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The PPT in Post-BEPS Tax Treaty Law: It Is a GAAR but Just a GAAR!

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In this article, the author discusses the principal purpose test (PPT) included in article 29 of the OECD and UN Models (2017), arguing in particular that while the PPT certainly permits a purposive interpretation, it may not be used to build into tax treaty law additional requirements that were never intended. Finally, the author concludes by looking at the other side of the coin and wonders whether a comparable “PPT” should not regulate the performance by States of their treaty obligations.

1. Introduction

The principal purpose test (PPT), which has been incorporated into the OECD Model (2017)^[1] and the UN Model (2017),^[2] today represents the minimum multilateral standard to combat tax treaty abuse. While the PPT is not entirely new and to a large extent codifies the so-called “guiding principle” introduced in the Commentary on Article 1 of the OECD Model (2003),^[3] it is, however, fair to say that it has caused a significant degree of anxiety among taxpayers. For tax administrations as well, the PPT may seem difficult to apply and further guidance would be welcome.^[4]

Arguably, the problem lies first of all in the fact that the PPT is by essence vague. How should “one of the principal purposes of any arrangement or transaction” be understood? And when is the granting of treaty benefits “in accordance with the object and purpose of the relevant provisions of this Convention”? What is the difference between taking into account the “object and purpose of the relevant provisions” under article 29(9) of the OECD Model (2017) and a proper interpretation of treaty law in accordance with article 31 of the Vienna Convention on the Law of Treaties (the “Vienna Convention”) (1969)?^[5] But these questions alone do not explain the uncertainty surrounding the PPT. After all, general anti-avoidance rules (GAARs) drafted along the lines of the PPT are well-known both in domestic and tax treaty practice. In the author’s opinion, the source of the confusion is also due to the fact that the PPT is part of a holistic project – the OECD/G20 Base Erosion and Profit Shifting (BEPS) initiative – founded on common pillars: coherence, substance and transparency. Naturally, therefore, the relevance of other BEPS Action items for purposes of interpreting the PPT arises. The commentaries on the PPT also fuel this controversy by referring, inter alia, to notions that seemed to be inspired from transfer pricing principles. These references have, therefore, prompted certain commentators to question whether a link should for instance be established between the PPT and BEPS Action 8-10 relating to the alignment of transfer pricing outcomes with value creation.^[6] One could even wonder if, more generally, the PPT should not serve to ensure an allocation of taxing rights between the Contracting States that is in line with an overriding concept of value creation governing

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1. *OECD Model Tax Convention on Income and on Capital* (21 Nov. 2017), Treaties & Models IBFD.
2. *UN Model Double Taxation Convention between Developed and Developing Countries* (1 Jan. 2017), Treaties & Models IBFD.
3. *OECD Model Tax Convention on Income and on Capital: Commentary on Article 1* para. 9.5 ad art. 1 (28 Jan. 2003), Treaties & Models IBFD.
4. The relation between the PPT and tax certainty is mentioned in the International Monetary Fund (IMF)/OECD, *Report for the G20 Finance Ministers and Central Bank Governors: Update on Tax Certainty* para. 2.1.2., p. 12 (IMF/OECD July 2018), available at www.oecd.org/ctp/tax-policy/tax-certainty-update-oecd-imf-report-g20-finance-ministers-july-2018.pdf: “The implementation of PPT rules in bilateral treaties, while effective in reducing aggressive tax planning, is perceived as potentially increasing tax uncertainty. Various stakeholders have in fact expressed concerns on the implementation of the PPT. These concerns are expressed notwithstanding the extensive work already carried on by the OECD on tax conventions and related questions on the development on Commentary on the application of the PPT or on the work carried on the possible inadvertent effects of the PPT on the treaty entitlement of non-collective investment vehicles (CIVs) funds. To increase tax certainty in the application of the PPT, the OECD has formed an informal group of interested delegates that would explore various areas where more tax certainty could be provided in the PPT, including best practices in the area of the general anti-avoidance rules and would report back with recommendation.” Presumably, much progress was not made on this front because of the ongoing full attention on the digital economy debate.
5. *UN Vienna Convention on the Law of Treaties* (23 May 1969), Treaties & Models IBFD [hereinafter the *Vienna Convention* (1969)].
6. OECD/G20, *Aligning Transfer Pricing Outcomes with Value Creation – Actions 8-10: 2015 Final Report* (OECD 2015), Primary Sources IBFD.