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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) and the UN Model (2017), 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), 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.

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)? 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. 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 the performance by States of their treaty obligations.

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