordance with the provisions of the Article.

Time limits

Presentation of the case

1.223 A taxpayer seeking to use this procedure must present the case to the competent authority of the country in which the taxpayer is a resident within three years from the first notification of the action resulting in taxation not in accordance with the provisions of the treaty. This time limit overrides any time limits that may operate under the domestic law of the country. ***[Article 24, paragraph 1]***

Implementation of a solution

1.224 The solution reached by mutual agreement between the competent authorities of the relevant countries shall be implemented notwithstanding any time limits in the domestic laws of the tax

Convention countries. This allows the competent authorities the flexibility to reach a satisfactory solution and avoids problems that might arise where each country has a different time limit in their domestic law. ***[Article 24, paragraph 2]***

Consultation on general problems

1.225 This Article also authorises consultation between the competent authorities of the two countries for the purpose of resolving any difficulties that arise regarding the interpretation or application of the Convention and to give effect to it. This may allow, for example, the competent authorities to agree to apply an agreed solution to a broader range of taxpayers, notwithstanding that the original uncertainty may have arisen in connection with an individual case that comes under the procedure outlined in paragraphs 1 and 2 of this Article.

1.226 This Article specifically allows the competent authorities to consult with the aim of agreeing to the same allocation of income between associated enterprises mentioned in Article 9 (*Associated Enterprises*). This additional sentence (which is not included in most of Australia's treaties) is included merely for increased clarity and is not intended to suggest that such consultation would not be permitted under the mutual agreement procedure in the absence of such specification.

1.227 Paragraph 3 of this Article also enables the competent authorities to deal with cases of double taxation that do not come within the scope of the France Convention. ***[Article 24, paragraph 3]***

Methods of communication between competent authorities

1.228 The competent authorities are permitted to communicate directly with each other without having to go through diplomatic channels. This may be done by letter, facsimile transmission, telephone, direct meetings or any other convenient means. ***[Article 24, paragraph 4]***

General Agreement on Trade in Services (GATS) dispute resolution process

1.229 Paragraph 5 of this Article deals with disputes that may be brought before the World Trade Organisation Council for Trade in Services under the dispute resolution processes of the GATS. ***[Article 24, paragraph 5]***

Background

1.230 Australia and France are both parties to the GATS. Article XVII (*National Treatment*) of the GATS requires a party to accord the same

treatment to services and service suppliers of other parties as it accords to its own like services and service suppliers.

1.231 Articles XXII (*Consultation*) and XXIII (*Dispute Settlement and Enforcement*) of the GATS provide for discussion and resolution of disputes. Where a measure of another party falls within the scope of a tax treaty, paragraph 3 of Article XXII (*Consultation*) provides that the other party to the tax treaty may not invoke Article XVII (*National Treatment*). However, if there is a dispute as to whether a measure actually falls within the scope of a tax treaty, either country may take the matter to the Council on Trade in Services for referral to binding arbitration.

1.232 Notwithstanding paragraph 3 of Article XXII (*Consultation*) of the GATS, Australia and France have agreed that the consent of both countries is required before a dispute as to whether a measure falls within the scope of this Convention may be brought before the Council on Trade in Services. This is seen as the most effective way of dealing with such disputes, and avoids difficult questions as to when a disputed issue falls within the dispute resolution mechanism of this Convention or of the GATS dispute.

1.233 This provision is based, in all essential respects, on an OECD Model Commentary recommendation, and is common in recent international treaty practice. ***[Article 24, paragraph 5]***

Article 25 — Exchange of Information

1.234 The France Convention aligns the information exchange provisions to the 2005 OECD standard. The Article differs from the previous approach in the following ways:

- the scope is expanded to a wider range of taxes;
- the new provision clarifies that the Commissioner is obliged to obtain information for French tax authorities regardless of whether Australia has a domestic tax interest in the information sought; and
- bank secrecy laws do not limit the exchange of information.

Foreseeably relevant information

1.235 Article 25 authorises and limits the exchange of information by the two competent authorities to information foreseeably relevant to the administration or enforcement of the relevant taxes. The exchange of information is not restricted by Article 1 (*Persons Covered*) of the

Convention, and may therefore cover persons who are not residents of Australia or France.

1.236 The standard of foreseeable relevance is intended to ensure that information may be exchanged to the widest possible extent. However, competent authorities are not entitled to request information from the other country which is unlikely to be relevant to the tax affairs of a taxpayer, or to the administration and enforcement of tax laws. ***[Article 25, paragraph 1]***

1.237 The change in wording from that used in the corresponding Article of the existing France treaty to a 'foreseeably relevant' standard reflects the wording in Article 26 of the OECD Model and no difference in effect is intended.

Taxes to which this Article applies

1.238 Under the corresponding Article in the existing France treaty, the information that could be requested and obtained between the two countries was limited to information in relation to taxes to which the treaty applied (generally income taxes).

1.239 Under this Convention, the range of taxes for which information may be exchanged has been expanded. The Australian competent authority can now request and obtain information concerning all federal taxes administered by the Commissioner from their counterpart in France. This means, for example, that information concerning Australian indirect taxes (ie, the GST) may be requested and obtained from France.

1.240 Similarly, in the case of France, the French competent authority can now request and obtain information concerning taxes of every kind and description imposed under its tax laws, from the Australian competent authority to the extent that the requested information relates to taxes administered by the Commissioner.

Use of exchanged information

1.241 The purposes for which the exchanged information may be used and the persons to whom it may be disclosed are restricted consistent with the former Article and the approach taken in the OECD Model. Any information received by a country must be treated as secret in the same manner as information obtained under the domestic law of that country and can only be disclosed to the persons identified in paragraph 2 of the Article. ***[Article 25, paragraph 2]***

No domestic tax interest required

1.242 When requested, a country is required to obtain information in the same manner as if it were administering its domestic tax system, notwithstanding that the country may not require the information for its own purposes. Australia would recognise this obligation to obtain relevant information for treaty partner countries, even in the absence of an explicit provision to this effect. ***[Article 25, paragraph 4]***

Limitations

1.243 The country requested to provide information under this Article is not required to do so where:

- it would be required to carry out administrative procedures incompatible with its own law or the domestic law and administrative practice, of either Australia or France; or
- such information is not obtainable under the domestic law or in the normal course of administration by the competent authority in either Australia or France. Australia is not obliged, for example, to use police powers to obtain information requested by France, although information gathered in that way which is already in the possession of the Commissioner may be exchanged.

[Article 25, subparagraphs 3(a) and (b)]

1.244 Also, in no case is the country receiving the request obliged to supply information under this Article that would:

- disclose any trade, business, industrial, commercial or professional secret or trade process; or
- be contrary to public policy.

[Article 25, subparagraph 3(c)]

Information held by banks, other financial institutions, nominees etc

1.245 This paragraph ensures that paragraph 3 of this Article cannot be used to prevent the supply of information solely because the information is held by banks, other financial institutions, nominees etc. The inclusion of this paragraph in the France Convention should not be interpreted as suggesting the corresponding Article of the existing France treaty did not cover the exchange of such information. Inclusion of paragraph 5 merely clarifies Australia's current treaty practice, and reflects recent changes to

Article 26 (*Exchange of Information*) of the OECD Model. ***[Article 25, paragraph 5]***

Article 26 — Assistance in Recovery

Assistance in the collection of taxes

1.246 Article 26 (*Assistance in Recovery*) authorises and requires Australia and France to provide assistance to each other in the collection of revenue claims. This assistance is not to be restricted by the terms of Article 1 (*Personal Scope*) of the treaty. Assistance must therefore be provided as regards a revenue claim owed to either country by any person, whether or not a resident of Australia or France. The form of the assistance is set out in paragraphs 3 and 4 of this Article. ***[Article 26, paragraph 1]***

1.247 The term ***revenue claim*** is defined for the purposes of this Article to mean an amount owed in respect of taxes referred to in Article 2 (*Taxes Covered*) of the treaty. A revenue claim may cover any French tax, or any Australian federal tax administered by the Commissioner, but only insofar as the imposition of such taxes is not contrary to this treaty or any other instrument in force between Australia and France. It also applies to interest, administrative penalties and costs of collection or conservancy related to such amount. ***[Article 26, paragraph 2]***

1.248 This Article will apply from the date agreed in an exchange of notes through the diplomatic channel. ***[Article 30, subparagraph 1(d)]***

Enforceable revenue claims

1.249 Assistance in collection will only be provided by Australia in relation to a revenue claim that is enforceable in France. Similarly, France is not required to provide assistance in collection in respect of an Australian revenue claim that is not enforceable in Australia. A revenue claim will be enforceable where the requesting country has the right, under its domestic law, to collect the revenue claim. Further, the revenue claim must be owed by a person who, at that time, under the law of that country, has no administrative or judicial rights to prevent its collection.

1.250 Paragraph 3 of this Article regulates the way in which the revenue claim of the requesting country is to be collected by the requested country. Other than in relation to time limits and priority (see paragraphs 1.254 and 1.255), the requested country is required to collect the revenue claim as though it were its own revenue claim. This obligation applies even if, at that time, the requested country has no need to undertake collection actions related to that taxpayer for its own tax purposes. ***[Article 26, paragraph 3]***

1.251 Where a request from France concerns a tax that does not exist in Australia, Australia will follow the procedure applicable to a claim for a similar Australian tax or any other appropriate procedure if no similar tax exists.

Measures of conservancy

1.252 Paragraph 4 of this Article enables Australia or France to request the other country to take measures of conservancy even where it cannot yet ask for assistance in collection, such as where the revenue claim is not yet enforceable or when the debtor still has the right to prevent its collection. An example of a conservancy measure is the seizure or the freezing of assets before final judgment to guarantee that the assets will still be available when collection can subsequently take place.

1.253 If requested to do so by France, Australia is required to take measures of conservancy in respect of the revenue claim in accordance with the provisions of Australian law as if the revenue claim were an Australian revenue claim. Although Australia does not have specific conservancy measures, the Commissioner may apply for a *Mareva* injunction, which would prevent the taxpayer and the taxpayer's associates from dealing with certain assets. ***[Article 26, paragraph 4]***

Time limits

1.254 Paragraph 5 of this Article provides that the requested country's domestic law time limitations beyond which a revenue claim cannot be enforced or collected do not apply to a revenue claim in respect of which the other country has made a request for assistance in collection. Rather, the time limits of the requesting country apply. ***[Article 26, paragraph 5]***

Priority of claims

1.255 Paragraph 5 of this Article also provides that any rules of Australia and France which give priority to tax debts over the claims of other creditors do not apply to a revenue claim of the other country. This restriction applies regardless of the fact that the requested country must generally treat the claim as its own revenue claim.

1.256 The words 'by reason of its nature as such' in paragraph 5 indicate that any time limits and priority rules to which the paragraph applies are only those that are specific to unpaid taxes. Consequently, paragraph 5 does not prevent the application of general rules concerning time limits or priority which would apply to all debts, such as rules giving priority to a claim by reason of that claim having arisen or having been registered before another one. ***[Article 26, paragraph 5]***

Restriction on judicial and administrative proceedings

1.257 Paragraph 6 of this Article ensures that any legal or administrative objection concerning the existence, validity or the amount of a revenue claim of the requesting country is to be exclusively dealt with in that country. For example, no legal or administrative proceedings, such as a request for judicial review, may be initiated in Australia with respect to the existence, validity or amount of a French revenue claim. ***[Article 26, paragraph 6]***

Change in circumstances

1.258 Paragraph 7 of this Article deals with the situation where the conditions in paragraph 3 or 4 are no longer satisfied after a request for assistance has been made, but before the revenue claim has been collected and remitted by the requested country. An example of such a situation would be where a request for assistance in collection has been made by France, but the revenue claim ceases to be enforceable in France prior to its collection by Australia.

1.259 Where the relevant conditions in paragraph 3 or 4 of this Article are no longer satisfied, paragraph 7 requires the competent authority of the requesting country to promptly notify the competent authority of the requested country of that fact.

1.260 Following such notification, the requested country has the option to ask the requesting country to either suspend or withdraw its request for assistance. If the request is suspended, the suspension applies until such time as the requesting country informs the other country that the conditions necessary for making a request as regards the revenue claim are again satisfied or that it withdraws its request. ***[Article 26, paragraph 7]***

Limitations

1.261 Paragraph 8 of this Article contains certain limitations to the obligations imposed on the country which receives a request for assistance. The requested country is permitted to refuse the request for assistance where those limitations apply.

1.262 The first limitation is that the requested country is not required to exceed the bounds of its own domestic laws and administrative practice or those of the other country in fulfilling its obligations under the Article. ***[Article 26, subparagraph 8(a)]***

1.263 However, subparagraph 8(a) of this Article does not prevent Australia from applying administrative measures to collect a French

revenue claim, even though invoked solely to provide assistance in the collection of French taxes.

1.264 Subparagraph 8(b) limits the application of this Article where it would require the carrying out of measures that are contrary to public policy, such as where providing assistance may affect the vital interests of the country itself. ***[Article 26, subparagraph 8(b)]***

1.265 The third limitation provides that neither country is obliged to satisfy a request for assistance if the other country has not pursued all reasonable measures of collection or conservancy that are available under its own laws or administrative practice. ***[Article 26, subparagraph 8(c)]***

1.266 Under subparagraph 8(d) of this Article either country may reject a request for assistance on the basis of practical administrative considerations such as when the costs of recovering a revenue claim would exceed the amount of the revenue claim itself. ***[Article 26, subparagraph 8(d)]***

1.267 The final limitation allows either country to refuse to provide assistance if it considers that the taxes with respect to which assistance is requested are imposed contrary to generally accepted taxation principles. ***[Article 26, subparagraph 8(e)]***

Article 27 — Diplomatic and Consular Privileges

1.268 The purpose of this Article is to ensure that the provisions of the tax treaty do not result in members of diplomatic missions, permanent missions and consular posts receiving less favourable treatment than that to which they are entitled in accordance with international conventions. Such persons are entitled, for example, to certain fiscal privileges under the *Diplomatic Privileges and Immunities Act 1967* and the *Consular Privileges and Immunities Act 1972* which reflect Australia's international diplomatic and consular obligations. ***[Article 27, paragraph 1]***

1.269 Paragraph 2 of this Article ensures that international organisations, and organs or officials of such organisations, who are liable to tax in Australia and France only to the extent income is sourced in those jurisdictions, shall not benefit from this Convention. Further, members of a diplomatic mission or consular post of a country other than Australia or France, who are located in Australia or France are only entitled to the benefits of this treaty if they are treated in the same way as residents of either Australia or France for income taxation purposes, that is, they are generally taxable on their worldwide income. ***[Article 27, paragraph 2]***

Article 28 — Miscellaneous

1.270 This Article will operate to ensure that Australian citizens who reside temporarily in France will not be subject to the French capital tax (*l'impôt de solidarité sur la fortune*) on property that is situated outside France.

1.271 Property located outside France that the individual owns on 1 January in each of the five calendar years following that in which the individual becomes a resident of France will not be included in the basis on which the capital tax in France is calculated.

1.272 Where that individual ceases to be a resident of France for a period of at least three years, they will be entitled to claim the benefit of the exemption under this Article for a further five years in relation to property the individual owns that is situated outside France.

1.273 This provision will not apply to Australian citizens who are also French nationals. ***[Article 28]***

Example 1.4

> Ken, an Australian citizen, moves to France to live and work for a period of four years. During that time, Ken owns real property in Sydney that he purchased prior to moving to France. As Ken is not a French national, and is a French resident for less than five years, he will not be subject to French capital tax in respect of his real property in Sydney.

Article 29 — Partnerships

1.274 The purpose of this Article is to ensure that Australian and French resident partners of certain partnerships are entitled to receive benefits under the France Convention. The Article is included in the France Convention in response to France's Observation on the OECD Model Commentary on Article 1 (*Persons Covered*) which notes that France would not consider members of a partnership that is treated as fiscally transparent as being entitled to treaty benefits in the absence of specific provisions in the treaty to that effect.

1.275 This Article complements paragraph 5 of Article 4 (*Residence*) in which the term ***resident of a Contracting State*** is deemed to include any partnership or group of persons that has its place of effective management in France and all its members are personally liable to tax pursuant to the French domestic laws in respect of their share of the profits of that partnership or group of persons.

1.276 Article 1 (*Persons Covered*) provides that only persons who are residents of Australia or France are entitled to the benefits of the France Convention. The fact that certain partnerships are to be treated as residents of France means that partners in those partnerships may no longer be entitled to the benefits of the tax Convention in relation to their share of the income, profits or gains of the partnerships as they will be treated as deriving those amounts indirectly through the partnership.

Australian partnerships

1.277 Paragraph 1 of this Article deals with partnerships or similar entities that have their place of effective management in Australia and that are treated as fiscally transparent in Australia (ie, partnerships other than corporate limited partnerships).

1.278 The paragraph operates to ensure that an Australian resident partner of an Australian partnership is entitled to benefits under the France Convention relating to the partner's share of income, profits or gains of the partnership arising in France, such as lower rates of withholding tax. This is achieved by treating the partner's share of the partnership's income, profits or gains arising in France as though the partner had derived such amounts directly. France would not do this in the absence of this provision, that is, France would not treat the partnership as being transparent. ***[Article 29, subparagraph 1(a)]***

1.279 A partner of the Australian partnership who is a resident of France is also entitled to tax treaty benefits in relation to the partner's share of the partnership's income, profits or gains arising in Australia as though the partner had derived such amounts directly. Thus withholding tax limits in the France Convention will apply to a French resident partner. ***[Article 29, sub-subparagraph 1(b)(i)]***

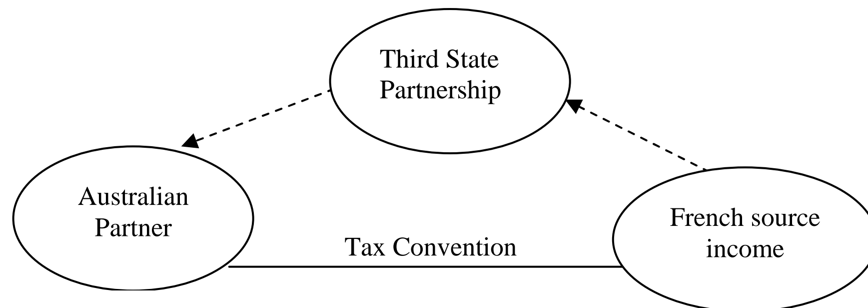
1.280 This same treatment of the French partner extends to income, profits or gains arising in France. However, where such amounts are taxed in Australia, they will be deemed to have an Australian source for the purposes of paragraph 2 of Article 23 (*Elimination of Double Taxation*). This provision is largely unnecessary given that Australia only taxes the non-resident partners in a partnership based on their share of the partnership profits from sources in Australia. It would, however, apply to income, profits or gains arising in France but attributable to a permanent establishment of the French partner in Australia. ***[Article 29, sub-subparagraph 1(b)(ii)]***

Third country partnerships

1.281 Paragraph 2 of this Article operates to ensure that an Australian or French resident who is a partner in a partnership that has its place of

effective management in a country other than Australia or France receives benefits under this tax treaty on their share of the partnership income, profits or gains arising in Australia or France. The partner may receive such treatment where the partnership is treated as fiscally transparent in the third country and where the partner's country of residence treats the partner's share of the income, profits or gains of the partnership as though those amounts had been derived directly by the partner.

Diagram 1.1



1.282 The partner's entitlement to tax treaty benefits relating to their share of the income, profits or gains of the third country partnership is subject to the following conditions:

- there are not contrary provisions in a tax treaty between either Australia or France and the third country;
- the partner's share of the income, profits or gains of the partnership is taxed in the same manner (including the nature or source of those amounts and the time when those amounts are taxed) as it would be taxed had those amounts been derived by the partner directly; and
- information relating to the partnership or partners may be exchanged between the country where the income arises (either Australia or France) and the third country under a tax treaty between the relevant countries.

[Article 29, paragraph 2]

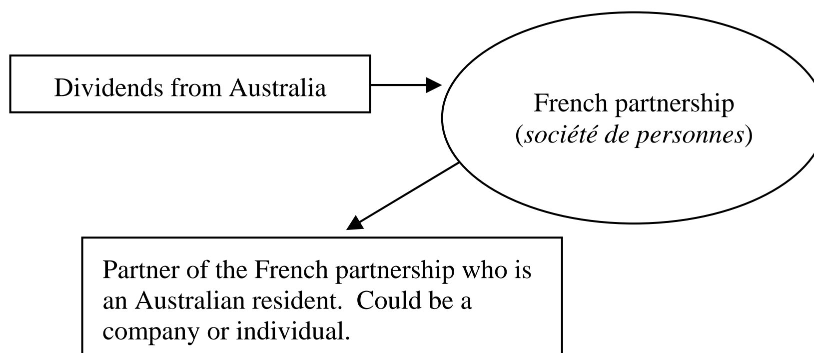
1.283 Paragraph 3 of this Article makes clear that a partner's share of the income, profits or gains which are attributable to a permanent establishment of the partnership may be taxed in the country in which the permanent establishment is situated. This is achieved by deeming that those amounts have a source in the country in which the permanent establishment is situated. This provision allows France to treat income attributable to the permanent establishment of a transparent Australian or third State partnership as arising in France for the purpose of taxing the

partners under paragraphs 1 and 2. This could include Australian and third State sourced profits where they are attributable to the partnership's French permanent establishment. ***[Article 29, paragraph 3]***

1.284 Paragraph 4 of this Article seeks to address possible implications of the decision in *Padmore v Inland Revenue Commissioners* (1989) Simon's Tax Cases 493 by ensuring that Australia is not prevented from taxing an Australian resident partner on their share of the income, profits or gains of a partnership which is treated as a resident of France under the treaty.

1.285 Paragraph 4 clarifies that where a partnership or other group of persons is subject to tax as a resident of France and income, profits or gains of that partnership are relieved from tax in Australia under the treaty, Australia may nevertheless tax any Australian resident partner on their share of the partnership income, profits or gains. However, Australia, as the country of residence of the partner, is required under Article 23 (*Elimination of Double Taxation*) to provide relief for tax imposed on those amounts in France. For this purpose, the income, profits or gains are deemed to have a source in France. ***[Article 29, paragraph 4]***

Diagram 1.2

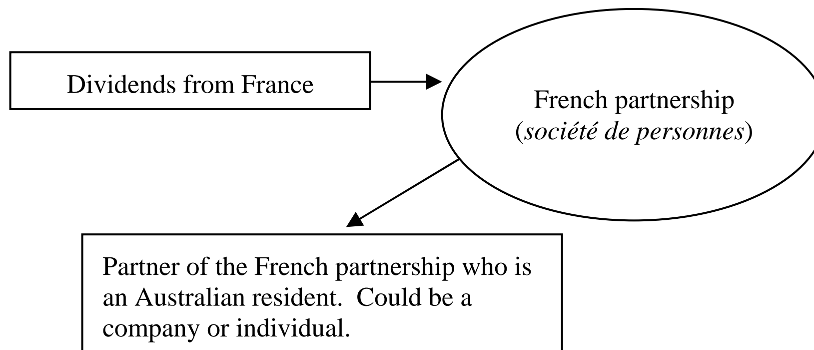


In this example, income arising in Australia is paid to a French partnership of which an Australian resident is a partner. Australia would be required to provide treaty benefits in respect of dividends, interest and royalties flowing to the French resident partnership. The Australian resident partner remains subject to Australian tax on their share of the dividends, interest and royalties and a credit allowed for any additional tax that the French may impose on the dividends, interest or royalties in the hands of the partnership.

1.286 In the case of dividends, interest and royalties arising in France and paid to a French resident partnership with an Australian resident partner, the income will not, as is the case under the existing France

treaty, benefit from the rates of withholding provided in this Convention. The result obtains, even though under Australian law the Australian resident partner would have been so entitled on the basis that a partnership is treated as transparent. Under the France Convention, the French partnership is treated as a resident of France, so that the income is regarded as French sourced income derived by a French resident.

Diagram 1.3



Article 30 — Entry into Force

Date of entry into force

1.287 This Article provides for the entry into force of the France Convention. The treaty will enter into force on the first day of the second month following the date on which diplomatic notes are received notifying that the domestic processes to give the France Convention the force of law in the respective countries has been completed. In Australia, enactment of the legislation giving the force of law in Australia to the France Convention along with tabling the treaty in Parliament are prerequisites to the exchange of diplomatic notes. ***[Article 30, paragraph 1]***

Date of application for Australian taxes

1.288 Once it enters into force the France Convention will apply in Australia in respect of withholding tax on income that is derived by a non-resident on or after 1 January next following the date on which the treaty enters into force. ***[Article 30, sub-subparagraph 1(a)(i)]***

1.289 The France Convention will first apply to other Australian taxes on income, profits or gains of the Australian year of income beginning on or after 1 July in the calendar year next following the date on which the treaty enters into force.

1.290 Where a taxpayer has adopted an accounting period ending on a date other than 30 June, the accounting period that has been substituted

for the year of income beginning on 1 July in the calendar year next following the date on which the France Convention enters into force will be the relevant year of income for the purposes of the application of such Australian tax. ***[Article 30, sub-subparagraph 1(a)(ii)]***

Date of application in France

1.291 In France, the France Convention will first apply in respect of taxes on income withheld at source for amounts that are taxable after the calendar year in which the treaty enters into force. ***[Article 30, sub-subparagraph 1(b)(i)]***

1.292 The treaty will first have effect, in relation to taxes on income that are not withheld at source, for income relating to any calendar year or accounting period beginning after the calendar year in which the treaty enters into force. ***[Article 30, sub-subparagraph 1(b)(ii)]***

1.293 The treaty will first have effect, in relation to other taxes, for taxation where the taxable event occurs after the calendar year in which the treaty enters into force. ***[Article 30, sub-subparagraph 1(b)(iii)]***

Exchange of information application date

1.294 Article 25 (*Exchange of Information*) will first apply from the date of entry into force of the treaty. It applies to requests for exchange of information, in respect of taxes of every kind and description imposed under the federal tax laws administered by the Commissioner, received on or after that date. However, a request for information may relate to the income tax affairs of a taxpayer that may predate entry into force of the Convention. ***[Article 30, subparagraph 1(c)]***

Assistance in recovery date of application

1.295 Article 26 (*Assistance in Recovery*) will first have effect from the date to be agreed in an exchange of notes between Australia and France. ***[Article 30, subparagraph 1(d)]***

Termination of the existing France treaty as amended by the Protocol

1.296 The existing France treaty and the Airline Profits Agreement shall cease to have effect from the dates on which the France Convention commences to have application for the respective taxes. ***[Article 30, paragraph 2]***

Transitional arrangements for visiting professors and teachers

1.297 At the date of entry into force of the new treaty, an individual who is entitled to benefits under Article 19 of the existing France treaty, as amended by the 1989 Protocol, shall continue to have access to the benefit provided for a limited period.

1.298 To qualify for the exemption under Article 19 of the existing France treaty for remuneration from specified teaching activities, the visit must be for a period not exceeding two years. This effectively limits these transitional arrangements to a maximum of two years from the date of entry into force of the new treaty. The actual period that a particular individual will qualify for the exemption will depend on their circumstances and the date they became eligible for the exemption under Article 19 of the existing France treaty. ***[Article 30, paragraph 3]***

Article 31 — Termination

1.299 The France Convention is to continue in effect indefinitely. However, either country may give written notice of termination of the France Convention through the diplomatic channel at least six months before the end of any calendar year beginning after the expiration of five years from the date of its entry into force. ***[Article 31]***

Cessation in Australia

1.300 In the event of either country terminating the France Convention, the treaty would cease to be effective in Australia for the purposes of:

- withholding tax on income derived by a non-resident in relation to income derived on or after 1 January in the calendar year next following that in which the notice of termination is given; and

- other Australian taxes in relation to income, profits or gains in the Australian year of income commencing on or after 1 July in the calendar year next following that in which the notice of termination is given.

[Article 31, subparagraph (a)]

Cessation in France

1.301 The Convention would correspondingly cease to be effective in France for the purposes of:

- taxes on income withheld at source for amounts taxable after the calendar year in which the notice of termination is given;
- taxes on income that are not withheld at source, for income relating to any calendar year or accounting period beginning after the calendar year in which the notice of termination is given; and
- other French taxes when the taxable event occurs after the calendar year in which the notice of termination is given.

[Article 31, subparagraph (b)]

Chapter 2
2006 Australia-Norway tax Convention

Outline of chapter

2.1 Schedule 2 amends the *International Tax Agreements Act 1953*. This chapter explains the rules that apply in the 2006 Australia-Norway tax Convention.

Context of amendments

2.2 The *Convention between Australia and the Kingdom of Norway for the Avoidance of Double Taxation with respect to Taxes on Income and the Prevention of Fiscal Evasion* (referred to as 'the Convention', however, for the remainder of this chapter, referred to as the 'Norway Convention') was signed in Canberra on 8 August 2006.

2.3 Once in force the Norway Convention will replace the *Convention between Australia and the Kingdom of Norway for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital*, and its associated Protocol, signed in 1982 (the existing Norway treaty).

Summary of new law

Main features of the new Convention

2.4 The main features of the Norway Convention are as follows:

- Income from real property may be taxed in full by the country in which the property is situated. Income from real property for these purposes includes natural resource royalties ***[Article 6]***.

- Business profits (including income derived from furnishing of services) are generally to be taxed only in the country of residence of the recipient unless they are derived by a resident of one country through a branch or other prescribed permanent establishment in the other country, in which case

that other country may tax the profits. These rules also apply to business trusts ***[Article 7]***.

- Profits derived from the operation of ships and aircraft in international traffic are generally to be taxed only in the country of residence of the operator ***[Article 8]***.

- Profits of associated enterprises may be taxed on the basis of dealings at arm's length ***[Article 9]***.

- Dividends, interest and royalties may generally be taxed in both countries, but there are limits on the tax that the country in which the dividend, interest or royalty is sourced may charge on such income flowing to residents of the other country who are the beneficial owners of the income ***[Articles 10 to 12]***.

- In the case of dividends:

  – no source country tax is payable on intercorporate dividends where the dividend recipient is a company that holds directly at least 80 per cent of the voting power of the company paying the dividend, subject to certain conditions ***[Article 10, paragraph 3]***;

  – a 5 per cent rate limit applies to other intercorporate dividends where the dividend recipient is a company that holds directly at least 10 per cent of the voting power of the company paying the dividend ***[Article 10, subparagraph 2(a)]***; and

  – a 15 per cent limitation applies to all other dividends ***[Article 10, subparagraph 2(b)]***.

- The dividend rate limits apply to both franked and unfranked dividends.

- Source country taxation on interest is limited to 10 per cent ***[Article 11, paragraph 2]***. However, exemptions from source country taxation have been provided for interest paid to:

  – certain government bodies ***[Article 11, subparagraph 3(a)]***; and

  – financial institutions ***[Article 11, subparagraph 3(b)]***.

- The rate limit on source country taxation of royalties is 5 per cent ***[Article 12, paragraph 2].***

- The definition of royalty has also been amended to include payments or credits in respect of the use of, or right to use, some or all of the radiofrequency spectrum specified in a spectrum licence and to exclude payments or credits in respect of the use of, or right to use, industrial, commercial or scientific equipment ***[Article 12, paragraph 3].***

- Income, profits or gains from the alienation of real property may be taxed in full by the country in which the property is situated. Subject to that rule and other specific rules in relation to business assets and shares or other interests in land rich entities (which may be taxed in full by the country in which the property is situated), all other capital gains will be taxable only in the country of residence ***[Article 13].***

- Income from employment, that is, employee's remuneration, will generally be taxable in the country where the services are performed. However, where the services are performed during certain short visits to one country by a resident of the other country, the income will be exempt in the country visited ***[Article 14].***

- Directors' remuneration may be taxed in the country in which the company of which the person is a director is resident for tax purposes ***[Article 15].***

- Income derived by entertainers and sportspersons may generally be taxed by the country in which the activities are performed. However, if the visit is mainly supported by public funds of the other country, the income is taxable only in the country of which the person is a resident ***[Article 16].***

- Pensions and annuities will generally be taxed only in the country of residence of the recipient. Some public service pensions may be taxed only by the paying country. ***[Articles 17 and 18].***

- Income from government service (including government service pensions) will generally be taxed only in the country that pays the remuneration. However, the remuneration shall only be taxed in the other country where the services are rendered in that other country by a resident of that other country who is a national of that other country or did not

become a resident of that other country for the purpose of rendering the services ***[Article 18]***.

- Payments made from abroad to visiting students for the purposes of their maintenance or education will be exempt from tax in the country visited ***[Article 19]***.

- Income (including certain employment income) from offshore activities relating to exploration or exploitation of natural resources will generally be taxed by the country in which the activities are performed. However, where the activities are carried on during certain short visits to one country by a resident of the other country, the income will be exempt in the country visited ***[Article 20]***.

- Other income (ie, income not dealt with by other Articles) derived by a resident of one country from sources in the other country may generally be taxed in both countries, with the country of residence of the recipient providing double tax relief ***[Article 21]***.

- Source rules in the Norway Convention prescribe for domestic law and treaty purposes, the source of income or profits derived by a resident of one country which may be taxed in the other country ***[Article 22]***.

- Double taxation relief for income which, under the Norway Convention, may be taxed by both countries, is required to be provided by the country of which the taxpayer is a resident under the terms of the Convention as follows:

  – in Australia, by allowing a credit for the Norwegian tax against Australian tax payable on income derived by a resident of Australia from sources in Norway ***[Article 23, paragraph 1]***; and

  – in Norway, by allowing a deduction against Norwegian tax for the Australian tax paid on income derived by a resident of Norway from sources in Australia ***[Article 23, paragraph 2]***.

- In the case of Australia, effect will be given to the double tax relief obligations arising under the Norway Convention by application of the general foreign tax credit provisions of Australia's domestic law, or the relevant exemption provisions of that law where applicable.

- Rules in the new treaty will protect nationals from tax discrimination in the other country and will give them private rights of appeal. However, the Article does not preclude either country from applying its anti-avoidance rules (including thin capitalisation, transfer pricing and controlled foreign companies measures), rebates or credits for dividends paid by resident companies, research and development concessions, consolidation rules or capital gains deferral rules ***[Article 24]***.

- Consultation and exchange of information between the two taxation authorities is authorised by the Norway Convention. The Convention authorises and requires Australia to exchange information where the information relates to taxes administered by the Commissioner of Taxation (Commissioner) ***[Articles 25 and 26]***.

- The Norway Convention ensures the integrity of the tax system by providing for mutual assistance in the collection of tax debts. This will allow the Australian Taxation Office, in certain circumstances, to seek assistance from the Norwegian tax authorities to collect Australian taxation debts ***[Article 27]***.

Comparison of key features of new law and current law

New law	***Current law***
Updates all Articles, having regard to Australian, Norwegian and Organisation for Economic Co-operation and Development (OECD) tax treaty developments since the existing Norway treaty arrangements were entered into.	Not applicable

New law	*Current law*
Extends the coverage of the Norway Convention to Australian tax on capital gains and updates the list of taxes to which the new treaty arrangements apply. In the case of Australia, these taxes are: • the income tax; • the resource rent tax; and • any identical or substantially similar taxes imposed under the federal law of Australia. However, a broader range of taxes apply to certain Articles. In the case of Australia, the taxes are: • taxes of every kind and description for Article 24 (*Non-discrimination*); and • all federal taxes administered by the Commissioner for Article 26 (*Exchange of Information*) and Article 27 (*Assistance in Collection of Taxes*).	In the case of Australia, the taxes to which all Articles of the existing Norway treaty apply are: • the income tax; and • any identical or substantially similar taxes imposed under the federal law of Australia.
Updates the meaning of 'permanent establishment' in Article 5. In particular, under the new Convention an enterprise is deemed to have a ***permanent establishment*** if: • it has a building site etc (including connected supervisory activities) which lasts more than six months; • it furnishes services within a country for a period or periods aggregating more than six months within any 12-month period; or • it maintains substantial equipment for rental or other purposes for more than six months.	A building site constitutes a permanent establishment where the project lasts for more than 12 months. In addition, an enterprise is deemed to have a ***permanent establishment*** if: • it carries on supervisory activities for more than 12 months in connection with a building site; or • substantial equipment is being used in that country by for or under contract.
Broadens the meaning of 'real property' in Article 6 to include exploration for natural resources.	No equivalent.

New law	***Current law***
Aligns the treatment of income from independent personal services to the OECD standard under Article 7 (*Business Profits*). It also clarifies the application of this Article to business trusts.	Income from independent personal services is treated under the previous international standard in Article 14 (*Independent Personal Services*).
Reduces the rate of dividend withholding tax to: • zero for dividends on non-portfolio holdings of more that 80 per cent, subject to certain conditions; and • Five per cent for other non-portfolio holdings.	The rate of dividend withholding tax is limited to 15 per cent.
Reduces the rate of interest withholding tax from 10 per cent to zero where interest is derived by a financial institution.	No equivalent.
Reduces the rate of royalty withholding tax to 5 per cent of the gross royalty payment and extends the meaning of royalty to include spectrum licences. Leasing of industrial, commercial or scientific equipment will no longer constitute a royalty.	The rate of royalty withholding tax is limited to 10 per cent of the gross payment.
Includes a comprehensive *Alienation of Property* Article which allocates taxing rights over capital gains.	Limited coverage.
Provides that pensions (other than Government service pensions) will be taxable only in the State of residence of the recipient. Government service pensions (including any national insurance element of such a pension) will be taxable only in the State which created the fund out of which the pension is paid and to which the services were rendered unless the recipient is a resident and national of the other State.	All pensions currently taxable only in the country of residence of the recipient.

New law	***Current law***
Provides for a shared taxing right in respect of salary, wages and other similar remuneration arising from employment covered by the *Offshore Activities* Article. However, the State of residence of the employee will have the sole taxing right if the employment is carried out offshore for an employer who is not a resident of the State in which the offshore employment is carried out and the employment offshore does not exceed a period or periods aggregating 30 days in the year of income of that State.	Exclusive taxing right in the country where offshore activities are performed, provided the employment is carried on in that country for more than 30 days.
No equivalent.	Article 24 (*Capital*) dealing with various types of capital assets held by Australians in Norway.
Includes a comprehensive Article preventing discrimination in relation to tax laws (Article 24 (*Non-discrimination*)).	No *Non-discrimination* Article.
Closely aligns Article 26 (*Exchange of Information*) to the 2005 OECD standard. The effect of the changes is to expand the range of taxes to which the Article applies and to clarify that bank secrecy laws do not limit the exchange of information.	The existing rules apply to a narrower range of taxes.
Includes a new Article 27 (*Assistance in Collection of Taxes*) which authorises and requires Australia and Norway to provide assistance to each other in collection of cross-border tax debts.	No equivalent.

Detailed explanation of new law

Article 1 — Persons Covered

Scope

2.5 This Article establishes the scope of the application of the Norway Convention by providing for it to apply to persons (defined to include individuals, companies and any other body of persons) who are

residents of one or both of the countries. It generally precludes extra-territorial application of the treaty. ***[Article 1]***

2.6 The Norway Convention also applies to third country residents in relation to the *Non-discrimination* Article (Article 24) in its application to nationals of one of the treaty countries, the *Mutual Agreement Procedure* Article (Article 25) so far as the person is a national of one of the treaty countries and in relation to the exchange of information under the *Exchange of Information* Article (Article 26).

2.7 The application of the Norway Convention to persons who are dual residents (ie, residents of both countries) is dealt with in Article 4 (*Residence*).

Article 2 — Taxes Covered

Taxes covered

2.8 Article 2 specifies the existing taxes of each country to which the Norway Convention applies. These are, in the case of Australia:

- the Australian income tax (including that imposed on capital gains); and
- the resource rent tax in respect of offshore petroleum projects.

2.9 The new treaty extends the operation of the treaty to Australian tax on capital gains, which are not covered in the existing Norway treaty.

2.10 Although Australia considers the resource rent tax to be encompassed by the term 'income tax', a specific reference to this has been included in the Norway Convention to put beyond doubt that it is a tax covered. ***[Article 2, sub-subparagraph 1(a)(ii)]***

2.11 As with the existing Norway treaty, the Norway Convention generally does not cover Australia's goods and services tax (GST), wool tax and levies, customs duties, state taxes and duties and estate tax and duties. However, federal taxes administered by the Commissioner are covered for the purposes of the *Exchange of Information* and *Assistance in the Collection of Taxes* Articles while all taxes are covered for the purposes of the *Non-discrimination* Article. ***[Article 2, paragraphs 3 and 4]***

2.12 It is specifically stated in paragraphs 1 and 2 of this Article that the Norway Convention applies only to taxes imposed under the federal law of Australia. This is to ensure that, except with respect to

non-discrimination, the Norway Convention does not bind Australian states and territories and applies only to federal taxes. ***[Article 2, subparagraph 1(a) and paragraphs 2 and 3]***

2.13 For Norway, the tax treaty applies to:

- the tax on general income;
- the national tax on personal income;
- the special tax on petroleum income;
- the resource rent tax on income from production of hydro-electric power;
- the withholding tax on dividends; and
- the tax on remuneration to non-resident artistes, etc.

[Article 2, subparagraph 1(b)]

Identical or substantially similar taxes

2.14 The application of the Norway Convention will be automatically extended to any identical or substantially similar taxes which are subsequently imposed by either country in addition to, or in place of, the existing taxes. The competent authorities (ie, the Commissioner in Australia and the Minister for Finance or an authorised representative of the Minister in Norway, or their authorised representatives) are required to notify each other in the event of a significant change in the taxation law of the respective countries. ***[Article 2, paragraph 2]***

Special provisions

2.15 Paragraphs 3 and 4 specify the taxes to which Article 24 (*Non-discrimination*), Article 26 (*Exchange of Information*) and Article 27 (*Assistance in the Collection of Taxes*) will apply. The taxes to which these Articles apply are:

- Article 24, all taxes including sub-national taxes such as those imposed by the Australian states or local governments ***[Article 2, paragraph 3]***.
- Articles 26 and 27, in the case of Australia, all federal taxes administered by the Commissioner, and in the case of Norway, all taxes ***[Article 2, paragraph 4]***.

Article 3 — General Definitions

Definition of Australia

2.16 As with Australia's other modern tax treaties, 'Australia' is defined to include certain external territories and areas of the continental shelf. By reason of this definition, Australia preserves its taxing rights, for example, over mineral exploration and mining activities carried on by non-residents on the seabed and subsoil of the relevant continental shelf areas (under section 6AA of the *Income Tax Assessment Act 1936* (ITAA 1936), certain sea installations and offshore areas are to be treated as part of Australia). ***[Article 3, subparagraph 1(a)]***

Definition of Norway

2.17 For all practical purposes the definition remains unchanged from that in the existing Norway treaty. 'Norway' is defined to include the area over which Norway may exercise rights with respect to the seabed and subsoil and their natural resources under international law, but excludes the territories of Svalbard and Jan Mayen, as well as the Norwegian dependencies 'biland'. ***[Article 3, subparagraph 1(b)]***

Definition of company

2.18 The definition of 'company' in the Norway Convention accords with Australia's tax treaty practice.

2.19 The Australian tax law treats certain trusts (public unit trusts and public trading trusts) and corporate limited partnerships (limited liability partnerships) as companies for income tax purposes. These trusts and partnerships are included as companies for the purposes of the tax treaty. ***[Article 3, subparagraph 1(g)]***

Definition of international traffic

2.20 In this Convention, this term is of relevance for taxation of profits from shipping and air transport operations (Article 8 (*Shipping and Air Transport*)), income, profits or gains from the alienation of ships and aircraft (paragraph 3 of Article 13 (*Alienation of Property*)) and wages of crew (paragraphs 3 and 4 of Article 14 (*Income from Employment*)).

2.21 The definition of 'international traffic', covers international transport by a ship or aircraft operated by an enterprise of one country, as well as domestic transport within that country. However, it does not include transport where the ship or aircraft is operated solely between places in the other country, that is, where the place of departure and the place of arrival of the ship or aircraft are both in that other country,

irrespective of whether any part of the transport occurs in international waters. For example, a 'voyage to nowhere' which begins and ends in Sydney on a ship operated by a Norwegian enterprise would not come within the definition of international traffic, even if the ship travels through international waters in the course of the cruise. ***[Article 3, subparagraph 1(k)]***

Definition of national

2.22 The Norway Convention defines 'national' by reference to an individual's nationality or citizenship. A company will be a national if the company derives its status as a company from the laws of one of the countries, that is where it is incorporated. ***[Article 3, subparagraph 1(l)]***

2.23 The concept of nationality is used in subparagraph (b) of paragraph (3) of Article 4 (*Residence*), Article 18 (*Government Service*) and Article 24 (*Non-discrimination*).

Definition of person

2.24 The definition of 'person' includes individuals, companies and any other body of persons. This includes a partnership (as a body of persons). ***[Article 3, subparagraph 1(m)]***

Definition of tax

2.25 For the purposes of the Norway Convention, the term 'tax' does not include any amount of penalty or interest imposed under the respective domestic tax law of the two countries. This is important in determining a taxpayer's entitlement to a foreign tax credit under the double tax relief provisions of Article 23 (*Methods of Elimination of Double Taxation*) of the Convention.

2.26 In the case of a resident of Australia, any penalty or interest component of a liability determined under the domestic taxation law of Norway with respect to income that Norway is entitled to tax under the Norway Convention, would not be a creditable 'Norwegian tax' for the purposes of paragraph 1 of Article 23 (*Methods of Elimination of Double Taxation*). This is in keeping with the meaning of 'foreign tax' in subsection 6AB(2) of the ITAA 1936. Accordingly, such a penalty or interest liability would be excluded from calculations when determining the Australian resident taxpayer's foreign tax credit entitlement under paragraph 1 of Article 23 (pursuant to Division 18 of Part III of the ITAA 1936 — Credits in respect of foreign tax). ***[Article 3, subparagraph 1(n)]***

Definition of 'recognised stock exchange'

2.27 The term is used in relation to setting the appropriate withholding tax limits in Article 10 (*Dividends*). No withholding tax will apply to a dividend paid from an Australian resident company to a Norwegian resident company which holds 80 per cent of the voting power of the paying company where its principal class of shares is listed and regularly traded on a recognised stock exchange.

2.28 The stock exchanges that are recognised are the Australian Securities Exchange and any other Australian stock exchange recognised as such under Australian law, the Oslo Stock Exchange and any other Norwegian stock exchange recognised as such under Norwegian law and any other stock exchanges agreed to by the competent authorities under the Norway Convention. ***[Article 3, subparagraph 1(o)]***

Terms not specifically defined

2.29 Where a term is not specifically defined within this Convention, that term (unless used in a context that requires otherwise) is to be taken to have the same interpretative meaning as it has under the domestic taxation law of the country applying the Norway Convention at the time of its application. In that case the term's meaning under the taxation law of the country will have precedence over the meaning it may have under other domestic laws.

2.30 The same term may have a differing meaning and a varied scope within different Acts relating to specific taxation measures. For example, GST definitions are sometimes broader than income tax definitions. The definition more specific to the type of tax should be applied in such cases. For example, where the matter subject to interpretation is an income tax matter, but definitions exist in either the ITAA 1936 or the *Income Tax Assessment Act 1997* (ITAA 1997) and the *A New Tax System (Goods and Services Tax) Act 1999* (*GST Act*), the income tax definition would be the relevant definition to be applied.

2.31 If a term is not defined in the Norway Convention, but has an internationally understood meaning in tax treaties and a meaning under the domestic law, the context would normally require that the international meaning be applied. ***[Article 3, paragraph 2]***

Article 4 — Residence

Residential status

2.32 This Article sets out the basis by which the residential status of a person is to be determined for the purposes of the Norway Convention. Residential status is one of the criteria for determining each country's taxing rights and is a necessary condition for the provision of relief under the Convention. In the case of Australia, the concept of who is a resident is determined according to Australia's taxation law. In the case of Norway, residence is determined by reference to criteria such as domicile, residence, place of management and other similar criteria. ***[Article 4, paragraph 1]***

Residency of Governments and tax-exempt entities

2.33 The Article specifically provides that the government, a political subdivision or a local authority of a country are residents for the purposes of the Norway Convention. This means that the Federal Government, the State Governments and local councils will be residents for the purpose of the Convention. This does not necessarily mean that income, profits or gains derived by these bodies from sources in Norway will be subject to tax in Norway as sovereign immunity principles may apply. ***[Article 4, paragraph 1]***

2.34 The OECD *Model Tax Convention on Income and on Capital* (OECD Model) Commentary makes it clear that it has always been the understanding of member countries that the OECD Model applied to treat governments as residents even in the absence of an express reference to that effect.

Special residency rules

2.35 Paragraph 2 specifies that a person is not a resident of a country (for purposes of the Norway Convention) if that person is liable to tax in that State in respect only of income from sources in that State.

2.36 This paragraph deals with a person who may be considered to be a resident of a State according to its domestic laws but is only liable to taxation on income from sources in that State, such as, foreign diplomatic and consular staff. In the Australian context, this means that Norfolk Island residents who are generally subject to Australian tax on Australian source income only, will not be residents of Australia for the purposes of the Norway Convention. Accordingly, Norway will not have to forgo tax in accordance with the Norway Convention on income derived by residents of Norfolk Island from sources in Norway (which will not be subject to Australian tax). ***[Article 4, paragraph 2]***

Dual residents

2.37 This Article also includes a set of tie-breaker rules for determining how residency is to be allocated to one or other of the countries for the purposes of the Norway Convention if a taxpayer, whether an individual, a company or other taxable unit, qualifies as a dual resident, that is, as a resident of both countries in accordance with paragraph 1 of the Article.

2.38 The tie-breaker rules for individuals apply certain tests, in a descending hierarchy, for determining the residential status (for the purposes of the Norway Convention) of an individual who is a resident of both countries. These rules, in order of application, are:

- If the individual has a permanent home available to them in only one of the countries, the person is deemed to be a resident solely of that country for the purposes of the Norway Convention.
- If the individual has a permanent home available in both countries or in neither, then the person's residential status takes into account the person's personal or economic relations with Australia and Norway, and the person is deemed for the purposes of the Convention to be a resident only of the country with which the person has the closer personal and economic relations.
- Residency will be determined on the basis of an individual's citizenship or nationality where the foregoing test is not determinative.
- If the individual is a national (as defined) of both countries or of neither, the competent authority will endeavour to resolve the question of treaty residence by mutual agreement.

[Article 4, paragraph 3]

2.39 A dual resident remains, however, in relation to Australia, a resident for the purposes of Australian domestic law. Accordingly that person remains liable to tax in Australia as a resident, insofar as the Norway Convention allows.

2.40 Where a non-individual (such as a body corporate) is a resident of both countries in accordance with paragraph 1, the entity will be deemed for the purposes of the Norway Convention to be a resident of the country in which its place of effective management is situated. ***[Article 4, paragraph 4]***

Limitation of relief

2.41 The treaty provides that where an individual is a temporary resident of a country and is, for that reason, exempt from tax in that country on certain income or gains in that country, then the other country will not be required to provide any relief specified in the treaty in respect of such income or gains. ***[Article 4, paragraph 5]***

Article 5 — Permanent Establishment

Role and definition

2.42 The application of various provisions of the Norway Convention (principally Article 7 (*Business Profits*)) is dependent upon whether a person who is a resident of one country carries on business through a permanent establishment in the other country, and if so, whether income derived by that person is attributable to, or assets of that person are effectively connected with, that permanent establishment.

2.43 The definition of the term 'permanent establishment' in this Article corresponds generally with definitions of the term in Australia's more recent tax treaties. The term also fully encompasses the concept of 'fixed base', which is used in the existing Norway treaty in a separate Article dealing with independent personal services. In this regard the following notes reflect agreement reached during negotiation of the Norway Convention:

'In relation to Article 5 *Permanent Establishment*, and Article 7 *Business Profits*, it was agreed that 'permanent establishment' as defined fully encompasses the concept of a 'fixed base' previously used in Article 14 *Independent Personal Services* of the existing Norway treaty.'

As such services will now be dealt with under Article 7 (*Business Profits*), it is intended that places that constitute a fixed base for purposes of the existing Norway treaty would come within the meaning of permanent establishment for purposes of the new treaty.

Meaning of permanent establishment

2.44 The primary meaning of permanent establishment is expressed as being a fixed place of business through which the business of an enterprise is wholly or partly carried on. To be a permanent establishment within the primary meaning of that term, the following requirements must be met:

- there must be a place of business;

- the place of business must be fixed (both in terms of physical location and in terms of time); and
- the business of the enterprise must be carried on through this fixed place.

[Article 5, paragraph 1]

2.45 Other paragraphs of this Article elaborate on the meaning of the term by giving examples (by no means intended to be exhaustive) of what may constitute a permanent establishment — for example:

- an office;
- a factory; or
- an agricultural property.

2.46 Consistent with Australia's modern treaty practice, the definition also extends to places relating to the exploitation of and exploration for natural resources.

2.47 As paragraph 2 of this Article is subordinate to paragraph 1, the examples listed will only constitute a permanent establishment if the primary definition in paragraph 1 is satisfied. ***[Article 5, paragraph 2]***

Agricultural, pastoral or forestry activities

2.48 Most of Australia's tax treaties include as a permanent establishment an agricultural, pastoral or forestry property. This reflects Australia's policy of retaining taxing rights over exploitation of Australian land for the purposes of primary production. This approach ensures that the arm's length profits test provided for in Article 7 (*Business Profits*) applies to the determination of profits derived from these activities. This position is also reflected in this Convention. ***[Article 5, subparagraph 2(g)]***

Deemed permanent establishment

Building site or construction or installation project

2.49 Under paragraph 3, an enterprise is deemed to have a permanent establishment and to be carrying on business through that permanent establishment in a country if it has a building site or construction or installation project in that country which exists for more than six months. ***[Article 5, subparagraph 3(a)]***

Supervisory and consultancy activities

2.50 Supervisory and consultancy activities carried on for more than six months in connection with a building site or a construction or installation project are deemed to constitute a permanent establishment. This provision broadly aligns with Australia's reservation to Article 5 (*Permanent Establishment*) of the OECD Model.

2.51 The term 'building site or construction or installation project' includes not only the construction of buildings but also the construction of roads, bridges or canals, the renovation (involving more than mere maintenance or redecoration) of buildings, roads, bridges or canals, the laying of pipelines and excavating and dredging. Planning and supervision are considered part of the building site if carried out by the construction contractor. However, planning and supervision carried out by another unassociated enterprise will not be taken into account in determining whether the construction contractor has a permanent establishment in Australia. ***[Article 5, subparagraph 3(a)]***

Anti-avoidance provision

2.52 Given that subparagraph 3(a) contains certain time-frames, an anti avoidance rule is included to ensure that where associated enterprises carry on substantially the same activities, the periods will be aggregated in determining whether the enterprises have a permanent establishment in the country in which the activities are being carried on. Activities will be regarded as connected where, for example, different stages of a single project are carried out by different subsidiaries within a group of companies.

2.53 Paragraph 4 is an anti-avoidance measure aimed at counteracting contract splitting for the purposes of avoiding the application of the permanent establishment rules.

2.54 The Norway Convention provides that an enterprise shall be deemed to be associated with another enterprise if one enterprise is controlled directly or indirectly by the other or if both are controlled directly or indirectly by a third person or persons. It also provides that a period of concurrent activities by such associated enterprises is only counted as one period for aggregation purposes. ***[Article 5, paragraph 4]***

Furnishing of services

2.55 An enterprise will be deemed to have a permanent establishment where it undertakes service activities, including the provision of consultancy services, where those activities continue (for the same or a connected project) within a country for a period or periods aggregating

more than six months within any 12 month period. ***[Article 5, subparagraph 3(b)]***

Substantial equipment

2.56 Under subparagraph 3(c), an enterprise shall be deemed to have a permanent establishment if it has substantial equipment in a country for rental or other purposes for longer than six months, unless the equipment is leased under a 'hire-purchase' agreement. Under Australian law, the lessee under a 'hire-purchase' agreement (a lease accompanied by certain lessee purchase options or rights) is broadly treated for tax purposes as the owner of the leased property.

2.57 This provision reflects Australia's reservation to the OECD Model concerning the use of substantial equipment. Australia's experience is that the permanent establishment provision in the OECD Model may be inadequate to deal with high value mobile activities.

2.58 The meaning of the term 'substantial' depends on the relevant facts and circumstances of each individual case. However, some examples of substantial equipment would include:

- large industrial earthmoving equipment or construction equipment used in road building, dam building or powerhouse construction;
- manufacturing or processing equipment used in a factory;
- oil and drilling rigs, platforms and other structures used in the petroleum/mining industry; and
- grain harvesters and other large agricultural machinery.

2.59 For the purposes of the Norway Convention the enterprise is deemed to carry on business through the substantial equipment permanent establishment. ***[Article 5, subparagraph 3(c)]***

Manufacturing or processing on behalf of others

2.60 Subparagraph 3(d*)* is consistent with another of Australia's reservations to the OECD Model. It deals with situations where a person acts on behalf of another in manufacturing or processing that other person's goods. An example is the situation where a mineral plant refines minerals at cost, so that the plant operations produce no Australian profits. Title to the refined product remains with the mining consortium and profits on sale are realised mainly outside of Australia.

2.61 Subparagraph 3(d*)* deems such a plant to be a permanent establishment because the manufacturing or processing activity (which gives the processed minerals their real value) is conducted in Australia, and therefore Australia should have taxing rights over the business profits arising from the sale of the processed minerals to the extent that they are attributable to the processing activity carried on in Australia. This subparagraph prevents an enterprise which carries on substantial manufacturing or processing activities in a country through an intermediary from claiming that it does not have a permanent establishment in that country.

2.62 This subparagraph is in the existing Norway treaty. The inclusion of this subparagraph is insisted upon by Australia in its tax treaties and is consistent with Australia's policy of retaining taxing rights over profits from manufacturing or processing on behalf of others including, importantly, in the exploitation of Australia's mineral resources. ***[Article 5, subparagraph 3(d)]***

Preparatory and auxiliary activities

2.63 Certain activities do not generally give rise to a permanent establishment (eg, the use of facilities solely for storage, display or delivery).

2.64 Generally these activities are of a preparatory or auxiliary character and are unlikely to give rise to substantial profits. The necessary economic link between the activities of the enterprise and the country in which the activities are carried on does not exist in these circumstances.

2.65 Unlike the OECD Model, which provides that the listed activities are deemed not to constitute a permanent establishment, the Norway Convention provides that an enterprise will not be deemed to have a permanent establishment merely by reason of such activities. This is to prevent the situation where enterprises structure their business so that most of their activities fall within the exceptions when, viewed as a whole, the activities ought to be regarded as a permanent establishment.

2.66 Another feature consistent with Australia's tax treaty practice is that subparagraph 4(f) of Article 5 (*Permanent Establishment*) of the OECD Model — dealing with combinations of the activities of the kind referred to in subparagraphs 5(a) to 5(e) of this treaty — is not included. Australia does not consider that an enterprise undertaking multiple functions of the kind indicated in subparagraphs 5(a) to 5(e) would generally be regarded as only engaged in preparatory or auxiliary activities. ***[Article 5, paragraph 5]***

Dependent agents

2.67 Paragraph 6 reflects Australia's tax treaty practice in relation to a person who acts on behalf of an enterprise of another country of deeming that person to constitute a permanent establishment if that person has and habitually exercises an authority to conclude contracts on behalf of the enterprise.

2.68 Consideration ought to be given to all the relevant facts and circumstances in determining whether a person has authority or not to conclude contracts. In this regard the following notes reflect agreement reached during negotiation of the Norway Convention with regard to this provision:

> 'With respect to paragraph 6 of Article 5 *Permanent Establishment*, it was agreed that a person who substantially negotiates the essential parts of a contract on behalf of an enterprise will be regarded as exercising an authority to conclude contracts on behalf of that enterprise within the meaning of this provision, even if the contract is subject to final approval or formal signature by another person.'

2.69 Activities of a dependent agent will not give rise to a permanent establishment where that agent's activities are limited to the preparatory and auxiliary activities mentioned in paragraph 5. ***[Article 5, paragraph 6]***

Independent agents

2.70 Business carried on through an independent agent will not, of itself, give rise to a permanent establishment, provided that the independent agent is acting in the ordinary course of that agent's business as such an agent. ***[Article 5, paragraph 7]***

Subsidiary companies

2.71 Generally, a subsidiary company will not be a permanent establishment of its parent company. A subsidiary, being a separate legal entity, would not usually be carrying on the business of the parent company but rather its own business activities. However, a subsidiary company gives rise to a permanent establishment if the subsidiary permits the parent company to operate from its premises such that the tests in paragraph 1 of Article 5 are met, or acts as an agent of the parent company such that a dependent agent permanent establishment is constituted. ***[Article 5, paragraph 8]***

Other Articles

2.72 The principles set down in this Article are also to be applied in determining whether a permanent establishment exists in a third country or whether an enterprise of a third country has a permanent establishment in Australia (or Norway) when applying the source rule contained in:

- paragraph 7 of Article 11 (*Interest*); and
- paragraph 5 of Article 12 (*Royalties*).

[Article 5, paragraph 9]

Article 6 — Income from Real Property

Where income from real property is taxable

2.73 This Article provides that the income of a resident of one country from real property may be taxed by the country in which the real property is situated. Thus, income from real property in Australia will be subject to Australian tax laws. ***[Article 6, paragraph 1]***

Definition

2.74 Income from 'real property' (which is primarily defined as having the meaning which it has under the domestic law of the country where the property is situated) also extends, in the case of Australia, to income from:

- the direct use, letting or use of any form of real property, a lease of land and any other interest in or over land (including exploration and mining rights); and
- royalties and other payments relating to the exploration for or exploitation of mines or quarries or other natural resources or rights in relation thereto.

2.75 In the case of Norway, the definition generally follows the OECD Model definition of 'immovable property' and includes:

- property accessory to real property;
- rights to which the provisions of the general law respecting landed property apply including direct use, letting or any other use of such property;

- usufruct of real property (generally, a right to use property without degrading it and to retain any profits derived from it); and
- royalties and other payments relating to the exploitation of mines or quarries or other natural resources, or rights in relation thereto.

2.76 Ships and aircraft are excluded from the definition of real property. Therefore this Article does cover income from their use. ***[Article 6, paragraph 2]***

Deemed situs

2.77 Under Australian law the place where an interest in land, such as a lease, is situated (situs) is not necessarily where the underlying property is situated. This paragraph puts the situation of the interest or right beyond doubt by deeming the situs to be where the underlying real property over which the lease or right is granted is situated or where any exploration may take place. ***[Article 6, paragraph 3]***

Real property of an enterprise

2.78 Paragraph 5 extends the application of this Article to income derived from the use or exploitation of real property of an enterprise.

2.79 Accordingly, this Article (when read with Article 7 (*Business Profits*)) ensures that the country in which the real property is situated may impose tax on the income derived from that property by an enterprise of the other country, irrespective of whether or not that income is attributable to a permanent establishment of such an enterprise situated in the first-mentioned country. ***[Article 6, paragraph 5]***

Article 7 — Business Profits

2.80 This Article is concerned with the taxation by one country of business profits derived by an enterprise that is a resident of the other country.

2.81 The taxing of these profits depends on whether they are attributable to the carrying on of a business through a permanent establishment in that country. If a resident of one country carries on business through a permanent establishment (as defined in Article 5 (*Permanent Establishment*)) in the other country, the country in which the permanent establishment is situated may tax the profits of the enterprise that are attributable to that permanent establishment. ***[Article 7, paragraph 1]***

2.82 If an enterprise which is a resident of one country derives business profits in the other country other than profits attributable to a permanent establishment in that other country, the general principle of this Article is that the enterprise will not be liable to tax in the other country on such business profits (except where paragraph 7 of this Article applies — see the explanation in paragraphs 2.88 and 2.89).

Determination of business profits

2.83 Profits of a permanent establishment are to be determined for the purposes of this Article on the basis of arm's length dealings. The provisions in the Norway Convention correspond to international practice and the comparable provisions in Australia's other tax treaties. ***[Article 7, paragraphs 2 and 3]***

2.84 In respect of paragraph 3, no deductions are allowed in respect of expenses which would not be deductible if the permanent establishment were an independent enterprise which incurred the expense. ***[Article 7, paragraph 3]***

2.85 No profits are to be attributed to a permanent establishment merely because it purchases goods or merchandise for the enterprise. Accordingly, profits of a permanent establishment will not be increased by adding to them any profits attributable to the purchasing activities undertaken for the head office. It follows, of course, that any expenses incurred by the permanent establishment in respect of those purchasing activities will not be deductible in determining the taxable profits of the permanent establishment. ***[Article 7, paragraph 5]***

Inadequate information

2.86 The domestic law of the country in which the permanent establishment is situated (eg, Australia's Division 13 of Part III of the ITAA 1936) may be applied to determine the tax liability of a person, consistently with the principles of the Article. This is of particular relevance where, due to inadequate information, the correct amount of profits attributable on the arm's length principle basis to a permanent establishment cannot be determined, or can only be ascertained with extreme difficulty. This is of particular relevance, where there is no data available or the available data is not of sufficient quality to rely on the traditional transaction methods for the attribution of arm's length profits. Paragraph 4 explicitly recognises the right of each country to apply its domestic law in these circumstances. This is consistent with Australia's reservation to Article 7 (*Business Profits*) of the OECD Model. ***[Article 7, paragraph 4]***

Method of determining profits attributed to a permanent establishment

2.87 This paragraph follows the OECD Model and has been inserted at the request of Norway to lay down clearly in the treaty that a method of allocation once used should not be changed merely because in a particular year a more favourable result is produced under a different method. It also provides assurances of continuous and consistent tax treatment for business dealings through branches between the two countries, unless there is good and sufficient reason to change. ***[Article 7, paragraph 6]***

Profits dealt with under other Articles

2.88 Where income or gains are specifically dealt with under other Articles of the Norway Convention, the effect of those particular Articles is not overridden by this Article.

2.89 This provision lays down the general rule of interpretation that categories of income or gains which are the subject of other Articles of the Norway Convention (eg, Article 8 (*Shipping and Air Transport*), Article 10 (*Dividends*), Article 11 (*Interest*), Article 12 (*Royalties*) and Article 13 (*Alienation of Property*)) are to be treated in accordance with the terms of those Articles (except where otherwise provided, for example, by paragraph 5 of Article 10 (*Dividends*) where the asset in respect of which the income is paid is effectively connected with a permanent establishment). ***[Article 7, paragraph 7]***

Insurance with non–residents

2.90 Each country has the right to continue to apply any provisions in its domestic law relating to the taxation of income from insurance, other than life insurance. However, if the relevant law in force in either country at the date of signature of the treaty is subsequently varied (otherwise than in minor respects so as not to affect its general character), the countries must consult with each other with a view to agreeing to any amendment of this paragraph that may be appropriate. An effect of this paragraph is to preserve, in the case of Australia, the application of Division 15 of Part III of the ITAA 1936 (Insurance with Non-residents). This is consistent with Australia's reservation to Article 7 (*Business Profits*) of the OECD Model. ***[Article 7, paragraph 8]***

Trust beneficiaries

2.91 The principles of this Article will apply to profits which under the Norway Convention fall to be taxed under this Article and which are derived by a resident of one of the countries (directly or through one or more interposed trust estates) as a beneficiary of a trust estate other than a

trust estate which is treated as a company for tax purposes. ***[Article 7, paragraph 9]***

2.92 In accordance with this provision, Australia has the right to tax a share of business profits, originally derived by a trustee of a trust estate (other than a trust estate that is treated as a company for tax purposes) from the carrying on of a business through a permanent establishment in Australia, to which a resident of Norway is beneficially entitled under the trust estate. Article 7 paragraph 9 ensures that such business profits will be subject to tax in Australia where, in accordance with the principles set out in Article 5 (*Permanent Establishment*), the trustee of the relevant trust estate has a permanent establishment in Australia in relation to that business. The principles of this paragraph will also apply where relevant to other Articles of the Norway Convention, such as Article 13 (*Alienation of Property*) in its application to income profits or gains arising from the alienation of the assets of a permanent establishment or the permanent establishment itself.

Article 8 — Shipping and Air Transport

Profits from international traffic

2.93 The main effect of this Article is that the right to tax profits from the operation of ships or aircraft in international traffic, including a share of profits attributable to participation in a pool, a joint business, an international operating agency or the Norwegian partner of the air consortium Scandinavian Airline System (SAS), is generally reserved to the country in which the operator is a resident for tax purposes. ***[Article 8, paragraphs 1, 3 and 5]***

2.94 The profits covered consist in the first place of the profits directly obtained by the enterprise from the transportation of passengers or cargo by ships or aircraft (whether owned, leased or otherwise at the disposal of the enterprise) that it operates in international traffic. However, as international transport has evolved, shipping and air transport enterprises invariably carry on a large variety of activities to facilitate, or support their international operations. Consistent with the 2005 OECD Model Commentary on Article 8, paragraph 1 also covers profits from activities directly connected with such operations as well as profits from activities which are not directly connected with the operation of the enterprise's ships or aircraft in international traffic but which are ancillary to such operation.

Internal traffic

2.95 Paragraph 2 reflects Australia's treaty policy of reserving to the source country the right to tax profits from internal traffic and profits from

other coastal and continental shelf activities, including non-transport shipping and aircraft activities, within its own waters and airspace. Profits derived directly or indirectly by a Norwegian enterprise from the operation of ships or aircraft, to the extent that they relate to operations confined solely to places in Australia, may thus be taxed in Australia. ***[Article 8, paragraph 2]***

2.96 Australia's taxing rights are specifically preserved over profits from the carriage by ships or aircraft of passengers or cargo (including mail) where the passenger or cargo is shipped and discharged in Australia. ***[Article 8, paragraph 4]***

Example 2.1

A ship operated by a Norwegian enterprise, in the course of an international voyage from Bergen to Melbourne, makes a stop in Perth to pick up cargo. Profits derived from the transport of the goods loaded in Perth and discharged in Melbourne would be profits from operations confined solely to places in Australia. Australia would therefore have the right to tax the profits relating to such transport. Five per cent of the amount paid in respect of the transport of those goods would be deemed to be taxable income of the operator for Australian tax purposes pursuant to Division 12 of Part III of the ITAA 1936.

Example 2.2

A Norwegian enterprise operates sightseeing flights to observe whales in the Southern Ocean. Passengers board the aircraft in Hobart and disembark at the same airport later on the same day. These operations would be regarded as operations confined solely to places in Australia, notwithstanding that the aircraft passes through international airspace. Australia would therefore have the right to tax the profits relating to the carriage of these passengers.

2.97 Operations involving the use of ships or aircraft, such as haulage, survey or dredging activities, or other activities that are undertaken in Australia are also regarded as operations confined solely to places in Australia.

2.98 Exclusive residence country taxation will also apply to profits from the use, maintenance and rental of containers used for the transport of goods or merchandise, provided the rental or use is directly connected or ancillary to the operation by the enterprise of ships or aircraft in international traffic. The following notes reflect the agreement reached during renegotiation of the Norway Convention with regard to the application of the Article to containers:

'With reference to Article 8 *Shipping and Air Transport*, the delegations agreed that profits from the operation of ships or aircraft in international traffic will include profits of an enterprise from the use, maintenance or rental of containers used for the transport of goods or merchandise, provided the rental or use is directly connected or ancillary to the operation by that enterprise of ships or aircraft in international traffic.'

Article 9 — Associated Enterprises

Reallocation of profits

2.99 This Article deals with associated enterprises (such as parent and subsidiary companies and companies under common control). It authorises the reallocation of profits between related enterprises in Australia and Norway on an arm's length basis where the commercial or financial arrangements between the enterprises differ from those that might be expected to operate between unrelated enterprises dealing wholly independently with one another.

2.100 This Article would not generally authorise the rewriting of accounts of associated enterprises where it can be satisfactorily demonstrated that the transactions between such enterprises have taken place on normal, open market commercial terms. Consistent with Australia's recent treaty practice, the inclusion of the expression 'dealing wholly independently with one another' in paragraph 1 recognises dealings on a truly independent basis as the appropriate benchmark for determining whether the transactions have taken place on normal, open market commercial terms. ***[Article 9, paragraph 1]***

2.101 The broad scheme of Australia's domestic law provisions relating to international profit shifting arrangements under which profits are shifted out of Australia, whether by transfer pricing or other means, is to impose arm's length standards in relation to international dealings. Where the Commissioner cannot ascertain the arm's length consideration, it is deemed to be such an amount as the Commissioner determines.

2.102 Paragraph 2 of this Article specifically recognises the right of each country to apply its domestic law relating to the determination of the tax liability of a person (eg, Australia's Division 13 of the ITAA 1936) to its own enterprises, including in cases where the available information is inadequate, provided that such provisions are applied, so far as it is practicable to do so, consistently with the principles of the Article. This is of particular relevance where there is no data available or the available data is not of sufficient quality to rely on the traditional transaction methods for the attribution of arm's length profits. This reflects Australia's reservation to Article 9 (*Associated Enterprises*) of the OECD Model. ***[Article 9, paragraph 2]***

Correlative adjustments

2.103 Where a reallocation of profits is made (either under this Article or, by virtue of paragraph 2, under domestic law) so that the profits of an enterprise of one country are adjusted upwards, a form of double taxation would arise if the profits so reallocated continued to be subject to tax in the hands of an associated enterprise in the other country. To avoid this result, the other country — if it considers the adjustment justified — will make an appropriate compensatory adjustment to the amount of tax charged on the profits involved to relieve any such double taxation.

2.104 During negotiation of the Norway Convention, negotiators reached the following agreement:

'For purposes of paragraph 3 of Article 9 *Associated Enterprises*, negotiators for Australia and Norway agreed that an adjustment will be justified where a State agrees that the adjustment made by the other State in accordance with paragraph 1 of that Article is justified both in principle and as regards the amount, except in cases involving fraud, gross negligence or wilful default on the part of one or both of the enterprises.'

2.105 Where fraud, gross negligence or wilful default on the part of one or both enterprises is involved, compensatory adjustments are not required.

2.106 It would generally be necessary for the affected enterprise to apply to the competent authority of the country not initiating the reallocation of profits for an appropriate compensatory adjustment to reflect the reallocation of profits made by the other treaty partner country. If necessary, the competent authorities of Australia and Norway will consult with each other to determine the appropriate adjustment. ***[Article 9, paragraph 3]***

Article 10 — Dividends

2.107 This Article allocates taxing rights in respect of dividends flowing between Australia and Norway. The Article provides that:

- certain cross-border intercorporate dividends will be either exempt or subject to a maximum 5 per cent rate of source country tax;
- a maximum 15 per cent rate of source country tax may be applied on all other dividends;

- dividends paid in respect of a holding which is effectively connected with a permanent establishment are to be dealt with under Article 7 (*Business Profits*); and
- extra-territorial application by either country of taxing rights over dividend income is not permitted.

2.108 However, no such relief is available in cases that have been designed with a main purpose of taking advantage of this Article.

Permissible rate of source country taxation

Exemption for certain cross-border intercorporate dividends

2.109 No tax will be payable in the source country on dividends paid to a company that is the beneficial owner of those dividends and is resident in the other country where:

- the recipient company holds 80 per cent or more of the voting power of the company paying the dividend; and
- satisfies a 12-month holding requirement at the time of the declaration of the dividend in relation to the shares in respect of which the dividend is payable.

[Article 10, paragraph 3]

2.110 To qualify for the exemption, the company that is the beneficial owner of the dividends must either be:

- a company that has its principal class of shares;
  - listed on specified Australian or Norwegian stock exchanges; and
  - regularly traded on one or more recognised stock exchanges (as defined under Article 3 (*General Definitions*) of the treaty); or
- a company that is owned either directly or indirectly by such a company.

2.111 Dividends which are beneficially owned by a company that does not meet the conditions in the previous paragraph will also be exempt from tax in the source country if the competent authority of that country determines, in accordance with its domestic law, that the recipient company was established, acquired, or maintained for reasons other than

obtaining benefits under the treaty. Before concluding that a company is not entitled to benefits under this subparagraph (eg, because the arrangements had a principal purpose of obtaining such benefits), the competent authority is required to consult with the competent authority of that company's country of residence. ***[Article 10, subparagraphs 3(a) to (c)]***

2.112 For the purpose of the above tests, a recognised stock exchange includes:

- in Australia's case, the Australian Securities Exchange or any other Australian stock exchange recognised under Australian domestic law; and
- in Norway, the Oslo Stock Exchange or any other stock exchange recognised under Norwegian domestic law.

2.113 Under sub-subparagraph 1(o)(iii) of Article 3 *(General Definitions)*, provision has been made to allow the competent authorities to reach agreement that other stock exchanges constitute a recognised stock exchange for the purpose of the treaty. ***[Article 3, sub-subparagraph 1(o)(iii)]***

Five per cent rate limit on source country tax of certain cross-border intercorporate dividends

2.114 This Article allows both countries to tax other dividends flowing between them but limits the rate of tax that the country of source may impose on dividends paid by companies that are residents of that country under its domestic law to residents in the other country who are the beneficial owners of the dividends. ***[Article 10, paragraphs 1 and 2]***

2.115 A rate limit of 5 per cent will apply for dividends paid in respect of shareholdings of companies (other than partnerships) that do not qualify for the intercorporate dividend exemption under paragraph 3 of this Article, but constitute a direct voting interest of at least 10 per cent. ***[Article 10, subparagraph 2(a)]***

2.116 In relation to the exclusion of partnerships that are taxed like companies from the benefit of the source country tax rate limitation the following note reflects agreement reached during negotiation of the Norway Convention with respect to the treatment of Australian limited liability partnerships (corporate limited partnerships):

'With respect to paragraph 2(a) of Article 10, the two delegations noted that under Australian taxation law, Australian corporate limited partnerships are effectively treated as companies for tax purposes and that a reference to a partnership does not include a reference to a limited partnership. It is therefore understood that the reference to a partnership in paragraph 2(a) does not apply to such corporate limited partnerships.'

Fifteen per cent rate limit for all other dividends

2.117 In all other cases, the treaty provides that the source country will generally limit its tax to 15 per cent of the gross amount of the dividend. In the case of Australia, this will mean that the domestic rate of withholding tax imposed on unfranked dividends will be reduced from 30 per cent to 15 per cent. ***[Article 10, subparagraph 2(b)]***

2.118 Despite the provisions described above, the dividend withholding tax exemption provided by Australia under its domestic law for franked dividends paid to non-residents will continue to apply.

Future changes to either country's domestic tax treatment of dividends

2.119 If there is a material change to either country's general approach to taxing dividends (eg, a change to Australia's domestic law arrangements for franked dividends flowing overseas), the two countries are obliged to consult with each other to consider whether any amendment to paragraphs 2 and 3 of this Article would be appropriate as a consequence of the change to domestic law. ***[Article 10, paragraph 2]***

Dividends effectively treated as business profits

2.120 The limitation on the tax of the country in which the dividend is sourced does not apply to dividends derived by a resident of the other country who has a permanent establishment in the source country from which the dividends are derived, if the holding giving rise to the dividends is effectively connected with that permanent establishment.

2.121 Where the holding is so effectively connected, the dividends are to be treated as business profits and therefore subject to the full rate of tax applicable in the country in which the dividend is sourced in accordance with the provisions of Article 7 (*Business Profits*).

2.122 Franked and unfranked dividends paid by an Australian company will be included in the assessable income of a non-resident company or individual where the dividends are attributable to a permanent establishment situated in Australia. Expenses incurred in deriving the dividend income are allowable as a deduction from that income when calculating the taxable income of the non-resident. Further, a non-resident company or individual may be entitled to tax offsets in respect of any franked dividends under Australia's domestic law. ***[Article 10, paragraph 5]***

Extra–territorial application precluded

2.123 The extra-territorial application by either country of taxing rights over dividend income is precluded. Broadly, one country (the first country) will not tax dividends paid by a company resident solely in the other country, unless:

- the person deriving the dividends is a resident of the first country; or
- the shareholding giving rise to the dividends is effectively connected with a permanent establishment in the first country.

2.124 For example, Australia may not tax dividends paid by a Norwegian company to a resident of Norway out of profits derived from Australian sources, unless the Norwegian shareholder has a permanent establishment in Australia with which the holding is effectively connected.

2.125 These restrictions do not apply when the company is, for tax purposes, a resident of both Australia and Norway under the respective laws of the two countries. ***[Article 10, paragraph 6]***

Definition of dividends

2.126 The term ***dividends*** in this Article means income from:

- shares or other rights which participate in profits and are not debt-claims; and
- other amounts that are subject to the same taxation treatment as income from shares in the country of which the distributing company is resident.

[Article 10, paragraph 4]

Limitation of benefits

2.127 The source country rate limits and exemptions available under this Article will not apply where a creation or assignment of shares or other rights in respect of which dividends are paid, has been made with the main objective of, or one of the main objectives of, accessing the relief otherwise available under this Article. ***[Article 10, paragraph 7]***

Article 11 — Interest

2.128 This Article allocates taxing rights in respect of interest flows between Australia and Norway. The Article provides that:

- an exemption from source country tax applies to certain cross-border interest flows to:
  - the government, its monetary institutions or central banks; or
  - financial institutions;
- a maximum 10 per cent rate of source country tax may be applied on all other interest income;
- interest paid on an indebtedness which is effectively connected with a permanent establishment shall be subject to Article 7 (*Business Profits*);
- interest payments are deemed to have an Australian source (and may therefore be taxed in Australia) where:
  - the interest is paid by an Australian resident to a Norwegian resident; or
  - the interest is paid by a non-resident to a Norwegian resident and it is an expense of the payer in carrying on business in Australia through a permanent establishment;
- relief will be restricted to the gross amount of interest which would be expected to be paid on an arm's length dealing between independent parties.

2.129 However, no such relief is available in cases that have been designed with a main purpose of taking advantage of this Article.

Permissible rate of source country taxation

Ten per cent rate limit

2.130 This Article provides for interest income to be taxed by both countries but requires the country in which the interest arises to generally limit its tax to 10 per cent of the gross amount of the interest where a resident of the other country is the beneficial owner of the interest. ***[Article 11, paragraphs 1 and 2]***

Exemptions for interest paid to the Government

2.131 The exemption for interest paid to the Australian and Norwegian Governments reflects the principle of sovereign immunity and will apply to interest derived from the investment of the Government's official reserve assets. Similar exemptions apply in a number of Australia's tax treaties. ***[Article 11, subparagraph 3(a)]***

Exemptions for interest paid to financial institutions

2.132 The exemption for interest paid to financial institutions recognises that the agreed 10 per cent withholding tax rate on gross interest can be excessive given their cost of funds. The exemption will also broadly align the treatment of interest paid to Norwegian financial institutions with the Australian domestic law exemption for interest paid on widely distributed arm's length corporate debenture issues (section 128F of the ITAA 1936). ***[Article 11, subparagraph 3(b)]***

2.133 The term ***financial institution*** means a bank or other enterprise substantially raising debt finance in the financial markets or by taking deposits at interest and using those funds in carrying on the business of providing finance. It does not include a corporate treasury or a member of a group that performs the financing services of the group. ***[Article 11, subparagraph 3(b)]***

2.134 The exemption will not be available for interest paid as part of an arrangement involving back-to-back loans or other arrangement that is economically equivalent and structured to have a similar effect. The denial of the exemption for these back-to-back loan type arrangements is directed at preventing related party and other debt from being structured through financial institutions to gain access to a withholding tax exemption. The exemption will only be denied for interest paid on the component of a loan that is considered to be back-to-back. ***[Article 11, paragraph 4]***

2.135 A back-to-back arrangement would include, for instance, a transaction or series of transactions structured in such a way that:

- a Norwegian financial institution receives or is credited with an item of interest arising in Australia; and
- the financial institution pays or credits, directly or indirectly, all or substantially all of that interest (at any time or in any form, including commensurate benefits) to another person who, if it received the interest directly from Australia, would not be entitled to similar benefits with respect to that interest.

2.136 However, a back-to-back arrangement would generally not include a loan guarantee provided by a related party to a Norwegian financial institution.

Definition of interest

2.137 The term ***interest*** is defined for the purposes of this Article to include interest from:

- government securities;
- bonds and debentures;
- any other forms of indebtedness; and
- income which is subjected to the same taxation treatment as income from money lent by the law of the Contracting State in which the income arises.

[Article 11, paragraph 5]

Interest effectively treated as business profits

2.138 Interest derived by a resident of one country which is paid in respect of an indebtedness which is effectively connected with a permanent establishment of that person in the other country, will form part of the business profits of that permanent establishment and be subject to the provisions of Article 7 (*Business Profits*). Accordingly, the rate limitation of 10 per cent and the exemption for financial institutions do not apply to such interest in the country in which the interest is sourced. ***[Article 11, paragraph 6]***

Deemed source rules

2.139 The source rules which determine where interest arises for purposes of the Article are set out in paragraph 7. They operate to allow Australia to tax interest paid by a resident of Australia to a resident of Norway who is the beneficial owner of that interest. Australia may also tax interest paid by a non-resident, being interest which is beneficially owned by a Norwegian resident, if it is an expense incurred by the payer of the interest in carrying on a business in Australia through a permanent establishment.

2.140 However, consistent with Australia's interest withholding tax provisions, an Australian source is not deemed in respect of interest that is an expense incurred by an Australian resident in carrying on a business through a permanent establishment outside both Australia and Norway (ie, the permanent establishment is in a third country). In that case the interest is deemed to arise in the country in which the permanent establishment is situated. ***[Article 11, paragraph 7]***

2.141 In determining whether a permanent establishment exists in a third country, the principles set out in Article 5 (*Permanent Establishment*) apply. ***[Article 5, paragraph 9]***

Related persons

2.142 This Article includes a general safeguard against payments of excessive interest where a special relationship exists between the persons associated with a loan transaction — by restricting the amount on which the 10 per cent source country tax rate limitation applies to an amount of interest which might have been expected to have been agreed upon if the parties to the loan agreement were dealing with one another at arm's length. Any excess part of the interest remains taxable according to the domestic law of each country but subject to the other Articles of the tax treaty. ***[Article 11, paragraph 8]***

2.143 Examples of cases where a special relationship might exist include payments to a person (either individual or legal):

- who controls the payer (whether directly or indirectly);
- who is controlled by the payer; or
- who is subordinate to a group having common interests with the payer.

2.144 It also covers relationships of blood or marriage and, in general, any community of interests.

Limitation of benefits

2.145 The source country rate limit and exemptions available under this Article will not apply where a creation or assignment of the indebtedness in respect of which interest paid has been made with the main objective, or one of the main objectives, of accessing the relief otherwise available under this Article. ***[Article 11, paragraph 9]***

Article 12 — Royalties

2.146 This Article allocates taxing rights in respect of royalties paid or credited between Australia and Norway. The Article provides that:

- a maximum 5 per cent rate of source country tax may be levied on the gross amount of the royalties;
- royalties paid in respect of a right or property which is effectively connected with a permanent establishment are subject to Article 7 (*Business Profits*);
- equipment royalties are not included within the definition of royalties and will be taxed in accordance with either Article 7 (*Business Profits*) or Article 8 (*Shipping and Air Transport*);
- royalties include payments for spectrum licences;
- royalties are deemed to have an Australian source (and may therefore be taxed in Australia) where:
  - the royalties are paid by an Australian resident to a Norwegian resident; or
  - the royalties are paid by a non-resident to a Norwegian resident and are an expense of the payer in carrying on business in Australia through a permanent establishment; and
- relief will be restricted to the gross amount of royalties which would be expected to be paid on an arm's length dealing between independent parties.

2.147 However, no such relief is available in cases that have been designed with a main purpose of taking advantage of this Article.

Permissible rate of source country taxation

2.148 This Article in general allows both countries to tax royalty flows but limits the tax of the country of source to 5 per cent of the gross amount of royalties beneficially owned by residents of the other country. ***[Article 12, paragraphs 1 and 2]***

2.149 In the absence of a tax treaty, Australia taxes royalties paid to non-residents at 30 per cent of the gross royalty.

2.150 The 5 per cent rate limitation does not apply to natural resource royalties, which, in accordance with Article 6 (*Income from Real Property*), remain taxable in the country of source without limitation of the tax that may be imposed.

Definition of royalties

2.151 The definition of 'royalties' in the Norway Convention reflects most elements of the definition in Australia's domestic income tax law. It includes payments for the supply of scientific, technical, industrial or commercial know-how but not payments for services rendered, except as provided for in subparagraph 3(c). The definition also includes payments for the use of intellectual property stored on various mediums and used in connection with television, radio or other broadcasting (eg, satellite, cable and Internet broadcasting). ***[Article 12, paragraph 3]***

2.152 Payments for the use of, or the right to use industrial, commercial or scientific equipment, which are included in the definition of royalties in the existing Norway treaty, are not included in the definition under the Norway Convention. Such payments for equipment leasing will either be treated as business profits under Article 7 (*Business Profits*) or as profits from international transport operations (for certain leases of ships, aircraft and containers) under Article 8 (*Shipping and Air Transport*). The exclusion of payments for the use of equipment from the *Royalties* Article reflects common international tax treaty practice and recognises that source country taxation on a gross basis may be excessive given low profit margins.

Payments for the supply of know-how versus payments for services rendered

2.153 The OECD Model Commentary deals with the need to distinguish these two types of payments at paragraph 11.3 of the Commentary on Article 12. The Commentary cites the following criteria as relevant for the purpose of making the distinction:

- Contracts for the supply of know-how concern information of the kind described in paragraph 11 (of the Commentary) that already exists or concern the supply of that type of information after its development or creation and include specific provisions concerning the confidentiality of that information.
- In the case of contracts for the provision of services, the supplier undertakes to perform services which may require the use, by that supplier, of special knowledge, skill and expertise but not the transfer of such special knowledge, skill or expertise to the other party.
- In most cases involving the supply of know-how, there would generally be very little more which needs to be done by the supplier under the contract other than to supply existing information or reproduce existing material. On the other hand, a contract for the performance of services would, in the majority of cases, involve a very much greater level of expenditure by the supplier in order to perform their contractual obligations. For instance, the supplier, depending on the nature of the services to be rendered, may have to incur salaries and wages for employees engaged in researching, designing, testing, drawing and other associated activities or payments to sub-contractors for the performance of similar services.

2.154 Payments for design, engineering or construction of plant or building, feasibility studies, component design and engineering services may generally be regarded as being in respect of a contract for services, unless there is some provision in the contract for imparting techniques and skills to the buyer.

2.155 In cases where both know-how and services are supplied under the same contract, if the contract does not separately provide for payments in respect of know-how and services, an apportionment of the two elements of the contract may be appropriate.

2.156 Payments for services rendered are to be treated under Article 7 (*Business Profits*).

Image or sound reproduction or transmission

2.157 The royalty definition includes payments made for the use of, or the right to use, motion picture films. It also covers payments for the use of, or the right to use images or sounds, however reproduced or transmitted, for use in connection with broadcasting. Such images or sounds may be reproduced on any form of media, such as film, tape, CD or DVD, or transmitted electronically, such as by satellite, cable or Internet. Where the images or sounds are for use in connection with any form of broadcasting, such as television, radio or web-casting, the payments will constitute a royalty. ***[Article 12, subparagraph 3(d)]***

Spectrum licences

2.158 Under the Norway Convention payments made for the use of, or right to use, radiofrequency spectrum are treated as royalties. This provision preserves Australia's ability to tax payments for the use in Australia of any part of the radiofrequency spectrum (within the meaning of the *Radiocommunications Act 1992)* specified in such a licence. ***[Article 12, subparagraph 3(e)]***

Forbearance

2.159 Consistent with the existing Norway treaty and Australian tax treaty practice, subparagraph 3(f) expressly treats as a royalty, amounts paid or credited in respect of forbearance to grant to third persons, rights to use property covered by this Article. This is designed to address arrangements along the lines of those contained in *Aktiebolaget Volvo v Federal Commissioner of Taxation* (1978) 8 ATR 747; 78 ATC 4316, where instead of amounts being payable for the exclusive right to use the property they were made for the undertaking that the right to use the property will not be granted to anyone else. This provision ensures that such payments are subject to tax as a royalty payment under the terms of the *Royalties* Article. ***[Article 12, subparagraph 3(f)]***

Other royalties effectively treated as business profits

2.160 As in the case of interest income, the withholding tax rate limitation does not apply to royalties paid in respect of property or rights which are effectively connected with a permanent establishment in the country in which the income is sourced. Such income is subject to full taxation under Article 7 (*Business Profits*). ***[Article 12, paragraph 4]***

Deemed source rules

2.161 The source rules which determine where royalties arise for purposes of this Article effectively correspond, in the case of Australia, with the deemed source rule contained in section 6C (source of royalty income derived by a non-resident) of the ITAA 1936 for royalties paid to non-residents of Australia. They broadly mirror the source rule for interest income contained in paragraph 7 of Article 11 (*Interest*).

2.162 Consistent with Australia's royalty withholding tax provisions, royalty payments that are an expense incurred by an Australian resident in carrying on a business through a permanent establishment outside both Australia and Norway (ie, the permanent establishment is in a third country) will not be subject to tax in Australia. Those royalties are deemed to be sourced in the country in which the permanent establishment is situated. ***[Article 12, paragraph 5]***

2.163 In determining whether a permanent establishment exists in a third country, the principles set out in Article 5 (*Permanent Establishment*) apply. ***[Article 5, paragraph 9]***

Related persons

2.164 Where a special relationship exists between the payer and the beneficial owner of the royalties, the 5 per cent source country tax rate limitation will apply only to the extent that the royalties are not excessive. Any excess part of the royalty remains taxable according to the domestic law of each country but subject to the other Articles of the Norway Convention.

2.165 Examples of special relationships have been provided in respect of the corresponding paragraph in Article 11. ***[Article 12, paragraph 6]***

Limitation of benefits

2.166 The source country rate limit available under this Article will not apply where a creation or assignment of the rights in respect of which royalties paid or credited has been made with the main objective, or one of the main objectives of accessing the relief available under this Article. ***[Article 12, paragraph 7]***

Article 13 — Alienation of Property

Taxing rights

2.167 This Article allocates between the respective countries taxing rights in relation to income, profits or gains arising from the alienation of real property and other items of property.

2.168 The reference to 'income, profits or gains' in this Article is designed to put beyond doubt that a gain from the alienation of property which in Australia is income or a profit under ordinary concepts, will also be taxed in accordance with this Article, rather than Article 7 (*Business Profits*), together with relevant capital gains.

Real property

2.169 Income, profits or gains from the alienation of 'real property' may be taxed by the country in which the property is situated. For the purpose of this Article, the term 'real property' has the same meaning as it has under paragraph 2 of Article 6. Where the property is situated is determined in accordance with paragraph 3 of Article 6 (*Income from Real Property*). ***[Article 13, paragraph 1]***

Permanent establishment

2.170 Paragraph 2 deals with income, profits or gains arising from the alienation of property (other than real property covered by paragraph 1) forming part of the business assets of a permanent establishment of an enterprise. It also applies where the permanent establishment itself (alone or with the whole enterprise) is alienated. Such income, profits or gains may be taxed in the country in which the permanent establishment is situated. This corresponds to the rules for taxation of business profits contained in Article 7 (*Business Profits*). ***[Article 13, paragraph 2]***

Disposal of ships or aircraft

2.171 Income, profits or gains derived by a resident of a country from the disposal of ships or aircraft operated by that resident in international traffic, or of associated property (other than real property covered by paragraph 1), are taxable only in that country. This rule corresponds to the operation of Article 8 (*Ships and Air Transport*) in relation to profits from the international operation of ships or aircraft. ***[Article 13, paragraph 3]***

2.172 For the purposes of this Article, the term 'international traffic' does not include any transportation which commences at a place in a country and returns to another place in that country, after travelling

through international airspace or waters (eg, so-called 'voyages to nowhere' by cruise ships). ***[Article 3, subparagraph 1(k)]***

Shares and other interests in land-rich entities

2.173 Paragraph 4 applies to situations involving the alienation of shares or other interests in companies and other entities, where more than 50 per cent of the value of the assets of that company or other entity is derived, whether directly or indirectly through one or more other interposed entities, from real property situated in the other country. Income, profits or gains from alienation of such shares or interests may be taxed by the country in which the real property is situated. This paragraph complements paragraph 1 of this Article and is designed to cover arrangements involving the effective alienation of incorporated real property, or like arrangements.

2.174 This provision is in line with international practice and ensures that capital gains on a non-resident's indirect, as well as direct, interests in certain targeted assets are taxable by Australia. (Such treatment applies whether the real property is held directly or indirectly through a chain of interposed entities.) While not limited to chains of companies, or even chains of entities, only some of which are companies, the example of chains of companies is used to make clear that the corporate veil should be lifted in examining direct or indirect ownership.

2.175 This provision responds to the tax planning opportunities exposed by the decision of the Full Federal Court in the *Commissioner of Taxation v Lamesa Holdings BV* (1997) 77 FCR 597. It is designed to protect Australian taxing rights over income or gains on the alienation or effective alienation of Australian real property (as defined) despite the presence of interposed bodies corporate or other entities. ***[Article 13, paragraph 4]***

Capital gains

2.176 This Article contains a sweep up provision which reserves the right to tax any capital gains from the alienation of other types of property to the country in which the person deriving the gains is a resident. These would include, for example, gains from the disposal of shares or other interests in an entity (other than a land-rich entity). Such gains derived by Australian residents will be taxable only in Australia, regardless of where the property is situated, and will not be taxed in Norway. The liability of the Australian resident to taxation on such gains will be determined in accordance with Australia's domestic law. ***[Article 13, paragraph 5]***

Article 14 — Income from Employment

Basis of taxation

2.177 This Article generally provides the basis upon which the remuneration of visiting employees is to be taxed. However this Article does not apply in respect of income dealt with separately in:

- Article 15 (*Directors' Fees*);
- Article 16 (*Entertainers and Sportspersons*);
- Article 17 (*Pensions and Annuities*); and
- Article 18 (*Government Service*).

2.178 Generally, salaries, wages and similar remuneration derived by a resident of one country from an employment exercised in the other country may be taxed in that other country. However, subject to specified conditions, there is a conventional provision for exemption from tax in the country being visited where visits of only a short-term nature are involved. ***[Article 14, paragraphs 1 and 2]***

2.179 The following notes reflect agreements reached during the renegotiation of the Norway Convention with regard to the meaning of the term 'employer':

'For purposes of paragraph 2 of Article 14 *Income from Employment*, the two delegations agreed that the term "employer" refers to the person having the rights on the work produced and bearing the relative responsibility and risks. In this context, the substance of any labour hire arrangement will prevail over the form.

Where an intermediary hirer is involved, such as in cases of international hiring out of labour, the employer for purposes of paragraph 2 will be determined having regard to whether the functions of employer were exercised mainly by the hirer or by the user of the labour. Relevant factors that may lead to a conclusion that the user, and not the hirer, is the employer include:

- the hirer does not bear the responsibility or risk for the results produced by the employee's work;
- the authority to instruct the worker lies with the user;
- the work is performed at a place which is under the control and responsibility of the user;

- the remuneration to the hirer is calculated on the basis of the time utilised, or there is in other ways a connection between this remuneration and wages received by the employee;

- tools and materials are essentially put at the employee's disposal by the user;

- the number and qualifications of the employees are not solely determined by the hirer.'

Short-term visit exemption

2.180 The conditions for the exemption for short-term visits are that:

- the period of the visit or visits does not exceed, in the aggregate, 183 days in any 12-month period commencing or ending in the year of income of the visited country;

- the remuneration is paid by, or on behalf of, an employer who is a resident of the same country as the employee; and

- the remuneration is not borne by a permanent establishment which the employer has in the country being visited.

2.181 Where all of these conditions are met, the remuneration so derived will be liable to tax only in the country of residence of the recipient. ***[Article 14, paragraph 2]***

2.182 Where a short-term visit exemption is not applicable, remuneration derived by a resident of Australia from employment in Norway may be taxed in Norway. However, this Article does not allocate sole taxing rights to Norway in that situation.

2.183 Accordingly, Australia would also be entitled to tax that remuneration in accordance with the general rule of the ITAA 1997 that a resident of Australia remains subject to tax on worldwide income. However, in accordance with Article 23 (*Methods of Elimination of Double Taxation*) Australia would be required to in this situation relieve the double taxation.

2.184 Although Article 23 provides for the double tax relief to be provided by Australia to be in the form of the grant of a credit against the Australian tax for the Norwegian tax paid, the exemption with progression method of providing double tax relief in relation to employment income derived in the situation described would normally be applicable in practice pursuant to the foreign service income provisions of section 23AG of the ITAA 1936. This method exempts the income from

foreign employment from tax in Australia, but takes into account the foreign earnings when calculating the Australian tax on other assessable income the person has derived.

Employment on a ship or aircraft

2.185 Income from an employment exercised aboard a ship or aircraft operated in international traffic may be taxed in the country of which the enterprise operating the ship or aircraft is a resident.

2.186 However, income derived in respect of employment exercised aboard either:

- a ship registered in the Norwegian International Ships' register; or
- a Scandinavian Airlines System (SAS) aircraft,

may be taxed only in the country of which the employee is resident. ***[Article 14, paragraphs 3 and 4]***

Article 15 — Directors' Fees

2.187 This Article relates to remuneration received by a resident of one country in the person's capacity as a member of a board of directors, or of a body which performs a similar role to that of a board of directors, of a company which is a resident of the other country. To avoid difficulties in such cases of ascertaining in which country a director's services are performed, and consequently where the remuneration is to be taxed, the article provides that directors' fees and similar payments may be taxed in the country of residence of the company. ***[Article 15]***

Article 16 — Entertainers and Sportspersons

Personal activities

2.188 Under this Article, income derived by visiting entertainers and sportspersons from their personal activities as such may be taxed in the country in which the activities are exercised, irrespective of the duration of the visit. The term 'entertainer' is intended to have a broad meaning and would include, for example, actors and musicians as well as other performers whose activities have an entertainment character, such as comedians, talk-show hosts, participants in chess tournaments or racing drivers. The application of this Article extends to income generated from promotional and associated kinds of activities engaged in by the

entertainer or sportsperson while present in the visited country. ***[Article 16, paragraph 1]***

Safeguard

2.189 Paragraph 2 is designed to ensure that income in respect of personal activities exercised by an entertainer or sportsperson, where derived by another person (eg, a separate enterprise which formally provides the entertainer's or sportsperson's services), may be taxed in the country in which the entertainer or sportsperson performs, whether or not that other person has a permanent establishment in that country. ***[Article 16, paragraph 2]***

Government supported events

2.190 Consistent with the existing Norway treaty, paragraph 3 excludes from the scope of paragraphs 1 and 2 income derived by entertainers or sportspersons from activities performed in a country where the event is wholly or mainly supported by government funds of the other country. In such a case, the income is taxable only in the country of which the entertainer or sportsperson is a resident. ***[Article 16, paragraph 3]***

Article 17 — Pensions and Annuities

2.191 Pensions (not including government service pensions) and annuities (the term 'annuity' as used in this Article is defined in paragraph 2) are taxable only by the country of which the recipient is a resident. The application of this Article extends to pensions and annuity payments made to dependants, for example, a widow, widower or children of the person in respect of whom the pension or annuity entitlement accrued where, upon that person's death, such entitlement has passed to that person's dependants. ***[Article 17, paragraphs 1 and 2]***

Eligible termination payments

2.192 Lump sum payments on the termination of employment are not considered to be pensions and are not covered by this Article. Article 21 (*Other Income*) applies to such payments.

Alimony payments

2.193 Consistent with the existing Norway treaty, the taxing right in respect of alimony and other maintenance payments is allocated solely to the country of residence of the payer. The purpose of this paragraph is to remove any possibility of double taxation of such payments arising by reason of the treatment accorded such payments under the respective domestic law of the two countries. In the case of Australia, those

payments will generally remain exempt from Australian tax under the ITAA 1936 and the ITAA 1997 in the hands of the recipient and non-deductible to the payer. ***[Article 17, paragraph 3]***

Article 18 — Government Service

Salary and wage income

2.194 Salary and wage type income, other than government service pensions or annuities, paid to an individual for services rendered to a government (including a political subdivision or local authority) of one of the countries, is to be taxed only in that country. However, such remuneration will be taxable only in the other country if:

- the services are rendered in that other country;
- the recipient is a resident of, and a national of, that other country; and
- the recipient did not become a resident of that other country solely for the purpose of rendering the services.

[Article 18, paragraph 1]

Government service pensions

2.195 Similarly, any pension (including, in the case of Norway, any national insurance element of that pension) paid to an individual in respect of services rendered to a government (including a political subdivision or local authority) of one of the countries, is to be taxed only in that country. However, such pensions will be taxable only in the other country if the recipient is both a resident and a national of that country. ***[Article 18, paragraph 2]***

Business income

2.196 Remuneration or pensions in respect of services rendered in connection with a business carried on by any governmental authority referred to in paragraph 1 or 2 of this Article is excluded from the scope of the Article. Such remuneration will remain subject to the provisions of Article 14 (*Income from Employment*), Article 15 (*Directors' Fees*) or Article 16 (*Entertainers and Sportspersons*) or Article 17 (*Pensions or Annuities*). ***[Article 18, paragraph 3]***

Article 19 — Students

Exemption from tax

2.197 This Article applies to students who are temporarily present in one of the countries solely for the purpose of their education if the students are, or immediately before the visit were, resident in the other country. In these circumstances, payments from abroad received by the students solely for their maintenance or education will be exempt from tax in the country visited. This will apply even though the student may qualify for tax purposes as a resident of the country visited during the period of their visit.

2.198 The exemption from tax provided by the visited country is treated as extending to payments received by the student for the maintenance of dependent family members who have accompanied the student to the visited country.

Employment income

2.199 Where, however, a student from Norway who is visiting Australia solely for educational purposes undertakes any employment in Australia, for example:

- undertakes some part-time work with a local employer; or
- during a semester break undertakes work with a local employer,

the income earned by that student as a consequence of that employment may, as provided for in Article 14 (*Income from Employment*), be subject to tax in Australia. In this situation, the payments received from abroad for the student's maintenance or education will not, however, be taken into account in determining the tax payable on the employment income that is subject to tax in Australia. No Australian tax would be payable on the employment income if the student qualifies as a resident of Australia for tax purposes during the visit and the taxable income of the student does not exceed the tax-free threshold applicable to Australian residents for income tax purposes.

Article 20 — Offshore Activities

2.200 This Article largely reflects the *Offshore Activities* Article in the existing Norway treaty and gives both countries broad taxing rights over income from offshore activities in connection with exploration for, or exploitation of, natural resources.

Relationship to other Articles

2.201 The *Offshore Activities* Article governs the taxation treatment to apply to activities undertaken in either country's territorial waters or on either country's continental shelf. Where activities fall within the provisions of the Article, this Article will apply over other provisions of the Convention where taxation of the income arising from those activities differs from the result that applies under Article 20 (eg, Article 5 (*Permanent Establishment*) and Article 14 (*Income from Employment*)). ***[Article 20, paragraph 1]***

Deemed permanent establishment and carrying on of business

2.202 A person who is resident in one country and who is carrying on offshore activities in the other country is deemed in relation to the activities to be carrying on business in the other country through a permanent establishment in the other country, where the activities are carried on for a period or periods of more than 30 days in any 12-month period.

2.203 The provision ensures that an enterprise engaged in the exploration for, or exploitation of, natural resources will be treated as having a permanent establishment where, for example, it operates a drilling rig or carries on activities on such a rig, in circumstances where it may not satisfy the definition of permanent establishment contained in Article 5 (*Permanent Establishment*). The provision reflects the importance Australia and Norway place on being able to tax the substantial profits that can flow from offshore activities in the resources sector. ***[Article 20, paragraph 2]***

2.204 The scope of the Article is confined to activities connected with the exploration or exploitation of the seabed or subsoil of the territorial sea and continental shelf of both countries or to the exploration or exploitation of the natural resources of the seabed or subsoil. For the purpose of this Article the term 'natural resources' is not defined and it would accordingly be interpreted having regard to the rules in paragraph 2 of Article 3 (*General Definitions*). ***Natural resource*** is, in the case of Australia, defined under the ITAA 1936 as meaning 'minerals or any other non-living resource of the land, sea-bed or sea'.

Exception to the deemed permanent establishment rule

2.205 Offshore activities will not be deemed to constitute the carrying on of a business through a permanent establishment where the period or periods during which the activities are carried on do not in aggregate exceed 30 days in any 12-month period commencing or ending in the year of income of the country in which the activities are carried out.

2.206 The Article includes an anti-avoidance rule, similar to that in paragraph 4 of Article 5 (*Permanent Establishment*), aimed at countering contract-splitting by related enterprises. This rule ensures that, where associated enterprises carry on substantially the same activities in a country, the periods will be aggregated in determining whether the enterprises have a permanent establishment in the country in which the activities are being carried on.

2.207 As with paragraph 4 of Article 5, concurrent activities of the enterprise and its associates are only counted once, and enterprises are deemed to be associated for the purposes of this paragraph if one is controlled directly or indirectly by the other or if both are controlled directly or indirectly by the same third person or persons. ***[Article 20, paragraph 3]***

Offshore employment income

2.208 Residents of one country who are employed in offshore activities may be taxed in both countries if the employment is exercised offshore in the other country for an aggregate period in excess of 30 days in any 12-month period beginning or ending in the income year of the country in which the employment is exercised. ***[Article 20, paragraph 4]***

2.209 The country of which the employee is a resident will provide a credit for tax paid in the country in which the employment is performed in accordance with Article 23 (*Methods of Elimination of Double Taxation*). In Australia, the provisions of section 23AG will apply to exempt from Australian tax income of a resident from employment that occurs over a continuous period of 91 days or more. In cases where the continuous period or periods is less than 91 days a credit will be allowed by Australia for Norwegian tax on offshore activities employment income against the Australian tax paid on such income.

2.210 No source country tax will be payable by an employee resident in one country and employed in offshore activities exercised in the other if the employee exercises the employment in the other country for a period or periods of 30 days or less and the employer is resident outside the other country. This is measured in the same way as for business activities (see paragraph 2.205). In these circumstances the employee's remuneration will be subject to tax only in the country of which the employee is a resident.

Article 21 — Other Income

Allocation of taxing rights

2.211 This Article provides rules for the allocation between the two countries of taxing rights with respect to items of income not dealt with in the preceding Articles of the Norway Convention. The scope of the Article is not confined to such items of income arising in one of the countries — it extends also to income from sources in a third country.

2.212 Broadly, such income derived by a resident of one country is to be taxed only in the country of residence unless it is from sources in the other country, in which case the income may also be taxed in the other country. This is consistent with Australia's reservation to Article 21 (*Other Income*) of the OECD Model. ***[Article 21, paragraphs 1 and 3]***

2.213 Where the income may be taxed in both countries in accordance with this provision, the country of residence of the recipient of the income is obliged by Article 23 (*Methods of Elimination of Double Taxation*) to provide double taxation relief.

2.214 This Article does not apply to income (other than income from real property as defined in paragraph 2 of Article 6 (*Income from Real Property*) where the right or property in respect of which the income is paid is effectively connected with a permanent establishment which a resident of one country has in the other country. In such a case, Article 7 (*Business Profits*) will apply. ***[Article 21, paragraph 2]***

Article 22 — Source of Income

Deemed source

2.215 This Article effectively deems income, profits or gains derived by a resident of a country which, in accordance with the Norway Convention, may be taxed in the other country, to have a source in that other country. It therefore avoids any difficulties arising under domestic law source rules in respect of the exercise by Australia of the taxing rights allocated to Australia by the Convention over income derived by residents of Norway. ***[Article 22, paragraph 1]***

Source of income — double taxation relief

2.216 Paragraph 2 of this Article deems income, profits or gains of a resident of one country to arise in the other country if those amounts are taxable in the other country under the treaty. The paragraph applies for the purposes of Article 23 (*Methods of Elimination of Double Taxation*)

and for the purposes of the domestic tax laws of the country in which the recipient of the income is resident. ***[Article 22, paragraph 2]***

2.217 This provision is variously included in Article 21 (*Source of Income*) or Article 22 (*Elimination of Double Taxation*) of Australia's tax treaties. It is intended to ensure that where an item of income, profit or gain is taxable in both countries, double taxation relief will be given by the recipient's country of residence in accordance with Article 23, regardless of whether the amount would be regarded as having a source in the country of residence under its ordinary source rules. In this way, income, profits or gains derived by a resident of Australia, which is taxable by Norway under this Convention, will be treated as being foreign income for the purposes of the ITAA 1936 and the ITAA 1997, including the foreign tax credit provisions of the ITAA 1936.

Article 23 — Methods of Elimination of Double Taxation

2.218 Double taxation does not arise in respect of income flowing between Australia and Norway:

- where the terms of the tax treaty provide for the income to be taxed only in one country; or
- where the domestic taxation law of one of the countries exempts the income from its tax.

Tax credit

2.219 It is necessary, however, to prescribe a method for relieving double taxation for other classes of income, profits or gains which, under the terms of the tax treaty, remain subject to tax in both countries. In accordance with international practice, Australia's tax treaties provide for double tax relief to be provided by the country of residence of the taxpayer by way of a credit basis of relief against its tax for the tax of the country of source. This Article also reflects that approach.

Australian method of relief

2.220 This Article requires Australia to provide Australian residents a credit against their Australian tax liability for Norwegian tax paid in accordance with the Norway Convention on income derived from Norwegian sources which are taxable in Australia. The term 'income' in this context is intended to have a broad meaning and includes items of profit or gains which are dealt with under the income tax law. ***[Article 23, paragraph 1]***

2.221 Australia's general foreign tax credit system, together with the terms of this Article and of the Norway Convention generally, will form the basis of Australia's arrangements for relieving a resident of Norway from double taxation on income, profits or gains arising from sources in Norway.

2.222 Accordingly, effect is to be given to the tax credit relief obligation imposed on Australia by paragraph 1 of this Article by application of the general foreign tax credit provisions (Division 18 of Part III) of the ITAA 1936.

2.223 Notwithstanding the credit basis of relief provided for by paragraph 1 of this Article, in relation to salary and wages and like remuneration derived by a resident of Australia during a continuous period of foreign service (as defined in subsection 23AG(7) of the ITAA 1936) in Norway, the exemption with progression method of relief will be applicable.

2.224 Dividends and branch profits derived from Norway by an Australian resident company that are exempt from Australian tax under the foreign source income measures (eg, sections 23AH or 23AJ of the ITAA 1936) will continue to qualify for exemption from Australian tax under those provisions. As double taxation does not arise in these cases, the credit form of relief will not be relevant.

Norwegian relief

2.225 In the case of a resident of Norway who is taxable in Norway on income which is also taxable in Australia under this Convention, this Article requires Norway to allow the Norwegian resident a deduction for the amount of Australian tax paid on that income. The deduction shall not exceed that part of the Norwegian tax which is attributable to the income that is taxable in Australia. ***[Article 23, subparagraph 2(a)]***

2.226 In the case of income derived by a resident of Norway, which is exempted in Norway under the Norway Convention, Norway may nevertheless include such income in the tax base, but shall allow the Norwegian resident a deduction from Norwegian tax for the amount of Norwegian tax attributable to that income. ***[Article 23, subparagraph 2(b)]***

Article 24 — Non-discrimination

2.227 The Norway Convention includes rules to prevent tax discrimination. The Australian tax system is generally non-discriminatory. However, for clarity the Article provides that certain pillars of the Australia tax system should not be seen as coming within the

Article's terms. The measures identified can be characterised as being an integral part of today's administration of Australia's economic and tax policy and the collection of its taxes. As such it has been recognised that the measures carved out do not offend the spirit or intendment of a *Non-discrimination* Article based on the OECD Model Article 24 (*Non-discrimination*).

Discrimination based on nationality

2.228 This Article prevents discrimination on the grounds of nationality by providing that nationals of one country may not be less favourably treated than nationals of the other country in the same circumstances. ***[Article 24, paragraph 1]***

2.229 The discrimination that the Article precludes applies to both taxation and any requirement connected therewith. Accordingly, discrimination in the administration of the tax law is also generally precluded.

2.230 The term ***national*** is defined in Article 3 (*General Definitions*) of the Norway Convention and covers both individuals who have the nationality or citizenship of one country or the other, and companies which 'derive their status as such from the laws in force in that Contracting State'. Accordingly, a company that is incorporated in Australia would be a national of Australia while a company that is incorporated or otherwise constituted under a law of Norway would be a national of Norway for the purposes of this paragraph. ***[Article 3, subparagraph 1(l)]***

The meaning of 'in the same circumstances' and 'in particular with respect to residence'

2.231 The expression 'in the same circumstances' refers to persons who, from the point of the application of the ordinary taxation laws and regulations, are in substantially similar circumstances both in law and in fact.

2.232 Where a person operates in an industry that is subject to government regulation such as prudential oversight, another person operating in the same industry but not subject to the same oversight, would not be in the same circumstances.

2.233 The inclusion of the further clarification 'in particular with respect to residence' makes clear that the residence of the taxpayer is one of the factors that are relevant in determining whether taxpayers are placed in similar circumstances. Therefore, different treatment accorded to a Norwegian resident compared to an Australian resident will not

constitute discrimination for purposes of this Article. A potential breach of paragraph 1 of this Article only arises if two persons who are residents of the same country are treated differently solely by reason of one being a national of Australia and the other a national of Norway.

The meaning of 'other' or 'more burdensome'

2.234 The words 'more burdensome' taxation refer to the quantum of taxation while 'other' taxation may refer to some form of income tax other than the form of income tax to which a national of the country is subject (*Woodend Rubber Co. v Commissioner of Inland Revenue* [1971] A.C. 321 at 332).

2.235 The phrase is also applicable to administrative or compliance requirements that a taxpayer may be called upon to meet where those requirements differ based on nationality grounds.

Non-residents of Australia/Norway

2.236 Unlike paragraph 1 of Article 24 (*Non-discrimination*) of the OECD Model, paragraph 1 of this Article does not apply to persons who are not residents of either Australia or Norway. It follows that residents of third countries cannot seek the benefits of this provision. The provision also does not extend to residents of either country who are not nationals (as defined in Article 3 (*General Definitions*)) of either country.

Non-discrimination and permanent establishments

2.237 Paragraph 2 of this Article provides that the tax on permanent establishments of enterprises of the other country shall not be levied less favourably than on the country's own enterprises carrying on the same activities in similar circumstances. This provision applies to all residents of a treaty country, irrespective of their nationality, who have a permanent establishment in the other country. ***[Article 24, paragraph 2]***

2.238 Paragraph 2 of this Article contains the additional proviso that, for this paragraph to apply, the enterprises of both countries must be 'in similar circumstances'. Therefore, the comparison must be made between a permanent establishment and local enterprises which are not only carrying on the same activities but are also carrying on those activities 'in similar circumstances'. This is to address situations where resident and non-resident enterprises may be carrying on the same activities but the circumstances in which they do so are very different. For example, one may be conducting dealings on a non-arm's length basis and the other on an arm's length basis. The provision recognises that appropriate differences in taxation treatment are not precluded because of the differing circumstances.

2.239 Permanent establishments of non-resident enterprises may be treated differently from resident enterprises as long as the treatment does not result in more burdensome taxation for the former than for the latter. That is, a different mode of taxation may be adopted with respect to non-resident enterprises, to take account of the fact that they often operate in different conditions to resident enterprises. The provision would not affect, for example, domestic law provisions that tax a non-resident by withholding, provided that calculation of the tax payable is not greater than that applying to a resident taxpayer.

Deductions paid to non-residents

2.240 Paragraph 3 of this Article requires the treaty partner countries to allow the same deductions for interest, royalties and other disbursements paid to residents of the other country as it does for such payments to its own residents. However, the paragraph allows the treaty countries to reallocate profits between related enterprises on an arm's length basis under Article 9 (*Associated Enterprises*) and to limit deductions in accordance with paragraph 8 of Article 11 (*Interest*), and paragraph 6 of Article 12 (*Royalties*). ***[Article 24, paragraph 3]***

Companies owned or controlled abroad

2.241 Paragraph 4 of this Article prevents a country from giving less favourable treatment to an enterprise, the capital of which is owned or controlled, wholly or partly, directly or indirectly, by one or more residents of the other country. That is, Australian companies owned or controlled by Norwegian residents may not be given other or more burdensome treatment than locally owned or controlled Australian companies. ***[Article 24, paragraph 4]***

2.242 Differential tax treatment based on residency is not affected by this paragraph. Nor does the paragraph require the same treatment of non-resident shareholders in the company as resident shareholders. Accordingly, there is no obligation under this provision or any other provision of the Article to allow imputation credits to non-resident shareholders.

Exclusions

2.243 Non-resident individuals do not have to be granted the personal allowances, reliefs or reductions available to residents of the tax treaty countries. ***[Article 24, paragraph 5]***

2.244 This means that Australia will continue to be able to grant to resident individuals rebates such as the dependent spouse rebate that are not available to non-residents.

2.245 Unlike paragraph 3 of Article 24 (*Non-discrimination*) of the OECD Model, paragraph 5 of this Article is not just limited to those benefits conferred by a country relating to civil status or family responsibilities of the individual. For Australian tax purposes, it also extends, for example, to the tax-free threshold which may be considered not to be based either on civil status or family responsibilities.

2.246 Paragraph 6 of this Article excludes from the operation of the Article certain provisions of the law of both countries that are important for purposes of economic regulation and integrity of the tax system. Although most are generally recognised by the international community as not being discriminatory, the specific exclusion of these provisions will ensure that they can continue to operate for their intended purpose. The provisions of the law of Australia and Norway to be excluded are those that:

- prevent the avoidance or evasion of taxes;
- defer tax where an asset is transferred out of the jurisdiction;
- provide for consolidation of group entities;
- do not allow tax rebates or credits in relation to dividends paid by a company;
- provide for deductions for research and development expenditure; or
- are agreed in an Exchange of Notes between the two Governments to be unaffected by the Article.

[Article 24, paragraph 6]

Avoidance or evasion provisions

2.247 Subparagraph 6(a) of this Article ensures that the operation of domestic measures to combat avoidance and evasion is not affected by this Article. Paragraph 7 of this Article provides that the reference to laws designed to prevent avoidance or evasion of taxes includes thin capitalisation, dividend stripping, transfer pricing, controlled foreign company, transferor trust and foreign investment fund provisions, and collection measures including conservancy. Although it is commonly accepted by most OECD member countries that such provisions do not contravene *Non-discrimination* Articles, this outcome is specifically provided for in this Convention by the exclusion of such rules from the operation of this Article. ***[Article 24, subparagraph 6(a) and paragraph 7]***

2.248 The enforcement and operation of the various aspects of the withholding tax provisions relating to non-residents are preserved by the operation of subparagraph 6(a) and paragraph 7 of this Article. For example, section 221YRA (Recovery of amounts by the Commissioner) of the ITAA 1936 provides that where interest or royalties are paid to a non-resident and the payer fails to deduct withholding tax that the interest or royalty cannot be claimed as a deduction. No similar measure exists in relation to payments from a resident to another resident.

Capital gains roll-over relief

2.249 This Article will not affect the operation of any provision of domestic tax legislation which does not permit the deferral of tax arising on the transfer of an asset where the transfer of the asset by the transferee would take the asset beyond the taxing jurisdiction of the country. ***[Article 24, subparagraph 6(b)]***

2.250 Under Australia's domestic tax legislation permanent establishments generally enjoy the same tax treatment as resident enterprises. However, roll-over relief is denied to a permanent establishment where an asset with the necessary connection with Australia is transferred to a non-resident if the asset is not an asset with the necessary connection with Australia in the hands of the transferee. Subparagraph 6(b) ensures that Australia will be able to continue to deny roll-over relief in these circumstances.

Consolidation

2.251 Domestic law rules which provide for single entity treatment of a group of entities are excluded from the operation of this Article, provided that there is no discrimination regarding access to consolidation treatment between Australian resident companies on the basis of ownership of the company.

2.252 Australia's consolidation measures are restricted to wholly-owned Australian resident groups. The Article will not apply to these measures, with the result that domestic law provisions continue to operate to preclude permanent establishments of non-resident companies from consolidating with resident entities that may be wholly-owned by a non-resident. ***[Article 24, subparagraph 6(c)]***

Rebates or credits paid by a company

2.253 Domestic law rules of either country which allow an intercorporate dividend rebate or credit are excluded from the operation of this Article. In relation to credits, Australia does not permit non-residents to offset imputation credits against their Australian source income, or to

seek a refund of any excess imputation credits. Subparagraph 6(d) ensures that this Article does not operate to preclude this treatment. ***[Article 24, subparagraph 6(d)]***

Research and development expenditure

2.254 The domestic law research and development provisions are excluded from the operation of this Article. It follows that Australia will be able to continue to apply its domestic law rules concerning access to concessions in respect of research and development expenditure. Currently, these concessions are only available to companies that are incorporated in Australia. ***[Article 24, subparagraph 6(e)]***

Power to carry out an Exchange of Notes

2.255 Subparagraph 6(f) of this Article provides a mechanism for the two Governments to exclude other provisions of domestic law from the operation of the Article. The two countries may agree in an Exchange of Notes that other domestic law provisions will not be affected by the requirements of the Article. ***[Article 24, subparagraph 6(f)]***

Taxes to which the Non-discrimination Article applies

2.256 In the case of Australia, the relevant taxes are primarily the income tax (including the petroleum resource rent tax and tax on capital gains) and the GST and fringe benefits tax. The provisions of this Article also apply to taxes imposed by the Australian states and territories (see also commentary to Article 2 (*Taxes Covered*)).

2.257 In the case of Norway, the relevant taxes are primarily the tax on general income, the tax on personal income, the special tax on petroleum income, the resource rent tax on income from production of hydro-electric power, the withholding tax on dividends and the tax on remuneration to non-resident artistes, etc.

More favourable treatment

2.258 Nothing in this Article prevents either country from treating residents of the other country more favourably than its own residents.

Article 25 — Mutual Agreement Procedure

Consultation on specific cases

2.259 This Article provides for consultation between the competent authorities of the two countries with a view to reaching a solution in cases where a person is able to demonstrate actual or potential imposition of

taxation contrary to the provisions of the Norway Convention. ***[Article 25, paragraph 2]***

2.260 A person wishing to use this procedure may present a case to the competent authority of the country of which the person is a resident. If the case comes under paragraph 1 of Article 24 (*Non-discrimination*) of this Convention, the person must present a case to the competent authority of the country of which the person is a national.

2.261 Presentation of a case by a person to a competent authority must be made within three years of the first notification of the action which the taxpayer considers gives rise to taxation not in accordance with the Norway Convention. Presentation of a case does not deprive the person of access to, or affect their rights in relation to, other legal remedies available under the domestic laws of the countries. ***[Article 25, paragraph 1]***

2.262 If the person's claim seems to the competent authority to which the case has been presented to be justified, and that competent authority is not itself able to solve the problem, then the competent authority is required to seek to resolve the case by mutual agreement with the competent authority of the other country, with a view to avoiding taxation not in accordance with the treaty. ***[Article 25, paragraph 2]***

2.263 If, after consideration by the competent authorities, a solution is reached, it shall be implemented in accordance with the provisions of the Article.

Implementation of a solution

2.264 The solution reached by mutual agreement between the competent authorities of the relevant countries shall be implemented notwithstanding any time limits in the domestic laws of the tax treaty countries. This allows the competent authorities the flexibility to reach a satisfactory solution and avoids problems that might arise where each country has a different time limit in their domestic law. ***[Article 25, paragraph 2]***

Consultation on general problems

2.265 This Article also authorises consultation between the competent authorities of the two countries for the purpose of resolving any difficulties that arise regarding the interpretation or application of the treaty and to give effect to it. This may allow, for example, the competent authorities to agree to apply an agreed solution to a broader range of taxpayers, notwithstanding that the original uncertainty may have arisen in connection with an individual case that comes under the procedure outlined in paragraphs 1 and 2 of this Article.

2.266 Paragraph 3 of this Article also enables the competent authorities to deal with cases of double taxation that do not come within the scope of the Norway Convention. ***[Article 25, paragraph 3]***

Methods of communication between competent authorities

2.267 The competent authorities are permitted to communicate directly with each other without having to go through diplomatic channels. This may be done by letter, facsimile transmission, telephone, direct meetings or any other convenient means. ***[Article 25, paragraph 4]***

General Agreement on Trade in Services (GATS) dispute resolution process

2.268 Paragraph 5 of this Article deals with disputes that may be brought before the World Trade Organisation Council for Trade in Services under the dispute resolution processes of the GATS. ***[Article 25, paragraph 5]***

Background

2.269 Australia and Norway are both parties to the GATS. Article XVII (*National Treatment*) of the GATS requires a party to accord the same treatment to services and service suppliers of other parties as it accords to its own like services and service suppliers.

2.270 Articles XXII (*Consultation*) and XXIII (*Dispute Settlement and Enforcement*) of the GATS provide for discussion and resolution of disputes. Where a measure of another party falls within the scope of a tax treaty, paragraph 3 of Article XXII (*Consultation*) provides that the other party to the tax treaty may not invoke Article XVII (*National Treatment*). However, if there is a dispute as to whether a measure actually falls within the scope of a tax treaty, either country may take the matter to the Council on Trade in Services for referral to binding arbitration.

2.271 Notwithstanding paragraph 3 of Article XXII (*Consultation*) of the GATS, Australia and Norway have agreed that the consent of both countries is required before a dispute as to whether a measure falls within the scope of this Convention may be brought before the Council on Trade in Services. This is seen as the most effective way of dealing with such disputes, and avoids difficult questions as to when a disputed issue falls within the dispute resolution mechanism of this Convention or of the GATS dispute.

2.272 This provision is based, in all essential respects, on an OECD Model commentary recommendation, and is common in recent international treaty practice. ***[Article 25, paragraph 5]***

Article 26 — Exchange of Information

2.273 The Norway Convention aligns the information exchange provisions to the 2005 OECD standard. The Article differs from the previous approach in the following ways:

- The scope is expanded to a wider range of taxes.
- The new provision clarifies that the Commissioner is obliged to obtain information for Norwegian tax authorities regardless of whether Australia has a domestic tax interest in the information sought.
- Bank secrecy laws do not limit the exchange of information.

Foreseeably relevant information

2.274 Article 26 authorises and limits the exchange of information by the two competent authorities to information foreseeably relevant to the administration or enforcement of the relevant taxes. The exchange of information is not restricted by Article 1 (*Persons Covered*) of the treaty, and may therefore cover persons who are not residents of Australia or Norway.

2.275 The standard of foreseeable relevance is intended to ensure that information may be exchanged to the widest possible extent. However, competent authorities are not entitled to request information from the other country which is unlikely to be relevant to the tax affairs of a taxpayer, or to the administration and enforcement of tax laws. ***[Article 26, paragraph 1]***

2.276 The change in wording from that used in the corresponding Article in the existing Norway treaty to a 'foreseeably relevant' standard reflects the wording in Article 26 of the OECD Model and no difference in effect is intended.

Taxes to which this Article applies

2.277 Under the corresponding Article in the existing Norway treaty, the information that could be requested and obtained between the two countries was limited to information in relation to taxes to which the treaty applied (generally income taxes).

2.278 Under this Convention, the range of taxes for which information may be exchanged has been expanded. The Australian competent authority can now request and obtain information concerning all federal taxes administered by the Commissioner from their counterpart in

Norway. This means, for example, that information concerning Australian indirect taxes (ie, the GST) may be requested and obtained from Norway. ***[Article 26, paragraph 1]***

2.279 Similarly, in the case of Norway, the Norwegian competent authority can now request and obtain information concerning taxes of every kind and description imposed under Norwegian tax laws, from the Australian competent authority to the extent that the requested information relates to taxes administered by the Commissioner.

Use of exchanged information

2.280 The purposes for which the exchanged information may be used and the persons to whom it may be disclosed are restricted consistent with the former Article and the approach taken in the OECD Model. Any information received by a country must be treated as secret in the same manner as information obtained under the domestic law of that country and can only be disclosed to the persons identified in paragraph 2 of the Article. ***[Article 26, paragraph 2]***

No domestic tax interest required

2.281 When requested, a country is required to obtain information in the same manner as if it were administering its domestic tax system, notwithstanding that the country may not require the information for its own purposes. Australia would recognise this obligation to obtain relevant information for treaty partner countries, even in the absence of an explicit provision to this effect. ***[Article 26, paragraph 4]***

Limitations

2.282 The country requested to provide information under this Article is not obliged to do so where:

- it would be required to carry out administrative procedures incompatible with its own law or the domestic law and administrative practice, of either Australia or Norway; or

- such information is not obtainable under the domestic law or in the normal course of administration by the competent authority in either Australia or Norway. Australia is not obliged, for example, to use police powers to obtain information requested by Norway, although information gathered in that way which is already in the possession of the Commissioner may be exchanged.

[Article 26, subparagraphs 3(a) and (b)]

2.283 Also, in no case is the country receiving the request obliged to supply information under this Article that would:

- disclose any trade, business, industrial, commercial or professional secret or trade process; or
- be contrary to public policy.

[Article 26, subparagraph 3(c)]

Information held by banks, other financial institutions, nominees etc

2.284 This paragraph ensures that paragraph 3 of this Article cannot be used to prevent the supply of information solely because the information is held by banks, other financial institutions, nominees etc. The inclusion of this paragraph in the Norway Convention should not be interpreted as suggesting the corresponding Article of the existing Norway treaty did not cover the exchange of such information. Inclusion of paragraph 5 merely clarifies Australia's current treaty practice, and reflects recent changes to Article 26 (*Exchange of Information*) of the OECD Model. ***[Article 26, paragraph 5]***

Article 27 — Assistance in the Collection of Taxes

Assistance in the collection of taxes

2.285 Article 27 (*Assistance in the Collection of Taxes*) authorises and requires Australia and Norway to provide assistance to each other in the collection of revenue claims. This assistance is not to be restricted by the terms of Article 1 (*Personal Scope*) of the treaty. Assistance must therefore be provided as regards a revenue claim owed to either country by any person, whether or not a resident of Australia or Norway. The form of the assistance is set out in paragraphs 3 and 4 of this Article. ***[Article 27, paragraph 1]***

2.286 The term ***revenue claim*** is defined for the purposes of this Article to mean an amount owed in respect of taxes referred to in Article 2 (*Taxes Covered*) of the treaty. A revenue claim may cover any Norwegian tax, or any Australian federal tax administered by the Commissioner, but only insofar as the imposition of such taxes is not contrary to this treaty or any other instrument in force between Australia and Norway. It also applies to interest, administrative penalties and costs of collection or conservancy related to such amount. ***[Article 27, paragraph 2]***

2.287 This Article will apply from the date agreed in an exchange of notes through the diplomatic channel. ***[Article 29, subparagraph 1(d)]***

Enforceable revenue claims

2.288 Assistance in collection will only be provided by Australia in relation to a revenue claim that is enforceable in Norway. Similarly, Norway is not required to provide assistance in collection in respect of an Australian revenue claim that is not enforceable in Australia. A revenue claim will be enforceable where the requesting country has the right, under its domestic law, to collect the revenue claim. Further, the revenue claim must be owed by a person who, at that time, under the law of that country, has no administrative or judicial rights to prevent its collection.

2.289 Paragraph 3 of this Article regulates the way in which the revenue claim of the requesting country is to be collected by the requested country. Other than in relation to time limits and priority (see paragraphs 2.293 to 2.294), the requested country is required to collect the revenue claim as though it were its own revenue claim. This obligation applies even if, at that time, the requested country has no need to undertake collection actions related to that taxpayer for its own tax purposes. ***[Article 27, paragraph 3]***

2.290 Where a request from Norway concerns a tax that does not exist in Australia, Australia will follow the procedure applicable to a claim for a similar Australian tax or any other appropriate procedure if no similar tax exists.

Measures of conservancy

2.291 Paragraph 4 of this Article enables Australia or Norway to request the other country to take measures of conservancy even where it cannot yet ask for assistance in collection, such as where the revenue claim is not yet enforceable or when the debtor still has the right to prevent its collection. An example of a conservancy measure is the seizure or the freezing of assets before final judgment to guarantee that the assets will still be available when collection can subsequently take place.

2.292 If requested to do so by Norway, Australia is required to take measures of conservancy in respect of the revenue claim in accordance with the provisions of Australian law as if the revenue claim were an Australian revenue claim. Although Australia does not have specific conservancy measures, the Commissioner may apply for a *Mareva* injunction, which would prevent the taxpayer and the taxpayer's associates from dealing with certain assets. ***[Article 27, paragraph 4]***

Time limits

2.293 Paragraph 5 of this Article provides that the requested country's domestic law time limitations beyond which a revenue claim cannot be enforced or collected do not apply to a revenue claim in respect of which the other country has made a request for assistance in collection. Rather, the time limits of the requesting country apply. ***[Article 27, paragraph 5]***

Priority of claims

2.294 Paragraph 5 of this Article also provides that any rules of Australia and Norway which give priority to tax debts over the claims of other creditors do not apply to a revenue claim of the other country. This restriction applies regardless of the fact that the requested country must generally treat the claim as its own revenue claim.

2.295 The words 'by reason of its nature as such' in paragraph 5 indicate that any time limits and priority rules to which the paragraph applies are only those that are specific to unpaid taxes. Consequently, paragraph 5 does not prevent the application of general rules concerning time limits or priority which would apply to all debts, such as rules giving priority to a claim by reason of that claim having arisen or having been registered before another one. ***[Article 27, paragraph 5]***

Restriction on judicial and administrative proceedings

2.296 Paragraph 6 of this Article ensures that any legal or administrative objection concerning the existence, validity or the amount of a revenue claim of the requesting country is to be exclusively dealt with in that country. For example, no legal or administrative proceedings, such as a request for judicial review, may be initiated in Australia with respect to the existence, validity or amount of a Norwegian revenue claim. ***[Article 27, paragraph 6]***

Change in circumstances

2.297 Paragraph 7 of this Article deals with the situation where the conditions in paragraph 3 or 4 are no longer satisfied after a request for assistance has been made, but before the revenue claim has been collected and remitted by the requested country. An example of such a situation would be where a request for assistance in collection has been made by Norway, but the revenue claim ceases to be enforceable in Norway prior to its collection by Australia.

2.298 Where the relevant conditions in paragraph 3 or 4 of this Article are no longer satisfied, paragraph 7 requires the competent authority of

the requesting country to promptly notify the competent authority of the requested country of that fact.

2.299 Following such notification, the requested country has the option to ask the requesting country to either suspend or withdraw its request for assistance. If the request is suspended, the suspension applies until such time as the requesting country informs the other country that the conditions necessary for making a request as regards the revenue claim are again satisfied or that it withdraws its request. ***[Article 27, paragraph 7]***

Limitations

2.300 Paragraph 8 of this Article contains certain limitations to the obligations imposed on the country which receives a request for assistance. The requested country is permitted to refuse the request for assistance where those limitations apply.

2.301 The first limitation is that the requested country is not required to exceed the bounds of its own domestic laws and administrative practice or those of the other country in fulfilling its obligations under the Article. ***[Article 27, subparagraph 8(a)]***

2.302 However, subparagraph 8(a) of this Article does not prevent Australia from applying administrative measures to collect a Norwegian revenue claim, even though invoked solely to provide assistance in the collection of Norwegian taxes.

2.303 Subparagraph 8(b) limits the application of this Article where it would require the carrying out of measures that are contrary to public policy, such as where providing assistance may affect the vital interests of the country itself. ***[Article 27, subparagraph 8(b)]***

2.304 The third limitation provides that neither country is obliged to satisfy a request for assistance if the other country has not pursued all reasonable measures of collection or conservancy that are available under its own laws or administrative practice. ***[Article 27, subparagraph 8(c)]***

2.305 Under subparagraph 8(d) of this Article either country may reject a request for assistance on the basis of practical administrative considerations such as when the costs of recovering a revenue claim would exceed the amount of the revenue claim itself. ***[Article 27, subparagraph 8(d)]***

2.306 The final limitation allows either country to refuse to provide assistance if it considers that the taxes with respect to which assistance is requested are imposed contrary to generally accepted taxation principles. ***[Article 27, subparagraph 8(e)]***

Article 28 — Members of Diplomatic Missions and Consular Posts

2.307 The purpose of this Article is to ensure that the provisions of the tax treaty do not result in members of diplomatic missions, permanent missions and consular posts receiving less favourable treatment than that to which they are entitled in accordance with international conventions. Such persons are entitled, for example, to certain fiscal privileges under the *Diplomatic Privileges and Immunities Act 1967 and the Consular Privileges and Immunities Act 1972* which reflect Australia's international diplomatic and consular obligations. ***[Article 28, paragraph 1]***

Prevention of double non-taxation

2.308 Consistent with Norwegian treaty practice, paragraph 2 ensures that double non-taxation does not arise where income is not subject to tax in the country to which the diplomat or consular official is posted as a result of tax privileges granted to diplomats and consular officers under general rules of international law or under international agreements. In these circumstances, paragraph 2 provides that the country of which the diplomat or consular official is a representative will have the right to tax that income. ***[Article 28, paragraph 2]***

Article 29 — Entry into Force

Date of entry into Force

2.309 This Article provides for the entry into force of the Norway Convention. The treaty will enter into force on the last date on which diplomatic notes are exchanged notifying that the domestic processes to give the Convention the force of law in the respective countries has been completed. In Australia, enactment of the legislation giving the force of law in Australia to the Convention along with tabling the treaty in Parliament are prerequisites to the exchange of diplomatic notes. ***[Article 29, paragraph 1]***

Date of application for Australian taxes

Withholding taxes

2.310 Once it enters into force, the Norway Convention will apply in Australia in respect of withholding tax on income that is derived by a non-resident in relation to income derived on or after 1 January in the calendar year next following the date on which the tax treaty enters into force. ***[Article 29, sub-subparagraph 2(a)(i)]***

Other Australian taxes

2.311 The Norway Convention will first apply to other Australian taxes on income, profits or gains of the Australian year of income beginning on or after 1 July in the calendar year next following the date on which the tax treaty enters into force.

2.312 Where a taxpayer has adopted an accounting period ending on a date other than 30 June, the accounting period that has been substituted for the year of income beginning on 1 July in the calendar year next following the date on which the Norway Convention enters into force will be the relevant year of income for the purposes of the application of such Australian tax. ***[Article 29, sub-subparagraph 2(a)(ii)]***

Date of application in Norway

2.313 In Norway, the Norway Convention will have effect in relation to taxes on income, in the calendar year next following that in which the treaty enters into force and subsequent years. A calendar year includes accounting periods beginning in any such year. ***[Article 29, subparagraph 2(b)]***

Exchange of information application date

2.314 Article 26 (*Exchange of Information*) will first apply from the date of entry into force of the treaty. It applies to requests for exchange of information in respect of taxes of every kind and description imposed under the federal tax laws administered by the Commissioner, received on or after that date. However, information that may relate to the income tax affairs of a taxpayer may predate entry into force of the Convention. ***[Article 29, subparagraph 2(c)]***

Assistance in collection of taxes date of application

2.315 Article 27 (*Assistance in the Collection of Taxes*) will first have effect from the date agreed in an exchange of notes between Australia and Norway. ***[Article 29, subparagraph 2(d)]***

Termination of the existing Norway treaty

2.316 The existing Norway treaty shall be terminated and cease to have effect from the dates on which the Norway Convention commences to have application for the respective taxes. ***[Article 29, paragraph 3]***

Article 30 — Termination

2.317 The Norway Convention is to continue in effect indefinitely. However, either country may give written notice of termination of the Convention through the diplomatic channel at least six months before the end of any calendar year beginning after the expiration of five years from the date of its entry into force. ***[Article 30]***

Cessation in Australia

2.318 In the event of either country terminating the Norway Convention, the tax treaty would cease to be effective in Australia for the purposes of:

- withholding tax on income derived by a non-resident in relation to income derived on or after 1 January in the calendar year next following that in which the notice of termination is given; and
- other Australian taxes in relation to income, profits or gains in the Australian year of income commencing on or after 1 July in the calendar year next following that in which the notice of termination is given.

[Article 30, subparagraph (a)]

Cessation in Norway

2.319 The Norway Convention would correspondingly cease to be effective in Norway for the purposes of taxes on income relating to the calendar year (including accounting periods beginning in such year) next following that in which the notice is given. ***[Article 30, subparagraph (b)]***

Chapter 3
Regulation impact statement for the 2006 France Convention

Background

How tax treaties operate

3.1 Tax treaties reduce or eliminate double taxation caused by the exercise of source and residence country taxing rights on cross-border income flows. They do so by treaty partners agreeing (in certain situations) to limit taxing rights over various types of income. The respective countries also agree on methods of reducing double taxation where both countries exercise their right to tax.

3.2 In addition, tax treaties provide an agreed basis for determining the allocation of profits within a multinational company and whether the profits on related party dealings by members of a multinational group operating in both countries reflect the pricing that would be adopted by independent parties. Tax treaties are therefore an important tool in dealing with international profit shifting through transfer pricing.

3.3 To prevent fiscal evasion, tax treaties include provision for exchange of information held by the respective revenue authorities. Treaties may also provide for cross-border collection of tax debts, and may preclude certain types of tax discrimination. Taxpayers can also avail themselves of the mutual agreement procedures provided for in treaties which allow the two revenue authorities to consult with a view to developing a common interpretation and to resolving differences arising out of application of the treaty.

3.4 Australia seeks an appropriate balance between source and residence country taxing rights. Generally the allocation of taxing rights under Australian tax treaties is similar to international practice as set out in the Organisation for Economic Co-operation and Development (OECD) *Model Tax Convention on Income and on Capital* (OECD Model) (Australia being a member of the OECD and involved in the development of that Model). There are, however, a number of instances where Australian practice favours source country taxing rights rather than the residence approach of the OECD Model.

The France tax treaty

3.5 The existing tax treaty with France was signed on 13 April 1976 (the existing France treaty) and has been in effect in Australia since the income year commencing 1 July 1972 in respect of income taxes and 1 January 1973 in respect of withholding taxes. The treaty was amended by a Protocol signed on 19 June 1989 and having effect in Australia in respect of income taxes derived on or after 1 July 1991. Amendments to the *Royalties* Article and the *Pensions* Article took effect from 20 June 1989 and 1 July 1987 respectively.

3.6 There is also a separate *Agreement between the Government of the Commonwealth of Australia and the Government of the French Republic for the Avoidance of Double Taxation of Income Derived from International Air Transport* (the Airline Profits Agreement) with France which was signed on 27 March 1969 and which has been in effect in Australia since the income year commencing 1 July 1966.

3.7 With the entry into force of the Protocol to the United States (US) tax Convention on 12 May 2003 Australia is obliged, under the existing France treaty to provide most favoured nation (MFN) treatment in respect of the rates of tax applicable to dividends, interest and royalties[1].

3.8 With the entry into force of the new tax treaty with United Kingdom (UK) on 17 December 2003, Australia is also obliged to negotiate the inclusion of a non-discrimination Article that operates to protect taxpayers operating in foreign jurisdictions from discriminatory tax practices.

3.9 While the triggering of the MFN clauses imposes certain obligations on Australia, it also presents an opportunity to update certain aspects of the current France treaty including clarifying Australia's rights to apply capital gains tax (CGT).

1 Most favoured nation clauses require a country to enter into negotiations with a view to providing similar treatment to its treaty partner if it subsequently agrees with a third country to a certain specified tax treatment.

Australia's investment and trade relationship with the Republic of France[2]

Bilateral trade

3.10 Australia's commercial links with France are substantial but one-sided, with the balance of trade increasing further in France's favour in recent years. France is Australia's 14th largest merchandise trading partner and 11th largest supplier of imports but is ranked only 22nd as a destination for Australian merchandise exports.

3.11 Australia's merchandise exports to France for 2005 stood at A$1.1 billion, while Australian merchandise imports from France were A$5.3 billion for the same period. Australia's merchandise trade deficit with France totalled A$4.2 billion in 2005-06. Australia's exports to France in 2005-06 were dominated by commodities, particularly coal and iron ore. Medical instruments, medicaments and aircraft and parts were the major manufactured export items. Major products imported from France in 2005-06 were aircraft and parts, medicaments and passenger motor vehicles.

3.12 Two way services trade between Australia and France stood at a total of A$1.18 billion (with a French surplus of A$164 million) in 2005-06.

Bilateral investment

3.13 Total French investment in Australia as at 31 December 2005 was valued at A$15.1 billion. Foreign direct investment from France in Australia was valued at A$8.3 billion, making France the 7th largest direct investor in Australia. Major French investments have been made in the financial services, telecommunications, pharmaceuticals, energy, resources and agribusiness sectors. Some important examples include:

- the acquisition of a 51 per cent stake in National Mutual by insurer AXA;
- Pernod-Ricardi's purchase of the Orlando-Wyndham group;
- the participation of Vivendi in the successful bid for the A$1.5 billion project to manage South Australian Water;

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2 Source: Department of Foreign Affairs and Trade.

- Transroute's participation in the construction consortium concerning the A$1.5 billion Melbourne City link toll-road; and

- the purchase of Australian Defence Industries by Thales, as part of a 50/50 joint venture with Australian engineering group, Transfield.

3.14 There are now close to 300 companies in Australia with a French association employing some 70,000 people, with an annual turnover of 12 billion Euros, or A$20 billion. A number of companies have chosen to headquarter their regional operations in Australia — such as AXA — or to build very substantial offices with considerable regional responsibilities — such as the hotel group Accor.

3.15 In December 2001, the Australian Defence Material Organisation signed an A$1.3 billion contract with France-based company Eurocopter for the delivery and through-life support of 22 'Tiger Armed Reconnaissance' helicopters for the Australian Army, with four to be built in Europe and the remaining 18 assembled at the Australian Aerospace facility in Brisbane, generating up to 180 jobs during the assembly phase. The first two helicopters arrived in Australia in November 2004 and the first Australian built helicopter rolled out on 18 July 2005. In August 2004, Australia also signed an A$1 billion contract with Eurocopter for the delivery of 12 MRH-90 'troop lift' helicopters to the Australian Defence Force.

3.16 Australian investment in France received a significant boost in December 2005 with the French Government's announcement of Macquarie Bank's successful tender — with its French partner Eiffage — for the privatisation of the Autoroutes Paris Rhin Rhône tollway. Macquarie is expected to invest around A$3.9 billion in the project. Prior to this, total Australian investment in France (as at 31 December 2005) was valued at A$14.9 billion, including investments in the south west of France by the surf and sportswear companies, Billabong and Rip Curl; Oceanis Australia Pty Ltd's construction of the largest aquarium in France; VitaMan's launch of the first Australian grooming range for men in France; and Ingeus's involvement in the French employment services market.

Specification of policy objectives

3.17 The objective of the measure is to:

- meet Australia's MFN obligations[3];
- promote closer economic cooperation between Australia and France by reducing possible tax barriers to trade and investment between the two countries; and
- upgrade the framework through which the tax administrations of Australia and France can prevent international fiscal evasion.

Identification of implementation options

3.18 The internationally accepted approach to meeting the policy objectives specified above is to:

- amend an existing treaty to reflect current policies (amending Protocol); or
- conclude a new bilateral tax treaty [4].

Option 1: Limited amending Protocol (most favoured nation obligations) — rely on the existing France tax treaty measures

3.19 In general terms, option 1 relies on the existing France tax treaty measures with an amending Protocol covering, at a minimum, Australia's MFN obligations (dividends, interest and royalties[5]). Australia would also seek to clarify Australia's rights to tax capital gains.

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3 Australia's MFN obligations will be met by the conclusion of the new France Convention even though negotiators were not able to agree on satisfactory rules dealing with non-discrimination. Since the current French and Australian tax systems generally do not discriminate in ways that would breach non-discrimination rules, and European Union law constraints are likely to ensure that the French tax system remains non-discriminatory, the non-inclusion of such rules is unlikely to have a negative impact for taxpayers.

4 There are very few multilateral tax treaties, which reflect the widely differing economic interests and unique tax law structures of most countries.

5 See footnote 3 for details on the non-discrimination MFN obligation.

Option 2: Amending Protocol covering most favoured nation obligations and revising the current treaty to the extent possible without entering into a complete renegotiation

3.20 Option 2 is to deal with a number of other issues, in addition to those proposed under option 1, on which both sides would like to modify the treatment in the current treaty but which are not likely to be contentious. Additional areas include the tax treatment of residual types of income not covered by the other Articles of the treaty, integrity measures and clarifying the application of the treaty to each country's controlled foreign corporation regimes (a French requirement).

Option 3: Conclude a new tax treaty

3.21 Option 3 is to conclude a new bilateral tax treaty to reflect the current tax treaty policies and practice of both countries.

3.22 A new tax treaty would be largely based on the current OECD Model and the United Nations *Model Double Taxation Convention between Developed and Developing Countries* (UN Model), with some mutually agreed variations reflecting the economic, legal and cultural interests of the two countries. It would also dispense with the need for the separate 1969 Airline Profits Agreement with France.

3.23 Both countries have particular policy objectives to achieve in updating the tax treaty and the end result ultimately represents compromises necessary to achieve a mutually acceptable agreement. The key changes in the new tax treaty are:

- a reduction in the maximum royalty withholding tax rates from 10 per cent to 5 per cent;

- a reduction in interest withholding tax from 10 per cent to zero where interest is paid to a financial institution or body performing governmental functions;

- a reduction of dividend withholding tax from 15 per cent to zero for dividends paid out of profits that have borne the normal rate of company tax on non-portfolio holdings of 10 per cent or more and to 5 per cent dividend withholding tax for other non-portfolio holdings;

- the inclusion of a comprehensive *Alienation of Property* Article which allocates taxing rights over capital gains; and

- improved integrity measures — in particular, rules to allow for the cross-border collection of tax debts and updated rules for the exchange of information on tax matters.

Assessment of impacts (costs and benefits) of each option

Difficulties in quantifying the impacts of tax treaties

3.24 Only a partial analysis of costs and benefits can be provided because all the impacts of tax treaties cannot be quantified. While the direct cost to Australian revenue of withholding tax changes can be quantified relatively easily, other cost impacts such as compliance costs are inherently difficult to quantify. There are also efficiency and economic growth factors that make the gains or losses to Australia difficult to estimate (especially as the impact will differ across different sectors of the economy). Analysis has been conducted to establish plausible impacts on Australian economic activity and consequent tax revenue flowing from implementation of the tax treaty. The tax revenue estimates are subject to more uncertainty than the estimates of costs but are best estimates based on the available information, current estimation techniques, likely behavioural responses, and data accuracy.

3.25 Benefits that flow to business are generally equally difficult to quantify. The evidence from international consideration of the costs and benefits of treaties previously undertaken (eg, by the OECD) and from consultation with business strongly indicates, however, that while the quantum of benefits is very difficult to assess, a modern tax treaty provides a clear positive benefit to trade and investment relationships.

Impact group identification

3.26 A revised tax treaty with France is likely to have an impact on:

- Australian residents doing business with France, including principally:
  - Australian residents investing directly in France (either by way of a subsidiary or a branch);
  - Australian banks lending to French borrowers and vice versa;
  - Australian residents supplying technology and know-how to French residents and vice versa;

  - Australian residents supplying consultancy services to France; and
  - Australian residents exporting to France;
- Australian residents receiving pensions from France;
- the Australian Government; and
- the Australian Taxation Office (ATO).

Assessment of benefits

3.27 All options would address long term business concerns about the lack of competitiveness of Australia's tax treaty network, with business particularly seeking reductions in withholding tax rates.

3.28 These issues were addressed in the updated Convention with the UK and the Protocol amending the Convention with the US. Extending similar treatment to France aligns treatment, where possible, in Australia's recent tax treaties, maintains the integrity of Australia's treaty network and discourages treaty shopping (and the consequent degradation of the tax base of countries where the costs of capital and intellectual property are higher under their treaties as a result of the higher withholding tax rates). While a reduction in maximum withholding tax rates will involve a cost to revenue, there are expected to be benefits to the revenue and to the wider economy arising out of increased business and investment activity, with the most direct benefits accruing to business.

Benefits common to all options

3.29 The economic benefits of the expected major changes which are common to all three options, are summarised in paragraphs 3.30 to 3.34.

Dividends

3.30 A lower rate of withholding tax on non-portfolio dividends (10 per cent ownership requirement) would, as the MFN clause in the existing treaty aims to do, reduce the cost of capital to Australian business, as well as reduce distortions in the raising of capital that results from the more favourable terms that apply bilaterally in the case of the US and the UK. This provides broad reciprocity with Australia's domestic exemption for franked dividends.

Interest

3.31 A nil Australian interest withholding tax rate on interest derived by French financial institutions will be consistent with the exemption currently provided under domestic law for interest derived from widely distributed arm's length debenture issues. It also recognises that a 10 per cent interest withholding tax rate on gross interest derived by financial institutions may be excessive given their cost of funds. It should, accordingly, lower the costs of borrowing in those cases where the financial institution can pass the cost represented by the withholding tax on to the Australian borrower. Conversely, it may encourage French businesses to source funds from Australian banks.

Royalties

3.32 Australian residents required to meet the cost of Australian royalty withholding tax on royalty payments made to French residents would benefit from a reduced royalty withholding tax rate. Commercial practice indicates that, as with interest, the cost represented by the royalty withholding tax is commonly passed on to the payer of the royalty. This means that they may bear the cost of higher rates of withholding tax and place them at a competitive disadvantage in competing with businesses from other countries with lower rates. The effect of lowering the cost of new technology and intellectual property may encourage the development of Australia's economy through use of the most up to date technology and processes. Conversely, it may encourage the French to use Australian technology and intellectual property.

Alienation of Property

3.33 The updating of the *Alienation of Property* Article to address taxing rights over capital gains would provide certainty to taxpayers and reduce the risk of double taxation. Australia's source country taxing rights over capital gains on real property, land-rich companies and assets which form the business property of a permanent establishment in Australia would be retained. More generally, the changes bring into line Australia's treaty practice with international practice. This will encourage investment in Australia and result in generally lower compliance costs.

Compliance and administration cost reduction benefits

3.34 Tax exemptions in respect of withholding taxes are likely to reduce compliance and administration costs associated with remitting and claiming credits for such tax.

Comparative advantage of option 1

3.35 Option 1 involves minimal changes to the existing treaty.

Comparative advantages of option 2

3.36 The advantage of option 2 is that Australia, in addition to addressing its MFN obligations, would be able to achieve improved integrity measures, in particular, rules to allow for the cross-border collection of tax debts and updated rules for the exchange of information on tax matters.

3.37 This option represents an advance on option 1 and recognises that the rates of withholding tax negotiated in the US Protocol were agreed as part of an overall package of measures (including CGT coverage). It would allow Australia to seek a more balanced update of the existing treaty.

Comparative advantages of option 3

Renegotiation provides a better outcome for all stakeholders

3.38 While the existing France tax treaty has provided a good measure of protection against double taxation and prevention of fiscal evasion since coming into force, it is clear that it has become outdated (eg, no coverage of CGT) and no longer reflects current tax treaty policies and practices of either Australia or France.

3.39 A new tax treaty would provide benefits to Australian business and to the Australian revenue by ensuring certainty of legislative outcomes based on the treaty. It would be another step forward in providing Australian business with an internationally competitive tax treaty network and business tax system.

3.40 A renegotiated treaty will provide a better outcome for all stakeholders. Given the long-term nature of such arrangements, a revised tax treaty is expected to promote greater certainty than the existing tax treaty. It would also be consistent with the Government's decision in response to the *Review of International Taxation Arrangements,* to move towards a more residence-based tax treaty policy, and would contribute to the updating of Australia's ageing treaty network.

Other benefits

3.41 Where Australians invest directly in France, the existing treaty prevents France from taxing the business profits of an Australian resident unless that Australian resident carries on business through a permanent

establishment in France. A revised tax treaty would further refine the concept of when a permanent establishment should be taken to exist and the level of activity that would constitute a permanent establishment. This principle also applies where a French resident invests directly into Australia. Other benefits also include:

- the appropriate treatment of income derived through partnerships; and
- the protection of Australian expatriates who temporarily reside in France from paying French capital taxes on non-French assets.

Revenue benefits

3.42 New treaty arrangements with France would represent a significant step in facilitating a competitive and modern treaty network for Australian companies and would help to maintain Australia's status as an attractive place for business and investment. While a reduction in maximum withholding tax rates will involve a cost to revenue, there are expected to be benefits to the revenue and to the wider economy arising out of increased business and investment activity, with the most direct benefits accruing to business.

Compliance and administration cost reduction benefits

3.43 The closer alignment with more recent Australian and international treaty practice would generally be expected to reduce compliance costs. In particular, interpretative issues relating to the extent Australia can tax capital gains under the existing France tax treaty arrangements has resulted in considerable uncertainty and the risk of costly legal arguments.

3.44 Administrative costs in explaining the ATO view and responding to legal arguments would also be significantly reduced. Clarifying other areas of uncertainty, such as tax treaty tests of 'residency' and updating the treaty text, should also decrease compliance costs.

Improved international relationships

3.45 New treaty arrangements with France will also assist the bilateral relationship by updating an important treaty in the existing network of commercial treaties between the two countries. It would also promote greater cooperation between taxation authorities to prevent fiscal evasion and tax avoidance. Updating the tax treaty to take account of changes to the OECD Model would also help to maintain Australia's

status as an active OECD member, which in turn would maintain Australia's position in the international tax community.

Assessment of costs

Costs common to all options

Revenue costs

3.46 Treasury has estimated that the revenue impact of the first round effects of the proposals would be around $10 million per annum across the forward estimates period. The three options do not present material differences in estimated direct cost to revenue as the only identifiable costs to revenue are associated with the reductions in dividend, interest and royalty withholding tax rates.

Administrative costs

3.47 The administrative impacts on the ATO in administering the changes made by any revised treaty arrangements are considered to be minimal. Some formal interpretive advice may be required, for example, private binding rulings, concerning the application of the new treaty arrangements. ATO staff, clients and tax professionals will need to be made aware of the entry into force and changes from the previous treaty. Therefore a number of ATO information products will need to be updated.

3.48 The costs of negotiation and enactment of new tax treaty arrangements with France are minimal and have mostly been borne by Treasury and the ATO. There will also be an unquantified but small cost in terms of parliamentary time and drafting resources in enacting the proposed new tax treaty arrangements.

3.49 There are also 'maintenance' costs to the ATO associated with tax treaties in terms of dealing with enquiries, rulings and other interpretative decisions and mutual agreement procedures (including advance pricing arrangements). These costs also apply to the existing arrangements. By bringing the France treaty into basic conformity with recent treaty practice these costs would be reduced. However, as treaties are deals struck between the two countries that reflect specific features of the bilateral relationship, some level of differential treatment or wording between treaties, which may require interpretation or explanation by the ATO, is inevitable.

Other costs

3.50 Government policy flexibility in relation to taxation of French residents would be to some extent constrained by changes to treaty obligations, but as the more significant changes would accord with the Government's tax treaty policy the cost of such constraints should be outweighed by the benefits. Ultimately, the tax treaty could be terminated if it became inconsistent to a significant degree with Government policy. Such termination is very rare in international tax treaty practice, however, and could be expected to be resisted by the business community and others who benefit from the treaty.

3.51 The impact of new tax treaty arrangements on tax policy flexibility is generally quite minimal as tax treaties are based on broad and generally accepted taxation principles.

Costs common to options 1 and 2

3.52 Options 1 and 2 primarily represent a continuation of the current treaty position subject to adjustment to withholding tax rates. Accordingly, administration and compliance costs that apply to the existing France tax treaty would not change materially.

Taxpayers

3.53 Even though these options would address Australia's MFN obligations, they would leave a number of areas of significant difference or uncertainty unresolved. For example, the treatment of French partnerships would not be resolved under option 1 or 2. This may result in ongoing compliance costs for taxpayers.

Costs associated with option 3

Taxpayer costs

3.54 No material costs to taxpayers have been identified as likely to arise from the renegotiation of the France treaty. The closer alignment with more recent treaty practice and resolution of areas of current uncertainty would generally be expected to reduce compliance costs.

Administration costs

3.55 The requirement on the ATO to exchange information on a broader range of taxes and to provide assistance in the collection of tax debts are also considered to be of minimal impact. In most cases the ATO will already have the required information in its possession, and

safeguards in the treaty which limit the obligations to provide collection assistance will limit the related administrative costs.

Consultation

3.56 The Board of Taxation consulted widely during the *Review of International Taxation Arrangements* on the direction of Australia's tax treaty policy. The Board's recommendations supported a move towards a more residence-based treaty policy in substitution for treaty policies (reflected in most of Australia's treaties, including the existing France treaty) based on the source taxation of income.

3.57 The then Minister for Revenue and Assistant Treasurer's Press Release No. C101 of 6 November 2003 invited submissions from stakeholders and the wider community in relation to issues that might be raised during negotiations with MFN countries such as France. Prior to this announcement, Treasury had already sought comments from the business community through the Tax Treaties Advisory Panel.

3.58 In general, business and industry groups supported similar outcomes as those in the UK agreement and the Protocol with the US.

3.59 The state and territory Governments have been consulted through the Commonwealth/State Standing Committee on Treaties. Information on the negotiation of this treaty was included in the schedules of treaties to state and territory representatives from October 2003.

3.60 The proposed treaty arrangements have also been considered by the Joint Standing Committee on Treaties, which provides for public consultation in its hearings.

Conclusion and recommended option

3.61 While the existing France tax treaty has provided a good measure of protection against double taxation and prevention of fiscal evasion since coming into force, it has become outdated and no longer adequately reflects current tax treaty policies and practices of either Australia or France, nor modern international norms.

3.62 All options would address long term business concerns about the lack of competitiveness of Australia's tax treaty network with respect to withholding tax rates. They also address Australia's MFN obligations in the existing treaty.

3.63 However, developments in both countries' domestic law, commercial practices, and treaty policies and practices support a full revision of the treaty (option 3). This option also provides an opportunity to update the text in accordance with modern OECD practice.

3.64 The proposed new treaty arrangements with France are consistent with the Government's response to the *Review of International Taxation Arrangements,* moving towards a more residence-based treaty policy and contributing to the updating of Australia's ageing treaty network. It would bring Australia's arrangements with France more into line with international norms, as set out in the OECD Model and would provide outcomes similar to Australia's treaties with the US and UK.

3.65 There is a direct cost to revenue common to all options, largely sourced in reduced withholding tax collections. The compliance costs associated with option 3 are considered to be minimal. On balance, the benefits of concluding a new treaty outweigh the cost to revenue.

3.66 Option 3 is therefore recommended as the preferred option.

Chapter 4
Regulation impact statement for the 2006 Norway Convention

Background

How tax treaties operate

4.1 Tax treaties reduce or eliminate double taxation caused by the exercise of source and residence country taxing rights on cross-border income flows. They do so by treaty partners agreeing (in certain situations) to limit taxing rights over various types of income. The respective countries also agree on methods of reducing double taxation where both countries exercise their right to tax.

4.2 In addition, tax treaties provide an agreed basis for determining the allocation of profits within a multinational company and whether the profits on related party dealings by members of a multinational group operating in both countries reflect the pricing that would be adopted by independent parties. Tax treaties are therefore an important tool in dealing with international profit shifting through transfer pricing.

4.3 To prevent fiscal evasion, tax treaties include provision for exchange of information held by the respective revenue authorities. Treaties may also provide for cross-border collection of tax debts, and may preclude certain types of tax discrimination. Taxpayers can also avail themselves of the mutual agreement procedures provided for in treaties which allow the two revenue authorities to consult with a view to developing a common interpretation and to resolving differences arising out of application of the treaty.

4.4 Australia seeks an appropriate balance between source and residence country taxing rights. Generally the allocation of taxing rights under Australian tax treaties is similar to international practice as set out in the Organisation for Economic Co-operation and Development (OECD) *Model Tax Convention on Income and on Capital* (OECD Model) (Australia being a member of the OECD and involved in the development of that Model). There are, however, a few instances where Australian practice favours source country taxing rights rather than the residence approach of the OECD Model.

The Norway tax treaty

4.5 The existing Australia-Norway tax treaty was signed on 6 May 1982 and has effect from 1 July 1983 (for Australian tax purposes). With the entry into force of the Protocol to the United States (US) tax treaty on 12 May 2003, Australia was obliged, under the existing Norwegian treaty to provide most favoured nation (MFN) treatment in respect of the rates of tax applicable to dividends, interest and royalties[6].

4.6 While the triggering of the MFN clauses imposes certain obligations on Australia, it also presents an opportunity to update certain aspects of the current treaty including clarifying Australia's rights to apply capital gains tax (CGT).

Australia's investment and trade relationship with the Kingdom of Norway[7]

4.7 Major Australian merchandise exports to Norway (totalling A$96 million in 2005-06) include alumina, wine, gold, base metal manufactures, and medical instruments. Imports from Norway in 2005 totalled A$276.4 million and included pumps for liquids, telecommunication equipment, paper products, arms and ammunition and cheese/curd. These figures do not include, however, the very strong services trade between Norway and Australia in the education sector. Two-way trade in services was valued at A$423 million in 2005-06 and marginally (A$17 million) in favour of Norway. In 2005 there were just over 3,300 Norwegian students in Australia, of which 2,641 were undertaking higher education courses, making Australia one of the top destinations for Norwegian students overseas. The number of Norwegian students studying in Australia has declined from a high of 4,789 just two years earlier. This trend has been due to a Norwegian preference for students to remain in Norway to undertake higher education courses.

Investment

4.8 Norway has a significant level of investment in Australia, totalling just over A$2.2 billion.

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6 Most favoured nation clauses require a country to enter into negotiations with a view to providing similar treatment to its treaty partner if it subsequently agrees with a third country to a certain specified tax treatment.

7 Source: Department of Foreign Affairs and Trade.

4.9 Norway and Australia share common expertise in various industrial sectors, including oil and gas, mining, chemicals, and marine and shipping. This points to a receptive market for Australian technology and expertise in these sectors. There are a number of significant Norwegian companies with direct investments in Australia. These include the Kvaerner Group (oil and gas), Norsk Hydro (fertilisers/aluminium production) and Dyno Wesfarmers (explosives). In March 2005 the major Norwegian global investor Yara International ASA agreed to acquire a 30 per cent share of the world's largest ammonia plant (under construction) on the Burrup Peninsula in Western Australia, owned by Burrup Holdings Pty Ltd. It is estimated that the investment is in the order of $A100 million. In 2002 Yara had entered into a long term agreement with Burrup to market and sell 100 per cent of the production from the new plant. There is a small amount of direct Australian investment in Norway, largely concentrated in the mining sector.

Specification of policy objectives

4.10 The objective of the measure is to:

- meet Australia's MFN obligations;
- promote closer economic cooperation between Australia and the Kingdom of Norway by reducing tax barriers to trade and investment between the two countries; and
- upgrade the framework through which the tax administrations of Australia and the Kingdom of Norway can prevent international fiscal evasion.

Identification of implementation options

4.11 The internationally accepted approach to meeting the policy objectives specified above is to:

- amend the existing treaty to reflect current policies (amending Protocol); or
- conclude a new bilateral tax treaty.

Option 1: Limited amending Protocol (most favoured nation obligations) — rely on the existing Norway tax treaty measures

4.12 In general terms, option 1 relies on the existing Norway tax treaty measures with an amending Protocol covering, at a minimum, Australia's MFN obligations (dividends, interest and royalty withholding tax rates). Australia would also seek to clarify Australia's rights to tax capital gains.

Option 2: Amending Protocol covering most favoured nation obligations and revising the current treaty to the extent possible without entering into a complete renegotiation

4.13 Option 2 is to deal with a number of other issues, in addition to those proposed under option 1, on which both sides would like to modify and update the existing treaty. Additional areas include for example, improved integrity measures — in particular, updated rules for the exchange of information on tax matters to the 2005 OECD standard and rules to allow for the cross-border collection of tax debts.

Option 3: Conclude a new tax treaty

4.14 Option 3 is to replace the existing treaty with a new bilateral tax treaty that reflects current policies and practice of both countries.

4.15 A new tax treaty would be largely based on the current OECD Model and the United Nations *Model Double Taxation Convention between Developed and Developing Countries*, with some mutually agreed variations reflecting the economic, legal and cultural interests of the two countries.

4.16 Both countries have particular policy objectives to achieve in updating the tax treaty and the end result ultimately represents compromises necessary to achieve a mutually acceptable agreement. The key changes in a new treaty include:

- a reduction in the maximum royalty withholding tax rates from 10 per cent to 5 per cent;
- a reduction in interest withholding tax from 10 per cent to zero where interest is paid to a financial institution or body performing governmental functions;
- a reduction of dividend withholding tax from 15 per cent to zero for dividends on non-portfolio holdings of more than

80 per cent, subject to certain conditions and to 5 per cent dividend withholding tax for other non-portfolio holdings;

- the inclusion of a comprehensive *Alienation of Property* Article which allocates taxing rights over capital gains;
- improved integrity measures — in particular, rules to allow for the cross-border collection of tax debts and updated rules for the exchange of information on tax matters; and
- new rules to prevent tax discrimination against Australian nationals and businesses operating in Norway and vice versa.

Assessment of impacts (costs and benefits) of each option

Difficulties in quantifying the impacts of tax treaties

4.17 Only a partial analysis of costs and benefits can be provided because all the impacts of tax treaties cannot be quantified. While the direct cost to Australian revenue of withholding tax changes can be quantified relatively easily, other cost impacts such as compliance costs are inherently difficult to quantify. There are also efficiency and growth gains and losses to Australia that provide estimation problems. Analysis has been conducted to establish plausible impacts on Australian economic activity and consequent tax revenue flowing from implementation of the tax treaty. The tax revenue estimates are subject to more uncertainty than the estimates of costs but are best estimates given the technology of estimation, the availability of estimates of behavioural responses, and data.

4.18 Benefits that flow to business are generally equally difficult to quantify. The evidence from international consideration (eg, the OECD) and from consultation with business strongly indicates, however, that while the quantum of benefits is very difficult to assess, a modern tax treaty provides a clear positive benefit to trade and investment relationships. Tax treaties provide increased certainty and reduce complexity and compliance costs for business.

Impact group identification

4.19 A revised tax treaty with the Kingdom of Norway is likely to have an impact on:

- Australian residents doing business with Norway, including principally:
  - Australian residents investing directly in the Kingdom of Norway (either by way of a subsidiary or a branch);
  - Australians borrowing from Norwegian banks;
  - Australian residents using technology and know-how supplied by Norwegian residents;
  - Australian residents supplying consultancy services to the Kingdom of Norway; and
  - Australian residents exporting to the Kingdom of Norway;
- Australian employees working in the Kingdom of Norway;
- Australian residents receiving pensions from the Kingdom of Norway;
- the Australian Government; and
- the Australian Taxation Office (ATO).

Assessment of benefits

4.20 All options would address long term business concerns about the lack of competitiveness of Australia's tax treaty network with business particularly seeking reductions in withholding tax rates.

4.21 These issues were addressed in the 2003 Convention with the United Kingdom (UK) and the 2001 Protocol amending the Convention with the US. Extending similar treatment to Norway aligns treatment, where possible, in Australia's recent tax treaties, maintains the integrity of Australia's treaty network and discourages treaty shopping (and the consequent degradation of the tax base of countries where the costs of capital and intellectual property are higher under their treaties as a result of the higher withholding tax rates). While a reduction in maximum withholding tax rates will involve a cost to revenue, there are expected to

be benefits to the revenue and to the wider economy arising out of increased business and investment activity, with the most direct benefits accruing to business.

Economic benefits common to all options

4.22 The economic benefits of the expected major changes from the existing Norway tax treaty are summarised in paragraphs 4.23 to 4.29.

Dividends

4.23 An outcome such as that provided to the US and UK (no withholding tax on dividends paid to a company with an 80 per cent or greater voting interest in a listed company in the other jurisdiction — 5 per cent withholding tax where the interest is at least 10 per cent of the voting power and 15 per cent in other cases) would remove distortions in the raising of capital that results from the more favourable terms that currently apply bilaterally in the case of the US and the UK.

Interest

4.24 A nil Australian interest withholding tax rate on interest derived by Norwegian financial institutions will be consistent with the exemption currently provided under domestic law for interest derived from widely distributed arm's length debenture issues. It also recognises that a 10 per cent interest withholding tax rate on gross interest derived by financial institutions may be excessive given their cost of funds. It should, accordingly, lower the costs of borrowing in those cases where the financial institution can pass the cost represented by the withholding tax on to the Australian borrower.

4.25 Although Norway does not currently impose interest withholding tax on payments to Australian residents, locking in the rates will benefit Australian residents should Norway introduce such a tax in the future.

Royalties

4.26 Australian residents required to meet the cost of Australian royalty withholding tax on royalty payments made to Norwegian residents would benefit from a reduced royalty withholding tax rate. Commercial practice indicates that, as with interest, the cost represented by the royalty withholding tax is commonly passed on to the payer of the royalty. This means that they may bear the cost of higher rates of withholding tax and place them at a competitive disadvantage in competing with businesses from other countries with lower rates. The effect of lowering the cost of new technology and intellectual property may encourage the development

of Australia's economy through use of the most up-to-date technology and processes.

4.27 Although Norway does not currently impose a royalty withholding tax on payments to Australian residents, locking in the reduced royalty withholding tax rate will benefit Australian residents should Norway introduce such a tax in the future.

Alienation of Property

4.28 The updating of the *Alienation of Property* Article to address taxing rights over capital gains would provide certainty to taxpayers and reduce the risk of double taxation. Australia's source country taxing rights over capital gains on real property, land-rich companies and assets which form the business property of a permanent establishment in Australia would be retained. More generally, the changes bring into line Australia's treaty practice with international practice. This will encourage investment in Australia and result in generally lower compliance costs.

Compliance and administrative cost reduction benefits

4.29 Tax exemptions in respect of withholding taxes are likely to reduce compliance and administration costs associated with remitting and claiming credits for such tax.

Comparative advantage of option 1

4.30 Option 1 involves minimal changes to the existing treaty.

Comparative advantages of option 2

4.31 The advantage of option 2 is that Australia, in addition to addressing its MFN obligations, would be able to achieve improved integrity measures, in particular, rules to allow for the cross-border collection of tax debts, updated rules for the exchange of information on tax matters and rules to prevent tax discrimination against Australian nationals and businesses operating in Norway and vice versa.

4.32 This option represents an advance on option 1 and recognises that the rates of withholding tax negotiated in the 2001 US Protocol were agreed as part of an overall package of measures (including CGT coverage). It would allow Australia to seek a more balanced update of the existing treaty.

Comparative advantages of option 3

4.33 The advantages of option 2 are also common to option 3.

Renegotiation provides a better outcome for all stakeholders

4.34 While the existing Norway tax treaty has provided a good measure of protection against double taxation and prevention of fiscal evasion since coming into force, it has become outdated (eg, no coverage of CGT) and no longer adequately reflects current tax treaty policies and practices of either Australia or Norway.

4.35 A new tax treaty would provide benefits to Australian business and to the Australian revenue by ensuring certainty of legislative outcomes based on the treaty. It would be another step forward in providing Australian business with an internationally competitive tax treaty network and business tax system.

4.36 A renegotiated treaty will provide a better outcome for all stakeholders. Given the long-term nature of such arrangements, a revised tax treaty is expected to promote greater certainty than the existing tax treaty. It would also be consistent with the Government's decision in response to the *Review of International Taxation Arrangements,* to move towards a more residence-based tax treaty policy, and would contribute to the updating of Australia's ageing treaty network.

<u>Other benefits</u>

4.37 Where Australians carry on business activities in Norway, the existing treaty prevents Norway from taxing the business profits of an Australian resident unless that Australian resident carries on business through a permanent establishment in Norway. A new tax treaty would further refine the concept of when a permanent establishment should be taken to exist and the level of activity that would constitute a permanent establishment. This principle also applies where a Norwegian carries on business activities in Australia. Other benefits also include:

- the clarification of the residency rules;
- coverage of royalties from Australian spectrum licences;
- clarifying the treatment of income derived through trusts; and
- the inclusion of anti-avoidance rules.

<u>Revenue benefits</u>

4.38 New treaty arrangements with Norway would represent another step in facilitating a competitive and modern treaty network for Australian companies and would help to maintain Australia's status as an attractive place for business and investment. While a reduction in maximum

withholding tax rates will involve a small cost to revenue, there are expected to be benefits to the revenue and to the wider economy arising out of increased business and investment activity, with the most direct benefits accruing to business.

4.39 Small revenue benefits should also result from enhanced tax integrity measures over a broader range of taxes.

<u>Compliance and administration cost reduction benefits</u>

4.40 The closer alignment with more recent Australian and international treaty practice would generally be expected to reduce compliance costs. In particular, interpretative issues relating to the extent Australia can tax capital gains under the existing treaty arrangements has resulted in considerable uncertainty and the risk of costly legal arguments.

4.41 Administrative costs in explaining the ATO view and responding to legal arguments would also be significantly reduced. Clarifying other areas of uncertainty, such as tax treaty tests of 'residency' and updating the treaty text, should also decrease compliance costs and uncertainty.

<u>Improved international relationships</u>

4.42 New treaty arrangements with Norway will also assist the bilateral relationship by updating an important treaty in the existing network of commercial treaties between the two countries. It would also promote greater cooperation between taxation authorities to prevent fiscal evasion and tax avoidance. Updating the tax treaty to take account of changes to the OECD Model would also help to maintain Australia's status as an active OECD member, which in turn would maintain Australia's position in the international tax community.

Assessment of costs

Costs common to all options

Revenue costs

4.43 Treasury has estimated the impact of the first round effects on forward estimates as unquantifiable but probably negligible. The three options do not present material differences in estimated direct cost to revenue as the only identifiable costs to revenue are associated with the reductions in dividend, interest and royalty withholding tax rates.

Administrative costs

4.44 The administrative impacts on the ATO from the changes made by any new treaty arrangements are considered to be minimal. Some formal interpretive advice may be required, for example, private binding rulings, concerning the application of the new treaty arrangements. ATO staff, clients and tax professionals will need to be made aware of the entry into force and changes from the previous treaty. Therefore a number of ATO information products will need to be updated

4.45 The costs of negotiation and enactment of new tax treaty arrangements with Norway are minimal and have mostly been borne by Treasury and the ATO. There will also be an unquantified but small cost in terms of parliamentary time and drafting resources in enacting the proposed new tax treaty arrangements.

4.46 There are also 'maintenance' costs to the ATO associated with tax treaties in terms of dealing with enquiries, rulings and other interpretive decisions and mutual agreement procedures (including advance pricing arrangements). These costs also apply to the existing arrangements. By bringing the Norwegian treaty into basic conformity with recent treaty practice these costs would be reduced. However, as treaties are deals struck between the two countries that reflect specific features of the bilateral relationship, some level of differential treatment or wording between treaties, which may require interpretation or explanation by the ATO, is inevitable.

Other costs

4.47 Government policy flexibility in relation to taxation of Norwegian residents would be further constrained by changes to treaty obligations, for example, with respect to taxation of capital gains. However, as the more significant changes accord with the Government's tax treaty policy the cost of such constraints are outweighed by the benefits. Ultimately, the tax treaty could be terminated if it became out of step with Government policy. Such termination is very rare in international tax treaty practice, however, and could be expected to be resisted by the business community and others who benefit from the treaty.

4.48 The impact of new tax treaty arrangements on tax policy flexibility is generally quite minimal as tax treaties are based on broad and generally accepted taxation principles.

Costs associated with option 1

4.49 Option 1 primarily represents a continuation of the current treaty position subject to adjustment to withholding tax rates. Accordingly, administration and compliance costs that apply to the existing Norway tax treaty would not change materially.

Costs associated with options 2 and 3

Taxpayer costs

4.50 No material additional costs to taxpayers have been identified as likely to arise from the renegotiation of the Norwegian treaty.

Administrative costs

4.51 The requirement on the ATO to exchange information on a broader range of taxes and to provide assistance in the collection of tax debts are also considered to be of minimal impact. In most cases the ATO will already have the required information in its possession, and safeguards in the treaty which limit the obligations to provide collection assistance will limit the related administrative costs.

Consultation

4.52 The Board of Taxation consulted widely during the *Review of International Taxation Arrangements* on the direction of Australia's tax treaty policy. The Board's recommendations supported a move towards a more residence-based treaty policy in substitution for treaty policies (reflected in most of Australia's treaties, including the existing Norway treaty) based on the source taxation of income.

4.53 The then Minister for Revenue and Assistant Treasurer's Press Release No. C101 of 6 November 2003 announced proposed tax treaty negotiations, and invited submissions from stakeholders and the wider community in relation to issues that might be raised during negotiations with MFN countries such as Norway. Prior to this announcement, Treasury had already sought comments from the business community through the Tax Treaties Advisory Panel.

4.54 In general, business and industry groups supported similar outcomes to those in the 2003 UK Convention and the updated Australia-US tax treaty.

4.55 The state and territory Governments have been consulted through the Commonwealth/State Standing Committee on Treaties. Information on the negotiation of this treaty was included in the schedules of treaties to state and territory representatives from October 2003.

4.56 The proposed treaty arrangements have also been considered by the Joint Standing Committee on Treaties, which provides for public consultation in its hearings.

Conclusion and recommended option

4.57 While the existing Norway tax treaty has provided a good measure of protection against double taxation and prevention of fiscal evasion since coming into force, it has become outdated and no longer adequately reflects current tax treaty policies and practices of either Australia or Norway, nor modern international norms.

4.58 All options would address long term business concerns about the lack of competitiveness of Australia's tax treaty network with respect to withholding tax rates. They also address Australia's MFN obligation in the existing treaty.

4.59 However, developments in both countries' domestic law, commercial practices, and treaty policies and practices support a full revision of the treaty (option 3). This option also provides an opportunity to update the text in accordance with modern OECD practice.

4.60 The proposed new treaty arrangements with Norway are consistent with the Government's response to the *Review of International Taxation Arrangements,* moving towards a more residence-based tax treaty policy and contributing to the updating of Australia's ageing treaty network. It would bring Australia's arrangements with Norway more into line with international norms, as set out in the OECD Model and would provide outcomes similar to Australia's treaties with the US and the UK.

4.61 There is a direct cost to revenue common to all options, largely sourced in reduced withholding tax collections. The compliance costs associated with option 3 are considered to be minimal. On balance, the benefits of concluding a new treaty outweigh the cost to revenue.

4.62 Option 3 is therefore recommended as the preferred option.