

EXPLANATORY STATEMENT TO THE MULTILATERAL CONVENTION TO FACILITATE THE IMPLEMENTATION OF THE PILLAR TWO SUBJECT TO TAX RULE

Adopted by the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) on 15 September 2023.

Background

1. The *Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to Tax Rule* (the Convention) is one of the outcomes of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (the OECD/G20 Inclusive Framework on BEPS) Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy (the OECD/G20 Inclusive Framework Two-Pillar Solution), which following years of intensive negotiations to bring the international tax system into the 21st century, was agreed upon by the OECD/G20 Inclusive Framework on BEPS as set out in the [Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy on 8 October 2021](#) (the 2021 October Statement).
2. As part of the agreement on the OECD/G20 Inclusive Framework Two-Pillar Solution set out in the 2021 October Statement, members of the OECD/G20 Inclusive Framework on BEPS applying nominal corporate income tax rates below the minimum rate of nine per cent to interest, royalties and a defined set of other payments took on a commitment to implement the subject to tax rule (STTR) in their bilateral tax treaties when requested to do so by IF members identified as developing for this purpose (developing countries).
3. As part of the detailed implementation plan annexed to the 2021 October Statement members of the OECD/G20 Inclusive Framework on BEPS agreed to develop a multilateral instrument to facilitate the implementation of the STTR between the subset of jurisdictions described above. The aim was to provide an effective way to implement the STTR swiftly in relevant existing bilateral tax treaties. Alternatively, members of the OECD/G20 Inclusive Framework on BEPS may implement the STTR via bilateral negotiations.
4. The detailed implementation plan annexed to the 2021 October Statement mandated the development of a model treaty provision to give effect to the STTR, together with commentary explaining its operation. The STTR model treaty provision, together with its detailed commentary, are included in the Report on the Subject to Tax Rule (the STTR Report).¹
5. Working Party 1 on Tax Conventions and Related Questions (Working Party 1) has developed the text of the Convention which was adopted by the OECD/G20 Inclusive Framework on BEPS on 15 September 2023 and open for signature as of 2 October 2023.
6. Delegates of Working Party 1, which represented governments of the members of the OECD/G20 Inclusive Framework on BEPS on 15 September 2023, participated in the negotiation of the Convention on an equal footing. The Co-Chairs of Working Party 1 were Aart Roelofsen of the Netherlands and Carmel Peters of New Zealand.
7. As the substance of the STTR and its associated commentary had been stabilised by Working Party 1 under the guidance of the Steering Group of the OECD/G20 Inclusive

¹ OECD/G20 Inclusive Framework on BEPS (2023), Report on the Subject to Tax Rule.

Framework on BEPS, the development of the Convention focused on the way in which it would implement the STTR in relevant existing bilateral tax treaties.

8. The text of this explanatory statement to accompany the Convention (“Explanatory Statement”) was prepared by Working Party 1 to provide clarification of the approach taken in the Convention and how it amends existing bilateral tax agreements covered by the Convention (“Covered Tax Agreements”). It therefore reflects the agreed understanding of the negotiators with respect to the Convention. The OECD/G20 Inclusive Framework on BEPS adopted this Explanatory Statement on 15 September 2023 at the same time as adopting the text of the Convention.

9. The development of the STTR that is implemented by the Convention also included development of detailed commentary which is intended to be used in the interpretation of the STTR. While this Explanatory Statement is intended to clarify the operation of the Convention to amend existing bilateral tax treaties, it is not intended to address the interpretation of the underlying STTR. Accordingly, the provisions contained in the Convention should be interpreted in accordance with the ordinary principles of treaty interpretation, which is that a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose. In this regard, the object and purpose of the Convention is to facilitate the implementation of the STTR. The commentary that was developed by Working Party 1 and reflected in the STTR Report approved by the OECD/G20 Inclusive Framework on BEPS on 6 July 2023 has particular relevance in this regard.

Approach taken in the Convention

10. The Convention applies to Covered Tax Agreements that are existing bilateral tax treaties that are explicitly identified by each of the parties to those tax treaties (the Contracting Jurisdictions). It operates to directly amend those treaties in order to implement the STTR and other relevant accompanying provisions as annexes to those treaties.

11. The STTR is included in Annex I (The subject to tax rule) to the Convention and, where the Convention applies with respect to a Covered Tax Agreement, Annex I (The subject to tax rule) is added as an annex to the Covered Tax Agreement. A Covered Tax Agreement is any tax treaty in force between Parties to the Convention which has been notified by both Contracting Jurisdictions as an agreement they wish to be covered by the Convention.

12. The Convention does not amend the text, sequencing or numbering of existing provisions in Covered Tax Agreements. Instead, the Convention amends the Covered Tax Agreements to include the STTR and other relevant accompanying provisions as Annexes to the Covered Tax Agreement. Once included in a Covered Tax Agreement, the Annexes form an integral part of the Covered Tax Agreement.

13. The Convention, by directly amending existing bilateral tax treaties, functions like an amending protocol to a single existing bilateral tax treaty. Its functioning can be distinguished from the functioning of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (the BEPS Multilateral Convention), which applies alongside existing tax treaties and modifies their application in order to implement the measure developed in the course of the OECD/G20 Base Erosion and Profit Shifting Project.² As such, and unlike the BEPS Multilateral Convention, once

² The functioning of the BEPS Multilateral Convention is explained in paragraph 13 of the Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting: <https://www.oecd.org/tax/treaties/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf>. While the BEPS Multilateral Convention constituted the first use of a multilateral treaty to modify bilateral tax treaties, this mechanism had already been used in other areas. For example, a 2003 Agreement on Extradition between the European Union and the United States of America: <http://ec.europa.eu/world/agreements/downloadFile.do?fullText=yes&treatyTransId=10121>. See also Developing a

the Convention amends a relevant Covered Tax Agreement, the Convention no longer needs to be read in conjunction with the Covered Tax Agreement. As a result, Contracting Jurisdictions may wish to develop consolidated versions of their Covered Tax Agreements as they have been amended by the Convention.

14. It is important to note that the Convention is not intended to freeze in time the underlying agreement and Contracting Jurisdictions may decide to further amend the underlying agreement after it has been amended by the Convention. The right of the Contracting Jurisdictions to further amend their Covered Tax Agreements remains unaffected, irrespective of whether the further amendments relate to provisions that have been included by the Convention. This is reflected in Article 2 in Annex I (The subject to tax rule, Implications of the subject to tax rule), which provides that subsequent modifications to Covered Tax Agreements may be agreed between the Contracting Jurisdictions.

The Annexes to the Convention

15. **Annex I (The subject to tax rule)** of the Convention includes the STTR and, as mentioned above, is added in all Covered Tax Agreements.

16. The Convention contains four other Annexes which include additional provisions that are required for the operation of the STTR in certain circumstances. Those Annexes are added in certain Covered Tax Agreements, in addition to Annex I (The subject to tax rule), where specified objective conditions are met. The provisions in Part II (Inclusion of annexes in Covered Tax Agreements) of the Convention define the conditions under which each of those other Annexes are included in a Covered Tax Agreement in addition to Annex I (The subject to tax rule):

- **Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis)** of the Convention contains the additional provisions required for the determination of the tax rate in paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”) for taxes computed on an alternative basis. This Annex is included in a Covered Tax Agreement in addition to Annex I (The subject to tax rule) where at least one of the Contracting Jurisdiction to the Covered Tax Agreement applies a tax computed on an alternative basis. Parties that apply such taxes on an alternative basis are required to make a notification under the Convention and identify the name of the tax and relevant legal references. That notification triggers the inclusion of Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) in a Covered Tax Agreement.
- **Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution)** of the Convention contains the additional provisions required for the determination of the tax rate in paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”) for taxes imposed only at the point of distribution. This Annex is included in a Covered Tax Agreement in addition to Annex I (The subject to tax rule) where at least one of the Contracting Jurisdiction to the Covered Tax Agreement imposes tax only at the point of distribution. Parties that apply such taxes only at the point of distribution are required to make a notification under the Convention and identify the name of the tax and relevant legal references. That notification triggers the inclusion of Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) in a Covered Tax Agreement.

Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15 - 2015 Final Report p.35: http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/developing-a-multilateral-instrument-to-modify-bilateral-tax-treaties-action-15-2015-final-report_9789264241688-en#page1. Other examples, cited in the Annex to the 2014 Report (pp. 32-34), include the European Convention on Extradition (1957), European Convention on the Repatriation of Minors (1970), the Convention for the Suppression of Unlawful Acts against the Safety of Maritime Navigation (1988), the North American Free Trade Agreement (1994) and the International Convention for the Suppression of the Financing of Terrorism (1999).

- **Annex IV (Additions to the subject to tax rule: Recognised pension fund)** of the Convention contains a definition for the purposes of subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions). This Annex is included in a Covered Tax Agreement in addition to Annex I (The subject to tax rule) where at least one of the Contracting Jurisdictions to the Covered Tax Agreement chooses to include that definition. Parties that choose to include such a definition for the purposes of subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions) are required to make a notification under the Convention and include the list of their Covered Tax Agreements in which they choose to include such a definition. A notification made with respect to a Covered Tax Agreement triggers the inclusion of Annex IV (Additions to the subject to tax rule: Recognised pension fund) in the Covered Tax Agreement.
- **Annex V (Additions to the subject to tax rule: Circuit-breaker provision)** of the Convention contains a circuit-breaker provision. This Annex is included in a Covered Tax Agreement in addition to Annex I (The subject to tax rule) where at least one of the Contracting Jurisdictions to the Covered Tax Agreement chooses to include such a circuit-breaker in its Covered Tax Agreements. Parties that choose to include the circuit-breaker in their Covered Tax Agreements are required to make a notification under the Convention and this choice will apply to all of their Covered Tax Agreements. That notification made with respect to a Party's Covered Tax Agreements triggers the inclusion of Annex V (Additions to the subject to tax rule: Circuit-breaker provision) in its Covered Tax Agreements.

17. Annex I (The subject to tax rule), Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) and Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) reflect the STTR model treaty provision and additional provisions in the commentary on the STTR treaty provision with adaptations required to implement STTR in different existing bilateral tax treaties. Those adaptations include the replacement of cross-references to specific Articles and paragraphs with descriptions of those provisions. A number of paragraphs in the STTR interact with existing provisions of Covered Tax Agreements. Because existing tax treaties vary from each other, it would not be possible for the Convention to identify those provisions by referring to specific articles and paragraph numbers. Instead, where a reference to the provisions of existing tax agreements is necessary, the Convention uses descriptive language to identify those provisions.

18. Similarly, throughout Annex I (The subject to tax rule), and throughout Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis), Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution), Annex IV (Additions to the subject to tax rule: Recognised pension fund), and Annex V (Additions to the subject to tax rule: Circuit-breaker provision), a Covered Tax Agreement is referred to as "this agreement" and a Contracting Jurisdiction is referred to as a "contracting jurisdiction". This reflects the fact that Annex I (The subject to tax rule) (and where conditions are met, one or more of Annexes II to V) will be included in a Covered Tax Agreement and adapts those references accordingly. The adapted references to "this agreement" and a "contracting jurisdiction", when an Annex is included in a Covered Tax Agreement, are sufficiently clear and neutral as to apply appropriately in Covered Tax Agreements: that are described in their title as a "Convention", an "Agreement", an "Arrangement", or using a similar term; or in which a party to the Covered Tax Agreement is referred to as a "Contracting State", "Contracting Jurisdiction", or a similar term.

Preamble

19. The preamble describes the overall purpose of the Convention to facilitate the implementation of the STTR that was developed as part of the OECD/G20 Inclusive Framework Two-Pillar Solution and that is an integral part of achieving a consensus for developing countries.

20. The penultimate paragraph of the preamble notes that the STTR is implemented in certain existing agreements for the avoidance of double taxation on income as part of the implementation of the OECD/G20 Inclusive Framework Two-Pillar Solution and that the provisions in this Convention do not otherwise reflect the tax treaty policies of members of the OECD/G20 Inclusive Framework on BEPS. This statement, which reflects subparagraphs a) and b) of paragraph 15 of the STTR model treaty provision in the STTR Report, sets out the context in which the STTR was developed and codifies the understanding of the negotiators that the STTR does not revisit the current allocation of taxing rights between Contracting Jurisdictions to a Covered Tax Agreement.

21. The inclusion of this statement in the preamble to the Convention is intended to confirm that the STTR does not otherwise reflect the tax treaty policies of either Contracting Jurisdiction to a Covered Tax Agreement. This confirms that the inclusion of the Covered Tax Agreement does not indicate that the Contracting Jurisdictions believe there should be any change to the principles reflected in that Covered Tax Agreement, including to the allocation of taxing rights.

Part I. - Scope and Interpretation of Terms

Article 1 - Scope of the Convention

22. Article 1 defines the scope of application of the Convention. The Convention amends all Covered Tax Agreements as defined in Article 2(1)(a).

Article 2 – Interpretation of Terms

Paragraph 1

Covered Tax Agreement

23. Paragraph 1(a) defines the term “Covered Tax Agreement”, which is the term used for the agreements that will be amended by the Convention. This includes agreements for the avoidance of double taxation with respect to taxes on income that are in force between two Parties to the Convention or, as noted below, jurisdictions for whose international relations a Party is responsible. This would include agreements that cover capital taxes in addition to income taxes. The Convention is not, however, intended to apply to agreements applying only to shipping and air transport or social security.

24. To avoid confusion or uncertainty about the scope of agreements covered, the Convention only amends an agreement that has been specifically identified in a notification to the Depository by each Party to the Convention that is either a Contracting Jurisdiction to that agreement or responsible for the international relations of a party to the agreement. This approach provides for flexibility as to which existing agreements are covered by the Convention.

25. Paragraph 1(a)(i)(B) enables a State that is a Party to the Convention to include in its list of Covered Tax Agreements tax agreements which have been entered into by a jurisdiction or territory for whose international relations the State Party is responsible. This is intended to cover the situation of jurisdictions or territories which, under the arrangements with the State responsible for their international relations, have the ability to conclude tax agreements in their own right. Accordingly, the Convention may cover tax agreements concluded by non-State jurisdictions or territories.

26. In cases where a State Party avails itself of paragraph 1(a)(i)(B), it shall make notifications in respect of the jurisdiction or territory in question, which will apply to all Covered Tax Agreements of that jurisdiction or territory. The notifications of that Party, or made by that Party in respect of Covered Tax Agreements entered into by or on behalf of a jurisdiction or territory for whose international relations that Party is responsible, can be different as described in Article 10(2) of the Convention.

27. The Convention may also cover tax agreements entered into by a State Party “on behalf” of a non-State jurisdiction or territory for whose international relations it is responsible. In such cases, the State Party would include those tax agreements in its list of tax agreements under paragraph 1(a)(i)(A) but has the possibility under Article 10(2) to make notifications in respect of that jurisdiction or territory which may differ from the State Party’s own list of notifications.

28. It is possible for a Party to include in the list of agreements provided under paragraph 1(a)(ii) an agreement which has been signed but has not yet entered into force. In such cases, the agreement can only become a Covered Tax Agreement when it enters into force. Where such an agreement enters into force after the entry into force of the Convention with respect to such Party pursuant to Article 11(2), the date on which the agreement enters into force is the date in which the agreement becomes a Covered Tax Agreement under the Convention.

Party

29. Paragraph 1(b) defines the term “Party”. The term is used throughout the Convention to refer to States for which the Convention is in force pursuant to Article 11.

Contracting Jurisdiction

30. Paragraph 1(c) defines the term “Contracting Jurisdictions”. The term refers to the States, jurisdictions or territories that are parties to a Covered Tax Agreement.

Signatory

31. Paragraph 1(d) defines the term “Signatory”, which is used exclusively in the final provisions of the Convention, and refers to States that have signed the Convention pursuant to Article 8(1) but for which the Convention is not yet in force.

Paragraph 2

32. This paragraph provides a general rule of interpretation for terms used in the Convention but not defined therein. Any term not defined in the Convention shall, unless the context otherwise requires, have the meaning that it has under the relevant Covered Tax Agreement at the time the Convention is being applied.

33. With respect to a term not explicitly defined in the Convention or in the relevant Covered Tax Agreement, Covered Tax Agreements generally provide that any term not defined shall, unless the context otherwise requires, have the meaning it has at the time the Covered Tax Agreement is being applied under the domestic law of the Contracting Jurisdiction applying the Covered Tax Agreement, the meaning given to that term under the tax laws of that Contracting Jurisdiction prevailing over a meaning given to the term under other laws of that Contracting Jurisdiction. Where this rule is present in a Covered Tax Agreement, it would apply for purposes of determining the meaning of undefined terms in the Convention, unless the context requires an alternative interpretation.

Part II. – Inclusion of Annexes in Covered Tax Agreements

Article 3 – Inclusion of Annex I (The subject to tax rule) in a Covered Tax Agreement

34. Article 3 provides that Annex I (The subject to tax rule) will be included in all Covered Tax Agreements and will form an integral part thereof.

Article 4 – Inclusion of Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) in a Covered Tax Agreement

Paragraph 1

35. Paragraph 1 requires a Party to notify the Depository of whether it applies a tax calculated other than on a net income basis that is covered under subparagraph b) of paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”) and if so, the name of the tax and relevant legal references.

Paragraph 2

36. Paragraph 2 provides that where one Contracting Jurisdiction to a Covered Tax Agreement has made a notification under paragraph 1, Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) will be included in that Covered Tax Agreement, in addition to Annex I (The subject to tax rule), and will form an integral part thereof.

Article 5 – Inclusion of Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) in a Covered Tax Agreement

Paragraph 1

37. Paragraph 1 requires a Party to notify the Depository of whether it does not impose corporate income tax on items of covered income when that income is earned, but instead imposes tax only at the point of profit distribution and if so, the name of the tax and relevant legal references.

Paragraph 2

38. Paragraph 2 provides that where one Contracting Jurisdiction to a Covered Tax Agreement has made a notification under paragraph 1, Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) will be included in that Covered Tax Agreement, in addition to Annex I (The subject to tax rule), and will form an integral part thereof.

Article 6 – Inclusion of Annex IV (Additions to the subject to tax rule: Recognised pension fund) in a Covered Tax Agreement

Paragraph 1

39. Paragraph 1 provides that a Party may choose to include the definition of the term “recognised pension fund” in Annex IV (Additions to the subject to tax rule: Recognised pension fund) for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions).

Paragraph 2

40. Paragraph 2 requires each Party that chooses to include the definition of the term “recognised pension fund” in Annex IV (Additions to the subject to tax rule: Recognised pension fund) to notify the Depository of its choice and that such notification must also include the list of its Covered Tax Agreements in which that Party chooses to include such a definition.

41. Circumstances in which a Party might wish to choose to include the definition of the term “recognised pension fund” in Annex IV (Recognised pension fund) for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions) in a Covered Tax Agreement include: when a Covered Tax Agreement does not include a definition of the term “recognised pension fund”; or when a Covered Tax Agreement includes such a definition of a term that means an entity, or a scheme, or an arrangement, that is established and operated to administer or provide retirement benefits and ancillary or incidental benefits to individuals and that is regulated as such by a jurisdiction or one of its political subdivisions or local authorities when that existing definition differs from the definition of the term “recognised pension fund” in paragraph 2 of Article 1 in Annex IV (Additions to the subject to tax rule: Recognised pension fund).

Paragraph 3

42. Paragraph 3 provides that where one Contracting Jurisdiction to a Covered Tax Agreement has made a notification under paragraph 2, Annex IV (Additions to the subject to tax rule: Recognised pension fund) will be included in that Covered Tax Agreement, in addition to Annex I (The subject to tax rule), and will form an integral part thereof.

43. Where Annex IV (Additions to the subject to tax rule: Recognised pension fund) is included in a Covered Tax Agreement, it will be used by both Contracting Jurisdictions to that Covered Tax Agreement for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions) in that Covered Tax Agreement.

Article 7 – Inclusion of Annex V (Additions to the subject to tax rule: Circuit-breaker provision) in a Covered Tax Agreement

Paragraph 1

44. Paragraph 1 provides that a Party may choose to include Annex V (Additions to the subject to tax rule: Circuit-breaker provision) in its Covered Tax Agreements and that this choice would apply to all of that Party’s Covered Tax Agreements.

Paragraph 2

45. Paragraph 2 requires each Party that chooses to include Annex V (Additions to the subject to tax rule: Circuit-breaker provision) in its Covered Tax Agreement to notify the Depository of its choice.

Paragraph 3

46. Paragraph 3 provides that where one Contracting Jurisdiction to a Covered Tax Agreement has made a notification under paragraph 2, Annex V (Additions to the subject to tax rule: Circuit-breaker provision) will be included in that Covered Tax Agreement, in addition to Annex I (The subject to tax rule), and will form an integral part thereof.

Part III. – Final provisions

Article 8 – Signature and Ratification, Acceptance or Approval

Paragraph 1

47. Paragraph 1 provides that the Convention will be open for signature as of 2 October 2023. It goes on to provide that the Convention is open for signature by all States.

Paragraph 2

48. Paragraph 2 provides that signature of the Convention shall be followed by ratification, acceptance or approval. The appropriate term will depend on domestic legal requirements. Once the domestic procedures have been completed, an instrument of ratification, acceptance or approval must be deposited with the Depositary and this is the event which triggers the rule for the entry into force of the Convention pursuant to Article 11 of the Convention.

Article 9 – Reservations

49. Article 9 provides that no reservation may be made to the Convention.

Article 10 - Notifications

Timing of Notifications

50. Paragraphs 1, 3 and 4 set out the timing for making notifications under the Convention. Essentially, the Convention requires that a provisional list of notifications be provided to the Depositary at the time of signature and that a final list of notifications, subject to subsequent changes to that list which are explicitly authorised by the provisions of Article 10(5) of the Convention, be provided to the Depositary at the time of the deposit of the instrument of ratification, acceptance or approval. At the same time, the Convention allows for the possibility that a final list of notifications, subject to subsequent changes to that list which are explicitly authorised by the provisions of Article 10(5) of the Convention, can be provided to the Depositary at the time of signature (in such cases, the document containing the notifications must explicitly specify that it is to be considered final).

Paragraph 1

51. Paragraph 1 provides that notifications made pursuant to certain provisions in the Convention shall be made either at the time of signature or when depositing the instrument of ratification, acceptance or approval. This general rule applies subject to Article 10(5) (the possibility to extend the list of agreements notified under Article 2(1)(a)(ii) and to make any additional notifications that may be required in respect of the newly added agreements as well as to make new notifications if a newly added agreement is the first inclusion in the list of a tax agreement entered into by or on behalf of a jurisdiction or territory for whose international relations the Party is responsible); and Article 12(8) (the notifications required when a Party makes a notification pursuant to Article 12(6) on entry into effect in order to allow for the completion of its internal procedures for that purpose).

52. Paragraph 1 sets out an exhaustive list of the required notifications by reference to the provision in which they are set out. These include notifications related to the inclusion of Annexes and the notification pursuant to Article 12(6).

Paragraph 2

53. Paragraph 2 requires a Party which has included, in its list of Covered Tax Agreements pursuant to Article 2(1)(a)(ii) of the Convention, one or more tax agreements entered into by or on behalf of a jurisdiction or territory for whose international relations it is responsible pursuant to Article 2(1)(a)(i)(B) of the Convention, to deposit a separate list

of notifications for that jurisdiction or territory. The notifications of that Party, or made by that Party in respect of Covered Tax Agreements entered into by or on behalf of a jurisdiction or territory for whose international relations that Party is responsible, can be different. This separate list of notifications will apply to all agreements entered into by or on behalf of that jurisdiction or territory which are covered by the Convention.

54. The word “territory” is used in addition to “jurisdiction” in order to capture the various terms used to refer to non-State entities for whose international relations a State is responsible. The words “by or on behalf of” are also intended to capture the various ways in which a tax agreement may be concluded in respect of a non-State jurisdiction or territory. In certain cases, the tax agreement may be entered into by the jurisdiction or territory itself while, in other cases, the State which is responsible for the international relations of the jurisdiction or territory may enter into the tax agreement on its behalf. In both situations, the State Party responsible for the international relations of the jurisdiction or territory shall provide a list of notifications in respect of that jurisdiction or territory, which may be different from the State Party’s own list of notifications.

55. Notifications to be applied in respect of the jurisdiction or territory shall apply to all tax agreements which are concluded by that jurisdiction or territory and which are or later become Covered Tax Agreements, including agreements which are added in the future pursuant to Article 10(5) of the Convention.

56. The deposit by a Party of the list of notifications in respect of a jurisdiction or territory pursuant to Article 10(2) shall take place either: (i) at the same time as the deposit of the list of notifications of the relevant Party if one or more tax agreements of the jurisdiction or territory are included in the Party’s initial list of tax agreements pursuant to Article 2(1)(a)(ii); or (ii) at the same time as the notification of an extension of the list of agreements pursuant to Article 10(5) of the Convention if that extension includes for the first time a tax agreement entered into by the jurisdiction or territory.

Paragraph 3

57. Paragraph 3 provides that if notifications are made at the time of signature, they shall be confirmed upon deposit of the instrument of ratification, acceptance or approval since this is the moment at which consent to be bound by the Convention is expressed following the completion of domestic procedures. At the time of the deposit of the instrument of ratification, acceptance or approval, changes may be made to the list of notifications including the addition or deletion of notifications or the modification of notifications made at the time of signature.

58. Paragraph 3 provides for an exception in a case in which a Party explicitly specifies that the list of notifications it makes at the time of signature is to be considered definitive. In such cases, no confirmation of the notifications would be required upon deposit of the instrument of ratification, acceptance or approval. The definitive nature of notifications made upon signature is, however, subject to the provisions of: Article 10(5) (the possibility to extend the list of agreements notified under Article 2(1)(a)(ii) and to make any additional notifications that may be required in respect of the newly added agreements as well as to make new notifications if a newly added agreement is the first inclusion in the list of a tax agreement entered into by or on behalf of a jurisdiction or territory for whose international relations the Party is responsible); and Article 12(8) (the notifications required when a Party makes a notification pursuant to Article 12(6) on entry into effect in order to allow for the completion of its internal procedures for that purpose).

Paragraph 4

59. Paragraph 4 provides that if notifications are not made at the time of signature, a provisional list of expected notifications shall be provided to the Depositary at that time. This provisional list is for transparency purposes only and is intended to give other Signatories a preliminary indication of the Signatory’s intended position. This takes account of the nature of the Convention which will operate to amend existing bilateral relationships.

Accordingly, provisional indications of intended positions are important to allow an understanding of the likely amendments to an existing tax agreement and to facilitate domestic ratification procedures as well as to prepare for the implementation of the amendments made by the Convention. The provisional list of expected notifications under Article 10(4) does not restrict the ability of that Signatory to submit a modified list of notifications upon deposit of the instrument of ratification, acceptance or approval.

Paragraph 5

60. Paragraph 5 provides that the list of agreements notified under Article 2(1)(a)(ii) may be extended at any time by means of a notification addressed to the Depository.

61. The Party must specify any additional notifications that are required under Article 10(1)(b) through (d) to reflect the inclusion of the additional agreements.

62. In addition, as noted above, if the extension results for the first time in the inclusion of a tax agreement entered into by or on behalf of a jurisdiction or territory for whose international relations a Party is responsible, the Party shall specify at that time any notifications that would apply to Covered Tax Agreements entered into by or on behalf of that jurisdiction or territory.

63. Finally, paragraph 5 provides that, on the date on which a newly added agreement becomes a Covered Tax Agreement under the Convention, the provisions on entry into effect in Article 12 will govern the date on which the Convention will have effect.

Paragraph 6

64. Paragraph 6 provides that the competent authorities of Contracting Jurisdictions to a Covered Tax Agreement shall notify each other in writing of any provisions in the Covered Tax Agreement that may interact with the STTR and that are described in Annex I (The subject to tax rule). Those include the provisions described in:

- paragraph 1 of Article 1 in Annex I (The subject to tax rule, Taxing right in source Jurisdiction where covered income taxed at below minimum rate);
- subparagraph a) of paragraph 4 of Article 1 in Annex I (The subject to tax rule, Covered income);
- subparagraph c) of paragraph 4 of Article 1 in Annex I (The subject to tax rule, Covered income);
- subparagraph b) of paragraph 6 of Article 1 in Annex I (The subject to tax rule, Preferential adjustment);
- subparagraph b) of paragraph 13 of Article 1 in Annex I (The subject to tax rule, Application to permanent establishment in source Jurisdiction); and
- paragraph 15 of Article 1 in Annex I (The subject to tax rule, Elimination of double taxation).

Paragraph 7

65. Paragraph 7 provides that the competent authority of a Contracting Jurisdiction to a Covered Tax Agreement shall notify the competent authority of the other Contracting Jurisdiction in writing where the first-mentioned Contracting Jurisdiction satisfies the condition for the lower threshold to apply in accordance with paragraph 12 of Article 1 in Annex I (The subject to tax rule, Materiality threshold).

Article 11 – Entry into Force

Paragraph 1

66. Paragraph 1 provides that the Convention will enter into force on the first day of the month following the expiration of a period of three calendar months beginning on the date of deposit of the second instrument of ratification, acceptance or approval. As of that date, the two Signatories which have deposited their instruments of ratification, acceptance or approval to the Convention will become Parties and be bound by the Convention.

67. In a case where the date of deposit of the second instrument of ratification, acceptance or approval takes place on the first day of a month, “the first day of the month following the expiration of a period of three calendar months beginning on the date of deposit” will be four months after the deposit of the instrument or instruments of ratification, acceptance or approval. For example, if the second instrument of ratification, acceptance or approval is deposited on 1 March 2024, the Convention will enter into force on 1 July 2024.

Paragraph 2

68. Paragraph 2 provides that for each Signatory ratifying, accepting or approving the Convention after the deposit of the second instrument of ratification, acceptance or approval, the Convention shall enter into force for that State or jurisdiction on the first day of the month following the expiration of a period of three calendar months after the date of the deposit by such State or jurisdiction of its instrument of ratification, acceptance or approval. As of this date, such State or jurisdiction will be bound by the Convention and its Covered Tax Agreements will be modified with effect from the date set out in Article 12.

69. In a case where the date of deposit of the instrument of ratification, acceptance or approval takes place on the first day of a month, the Convention will enter into force for that Signatory four months later as described with respect to Article 11(1).

Article 12 – Entry into Effect

70. Article 12 sets out when the provisions of the Convention shall have effect.

Paragraph 1

71. Paragraph 1 provides that, subject to the other paragraphs in Article 12, the provisions in the Convention take effect with respect to a Covered Tax Agreement on or after the latest of the dates on which the Convention enters into force for the Contracting Jurisdictions to that Covered Tax Agreement.

Paragraph 2

72. Paragraph 2 provides that the provisions in Annex I (The subject to tax rule) have effect in each Contracting Jurisdiction with respect to a Covered Tax Agreement for taxes levied in accordance with Annex I (The subject to tax rule) by a Contracting Jurisdiction, on or after the first day of a fiscal year beginning on or after the expiration of a period of six calendar months from the latest of the dates on which the STTR MLI enters into force for the Contracting Jurisdictions to that Covered Tax Agreement.

73. Under paragraph 2, Annex I (The subject to tax rule) can only have effect on the first day of a fiscal year. This is consistent with the approach to administration of the STTR in paragraph 14 of Article 1 in Annex I (The subject to tax rule, Administration) under which tax under the STTR is assessed and levied only following the end of a fiscal year.

Paragraph 3

74. Paragraph 3 provides that the provisions in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis), Annex III (Additions to the subject to tax

rule: Taxes imposed at the point of distribution), Annex IV (Additions to the subject to tax rule: Recognised pension fund), and Annex V (Additions to the subject to tax rule: Circuit-breaker provision) have effect with respect to a Covered Tax Agreement on or after the date on which the provisions in Annex I (The subject to tax rule) have effect for that Covered Tax Agreement.

Paragraph 4

75. Paragraph 4 provides for the entry into effect in each Contracting Jurisdiction of the Convention's provisions for Covered Tax Agreements which result from an extension pursuant to Article 10(5) of the list of agreements notified under Article 2(1)(a)(ii). The time period starts running as of the date of the communication by the Depositary of the notification of the extension of the list of agreements, rather than from the latest of the dates of the entry into force of the Convention for each of the Contracting Jurisdictions to the Covered Tax Agreement.

Paragraph 5

76. Paragraph 5 provides that a Party may choose to delay the entry into effect of the provisions of the Convention and thus the amendments of Covered Tax Agreements until that Party has completed its internal procedures for this purpose. In such cases, the rule on entry into effect set out in Article 12(2) and (5) would apply as from the date that is 30 days after the Depositary has received a notification from each notifying Party that it has completed its internal procedures with respect to a specific Covered Tax Agreement. If more than one Contracting Jurisdiction to a Covered Tax Agreement makes this notification, the trigger date for the rule on entry into effect would be 30 days after the Depositary has received a notification from the last notifying Contracting Jurisdiction that it has completed its internal procedures with respect to that Covered Tax Agreement.

77. Mechanically, this is achieved by replacing specific sections of paragraphs 2 and 5 such that the date from which the entry into effect of the Convention is calculated is modified to be the date 30 days after the date of receipt by the Depositary of the latest notification by each Contracting Jurisdiction making the notification that it has completed its internal procedures for the entry into effect of the provisions of the Convention with respect to that specific Covered Tax Agreement.

78. Such a notification with respect to the entry into effect of the provisions of the Convention, would be required from a notifying Party with respect to each Covered Tax Agreement.

79. An additional delay of 30 days between such notification and the entry into effect is provided for practical reasons, to avoid the risk that the implementation of provisions could be required without sufficient notice.

Paragraph 6

80. Paragraph 6 provides that each Party that chooses to apply paragraph 5 to its Covered Tax Agreement shall notify the Depositary of its choice and that such a notification shall cover all of its Covered Tax Agreements.

Paragraph 7

81. Paragraph 7 provides that where at least one Contracting Jurisdiction to a Covered Tax Agreement has made a notification under paragraph 6, paragraph 5 shall apply to that Covered Tax Agreement for both Contracting Jurisdictions. As such, if any Contracting Jurisdiction to a Covered Tax Agreement makes the notification in paragraph 6, the modified timelines for entry into effect will apply to all Contracting Jurisdictions to the Covered Tax Agreement.

Paragraph 8

82. Paragraph 8 provides that the Party which made the notification under paragraph 6 shall notify the confirmation of the completion of its internal procedures simultaneously to the Depositary and the other Contracting Jurisdiction to the Covered Tax Agreement to which the notification relates. This is important in order to provide the other Contracting Jurisdiction with notice as early as possible as to when the timelines for entry into effect will start running with respect to the Covered Tax Agreement.

Article 13 – Depositary

Paragraph 1

83. Paragraph 1 provides that the Secretary-General of the Organisation for Economic Co-operation and Development is the Depositary of the Convention.

Paragraph 2

84. Paragraph 2 sets out a non-exhaustive list of the acts, notifications or communications in relation to the Convention of which the Depositary will notify all Parties and Signatories. The Depositary must notify the Parties and Signatories within one calendar month of the act, notification or communication.

Paragraph 3

85. Paragraph 3 provides that the Depositary shall maintain publicly available lists of Covered Tax Agreements and notifications made by Parties.

Article 14 – Authentic Texts and Translation into Other Languages

Paragraph 1

86. Paragraph 1 provides that the Convention is authenticated in English and French, the text being equally authoritative in each language. It further clarifies that the original texts of the Convention in both languages must be deposited with the Secretary-General of the Organisation for Economic Co-operation and Development.

Paragraph 2

87. Paragraph 2 provides that the Contracting Jurisdictions to a Covered Tax Agreement may agree on translations of Annexes I to V into languages other than English and French for purposes of including these Annexes in their Covered Tax Agreements, which may be authenticated by the Contracting Jurisdictions to the Covered Tax Agreement in those other languages.

Annex I. – Subject to tax rule

Article 1 – The subject to tax rule

88. Article 1 (The subject to tax rule) is based on the model treaty provision included in Chapter I of the STTR Report, and explained in the commentary included in that Report, together with provisions based on the provisions included in Chapter II of that Report governing the interaction between the STTR model treaty provision and the elimination of double taxation provisions contained in Covered Tax Agreements.

Paragraph 1 – Taxing right in source Jurisdiction where covered income taxed at below minimum rate

89. Paragraph 1 is based on paragraph 1 of the model treaty provision included in the STTR Report (“the model provision”), which reads as follows:

Where in accordance with the provisions of Articles 7, 11, 12 and 21 the tax that may be charged in a Contracting State on an item of covered income arising in that State is limited, that income may, notwithstanding those provisions, be taxed in that State if it is subject to a tax rate below 9% in the Contracting State of which the person deriving that income is a resident.

90. Changes are made in paragraph 1 to the text of paragraph 1 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 1 of the model provision to a “Contracting State” are replaced with references to a “contracting jurisdiction” and the words “the provisions of Articles 7, 11, 12 and 21” are replaced by the provisions in subparagraphs a) to c) of paragraph 1.

91. Paragraph 1 of the model provision includes cross-references to Articles of the OECD Model Tax Convention (“OECD Model”) that limit a source Jurisdiction’s right to tax items of income included in paragraph 4 of the model provision (“covered income”): that is, Article 7 (business profits); Article 11 (interest); Article 12 (royalties); and Article 21 (other income).

92. The provision in paragraph 1 reflects changes to paragraph 1 of the model provision to adapt it to the provisions of Covered Tax Agreements that do not precisely align with the OECD Model, but have the effect of limiting a Contracting Jurisdiction’s right to tax items of covered income. The relevant provisions of a Covered Tax Agreement might not align with the OECD Model because, for example: although otherwise conforming to the equivalent OECD Model provision, they have divergent article numbering; or they are based on provisions in the United Nations Model Tax Convention between Developed and Developing Countries (“UN Model”), such as Article 12A of the UN Model. The provision in paragraph 1 therefore uses descriptive language to identify those provisions.

93. Subparagraph a) of paragraph 1 describes provisions of a Covered Tax Agreement that condition a Contracting Jurisdiction’s right to tax the profits of an enterprise of the other Contracting Jurisdiction upon that enterprise carrying on business in the first-mentioned Jurisdiction through a permanent establishment situated therein. This will include provisions equivalent to Article 7 of the OECD and UN Models.

94. Subparagraph b) of paragraph 1 describes provisions of a Covered Tax Agreement that apply to interest, royalties, or income from the provision of services arising in a Contracting Jurisdiction and either: allocate an exclusive taxing right over such income to the other Contracting Jurisdiction; or limit the rate at which such income may be taxed in the Jurisdiction the income arises. This will include provisions equivalent to Article 11 of the OECD and UN Models, Article 12 of the OECD Model, and Articles 12 and 12A of the UN Model. It does not include provisions equivalent to Article 8 of the OECD and UN Models, which allocate an exclusive taxing right to a Contracting Jurisdiction in respect of the profits of an enterprise from the operation of ships or aircraft in international traffic. Paragraph 1 of the model provision provides an exhaustive list of the provisions limiting a Contracting Jurisdiction’s right to tax covered income that are relevant for the purposes of

applying the STTR and does not include Article 8 of the OECD Model. Paragraph 1 of Article 1 in Annex I (The subject to tax rule, Taxing right in source Jurisdiction where covered income taxed at below minimum rate) is designed to produce the same effect when Annex I (The subject to tax rule) is included in a Covered Tax Agreement.

95. Subparagraph c) of paragraph 1 describes provisions of a Covered Tax Agreement that: apply to items of income not otherwise dealt with in the Covered Tax Agreement because the income does not have a classification specifically addressed in the provisions of that Covered Tax Agreement that allocate taxing rights over specific classes of income; and that either provide that such income is taxable only in the Contracting Jurisdiction of which the person deriving the income is a resident, or limit the rate at which the other Contracting Jurisdiction may tax such income. This includes provisions equivalent to Article 21 of the OECD Model.

Paragraph 2 – Source jurisdiction taxing right limited to a specified rate

96. Paragraph 2 is based on paragraph 2 of the model provision, which reads as follows:

However, the tax charged in accordance with paragraph 1 in the Contracting State in which the item of covered income arises shall not exceed the specified rate multiplied by the gross amount of the covered income. For the purposes of this Article, and subject to the second sentence of paragraph 3, the specified rate is equal to the difference between 9% and the tax rate determined in accordance with paragraph 5, on that item of covered income in the Contracting State of which the person deriving that income is a resident.

97. Changes are made in paragraph 2 to the text of paragraph 2 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 2 of the model provision to a “Contracting State” are replaced with references to a “contracting jurisdiction”.

Paragraph 3 – Interaction with other Articles

98. Paragraph 3 is based on paragraph 3 of the model provision, which reads as follows:

The provisions of paragraphs 1 and 2 shall not apply where the gross amount of the item of covered income may be taxed, in accordance with any other provision of this Convention, in the Contracting State in which it arises at a rate equal to or greater than the specified rate, as determined in accordance with paragraph 2. Where, in accordance with any other provision of this Convention, the gross amount of the item of covered income may be taxed in the Contracting State in which it arises at a rate that is lower than the specified rate, as determined in accordance with paragraph 2, that other provision shall continue to apply and the specified rate shall be reduced by deducting such lower rate.

99. Changes are made in paragraph 3 to the text of paragraph 3 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 3 of the model provision to “this Convention” are replaced with references to “this agreement” and references in paragraph 3 of the model provision to a “Contracting State” are replaced with references to a “contracting jurisdiction”.

Paragraph 4 – Covered income

100. Paragraph 4 is based on the model provision, which reads as follows:

For the purposes of this Article:

a) the term “covered income” means:

- (i) *interest, as defined in paragraph 3 of Article 11 (but omitting the words “as used in this Article”);*
 - (ii) *royalties, as defined in paragraph 2 of Article 12 (but omitting the words “as used in this Article”);*
 - (iii) *payments made in consideration for the use of, or the right to use, distribution rights in respect of a product or service;*
 - (iv) *insurance and reinsurance premiums;*
 - (v) *fees to provide a financial guarantee, or other financing fees;*
 - (vi) *rent or any other payment for the use of, or the right to use, industrial, commercial or scientific equipment; or*
 - (vii) *any income received in consideration for the provision of services.*
- b) *Notwithstanding the provisions of subparagraph a), the term “covered income” does not include:*
- (i) *rent or any other payment for the use of, or the right to use, a ship to be used for the transportation of passengers or cargo in international traffic on a bare boat charter basis; or*
 - (ii) *items of income derived by a person whose tax liability in respect of that income, under the laws of a Contracting State, is determined by reference to the tonnage of a ship.*
- c) *Paragraph 5 of Article 11 shall apply to determine whether interest within subdivision (i) of subparagraph a) is deemed to arise in a Contracting State. In all other cases, an item of covered income falling within subdivisions (ii) to (vii) of subparagraph a) shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying the item of covered income, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment in connection with which the liability to pay the item of covered income was incurred, and such item of covered income is borne by such permanent establishment, then such item of covered income shall be deemed to arise in the State in which the permanent establishment is situated.*

101. Changes are made in paragraph 4 to the text of paragraph 4 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 4 of the model provision to a “Contracting State” and “that State” are replaced with references to a “contracting jurisdiction” and “that jurisdiction”; subdivisions (i) and (ii) of subparagraph a) of paragraph 4 of the model provision are modified to replace cross-references to specific Articles of the OECD Model with descriptive references to provisions of the Covered Tax Agreement; subparagraph c) of paragraph 4 of the model provision is modified to apply existing sourcing rules in the Covered Tax Agreement; and subparagraph d) is added to paragraph 4 to provide a sourcing rule where the Covered Tax Agreement does not include such a rule for an item of covered income.

102. Subdivision (i) of subparagraph a) of paragraph 4 of the model provision includes a cross-reference to paragraph 3 of Article 11 of the OECD Model. That provision defines the term “interest”. The parenthetical language in subdivision (i) of the model provision then modifies that definition by providing that the words “as used in this Article” are omitted when applying it for the purposes of the model provision. The changes made in subdivision (i) of subparagraph a) of paragraph 4 replace that cross-reference to paragraph 3 of Article 11 of the OECD Model with a descriptive reference to the provisions of a Covered Tax Agreement that allocate taxing rights over interest, and apply for the purposes of Article 1 in Annex I (The subject to tax rule) the definition of interest used in the described provisions

of the Covered Tax Agreement. The parenthetical language in subdivision (i) is changed to omit the words “as used in this Article” only if those words are used in the definition of “interest” used in the described provision of the Covered Tax Agreement.

103. Subdivision (ii) of subparagraph a) of paragraph 4 of the model provision includes a cross-reference to paragraph 2 of Article 12 of the OECD Model. That provision defines the term “royalties”. The parenthetical language in subdivision (ii) of the model provision then modifies that definition by providing that the words “as used in this Article” are omitted when applying it for the purposes of the model provision. The changes made to subdivision (ii) of subparagraph a) of paragraph 4 replace that cross-reference to paragraph 2 of Article 12 of the OECD Model with a descriptive reference to the provisions of a Covered Tax Agreement that allocate taxing rights over royalties, and apply for the purposes of Article 1 in Annex I (The subject to tax rule) the definition of royalties used in the described provisions of the Covered Tax Agreement. The parenthetical language in subdivision (ii) is changed to omit the words “as used in this Article” only if those words are used in the definition of “royalties” used in the described provision of the Covered Tax Agreement.

104. The effect of the changes to subdivisions (i) and (ii) of subparagraph a) of paragraph 4 is to use, for the purposes of Article 1 in Annex I (The subject to tax rule), the existing definitions of “interest” and “royalties” used in a Covered Tax Agreement.

105. The first sentence of subparagraph c) of paragraph 4 of the model provision includes a cross-reference to paragraph 5 of Article 11 of the OECD Model. That provision provides a sourcing rule for interest income. The remainder of subparagraph c) of paragraph 4 of the model provision provides a sourcing rule for all other items of covered income. This approach is taken in the model provision because, under the OECD Model, only Article 11 (interest) includes a sourcing rule. The changes made in subparagraph c) of paragraph 4 replace the reference to paragraph 5 of Article 11 of the OECD Model, and the sourcing rule provided by subparagraph c) of paragraph 4 of the model provision, with a provision that describes sourcing rules included in provisions of a Covered Tax Agreement that correspond to the provisions described in paragraph 1; and apply those sourcing rules for the purposes of Article 1 in Annex I (The subject to tax rule). The effect of this change is to apply the existing sourcing rules in a Covered Tax Agreement, to the extent that there are such rules in a Covered Tax Agreement and they are applicable to items of covered income.

106. Paragraph 4 of the model provision does not include subparagraph d) of paragraph 4. Subparagraph d) of paragraph 4 serves a similar function to the second and third sentences of subparagraph c) of paragraph 4 of the model provision, but adapted to the provisions of a Covered Tax Agreement. Subparagraph d) of paragraph 4 applies where a Covered Tax Agreement does not include a sourcing rule described in subparagraph c) that applies to an item of covered income and, in that case, provides such a sourcing rule for the purposes of Article 1 in Annex I (The subject to tax rule). The sourcing rule provided by subparagraph d) of paragraph 4 in those cases is aligned with the sourcing rule provided by the second and third sentence of subparagraph c) of paragraph 4 of the model provision.

Paragraph 5 – Meaning of “tax rate”

107. Paragraph 5 is based on paragraph 5 of the model provision, which reads as follows:

For the purposes of this Article:

- a) ***the tax rate on an item of covered income in the Contracting State of which the person deriving that income is a resident is the statutory rate of tax applicable in that State on such income; however, where that person benefits from a preferential adjustment in respect of such income in that State, the tax rate shall be determined after taking into account the effect of that preferential adjustment;***

- b) *the taxes to be taken into account for the purposes of the tax rate determination are the taxes covered under Article 2 and any tax on net income (“relevant taxes”); and*
- c) *the competent authorities of the Contracting States shall, so far as it is relevant for the application of this Article, notify each other in writing of:*
 - (i) *the statutory rate (or any changes to those rates) applicable to residents of that Contracting State with respect to items of covered income; and*
 - (ii) *the provisions of their taxation law (or any changes to those provisions) that apply to items of covered income of residents of that Contracting State and may result in a preferential adjustment.*

108. Changes are made in paragraph 5 to the text of paragraph 5 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 5 of the model provision to a “Contracting State” and “that State” are replaced with references to a “contracting jurisdiction” and “that jurisdiction”; and subparagraph b) includes a reference to “this agreement” in place of the reference in the model provision to “Article 2”. This last change reflects the fact that Annex I (The subject to tax rule) will be included in a Covered Tax Agreement which will include provisions determining the taxes to which it applies; the replaced reference to “Article 2” in the model provision, in contrast, is to Article 2 of the OECD Model.

Paragraph 6 – Preferential adjustment

109. Paragraph 6 is based on paragraph 6 of the model provision, which reads as follows:

- a) *For the purposes of this Article, a preferential adjustment in respect of an item of covered income means a permanent reduction in the amount of the covered income subject to tax, or the tax payable on that income, in the Contracting State of which the person deriving the covered income is a resident, in the form of:*
 - (i) *a full or partial exemption or exclusion from income;*
 - (ii) *a deduction from the tax base that is computed on the basis of the amount of income and without regard to any corresponding payment or obligation to make a payment; or*
 - (iii) *a tax credit, excluding a credit for foreign taxes paid on the income, that is computed on the basis of the amount of income or tax on such income;*
that is directly linked to the item of covered income or that arises under a regime that provides a tax preference for income from geographically mobile activities.
- b) *For the purposes of this paragraph:*
 - (i) *no account shall be taken of any obligation to provide a[n] [exemption or] credit under the provisions of Article [23 A] [23 B]; and*
 - (ii) *the term “permanent reduction” means a reduction that is not expected to reverse over time. However, a permanent reduction shall also be deemed to arise where the person deriving an item of covered income has control over the point at which that income is recognised for tax purposes in the Contracting State of which that person is a resident and that income is not recognised for tax purposes in that State within three years following the end of the fiscal year in which that income arises.*

110. Changes are made in paragraph 6 to the text of paragraph 6 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 6 of the model provision to a “Contracting State” and “State” are replaced with references to a

“contracting jurisdiction” and “jurisdiction”; and subdivision (i) of subparagraph b) of paragraph 6 of the model provision is modified to replace cross-references Article 23 A and 23 B of the OECD Model with descriptive references to provisions of the Covered Tax Agreement.

111. Subdivision (i) of subparagraph b) of paragraph 6 of the model provision includes alternative cross-references to Article 23 A and 23 B of the OECD Model. The changes made in subdivision (i) of subparagraph b) of paragraph 6 replace those cross-references with descriptive references to the provisions of a Covered Tax Agreement (referred to as “this agreement”) to eliminate double taxation by exemption or credit. Clause (A) describes such provisions of a Covered Tax Agreement that require a Contracting Jurisdiction to eliminate double taxation by providing an exemption; and clause (B) describes such provisions of a Covered Tax Agreement that require a Contracting Jurisdiction to eliminate double taxation by providing a credit.

Paragraph 7 – Covered income attributable to permanent establishment in third jurisdiction

112. Paragraph 7 is based on paragraph 7 of the model provision, which reads as follows:

Where:

- a) for the purposes of paragraph 1 the tax rate applicable to an item of covered income arising in a Contracting State and derived by an enterprise of the other Contracting State is below 9%; and*
- b) that item of covered income is treated as attributable to a permanent establishment of the enterprise situated in a third jurisdiction by both the last-mentioned Contracting State and the third jurisdiction;*

the tax rate referred to in paragraph 5 shall be determined by reference to the statutory rate, and the effect of any preferential adjustment, applicable in that third jurisdiction to the item of covered income attributable to that permanent establishment (as if the references in subparagraph a) of paragraph 5 and paragraph 6 to the person deriving the income and its State of residence were, respectively, to the permanent establishment and the jurisdiction in which it is situated), if that rate after any preferential adjustment is higher than the applicable tax rate in the last-mentioned Contracting State.

113. Changes are made in paragraph 7 to the text of paragraph 7 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References to paragraph 7 of the model provision to a “Contracting State” are replaced with references to “contracting jurisdiction”.

Paragraph 8 – Exclusions

114. Paragraph 8 is based on paragraph 8 of the model provision, which reads as follows:

The preceding provisions of this Article shall not apply to an item of covered income arising in a Contracting State paid by an individual or derived by a resident of the other Contracting State that is:

- a) an individual;*
- b) not connected to the payer;*
- c) a recognised pension fund;*
- d) a non-profit organisation that is established and maintained exclusively for religious, charitable, scientific, artistic, cultural, sporting, educational, or other similar purposes;*

- e)
- (i) *that other State itself, or a political subdivision or local authority thereof;*
- (ii) *the central bank;*
- (iii) *an agency, mandatary or instrumentality of, or an entity or arrangement established or created by, a Contracting State, political subdivision or local authority; and*
- (iv) *any other person wholly or almost wholly owned directly or indirectly by a Contracting State, its political subdivisions or local authorities, agencies, mandataries or instrumentalities,*
provided, in the case of subdivisions (iii) or (iv), that their principal purpose is to fulfil a government function, and that they do not carry on a trade or business;
- f) *an international organisation;*
- g) *a professionally managed entity or arrangement designed to invest funds obtained from unconnected persons primarily to generate investment income or to provide protection against an event, for the benefit of those persons provided that the entity or arrangement, or its managers, are regulated. A company that is subject to regulation in that other Contracting State as an insurance company is deemed to satisfy this subparagraph, but only to the extent the covered income is derived from assets held for the purpose of meeting policyholder liabilities;*
- h) *an entity or arrangement the taxation of which achieves a single level of taxation either in the hands of the entity or arrangement or its interest holders (with at most one year of deferral) provided that the entity or arrangement is widely held and either:*
 - (i) *holds predominantly immovable property; or*
 - (ii) *the entity or arrangement or its interest holders (excluding persons described in this paragraph) are subject to a tax rate of at least 9% in the Contracting State of which the entity or arrangement is a resident; or*
- i) *an entity or arrangement that is wholly or almost wholly owned (directly or indirectly), or established or created, by one or more persons, entities, or arrangements referred to in subparagraphs c) to h):*
 - (i) *that is established and operated exclusively or almost exclusively to hold assets or manage or invest funds for the benefit of a person, entity, or arrangement referred to in subparagraphs c) to h) or that only carries out activities that are ancillary to those carried out by a person, entity, or arrangement referred to in subparagraphs c) to h); or*
 - (ii) *in the case of a person, entity or arrangement referred to in subparagraph e), is established and operated exclusively or almost exclusively to conduct the activities in subdivision (i) or to conduct related investment activities for a person, entity or arrangement referred to in that subparagraph.*

115. Changes are made in paragraph 8 to the text of paragraph 8 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 8 of the model provision to a “Contracting State” and “State” are replaced with references to a “contracting jurisdiction” and “jurisdiction”.

116. Changes are also made in subparagraph c) of paragraph 8 to the text of paragraph 8 of the model provision to include additional references to “pension fund”, “recognised pension scheme” or “pension scheme”. Subparagraph c) of paragraph 8 of the model

provision relies on the definition of a “recognised pension fund” in subparagraph i) of paragraph 1 of Article 3 of the OECD Model. The additional references to “pension fund”, “recognised pension scheme”, or “pension scheme” adapt subparagraph c) of paragraph 8 for inclusion in a Covered Tax Agreement that, while including a similar definition, does not use the precise term “recognised pension fund” but employs the alternative terminology “pension fund”, “recognised pension scheme”, or “pension scheme”.

Paragraph 9 – Mark-up threshold

117. Paragraph 9 is based on paragraph 9 of the model provision, which reads as follows:

The provisions of paragraphs 1 and 2 shall not apply to covered income falling within subdivisions (iii) to (vii) of subparagraph a) of paragraph 4 if the gross amount of the item or items of covered income does not exceed an amount equal to the costs incurred by the person deriving the income and that are directly or indirectly attributable to earning the income plus a mark-up of 8.5% on those costs. For the purposes of this paragraph:

- a) all income derived by a person under the terms of a single contractual arrangement during a fiscal year with respect to the same category of covered income and all costs incurred during the same fiscal year and that are directly or indirectly attributable to earning that covered income shall be aggregated for the purpose of determining the mark-up on costs;***
- b) all income derived by a person during a fiscal year with respect to more than one contractual arrangement or category of covered income, and all costs incurred during the same fiscal year and that are directly or indirectly attributable to earning that covered income, shall be aggregated for the purpose of determining whether the mark-up on costs if, taken as a whole, the covered income is so interrelated that an aggregate analysis is more reliable;***
- c) where a person deriving income described in subdivision (vii) of subparagraph a) of paragraph 4 incurs costs that are directly or indirectly attributable to earning that income and such costs include costs from transactions with a person that is a resident of a third jurisdiction and connected to the person deriving the income, the costs incurred from those transactions shall be disregarded to the extent that they exceed 80% of total costs if the connected person that is a resident of a third jurisdiction is subject, in respect of the income received from those transactions, to a tax rate below 9% in that third jurisdiction and:***
 - (i) the connected person provides the services directly to the person paying the consideration for the provision of services; or***
 - (ii) the connected person enters into transactions with another person connected to the person deriving the income and that other person is subject, in respect of the income derived from those transactions, to a tax rate below 9% in the jurisdiction of which that other person is a resident and that other person provides the services directly to the person paying the consideration of the provision of services.***

This paragraph does not apply where the item of covered income is an original or related payment, within the meaning of paragraph 11, in respect of which the conditions in subparagraphs a) to c) of paragraph 11 are met.

118. Changes are made in paragraph 9 to ensure that the mark-up threshold applies to the categories of income identified in the model provision. The mark-up threshold in the model provision applies to income identified in subdivisions (iii) to (vii) of subparagraph a) of paragraph 4. This means that the mark-up threshold applies to all covered income except

for interest and royalties. The model provision is consistent with the structure and terminology used in the OECD Model and so the definitions of “interest” and “royalties” for the purpose of the model provision are those in Articles 11 and 12 of the OECD Model.

119. However, Covered Tax Agreements may contain definitions of “interest” and “royalties” that do not follow the definitions in Articles 11 and 12 of the OECD Model. It is possible that items of covered income described in subdivisions (iii) to (vii) of subparagraph a) of paragraph 4 of the model provisions may be included in the definition of “interest” and “royalties” in a Covered Tax Agreement. If that were the case, the mark-up threshold would not apply as intended in the model provision.

120. To ensure the mark-up threshold applies as intended, paragraph 9 describes in full the income to which the mark-up threshold applies, rather than following paragraph 9 of the model provision which cross-references to the relevant categories of covered income in subparagraph a) of paragraph 4. The result is that the mark-up threshold applies to that income regardless of whether it is defined as “interest” or “royalties” in the Covered Tax Agreement. For example, paragraph 9 means that the mark-up threshold applies to income received in consideration of the provision of services even if such income is defined as a royalty in the Covered Tax Agreement.

Paragraph 10 – Connected persons

121. Paragraph 10 is based on paragraph 10 of the model provision, which reads as follows:

For the purposes of this Article, a person shall be considered to be connected to another person if, based on all the relevant facts and circumstances, one has control of the other or both are under the control of the same person or persons. In any case, a person shall be considered to be connected to another person if:

- a) one possesses directly or indirectly more than 50 per cent of the beneficial interest in the other (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company’s shares or of the beneficial equity interest in the company); or***
- b) another person possesses directly or indirectly more than 50 per cent of the beneficial interest (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company’s shares or of the beneficial equity interest in the company) in each person.***

122. No changes are made in paragraph 10 to the text of paragraph 10 of the model provision.

Paragraph 11 – Connected persons targeted anti-avoidance rule

123. Paragraph 11 is based on paragraph 11 of the model provision, which reads as follows:

Where:

- a) a payment of an item of covered income arising in a Contracting State (“the original payment”) is made by a person other than an individual to a resident of either Contracting State (the “intermediary”); and***
- b) the intermediary at any time during a 365 day period that includes the day of the original payment pays, directly or indirectly, an amount equal to all or substantially all of the original payment, in the form of payments (“related payments”):***
 - (i) to a person or persons (the “connected payee”), other than a person described in paragraph 8, that is connected to the person making the original payment;***

- (ii) *the connected payee is subject, in respect of the related payments, to a tax rate below 9% in the State of which it is a resident and a statutory rate of tax in the State of which the intermediary is a resident (taking into account of any reduction in that rate by virtue of a double taxation convention) (“intermediary tax rate”) that is also below 9%; and*
- (iii) *if the intermediary includes the original payment in its taxable income in the Contracting State of which it is a resident, the related payments are deductible in computing its taxable income in that State; and*
- c) *it is reasonable to conclude that the intermediary would not have made the related payments in the absence of the original payment;*
the original payment made to an intermediary or any related payment made to a connected payee that is a resident of the other Contracting State shall be treated, for the purposes of this Article, as if it had been covered income paid to a person connected to the payer that is a resident of that other State and the tax rate to which that item of covered income is subject shall be treated for the purposes of paragraphs 1, 2 and 5 as being:
- d) *in the case where the original payment is made to an intermediary that is a resident of that other State, the higher of the tax rate to which the connected payee is subject, in respect of the related payments, in the State of which it is a resident and the intermediary tax rate; or*
- e) *in the case where the original payment is made to an intermediary that is a resident of the Contracting State in which that item of covered incomes arises, the tax rate to which the connected payee is subject, in respect of the related payments, in the State of which it is a resident.*

124. Changes are made in paragraph 11 to the text of paragraph 11 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 11 of the model provision to a “Contracting State” and “State” are replaced with references to a “contracting jurisdiction” and “jurisdiction”.

Paragraph 12 – Materiality threshold

125. Paragraph 12 is based on paragraph 12 of the model provision, which reads as follow:

The provisions of paragraphs 1 and 2 shall not apply to an item of covered income arising in a Contracting State and derived by a person that is a resident of the other Contracting State (the “tested payee”) unless the sum of:

- a) *the gross amount of covered income paid by one or more residents of the first-mentioned Contracting State that are connected to the tested payee and derived by the tested payee or one or more residents of the other State that are connected to the tested payee; and*
- b) *the gross amount of covered income borne by one or more permanent establishments situated in the first-mentioned State through which the tested payee, or persons that are connected to the tested payee, carry on business and derived by the tested payee or one or more residents of the other State that are connected to the tested payee;*

is equal to or greater than [€Y] in the fiscal year concerned.

For the purposes of this paragraph:

- c) *no account shall be taken of the tax rate that is applicable to the covered income in that other State; and*

d) persons shall be deemed not to be connected if those persons are otherwise connected solely because of control exercised, or any beneficial interest (or, in the case of a company, the aggregate vote and value of the company's shares or beneficial equity interest) possessed directly or indirectly, by a person, entity or arrangement described in:

(i) subparagraph e) of paragraph 8; or

(ii) subparagraph i) of paragraph 8, replacing the references to "subparagraphs c) to h)" with "subparagraph e)".

126. Changes are made in paragraph 12 to the text of paragraph 12 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 12 of the model provision to a "Contracting State" and "State" are replaced with references to a "contracting jurisdiction" and "jurisdiction".

127. Changes are also made in paragraph 12 to the text of paragraph 12 of the model provision to include the two thresholds applicable contingent upon the gross domestic product (GDP) of the Contracting Jurisdictions. The model provision states that the threshold is [€Y] and a footnote provides that this will be set according to the size of the smallest economy of the two Contracting Jurisdictions; for Contracting Jurisdictions with GDP equal to or greater than EUR 40 billion, the threshold will be EUR 1 million and for Contracting Jurisdictions with GDP of less than EUR 40 billion, the threshold will be EUR 250,000. This footnote is given effect in paragraph 12 through clauses A) and B) of subdivision (ii) of subparagraph a) which contain those thresholds (replacing [€Y] in the model provision).

128. The applicable threshold is calculated by reference to the GDP of the Contracting Jurisdictions on the date that the provisions of Annex I (The subject to tax rule) have effect pursuant to Article 12 (Entry into effect). The GDP of the Contracting Jurisdiction with the lowest GDP at that date will determine the threshold in paragraph 12. The GDP figure to be used for this purpose is that for the most recent calendar year that ends prior to the date that the provisions of Annex I (The subject to tax rule) enter into effect as published by the United Nations or the World Bank Group. In the case that both the United Nations and the World Bank Group have published data for the most recent calendar year that ends prior to the date that the provisions of Annex I (The subject to tax rule) enter into effect, the data from the United Nations will be used. This figure will be converted from USD to EUR at the average exchange rate over the relevant calendar year. If neither the United Nations nor the World Bank Group have published the relevant GDP data for a Contracting Jurisdiction for any of the five calendar years prior to entry into effect of the provisions of Annex I (The subject to tax rule), GDP is determined by an approximation.

129. The changes made in paragraph 12 to the text of paragraph 12 of the model provision also include amended subparagraphs and consequential changes to the citations. These begin with the chapeau to the paragraph in the model provision which is subparagraph a) in paragraph 12. These changes are not intended to create any differences of application between paragraph 12 and paragraph 12 of the model provision.

Paragraph 13 – Application to permanent establishment in source Jurisdiction

130. Paragraph 13 is based on paragraph 13 of the model provision, which reads as follows:

If the person deriving the item of covered income, being a resident of a Contracting State, carries on business in the other Contracting State in which that income arises through a permanent establishment situated therein, the provisions of paragraphs 1 and 2 shall not apply:

a) to interest and royalties if the debt claim, right or property in respect of which the interest or royalties are paid is effectively connected with that permanent establishment;

b) to other items of covered income to the extent that they are attributable to that permanent establishment in accordance with the provisions of Article 7.

In such case, the provisions of Article 7 shall apply.

131. Changes are made in paragraph 13 to the text of paragraph 13 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 13 “Contracting State” are replaced with references to “contracting jurisdiction”; and subparagraph b) and the closing language of paragraph 13 are modified to replace cross-references Article 7 of the OECD Model with descriptive references to provisions of the Covered Tax Agreement (referred to as “this agreement”).

132. Subparagraph b) of paragraph 13 of the model provision includes a cross-reference to Article 7 of the OECD Model. A further reference to Article 7 of the OECD Model is made in the closing language of paragraph 13 of the model provision. The changes made in subparagraph b) replace that cross-reference to Article 7 of the OECD Model with descriptive references to the provisions of a Covered Tax Agreement that condition a Contracting Jurisdiction’s right to tax the profits of an enterprise of the other Contracting Jurisdiction upon that enterprise carrying on business in the first-mentioned Jurisdiction through a permanent establishment situated therein. The reference to Article 7 of the OECD Model in the closing language of paragraph 13 of the model provision is replaced with a reference to the “last-mentioned provisions”, these being the provisions of a Covered Tax Agreement that are described in subparagraph b).

Paragraph 14 – Administration

133. Paragraph 14 is based on paragraph 14 of the model provision, which reads as follows:

The tax chargeable in accordance with the provisions of this Article in a Contracting State in respect of an item of covered income arising in that State and derived by a resident of the other Contracting State in a fiscal year shall be determined following the end of that fiscal year and shall not be levied by the first-mentioned State until it is so determined. The competent authorities of the Contracting States may by mutual agreement settle the mode of application of the provisions contained in this Article.

134. Changes are made in paragraph 14 to the text of paragraph 14 of the model provision to adapt it for inclusion in a Covered Tax Agreement. References in paragraph 14 to a “Contracting State”, “State”, “States” are replaced with references to a “contracting jurisdiction”, “jurisdiction” and “jurisdictions”.

Paragraph 15 – Elimination of double taxation

135. Paragraph 15 is based on and replaces the additional provisions set out in Chapter II (Elimination of Double Taxation) of the STTR Report. Those additional provisions, for inclusion in Article 23 A and Article 23 B of the OECD Model, read as follows:

Article 23 A

5. The provisions of paragraph 1 shall not apply to income derived by a resident of a Contracting State which may be taxed in the other Contracting State only in accordance with the provisions of Article [STTR].

6. The provisions of paragraph 2 shall not apply to tax paid by a resident of a Contracting State in the other Contracting State in accordance with the provisions of Article [STTR].

Article 23 B

3. The provisions of paragraph 1 shall not apply to tax paid by a resident of a Contracting State in the other Contracting State in accordance with the provisions of Article [STTR].

136. The additional provisions included in Chapter II of the STTR Report are designed to modify the provisions of Article 23 A and Article 23 B of the OECD Model to govern the interaction of the model provision with the obligations to eliminate double taxation under Articles 23 A and B.

137. In the case of Article 23 A, additional paragraph 5 provides that the obligation on a Contracting State to exempt from tax income that may be taxed in the other Contracting State under paragraph 1 of Article 23 A does not apply to income that may be taxed in the other Contracting State only in accordance with the model provision. Additional paragraph 6 provides that the obligation on a Contracting State under paragraph 2 of Article 23 A to allow as a deduction from the tax on income an amount equal to the tax paid in the other Contracting State does not apply to tax paid in accordance with the model provision. In the case of Article 23 B, additional paragraph 3 provides that the obligation on a Contracting State under paragraph 1 of Article 23 B to allow as a deduction from the tax on income an amount equal to the tax paid in the other Contracting State does not apply to tax paid in accordance with the model provision. These modifications ensure that the application of the model provision, where it results in additional taxing rights in a Contracting State (the State in which the income arises), does not give rise to an obligation to exempt income from tax or to provide a deduction from tax in the other Contracting State (the State of residence of the person deriving the income) under Article 23 A or Article 23 B of the OECD Model that would not have arisen had the model provision not applied.

138. Paragraph 15 reproduces these outcomes, but does so without amending the existing elimination of double taxation provisions of a Covered Tax Agreement. Instead, paragraph 15 itself provides that the application of the provisions of Article 1 in Annex I (The subject to tax rule) shall not create any obligation under those existing elimination of double taxation provisions to exempt covered income from tax or to provide a deduction or credit for tax paid on covered income.

139. Subparagraph a) of paragraph 15 uses descriptive language to identify the provisions of a Covered Tax Agreement (referred to as “this agreement”) that require a Contracting Jurisdiction (referred to as a “contracting jurisdiction”) to exempt from tax income derived by a resident which may be taxed in the other Contracting Jurisdiction in accordance with the Covered Tax Agreement. This is the function of the language before the comma. The language after the comma, read together with the opening words of paragraph 15, then provides that the application of Article 1 in Annex I (The subject to tax rule) shall not create any obligation under the provisions so described to exempt from tax income that may be taxed in the other Contracting Jurisdiction only in accordance with Article 1 in Annex I (The subject to tax rule). The effect is that the Contracting Jurisdiction of which a person deriving an item of covered income that may be taxed in accordance with Article 1 in Annex I (The subject to tax rule) is a resident is not required to exempt that income from tax if it is only taxable in accordance with the Covered Tax Agreement because Article 1 in Annex I (The subject to tax rule) applies.

140. Subparagraph b) of paragraph 15 uses descriptive language to identify the provisions of a Covered Tax Agreement (referred to as “this agreement”) that require a Contracting Jurisdiction (referred to as a “contracting jurisdiction”) to provide a deduction or credit in respect of tax paid with respect to income derived by a resident which may be taxed in the other Contracting Jurisdiction in accordance with the Covered Tax Agreement. This is the function of the language before the comma. The language after the comma, read together with the opening words of paragraph 15, then provides that the application of Article 1 in Annex I (The subject to tax rule) shall not create any obligation under the provisions so described to provide a deduction or credit in respect of tax paid in the other Contracting Jurisdiction in accordance with Article 1 in Annex I (The subject to tax rule). The effect is that the Contracting Jurisdiction of which a person deriving an item of covered income that may be taxed in accordance with Article 1 in Annex I (The subject to tax rule) is a resident is not required to provide a deduction or credit in respect of tax paid in accordance with Article 1 in Annex I (The subject to tax rule).

Article 2 – Implications of the subject to tax rule

141. Paragraph 1 of Article 2 is based on the opening language and subparagraph c) of paragraph 15 of the model provision. Paragraph 15 of the model provision reads as follows:

It is understood that the provisions of this Article:

- a) are included in this Convention as part of the implementation of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy;*
- b) do not otherwise reflect the tax treaty policies of either Contracting State; and*
- c) are without prejudice to subsequent modifications to this Convention or any other Convention concluded by either of the Contracting States.*

142. Changes are made in paragraph 1 to the text of paragraph 15 of the model provision. Subparagraphs a) and b) of paragraph 15 of the model provision are omitted and those provisions are instead included as part of the preamble. The opening words of paragraph 15 of the model provision (“It is understood that the provisions of this Article”) are included in the opening language of paragraph 1, with one change: the reference to “this Article” is replaced with a reference to “this Annex” (being Annex I). The reference to “this Annex” ensures that paragraph 2 of Article 2 is also covered by the effect of paragraph 1.

143. The remaining language of paragraph 1 is based on subparagraph c) of paragraph 15 of the model provision. Changes are made in paragraph 1 to the text of subparagraph c) of paragraph 15 of the model provision to adapt it for inclusion in a Covered Tax Agreement. The reference in subparagraph c) of paragraph 15 of the model provision to “this Convention” is replaced with a reference to “this agreement” and the reference to the “Contracting States” is replaced with a reference to the “contracting jurisdictions”.

144. Paragraph 2 of Article 2 is an additional provision. Its function is to make clear that nothing in Annex I (The subject to tax rule) shall affect the application of any other provision of a Covered Tax Agreement (referred to as “this agreement”) that denies benefits available under any provision of the Covered Tax Agreement on the basis of an item of income not being subject to a certain level of taxation in a Contracting Jurisdiction. Paragraph 2 governs the interaction between three types of provision that might be included in a Covered Tax Agreement: first, a provision that provides a benefit, such as a limitation on the rate at which income may be taxed in the Contracting Jurisdiction in which it arises; second, a provision that denies that benefit where the income in respect of which the benefit is potentially available is not subject to a certain level of taxation in the Jurisdiction of which the person deriving the income is a resident; and third, Annex I (The subject to tax rule). Paragraph 2 provides that the inclusion of Annex I (The subject to tax rule) in a Covered Tax Agreement does not affect the application of the second type of provision, ensuring that the application of such a provision takes priority over, and applies instead of, Annex I (The subject to tax rule).

145. Examples of the second type of provision described above would include existing “subject to tax” provisions or a provision on special tax regimes conforming to the alternative provision set out at paragraph 85 of the Commentary on Article 1 in the OECD Model. A common feature of such provisions is that, when the conditions for their application are met, they deny entirely a benefit that would otherwise be available under a Covered Tax Agreement and allow a Contracting Jurisdiction to tax the affected item of income in accordance with its domestic law. Where such a provision applies, there is no limitation under the provisions of the Covered Tax Agreement potentially applying the benefit of such a limitation (the first type of provision described above) on the right of the Contracting Jurisdiction in which the income arises to tax that income. Where any other provision of a Covered Tax Agreement denies benefits otherwise available under that

Covered Tax Agreement and allows a Contracting Jurisdiction to tax an item of covered income in accordance with domestic law, Article 1 in Annex I (The subject to tax rule) will not apply.

Annex II. – Additions to the subject to tax rule: Taxes computed on an alternative basis

Article 1 – Additional provisions for taxes computed on an alternative basis

146. Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) introduces into a Covered Tax Agreement additional provisions required for the purposes of determining the tax rate for the purposes of applying Article 1 in Annex I (The subject to tax rule) where a Contracting Jurisdiction applies a tax, that is a covered tax for the purposes of the Covered Tax Agreement, on a basis other than on net income. Paragraph 1 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) is based on the provision mandated for inclusion in the model provision in those circumstances by paragraph 68 of the commentary on the model provision in the STTR Report. Paragraph 2 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) is based on the provision made available for inclusion in the model provision in those circumstances by paragraph 76 of the commentary on the model provision in the STTR Report. Those two provisions read as follows:

(ii) Notwithstanding subdivision (i) of subparagraph a), the tax rate with respect to an item of covered income subject to the [insert the name of the tax] in [insert the name of the residence State], shall be the rate that results from dividing the total amount of such tax paid by the resident of [insert the name of the residence State] in the year in which the covered income is reflected in its financial statements by the total amount of its net income of that same year reflected in those financial statements.

and

d) If a Contracting State imposes or makes significant changes to a relevant tax that is not a tax on net income then the competent authorities of the Contracting States shall agree the applicable tax rate in respect of that tax, or the methodology for determining that rate.

147. Changes are made in paragraph 1 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) to the text of the provision mandated in paragraph 68 of the commentary on the model provision, to adapt it for inclusion in a Covered Tax Agreement; and to reflect its inclusion in a Covered Tax Agreement in a separate annex (Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis)) that supplements Annex I (The subject to tax rule) rather than in the form of changes to the affected provisions of Annex I (The subject to tax rule).

148. The provision described in paragraph 68 of the commentary on the model provision is drafted as a new subdivision (ii) of subparagraph a) of paragraph 5 of the model provision, and would require subparagraph a) of paragraph 5 of the model provision to be reformatted as subdivision (i) of paragraph a) of paragraph 5 of the model provision. Because this reformatting is not a feature of paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”), and because the provision described in paragraph 68 of the commentary on the model provision is included in a separate annex (Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis)) that supplements Annex I (The subject to tax rule), changes are made in paragraph 1 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) to ensure that it interacts in the way intended with subparagraph a) of paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”). The change made to accommodate this need is the deletion of the reference to “subdivision (i) of” in the first line of the provision described in paragraph 68 of the commentary on the model provision.

149. Changes are also made in paragraph 1 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) to include appropriate cross-references to Annex I (The subject to tax rule) and to replace the placeholder reference in

the provision described in paragraph 68 of the commentary on the model provision (“[insert the name of the tax]”) with a reference to “the tax notified by a contracting jurisdiction”. Article 4 in Part II governs such notifications. Redundant placeholder references in the provision described in paragraph 68 of the commentary on the model provision (“[insert the name of the residence State]”) are deleted or replaced with a reference to “the first-mentioned jurisdiction” in paragraph 1 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis).

150. Paragraph 2 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) has been added to clarify the application of this Annex where a Contracting Jurisdiction applies both a tax calculated on a net income basis and a tax on an alternative basis to an item of covered income. In such case, the tax rate on that item of covered income for the purpose of applying the STTR shall be determined by adding together the tax rate determined in accordance with subparagraph a) of paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”), in the case of the tax on a net income basis, and the tax rate determined in accordance with paragraph 1, in the case of the tax calculated other than on a net income basis.

151. Changes are made in paragraph 3 of Article 1 in Annex II (Additions to the subject to tax rule: Taxes computed on an alternative basis) to the text of the provision described in paragraph 76 of the commentary on the model provision to adapt it for inclusion in a Covered Tax Agreement. References to a “Contracting State” and the “Contracting States” are replaced with references to a “contracting jurisdiction” and the “contracting jurisdictions”.

Annex III. – Additions to the subject to tax rule: Taxes imposed at the point of distribution

Article 1 – Additional provisions for taxes imposed at the point of distribution

152. Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) introduces into a Covered Tax Agreement additional provisions required for the purposes of determining the tax rate for the purposes of applying Article 1 in Annex I (The subject to tax rule) where a Contracting Jurisdiction does not impose tax on an item of covered income when the income is earned, but instead imposes tax on that income at the point of profit distribution. Article 1 in Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) is based on the provision mandated for inclusion in the model provision in those circumstances by paragraph 74 of the commentary on the model provision in the STTR Report, which reads as follows:

(ii) Notwithstanding subdivision (i) of subparagraph a), the tax rate with respect to an item of covered income subject to the [insert the name of the distribution tax] in [insert the name of the residence State], shall be the rate that results from dividing the total amount of such tax paid by the resident of [insert the name of the residence State] for the year in which the covered income is reflected in its financial statements and the two immediately preceding years by the total amount of its net income for that year and those two immediately preceding years reflected in those financial statements.

153. Changes are made in Article 1 in Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) to the text of the provision mandated in paragraph 74 of the commentary on the model provision, to adapt it for inclusion in a Covered Tax Agreement; and to reflect its inclusion in a Covered Tax Agreement in a separate annex (Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution)) that supplements Annex I (The subject to tax rule) rather than in the form of changes to the affected provisions of Annex I (The subject to tax rule).

154. The provision described in paragraph 74 of the commentary on the model provision is drafted as a new subdivision (ii) of subparagraph a) of paragraph 5 of the model provision, and would require subparagraph a) of paragraph 5 of the model provision to be reformatted as subdivision (i) of paragraph a) of paragraph 5 of the model provision. Because this reformatting is not a feature of paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”), and because the provision described in paragraph 74 of the commentary on the model provision is included in a separate annex (Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution)) that supplements Annex I (The subject to tax rule), changes are made in Article 1 in Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) to ensure that it interacts in the way intended with subparagraph a) of paragraph 5 of Article 1 in Annex I (The subject to tax rule, Meaning of “tax rate”). The change made to accommodate this need is the deletion of the reference to “subdivision (i) of” in the first line of the provision described in paragraph 74 of the commentary on the model provision.

155. Changes are also made in Article 1 in Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution) to include appropriate cross-references to Annex I (The subject to tax rule) and to replace the placeholder reference in the provision described in paragraph 74 of the commentary on the model provision (“[insert the name of the distribution tax]”) with a reference to “the taxes notified by a contracting jurisdiction”. Article 5 in Part II governs such notifications. Redundant placeholder references in the provision described in paragraph 74 of the commentary on the model provision (“[insert the name of the residence State]”) are deleted or replaced with a reference to “the first-mentioned jurisdiction” in Article 1 in Annex III (Additions to the subject to tax rule: Taxes imposed at the point of distribution).

Annex IV. – Additions to the subject to tax rule: Recognised pension fund

156. Annex IV (Additions to the subject to tax rule: Recognised pension fund) provides a uniform definition of the term “recognised pension fund” for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions) which excludes a “recognised pension fund”, a “pension fund”, a “recognised pension scheme”, or a “pension scheme” from the application of the STTR.

157. Article 6 in Part II allows a Party to choose to include Annex IV (Additions to the subject to tax rule: Recognised pension fund) in some of its Covered Tax Agreements, in addition to Annex I (The subject to tax rule).

158. A Party might choose to include the definition of the term “recognised pension fund” in Annex IV (Additions to the subject to tax rule: Recognised pension fund) for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions) in a Covered Tax Agreement when the Covered Tax Agreement does not include a definition of the term “recognised pension fund”, “pension fund”, “recognised pension scheme”, or “pension scheme”, or where such a definition is included in the Covered Tax Agreement but a Contracting Jurisdiction prefers to apply the definition in Annex IV (Additions to the subject to tax rule: Recognised pension fund) for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions).

159. The definition of the term “recognised pension fund” is based on the definition in subparagraph i) of paragraph 1 of Article 3 of the OECD Model which was included in 2017, when this term was added to paragraph 1 of Article 4 of the OECD Model in order to ensure that a pension fund that meets the definition is considered as a resident of the Contracting State in which it is established. The definition in Annex IV (Additions to the subject to tax rule: Recognised pension fund) also includes the provisions in paragraph 10.8, and additional language based on paragraph 10.10, of the Commentary on Article 3 of the OECD Model.

160. Such an addition was included in the Commentary on the OECD Model for funds that can be established in States for the main purpose of providing retirement benefits to individuals but that do not formally constitute a separate person under the taxation laws of the State in which they are established. The aim was to ensure that, where the taxation laws of the State in which those funds are established provide that the investment assets of the funds constitute a separate and distinct patrimony the income of which is not allocated to any person for tax purposes, they will be considered, for the purposes of a tax treaty, as a separate person treated as such under the taxation law of that State and all the assets and income to which the arrangement applies shall be treated as assets held and income derived by that separate person and not by another person.

Article 1 – Definition for the exclusion in subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule)

Paragraph 1

161. Paragraph 1 provides that, when Annex IV (Additions to the subject to tax rule: Recognised pension fund) is included in a Covered Tax Agreement in addition to Annex I (The subject to tax rule), the term “recognised pension fund” in subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions) takes its meaning from paragraph 2 of Article 1 in Annex IV (Additions to the subject to tax rule: Recognised pension fund). Paragraph 1 also provides that the definition in paragraph 2 supersedes a definition of “recognised pension fund”, “pension fund”, “recognised pension scheme”, or “pension scheme” included elsewhere in a Covered Tax Agreement, but only for the purposes of subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions).

Paragraph 2

162. Paragraph 2 contains the definition of the term “recognised pension fund” that will apply for the purposes of applying subparagraph c) of paragraph 8 of Article 1 in Annex I (The subject to tax rule, Exclusions).

163. Subparagraph a) provides that the term “recognised pension fund” of a jurisdiction means an entity or arrangement established in that jurisdiction that is treated as a separate person under the taxation laws of that jurisdiction and:

- Under subdivision (i), that is established and operated exclusively or almost exclusively to administer or provide retirement benefits and ancillary or incidental benefits or other similar amount to individuals and that is regulated as such by that jurisdiction or one of its political subdivisions or local authorities; or
- Under subdivision (ii), that is established and operated exclusively or almost exclusively to invest funds for the benefit of entities or arrangements referred to in subdivision (i).

164. Subparagraph b) includes an arrangement which is not treated as a separate person under the taxation law of the Contracting Jurisdiction in which that arrangement is established in the case where it meets either of the conditions in subdivisions (i) or (ii) of subparagraph a). Such an arrangement will be considered, for the purposes of Annex IV (Additions to the subject to tax rule: Recognised pension fund) and Annex I (The subject to tax rule), as a separate person treated as such under the taxation law of that jurisdiction and all the assets and income to which the arrangement applies will be treated as assets held and income derived by that separate person and not by another person.

Annex V. – Additions to the subject to tax rule: Circuit-breaker provision

165. Annex V (Additions to the subject to tax rule: Circuit-breaker provision) contains an optional circuit-breaker provision which could suspend the application of the provisions in Annex I (The subject to tax rule) with respect to a Covered Tax Agreement where a Contracting Jurisdiction to the Covered Tax Agreement, which was considered as a developing country for the purposes of the commitment to implement the STTR described in paragraph 2 of this Explanatory Statement, ceases to be a developing country as defined for a sustained period of five consecutive years.

166. When the circuit-breaker applies in a Covered Tax Agreement, its effect is not to remove the STTR from the Covered Tax Agreement. Instead, it suspends the application of the STTR. The circuit-breaker could then subsequently apply to “reactivate” the application of the provisions in Annex I (The subject to tax rule). For such a reactivation, the Contracting Jurisdiction that had ceased to be a developing country for a sustained period of five consecutive years, needs to subsequently again become a developing country as defined at any point in time.

167. Article 7 in Part II allows a Party to choose to include Annex V (Additions to the subject to tax rule: Circuit-breaker provision) in its Covered Tax Agreement, in addition to Annex I (The subject to tax rule).

Article 1 – Circuit-breaker provision

Paragraph 1

168. Paragraph 1 provides that the application of the provisions in Annex I (The subject to tax rule) is suspended in a Covered Tax Agreement where the following conditions are met:

- Under subparagraph a), a Contracting Jurisdiction to the Covered Tax Agreement was not classified as a high-income economy by the World Bank Group based on its gross national income per capita using the World Bank Atlas method at any time since 1 July 2020; and
- Under subparagraph b), that same Jurisdiction is classified as a high-income economy by the World Bank Group based on its gross national income per capita using the World Bank Atlas method for a period of five consecutive years at any time following the date on which the provisions in Annex I (The subject to tax rule) started to have effect in accordance with Article 12 (Entry into effect).

169. The condition in subparagraph a) applies by reference to the World Bank Group's classifications of jurisdictions as low-income, lower-middle-income, upper-middle-income, and high-income by reference to GNI per capita using the World Bank Atlas method. For the purposes of the commitment to implement the STTR described in paragraph 2 of this Explanatory Statement, a jurisdiction is classified as developing if it is not a high-income jurisdiction according to this measure. The condition in subparagraph a) is therefore met if a jurisdiction is classified as developing at any time since 1 July 2020.

170. The condition in subparagraph b) applies by reference to the same measure and is met if a jurisdiction that has met the condition in subparagraph a) (that is, a jurisdiction that was classified as developing at any time since 1 July 2020) is classified as high-income (and so is not classified as developing) for a period of five consecutive years at any time following the date on which the provisions in Annex I (The subject to tax rule) started to have effect.

171. When triggered, the circuit-breaker provision suspends the application of Annex I (The subject to tax rule) as of the first day of the fiscal year beginning on or after the expiration of a period of six calendar months from the date on which the Contracting Jurisdiction mentioned in subparagraphs a) and b) is classified as a high-income economy

by the World Bank Group based on its gross national income per capita using the World Bank Atlas method for a period of five consecutive years.

Paragraph 2

172. Paragraph 2 provides that, when paragraph 1 applied and suspended the application of Annex I (The subject to tax rule) in a Covered Tax Agreement, the application of the provisions in Annex I (The subject to tax rule) can be reactivated in the Covered Tax Agreement when the Contracting Jurisdiction mentioned in subparagraphs a) and b) of paragraph 1 (i.e. the developing country that became a high-income economy) ceases to be classified as a high-income economy.

173. When triggered, paragraph 2 reactivates the application of Annex I (The subject to tax rule) on the first day of a fiscal year beginning on or after the expiration of a period of six calendar months from the date on which the Contracting Jurisdiction mentioned in subparagraphs a) and b) of paragraph 1 first ceases to be classified as a high-income economy by the World Bank Group based on its gross national income per capita using the World Bank Atlas method.