The Tax Institute

The Tax Summit

# The Tax Summit

## Session 17.4: Treaties – Recent developments and their application

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# Contents

1. It seems to me that there is a paradigm shift occurring in the way we go about analysing the interpretation and operation of Australia's international agreements relating to Federal income taxation, and in particular our Double Tax Agreements, or DTAs (Usually expressed as an "Agreement for the avoidance of Double Taxation and the prevention of Fiscal Evasion with respect to Taxes on Income"). I believe this complicates the analysis of the relevance of a treaty to a client's fact pattern.

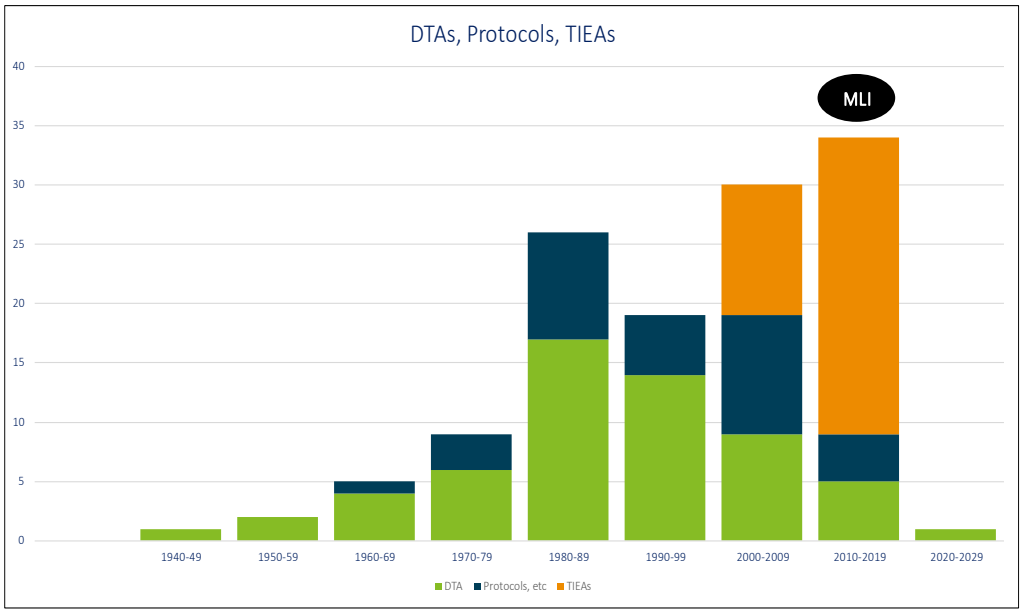
2. At one time it was a simple matter of considering the words of the treaty itself, perhaps looking for guidance in the commentary (although being uncertain about the weight it should be given) and considering the small number of domestic cases that dealt with treaties. But there is now an ever increasing body of OECD material relating to treaty issues, there is the multilateral instrument ("MLI") and then there are the Pillar 1 and Pillar 2 changes. In addition, the courts continue to explore issues that are prompted by treaties. It may also be relevant to consider the meaning of the terms under the taxation system of the treaty partner and the comments of the treaty partner on the agreement, and expert evidence may be needed. As multilateral instruments become more important it is conceivable the judgements of foreign courts may assume greater weight in Australia.

3. In this paper I discuss some of the material which affects our interpretation of treaties. I hope to state some propositions about aspects of treaty interpretation.

4. I want to start by discussing the mechanics of Australia's adoption of Treaties before I then discuss some issues concerning the operation of our treaties and the use of related materials. I would like to acknowledge this paper draws on some of the "Good Faith" paper I wrote as Australia's Branch Reporter for Subject 2 of the IFA 2023 Congress[1].

## International tax agreements: what agreements are relevant.

Tax treaties, etc since 29 October 1946




Based on data at: https://treasury.gov.au/tax -treaties/income -tax-treaties , per date of signature
Includes treaties no longer in force, and treaties in force
Excludes Portugal treaty: signed, not yet in force (Source, Treasury at IFA presentation 10 April 2024

3

5. Australia (meaning the Government of the Commonwealth of Australia, also sometimes referred to as "the Commonwealth") has (at May 2024) entered into 47 bilateral Conventions "for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income", or "tax treaties".

[1] P.J. McNab, Good faith in domestic and international tax law (IFA Cahiers vol. 107B , 2023) IFA online Cahiers collection

6. Treasury has advised that fourteen jurisdictions are active on the current treaty program: Bulgaria, Colombia, Croatia, Cyprus, Estonia, Latvia, Lithuania, Greece, Luxembourg, New Zealand, Brazil, Ukraine, Sweden, Republic of Korea. With the new treaty with Slovenia signed on Monday this week.

7. These are based on, but do not precisely replicate the terms of the OECD Model Tax Convention on Income and Capital, now in its 10th edition dated 2017 "the OECD Model". The OECD Model also has authorised "Commentaries", which elaborate on the meaning to be given to terms used in the model, and also document reservations that various nations have made to the terms of the OECD Model. Below, we later deal with the status of the text of the actual Model Convention and Commentaries.

8. The deviations from the OECD model are a product of the negotiations between Australia and the treaty partner and are from a desire to ensure the integrity of the domestic tax system. Care must be taken to consider the individual treaty in each case as the specific wording may differ. It is fair to say that the preservation of Australia's right to use the general anti avoidance provisions is one of the most significant deviations. This approach has been extended even further in some of our newer treaties. For instance, in the protocol to the treaty with Israel it is said that:

   1. *Nothing in this Convention shall prevent the application of any provision of the laws of a Contracting State which is designed to prevent the avoidance or evasion of taxes, including:*

      *a) measures designed to address thin capitalisation and dividend stripping;*

      *b) measures designed to address transfer pricing;*

      *c) controlled foreign company and transferor trust rules;*

      *d) measures designed to ensure that taxes can be effectively collected and recovered, including conservancy measures;*

      *e) foreign occupational company rules;*

      *f) in the case of Australia, Part IVA of the Income Tax Assessment Act 1936 or section 67 of the Fringe Benefits Tax Assessment Act 1986*;

      *g) in the case of Israel, Article 86 of the Income Tax Ordinance 5721-1961.*

9. Australia's tax treaties are "treaties" entered into under the Executive power in section 61 of the Australian Constitution[2]. Treaties are a legally binding commitment by the Commonwealth under international law, with another State, or an international organisation. They are an exercise of the prerogative powers of the Crown in right of Australia, represented by the Australian Governor General who is the head of the Executive Branch of Government in Australia. As such, treaties are executed by a representative of the Executive Branch of the Government.

## How do they arise?

10. The process involves the following steps (and typically takes 2 years):

    1. *Mandate* granted to the relevant Minister, by the Minister for Foreign Affairs or the Cabinet. Prime Minister and other Ministers with a portfolio interest must be informed.

    2. The lead agency *negotiates*, in consultation with other Commonwealth agencies, state and territory governments or other stakeholders.

    3. Federal Executive Council *(ExCo) approval*. Lead minister seeks agreement from Minister for Foreign Affairs, AG and other relevant ministers. Prime Minister to be informed. Either by correspondence or submitted to Cabinet. An eight-week process.

[2] Commonwealth of Australia Constitution Act 1900

4. *Signature*. If Prime Minister or Foreign Minister are not signing, Minister for Foreign Affairs issues an instrument of full powers authorising the representative to sign. In tax matters it is usually the Treasurer.

5. *Scrutiny by Parliament*. Treaty tabled in both Houses of Parliament for consideration by Joint Standing Committee on Treaties (JSCOT). Fifteen to twenty Joint sitting days are required. JSCOT tables its report within fifteen or 20 joint sitting days. Four to six months usually. JSCOT report contains a recommendation on signature. As part of this process, JSOT requires a National Interest Analysis be provided by Department of Foreign Affairs and Trade (DFAT), using a standard format. This includes information on consultation undertaken in relation to the proposed treaty. JSCOT will also consider questions referred to it relating to a treaty and any other matter referred by the Minister for Foreign Affairs.[3]

6. *Entry into force*. After JSCOT report and before entry into force any legislative changes to implement pass both Houses of Parliament. With bilateral, entry into force usually occurs via an exchange of diplomatic notes. For multilateral ExCo approval must be sought for deposit of instrument of ratification. [4]

11. The National Interest Analysis (NIA) for treaties can usually be found in Austlii. For the NIA in relation to the Convention on Mutual Administrative Assistance in Tax Matters (referred to below) see https://www.austlii.edu.au/au/other/dfat/ATNIA/2012/2.html. In relation to that NIA, for instance, key benefits are said to be the broader topics for information exchange and simultaneous audits. The Convention also introduced cross border recovery of tax debts.

12. Australia's treaty practice is governed by the 1969 Vienna Convention on the Law of Treaties which was acceded to by Australia in 1974 and has been in force since 21 January 1980.

13. Under the Vienna Convention, every treaty is binding on the parties to it and must be performed by them in good faith (Art 26). It is generally not possible for a party to a treaty to invoke the provisions of its internal laws as justification for its failure to perform its treaty obligations (Art 27), meaning that Treaty obligations will usually prevail over domestic law.

14. As McHugh J said in *Thiel*[5] (in the course of discussing the 1980 Swiss–Australia double tax agreement):

*"The Agreement is a treaty and is to be interpreted in accordance with the rules of interpretation recognised by international lawyers: Shipping Corporation of India Ltd v Gamlen Chemical Co (A/Asia) Pty Ltd (1980) 147 CLR 142 at 159. Those rules have been codified by the Vienna Convention on the Law of Treaties to which Australia, but not Switzerland, is a party. Nevertheless, because the interpretation provisions of the Vienna Convention reflect the customary rules for the interpretation of treaties, it is proper to have regard to the terms of the Convention in interpreting the Agreement, even though Switzerland is not a party to that Convention."*

15. His Honour went on to refer to Art 31 and 32 of the Vienna Convention and concluded that, because the meaning of the term "enterprise" in Art 3 and 7 of the Swiss 1980 agreement was ambiguous, it was proper to consider the "supplementary means of interpretation" contained in the 1977 OECD Model Tax Convention and the Commentaries thereon (Mason CJ and Brennan and Gaudron JJ agreed with McHugh J on this point).

16. It is important to distinguish treaties from other international memoranda which are not binding under international law ("memoranda of understanding"). The most common form for an instrument of less-than-treaty status is a Memorandum of Understanding (MOU). Other forms include arrangements,

[3] See for instance part 4 of Report 193 of the Joint Standing Committee on Treaties. "Strengthening the Trade Agreement and Treaty-Making Process in Australia. August 2021.

[4] https://www.dfat.gov.au/international-relations/treaties/treaty-making-process#:~:text=For%20multilateral%20treaties%2C%20ExCo%20approval,in%20accordance%20with%20its%20terms.: accessed 30 May 2024

[5] *Thiel* v *FC of T* 90 ATC 4717

exchanges of notes, letters recording understandings, records of discussion and joint communiqués. These do not of their own force create legal rights or obligations.

17. In tax, an interesting example of the latter is the "Agreement between the Australian Commerce and Industry Office and the Taipei Economic and Cultural Office concerning the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income". Which is a document of less than treaty status. While the language is in the approved format the parties are not States. It has been given force in domestic law as a schedule to the IAA.

18. There are several other agreements that are relevant to Australian International Taxation, including:

    1. Tax Information Exchange Agreements (intergovernmental, all taxes administered, criminal and civil, but limited to a particular investigation): often with Addition Benefits Agreements, being Treaties.,
    2. Convention on Mutual Administrative Assistance in Tax Matters (treaty, not separately legislated)
    3. Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI).
    4. *Airline* profits agreements (treaties, but only for airline profits. PRC, Greece and Italy)
    5. *Timor* Sea Treaty
    6. Other non tax treaties, such as Free Trade Agreements (which may have made an Australian Digital Services Tax difficult, for instance).

19. I want to just digress for a minute to talk about the information sharing processes under these different types of agreements, since the first category, especially, is pretty much principally concerned with this. Section 23 of the International Tax Agreements Act 1953 (ITAA 1953) provides that the Commissioner may use the "information gathering provisions" to get information to be exchanged under his obligations under an "international agreement". "Information gathering provisions" are broadly defined as any of his powers. and an "international agreement" means "an agreement given the force of law under this Act", or "some other agreement that allows for the exchange of information on tax matters between Australia" and another party.

20. As I also note later, Section 4 of the International Tax Agreements Act 1953 (ITAA 1953) incorporates the two Income Tax Assessment Acts into the ITAA 1953, giving primacy to the ITAA 1953 to the extent of any inconsistency. The prohibitions on information sharing in the Tax Administration Act 1953 (TAA 1953) then generally apply to any information gathered, but disclosure under an international agreement is specifically authorised under TAA 1953, s 355-50(2) of Sch 1, item 9 in the table.

21. Traditional tax treaties have an exchange of information article, which typically provides that:

> "*Any information received by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic law of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes to which this Convention applies. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions*[6]".

22. In addition, they specify some limits on the power, such as this in the UK convention:

[66] These items taken from article 27 of the UK Convention.

*3 In no case shall the provisions of paragraphs 1 or 2 of this Article be construed so as to impose on a Contracting State the obligation:*

*(a) to carry out administrative measures at variance with the laws or the administrative practice of that or of the other Contracting State;*

*(b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State; or*

*(c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or to supply information the disclosure of which would be contrary to public policy.*

23. In relation to the first item above, I note that these operate in relation to taxes "of every kind and description", unlike the limit to taxes covered by the treaty in traditional tax treaties. But the "…requested Party is not obliged to provide information which is neither held by its authorities nor in the possession of or obtainable by persons who are within its territorial jurisdiction". In addition, .

[7]*Any request for information shall be formulated with the greatest detail necessary and shall specify in writing:*

*(a) the identity of the person under examination or investigation;*

*(b) the period for which the information is requested;*

*(c) the nature of the information requested and the form in which the requesting Party would prefer to receive it;*

*(d) the tax purpose for which the information is sought;*

*(e) the reasons for believing that the information requested is foreseeably relevant to tax administration and enforcement of the requesting Party, with respect to the person identified in subparagraph (a) of this paragraph;*

*(f) the grounds for believing that the information requested is present in the requested Party or is in the possession of or obtainable by a person within the jurisdiction of the requested Party;*

*(g) to the extent known, the name and address of any person believed to be in possession of or able to obtain the information requested;*

*(h) a statement that the request conforms with the laws and administrative practice of the requesting Party, that if the requested information was within the jurisdiction of the requesting Party then the competent authority of the requesting Party would be able to obtain the information under the laws of the requesting Party or in the normal course of administrative practice and that it is in conformity with this Agreement;*

*(i) a statement that the requesting Party has pursued all means available in its own territory to obtain the information, except where that would give rise to disproportionate difficulty.*

24. In addition, there are provisions in relation to ATO officers acting in a foreign jurisdiction in Article 5.

1. *"With reasonable notice, the requesting Party may request that the requested Party allow representatives of the competent authority of the requesting Party to enter the territory of the requested Party, to the extent permitted under its domestic laws, to interview individuals and examine records with the prior written consent of the individuals or other persons concerned. The competent authority of the requesting Party shall notify the competent authority of the requested Party of the time and place of the intended meeting with the individuals concerned.*

[7] From the Guernsey TIEA.

2. *At the request of the competent authority of the requesting Party, the competent authority of the requested Party may permit representatives of the competent authority of the requesting Party to attend a tax examination in the territory of the requested Party.*

3. *If the request referred to in paragraph 2 is granted, the competent authority of the requested Party conducting the examination shall, as soon as possible, notify the competent authority of the requesting Party of the time and place of the examination, the authority or person authorised to carry out the examination and the procedures and conditions required by the requested Party for the conduct of the examination. All decisions regarding the conduct of the examination shall be made by the requested Party conducting the examination."*

25. Article 6 describes requests that may be refused:

1. *The competent authority of the requested Party may decline to assist:*
   - *(a) where the request is not made in conformity with this Agreement;*
   - *(b) where the requesting Party has not pursued all means available in its own territory to obtain the information, except where recourse to such means would give rise to disproportionate difficulty; or*
   - *(c) where the disclosure of the information requested would be contrary to public policy ('ordre public').*
2. *This Agreement shall not impose upon a requested Party any obligation to provide information subject to legal privilege, or any trade, business, industrial, commercial or professional secret or trade process, provided that information described in Article 4(4) shall not by reason of that fact alone be treated as such a secret or trade process.*

26. In relation to item .2, I don't want to dwell on it, but I would particularly like to call out articles 8 and 9 of that agreement. Which I have had the privilege of watching in practice. Leading to some quite surreal moments.

***Article 8 – Simultaneous tax examinations***

1. *At the request of one of them, two or more Parties shall consult together for the purposes of determining cases and procedures for simultaneous tax examinations. Each Party involved shall decide whether or not it wishes to participate in a particular simultaneous tax examination.*

2. *For the purposes of this Convention, a simultaneous tax examination means an arrangement between two or more Parties to examine simultaneously, each in its own territory, the tax affairs of a person or persons in which they have a common or related interest, with a view to exchanging any relevant information which they so obtain.*

***Article 9 – Tax examinations abroad***

1. *At the request of the competent authority of the applicant State, the competent authority of the requested State may allow representatives of the competent authority of the applicant State to be present at the appropriate part of a tax examination in the requested State.*

2. *If the request is acceded to, the competent authority of the requested State shall, as soon as possible, notify the competent authority of the applicant State about the time and place of the examination, the authority or official designated to carry out the examination and the procedures and conditions required by the requested State for the conduct of the examination. All decisions with respect to the conduct of the tax examination shall be made by the requested State.*

3. *A Party may inform one of the Depositaries of its intention not to accept, as a general rule, such requests as are referred to in paragraph 1. Such a declaration may be made or withdrawn at any time.*

27. Despite the initial 7 "joint reviews" in 2011 as countries signed up to the Convention under the banner of JITSIC, the practice seems to have become less used. No doubt because of the practicalities of the goals of each administration. Together with the increased domestic use of formal notices, particularly "offshore information notices" under section 353-25.

28. But back to process.

29. Section 61 of the Australian Constitution provides:

> *The executive power of the Commonwealth is vested in the Queen and is exercisable by the Governor-General as the Queen's representative, and extends to the execution and maintenance of this Constitution, and the laws of the Commonwealth.*

30. The High Court has held that the powers of the executive branch are not limited by section 61, but in fact extend to the prerogative powers of the Crown. These are exercised by the Governor-General, by convention on ministerial advice. They are, essentially, the powers that the Executive Branch has to act, without reference to the Parliament. Relevantly, the Executive may enter into international treaties.[8]

31. Once a treaty is concluded, section 51(xxix) of the Constitution allows Parliament to make laws implementing the terms of the treaty in order to fulfil our international obligations arising under. The High Court has held that such legislation is in fact necessary:

> *The provisions of an international treaty to which Australia is a party do not form part of Australian law unless those provisions have been incorporated into municipal law by statute and cannot operate as a direct source of individual rights and obligations under that law.*[9].

32. Australia is, then, what is referred to as a "dualist", rather than "monist" jurisdiction in international law, being one where international law, including treaties Australia has signed, have no domestic legal effect without enabling domestic legislation.

33. Since 2013, Australia's tax treaties are given the force of law in Australia by the passage of an Act of Federal Parliament inserting reference to the Agreement into the list of Agreements referred to in the section 3AAA of the International Agreements Act 1953, definition of "current agreements"), and amending section 5 to refer to any other provisions coming in to force with its date of effect.

34. A good example is the Treasury Laws Amendment (OECD Multilateral Instrument) Act 2018 (No 83, 2018), which gave effect to the MLI by declaring that the legislation referred to in its Schedule was amended in the manner described there.

35. Schedule 1 provided:

> **Schedule 1—Amendments**
>
> **Part 1—Multilateral Convention**
>
> ***International Tax Agreements Act 1953***
>
> **1 Subsection 3AAA(1)**
>
> Insert:

[8] The Executive Power of the commonwealth: its scope and limits – Parliament of Australia (aph.gov.au) Dr Max Spry. Research Paper 28 1995-96.

[9] Per Mason CJ, Deane and Toohey JJ in Minister for Immigration and Ethnic Affairs v Teoh (1995) 128 ALR 353 at p354.; see also Treaty-Making Options For Australia – Parliament of Australia (aph.gov.au) Susan Downing Current Issues Brief 17 1995-96: making us a "dualist jurisdiction".

> ***Multilateral Convention*** means the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* done at Paris on 7 June 2017.
>
> Note: In 2018, the text of this convention was accessible through the Australian Treaties Library on the AustLII website (www.austlii.edu.au).

*36.* The Explanatory Memorandum to the Act does discuss the effect and intention of the MLI at length and, together with the second reading speech, provides the usual aid in statutory interpretation that would be expected in interpreting domestic legislation. The EM from para 1.16 specifically refers to the OECD authorised "Explanatory Statement" as "providing clarification". It is interesting that section 15AB Acts Interpretation Act 1901 contemplates weight being given to an EM, but the "without limiting the generality" language in 15AB(2) would likely allow reference to the Explanatory Statement in appropriate cases. This may bring the explanatory material accompanying the MLI into domestic law in a more direct way than the Vienna Convention path discussed below.

## Domestic law relevant to using extrinsic material in treaty interpretation

***SECTION 15AB USE OF EXTRINSIC MATERIAL IN THE INTERPRETATION OF AN ACT***

***15AB(1)*** *Subject to subsection (3), in the interpretation of a provision of an Act, if any material not forming part of the Act is capable of assisting in the ascertainment of the meaning of the provision, consideration may be given to that material:*

> *(a) to confirm that the meaning of the provision is the ordinary meaning conveyed by the text of the provision taking into account its context in the Act and the purpose or object underlying the Act; or*
>
> *(b) to determine the meaning of the provision when:*
>
> > *(i) the provision is ambiguous or obscure; or*
> >
> > *(ii) the ordinary meaning conveyed by the text of the provision taking into account its context in the Act and the purpose or object underlying the Act leads to a result that is manifestly absurd or is unreasonable.*

***15AB(2)*** *Without limiting the generality of subsection (1), the material that may be considered in accordance with that subsection in the interpretation of a provision of an Act includes:*

> *...*
>
> *(d) any treaty or other international agreement that is referred to in the Act;*
>
> *(e) any explanatory memorandum relating to the Bill containing the provision, or any other relevant document, that was laid before, or furnished to the members of, either House of the Parliament by a Minister before the time when the provision was enacted;*
>
> *(f) the speech made to a House of the Parliament by a Minister on the occasion of the moving by that Minister of a motion that the Bill containing the provision be read a second time in that House;*
>
> *...*

37. In some cases, the EM to a Bill that implements a particular Convention may also include reference to other extrinsic material, raising similar questions of its usefulness. For instance, the EM to the Treasury Law Amendment (Refining and Improving Our Tax System) Act 2024 (No 20 2023), which implemented the Convention with Iceland makes the following comments:

1.9 Another key objective of the Convention is to prevent tax evasion and avoidance. This is made clear in the title and the preamble of the Convention which clarify that Australia and Iceland do not intend the provisions of the Convention to create opportunities for tax evasion and avoidance.

1.10 As members of the Inclusive Framework on BEPS, Australia and Iceland are committed to the implementation of the OECD/G20 BEPS Project. That project provides governments with solutions, designed to be implemented domestically and through treaty provisions, for closing the gaps in existing international tax rules that allow corporate profits to disappear or be artificially shifted to low/no tax environments. These solutions are outlined in the BEPS 2015 Final Reports.

1.11 The Convention adopts a range of the integrity and tax certainty provisions recommended by the BEPS Project. These are outlined in the table below.

| ***Icelandic convention provisions*** | ***BEPS Project 2015 Final Reports*** |
|---|---|
| Title | Action 6 |
| Preamble | Action 6 |
| Article 1 (Persons covered), paragraph 2 | Actions 2 and 6 |
| Article 1 (Persons covered), paragraph 3 | Action 6 |
| Article 4 (Residency), paragraph 3 | Action 2 |
| Article 5 (Permanent establishment), paragraphs 5, 6, 7, 9, 11 and subparagraph 8(a) | Action 7 |
| Article 7 (Business profits), paragraph 8 | Action 14 |
| Article 9 (Associated enterprises), paragraphs 2 and 3 | Action 14 |
| Article 10 (Dividends), paragraph 3 and subparagraph 2(a) | Action 6 |
| Article 13 (Alienation of property), paragraph 4 | Action 6 |
| Article 23 (Mutual agreement procedures), paragraphs 1, 2,3, 5 and 6 | Action 14 |
| Article 27 (Entitlement to Benefits), paragraphs, 1 and 2 | Action 6 |

***1.19 The following section provides an overview of the provisions of the Convention. As the OECD Model Commentary explains the provisions of the Convention that are identical to the equivalent provision in the OECD Model, the overview focusses on the departures from the OECD Model that were agreed to by Australia and Iceland.***

***1.20 Where particular provisions of the Convention are not explained in the following section, it is because those provisions are aligned with the equivalent provision in the OECD Model and their operation is explained by the OECD Model Commentary. (emphasis added)***

38. It would seem arguable that this language opens up the entire BEPS library and the OECD model commentary to consideration. But also raises a caution, since the EM would appear to have the effect of a "reservation" on the terms of the model and any related commentary.

39. Section 5 IAA then provides that "current agreements" have force of law from the date of their entry into force, according to their tenor (or, "as written"). Section 4 IAA provides that the provisions of the Assessment Acts are incorporated and read as one with the IAA, but that to the extent of any

inconsistency, the IAA has primacy. This primacy is limited in the case of some ITAA provisions such as the general anti-avoidance rule in Part IVA which prevails in the case of inconsistency[10].

40. The result is a system where both the tax treaties and the domestic Assessment Acts are both effectively consolidated into a single omnibus statute. All read together.

41. In relation to administrative agreements, it appears to sometimes be the case that no additional legislation is required. For instance (although the Treasury website does refer to Tax Information Exchange Agreements as "treaties" in parts) I could not identify enabling legislation for the majority of TIEAs. The exception being those where the agreement also allocated some tax rights between the parties, the ABAs.

42. The MLI has an unusual status in this scheme. The enabling legislation was the Treasury Laws Amendment (OECD Multilateral Instrument) Act 2018. It received royal assent on 24 August 2018 and Australia deposited its instrument of ratification on 26 September 2018. Australia provisionally nominated all treaties except Germany as "covered". Eleven of our partners have either not also nominated our treaties as "covered" or have not agreed to positions that amend the terms of the relevant treaty. But for others the actions of Australia and our partner have resulted in the terms of the treaty being amended by the MLI process. This is effectively a "paint by numbers" treaty amendment process. It is by the agreement of both parties, but choosing pre-determined elements rather than custom building a treaty. "Synthesised texts" are available for the resulting new treaty after MLI amendment.

43. It is also worth mentioning the status of the OECD "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations". The precise status of this material has always been uncertain, despite the fact that the Commissioner generally seems to have adopted them. The courts have considered the use of the OECD "Commentary" on the "Model Tax Convention on Income and on Capital". And the Commentary certainly says that its conclusions are based on the various OECD reports in transfer pricing, including the major work. The preamble to the commentary on article 9, for instance says:

> *The Committee has spent considerable time and effort (and continues to do so) examining the conditions for the application of this Article, its consequences and the various methodologies which may be applied to adjust profits where transactions have been entered into on other than arm's length terms. Its conclusions are set out in the report entitled Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations,1 which is periodically updated to reflect the progress of the work of the Committee in this area. That report represents internationally agreed principles and provides guidelines for the application of the arm's length principle of which the Article is the authoritative statement.*

44. These Transfer Pricing Guidelines guidelines are, however, also imported into the ITAA 1997 by Division 815, for certain specified purposes. It is possible that this specific and limited importation may prevent other material in the guidelines from being imported under the International Law principles discussed in the following parts of this paper. It is also noteworthy that the disarmingly titled "Miscellaneous Amendments to Treasury Portfolio Laws 2024" discussion draft from Treasury proposed to update the Guidelines directly referenced in the section to the 2022 version (In Division 5 of the draft Bill). Retrospectively to 2022.

*45.* Another recent legislative proposal with direct impact on treaties is the package of draft legislation designed to implement part of the OECD's "Two-Pillar Solution" in Australian law. This package includes an "Imposition Bill" which imposes three kinds of tax. These are assessed under the Assessment Bill: a top-up tax imposed under the Income Inclusion Rule (IIR), a domestic minimum top-up tax (DMT) and tax payable under the Undertaxed Profits Rule (UTPR). These new taxes are assessed separately to income tax and outside of the Income Tax Act 1986. This may, on the face of it, be inconsistent with our Treaty obligations. Except that, like the MLI they purport to be written consistently with the OECD "consensus" on BEPS. To facilitate this the "Taxation (Multinational –

[10] Section 177B(1) ITAA 1936

Global and Domestic Minimum Tax) (Consequential) Bill 2024 proposes (in section 31) to insert Section 5(5) into the International Agreements Act 1953. Section 5(3) of the IAA prevents treaties from overriding Federal or State taxes that are not income tax. This amendment was made to prevent treaties from overriding state land taxes and stamp duty surcharges applied to foreigners. The new taxes proposed under the Two-Pillar package are not, of course, "income taxes". And are therefore prevented from being overridden by treaties. The new section 5(5) will enable the Minister by legislative instrument to make a determination that a provision in an agreement actually ***does*** have effect in relation to these taxes.

46. The status of other international materials related to a treaty which may assist in its understanding is a little more complex under Australian law.

## International law: Treaty interpretation – good faith

47. The Vienna Convention also deals with the use of extrinsic materials in interpreting a treaty.

**SECTION 3. INTERPRETATION OF TREATIES**

Article 31

General rule of interpretation

1. 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 the light of its object and purpose.

2. ***The context for the purpose of the interpretation of a treaty shall comprise***, in addition to the text, including its preamble and annexes:

   (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;

   (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

3. There shall be taken into account, together with the context:

   (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;

   (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;

   (c) any relevant rules of international law applicable in the relations between the parties.

4. A special meaning shall be given to a term if it is established that the parties so intended.

"Article 32

Supplementary means of interpretation

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:

(a) leaves the meaning ambiguous or obscure; or
(b) leads to a result which is manifestly absurd or unreasonable.

48. I want to first pause on the concept of "good faith", and we will then come back to it again later. The High Court has observed that in fact "it is sometimes impossible to be certain of the meaning intended to be conveyed by such expressions as, for example, good faith and bad faith.[11]".

49. The Vienna Convention requires that we interpret tax treaties through the lens of "good faith". It is well accepted that article 31 of the Vienna Convention, with its requirement of interpretation "in good faith" applies to Australian tax treaties[12].

50. The concept of "good faith" traces back to Roman law which explains its limited role in Australian law. We can see it in contract law, where Courts appear to accept "a growing tendency" for an obligation of "good faith" to be implied as being required in the interpretation of contracts and in carrying out obligations under contracts[13]. It can be found in administrative law and in some specific statutes (Corporations Law for instance requires some director's duties to be exercised in good faith).

51. In the context of contract law, it has been said that "good faith" is "a principle of interpretation that can be defined as involving a finding that the purported intention and conduct of a party or parties is, or is not, appropriate for legal recognition given the factual and legal context. It can be described as a credibility finding because someone must engage in the activity of interpreting that intention and conduct as acceptable when viewed in light of its context".[14]

52. There are now a number of court decisions in Australia dealing with tax treaty interpretation, and acknowledging the role of the Vienna Convention and expressly reciting this requirement of "good faith"[15], but none of them deal with the meaning or operation of good faith. Each turn on other issues. Tax treaties are, however, regarded under domestic law as binding agreements entered into by Australia. It is conceivable that, in a suitable case, the actions of Australia in relation to a taxpayer may be challenged on the basis that the treaty interpretation supporting those actions was not arrived at in good faith. The question of the proper application of a tax treaty to a taxpayer is an act of interpretation by the ATO.

53. Review of taxation assessments (which are raised on an incorrect interpretation) in Australia normally occurs under the provisions of Part IVC of the Taxation Administration Act 1953 Cth. Through this mechanism a decision of the ATO that incorrectly interpreted a treaty may be set aside by a court[16]. It is not a relevant fact that the assessment was motivated by a lack of good faith. Australian courts also separately have jurisdiction to set aside assessments by the ATO where they are made for an improper purpose or in "bad faith"[17]. In tax matters, there is some indication that "acting other than in good faith" may be seen as the equivalent of acting "in bad faith"[18]. But Australian courts have not yet dealt with a matter where the taxpayer was able to provide satisfactory (to the court) evidence of bad faith, or lack of good faith on the part of the ATO[19]. It is possible that a taxpayer could base an action in such a case on the proposition that the tax treaty gave rise to a legitimate expectation that decisions would be made consistently with Australia's treaty obligations[20].

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[11] *The Queen* v *Toohey*; *Ex parte Northern Land Council* (1981) 151 CLR 170 at 232

[12] Thiel v Federal Commissioner of Taxation (1990) 94 ALR 647

[13] Ryal Botanic Gardens and Domain Trust v South Sydney City Council (2002) 240 CLR 45; esp at 17, 53.

[14] Corcoran ibid at 8.

[15] Thiel v Federal Commissioner of Taxation (1990) 94 ALR 647; Commissioner of Taxation v Lamesa Holdings BV (1997) 77 FCR 597; McDermott Industries (Aust) Pty Ltd v Commissioner of Taxation (2005) 142 FCR 134; Virgin Holdings SA v Commissioner of Taxation (2008) 214 FCR 278; Russell v Federal Cmr of Taxation (2011) 190 FCR 449; Federal Commissioner of Taxation v SNF (Australia) Pty Ltd (2011) 193 FCR 149; Resource Capital Fund III LP v Commissioner of Taxation (2013) 95 ATR 504; Tech Mahindra Ltd v Commissioner of Taxation [2015] FCA 1082; Bywater Investments Ltd v Commissioner of Taxation; Hua Wang Bank Berhad v Same [2016] HCA 45; Addy v Commissioner of Taxation [2021] HCA 34

[16] Such as in FC of T v Addy [2021] HCA 34

[17] DFC of T v Richard Walter Pty Ltd 95 ATC 4067; FC of T v Futuris Corporation Ltd [2020] HCA 32

[18] Kordan Pty Ltd v Federal Commissioner of Taxation [2000] ATC 4812, at 4815. Quoted in FC of T v Futuris Corporation Ltd [2008] ATC

[19] Futuris supra, at pages 19 and 20.

[20] Minister for Immigration and Ethnic Affairs v Teoh (1995) 128 ALR 353.

 

54. In Futuris[21] the Commissioner of Taxation effectively issued two assessments in relation to the same transaction. The taxpayer commenced proceedings for a review of the decision to issue the second assessment, arguing (in part) that it was not made in good faith. In the sense that the double counting was deliberate, and the second assessment was not a proper exercise of the power to assess. It was an application of the Act to facts which the Commissioner knew to be untrue. The High Court held that there was another factor, an intention to correct the situation in future, which prevented a conclusion that the totality of the evidence supported a finding of a lack of good faith.

55. In the last part of this paper, I will look at the question of whether there are matters which might raise a concern about whether Australia has performed its treaty obligations in good faith.

## International law: Treaty interpretation – extrinsic aids

56. The appropriate approach to interpretation of Australia's international treaties was considered in the High Court decision in *Applicant A*[22] . While that case dealt with the interpretation of the *Convention Relating to the Status of Refugees*, no distinction is to be drawn between the principles of interpretation applicable to double tax treaties and other international treaties[23].

57. It is clear, following the decision in the *Applicant A case*, that the records of a treaty's preparation are legitimate interpretative material under Australian law (per McHugh J 142 ALR 331 at p 355).

58. In *Applicant A*, McHugh J (at p 351–352) set out a number of propositions relating to the interpretation of international treaties.

1. A "holistic" approach to the interpretation of treaties was required by Art 31 of the Vienna Convention (see below). Primacy was to be given to the written text of the Convention but the context, object and purpose of the treaty must also be taken into consideration.

2. Taking the text as the starting point was consistent with the basic principle of interpretation that courts should focus their attention on the "four corners of the actual text" in discerning the meaning of that text. The need to give the text primacy in interpretation was accentuated by the tendency of multinational instruments to be the result of various compromises by various States or groups of States.

3. The mandatory requirement that courts look to the context, object and purpose of treaty provisions as well as the text was consistent with the general principle that international instruments should be interpreted in a more liberal manner than would be adopted if a court was required to construe exclusively domestic legislation.

4. International treaties often fail to exhibit the precision of domestic legislation. This was sometimes the necessary price paid for multinational political comity. The lack of precision in treaties confirmed the need to adopt interpretative principles which were founded on the view that treaties could not be expected to be applied with taut logical precision.

59. This approach was followed in McDermott[24]: Where it was said:

*"… The following principles can be said to be applicable:*

- *Regard should be had to the "four corners of the actual text". The text must be given primacy in the interpretation process. The ordinary meaning of the words used are presumed to be "the authentic representation of the parties' intentions"….*

[21] FC of T v Futuris Corporation Ltd [2008] HCA 32
[22] Applicant A v Minister for Immigration and Ethnic Affairs (1997) 142 ALR 331.
[23] FC of T v Lamesa Holdings BV 97 ATC 4752.
[24] McDermott Industries (Aust) Pty Ltd v Commissioner of Taxation (2005) 142 FCR 134, at para 38.

- *The courts must, however, in addition to having regard to the text, have regard as well to the context, object and purpose of the treaty provisions. The approach to interpretation involves a holistic approach.*
- *International agreements should be interpreted "liberally". Treaties often fail to demonstrate the precision of domestic legislation and should thus not be applied with "taut logical precision".”*

*60.* In a 2020 paper Justice Davies referred to as OECD materials as “soft law” in Australian tax law and suggested their full role remained to be explored.[25]. Davies J included in this category: “the *Model Convention* and its commentary, the OECD’s 2010 *Transfer Pricing Guidelines* and the commentaries on the *MLI*.” Although see above my comments in relation to arguments arising from the inclusion of references to much of this material in domestic EMs.

61. It will be noted that Art 32 only applies in certain circumstances, such as where a term’s meaning is ambiguous after it has been interpreted in accordance with Art 31. In *Thiel’s case*, Dawson J, concluded (as did McHugh J with whom the majority agreed) that the OECD Model Convention and Commentaries were a supplementary means of interpretation which could be used pursuant to Art 32 of the Vienna Convention. However, his Honour also went further and said that:

*“Article 31 of the Convention provides that a treaty is to 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 the light of its object and purpose’. The context includes, in addition to the text, any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty. For my part, I do not see why the OECD model convention and commentaries should not be regarded as having been made in connection with and accepted by the parties to a bilateral treaty subsequently concluded in accordance with the framework of the model.”*

62. Although he also referred to commentators who had doubted the applicability of Art 31 to the interpretation of double tax agreements, Dawson J’s comments appear to favour the wide use of the OECD Model Convention and Commentaries (via Art 31) on the basis that they form part of the context in which an agreement is signed. This would permit the use of the Model and Commentaries even where Art 32 does not apply.

63. There are now a number of decisions where the Commentary has been referred to in the interpretation of tax treaties, including the NSW Supreme Court in *Unisys Corporation Inc v Federal Commissioner of Taxation*[26], as well as the Federal Court in *McDermott* (see below)

64. The OECD commentary was also referred to at paragraph 10 of the IBM decision[27]

*“There is no dispute as to the relevant principles to be applied in the interpretation of the Treaty and the primacy to be given to the text. Regard is to be had to the context, object and purpose of the Treaty provisions (McDermott Industries (Aust) Pty Ltd v Commissioner of Taxation (2005) 142 FCR 134 at [38])”*.

65. McDermott considered the issue of whether a Singaporean company had a permanent establishment in Australia under Article 4 of the Australia/ Singapore tax treaty. In doing so, reference was made to the OECD commentary. At paragraph 37:

*“Double tax treaties are bilateral treaties entered into between two states. As such they are to be interpreted in accordance with the requirements of the Vienna Convention on the Law of Treaties (23 May 1969, entered into force on 22 January 1974) … and in particular Article 31 of the Convention.”*

66. At paragraph 42:

[25] Davies, Jennifer --- "Tax Stability" [2020] MelbULawRw 29; (2020) 44(1) Melbourne University Law Review 424 (austlii.edu.au)
[26] Unisys Corporation v Federal Commissioner of Taxation [2002] NSWSC 1115
[27] *International Business Machines Corporation* v *FC of T* 2011 ATC

*"A useful starting point is the commentary to the draft OECD Model Convention for the Avoidance of Double Taxation with respect to Taxes on Income and on Capital, presented in the 1963 ("OECD Model Convention"), which has served as a model for many although not all of Australia's double tax agreements. Certainly the commentary has been used to assist in the interpretation of double tax agreements based upon it…"*

## International law: more distant materials?

67. We have seen above the references to "soft law" by Justice Davies, and paths by which the OECD commentary, the MLI commentary and possibly other materials might be considered when trying to resolve treaty interpretation issues. But there are even more distant materials which may be relevant from time to time.

68. One current controversy revolves around the ATO focus on payments for software use, and in Software-as-a-service ("SaaS") businesses.

69. The debate is well publicised, and I don't wish to trawl through all of it, but to focus on one small point.

70. In TR2021/D4, the Commissioner of Taxation (**Commissioner**) provided a concession that the "simple use" of the software did not constitute a royalty (paragraph 67 to 72). The view expressed was that simple use of software does in fact involve the use of copyright but that this use is inevitable and necessary to facilitate the use of the software as a functional product and ultimately, the use of copyright is merely incidental. This was an echo of similar statements found in TR 93/12, which at paragraph 27 said:

*"Payments for any licence for **simple use** of computer software (i.e. where the end-user acquires only the right to run the program, whether on a single computer only or on the licensee's computer network, **and does not acquire any rights to use the copyright in the program**) are not royalties for purposes of income tax law."* (emphasis added)

71. The 1992 definition covered a situation where the end-user did not acquire any rights to use the copyright whereas the 2021 definition acknowledged that simple use may include cases where there is a grant of a right to use the copyright.

72. The concept can be traced back to a 1992 OECD publication on software[28]. It was used to label a purchase and use of software, as distinct to a 'rental' of software.

73. What is particularly interesting is that the 1992 OECD software report recommended against amending the Commentary to deal with the issues it raised. As a result, the expression "simple use" was not expressly included in the OECD model commentary. But the concept may be inferred from the commentary at paragraphs 14, 17.2 and 17.3.

74. The point is not so much the actual issues raised, but to note that there is an OECD report which lies behind the OECD commentary and which may inform the discussion. The status of which may be unclear as an aid to statutory interpretation. The reason it may be relevant is because essentially, TR2021/D4 focused on 'form over substance' whereas the OECD software report and Commentary prioritises 'substance over form'. These are broad issues of approach which are likely to be relevant to the issue if it were litigated.

75. Of course, TR2024/D1 omits the concept of "simple use" entirely, but the issue of the correct approach remains[29].

76. A final point at this stage is to note that there are a substantial body of OECD materials that relate to the issues raised in the Model Convention and that through reference to them in the Model Convention Commentary and the principles above they may be able to be put before a court in an appropriate matter.

[28] https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-2014-full-version/r-10-the-tax-treatment-of-software_9789264239081-103-en#page14 : at para 44. Located at this address on 03/06/2024

[29] TR2024/D1 para 183

## International law: Article 26 of the Vienna Convention?

77. I said I would come back to "good faith". And this is in the context of considering Article 26 of the Vienna Convention.

78. Article 26 of the Vienna Convention imposes a slightly different requirement to Article 31, and that is, that the treaty "must be performed by (the parties) in good faith":

> "Article 26
>
> "Pacta sunt servanda"
>
> Every treaty in force is binding upon the parties to it and must be performed by them in good faith.

79. This requirement goes to the behaviour of ongoing performance of the treaty, rather than only its interpretation. It would seem applicable to the behaviour of both the legislature and the executive. The executive in the context of our system would be the treasurer and Australian Tax Office. In our domestic system most tax decision making in relation to tax law are made by the legislature. The executive has little rule making power (presently) and in any event we have previously discussed the evidentiary difficulties taxpayers have found when trying to point to "bad faith" in executive decision making (as represented by the Australian Tax Office).

80. In CWY20[30] the Federal Court of Australia observed in the context of executive decision making in non-tax treaties that:

> "Article 26 of the *Vienna Convention on the Law of Treaties*, opened for signature 23 May 1969, 1155 UNTS 331 (entered into force 27 January 1980), and the principle of pacta sunt servanda, impose upon the Australian Government an obligation to observe and perform, in good faith, those treaties to which it is a party. Failure to do so exposes the nation to responsibility for internationally wrongful acts under the Draft Articles on Responsibility of States for Internationally Wrongful Acts, commended by the General Assembly on 28 January 2002, A/RES/56/83 and on 8 January 2008, A/RES/62/61, in which case Australia may face legal consequences (Art 28), including, but not limited to: cessation and non-repetition (Art 30), reparation (Art 31) in the form of restitution (Art 35), compensation (Art 36) and satisfaction (Art 37), in addition to countermeasures (Art 49). Whether or not these legal consequences in fact arise, a breach of a treaty is a breach of international law, which is a breach of law nonetheless."

81. The admonition to perform "in good faith" has not been further elaborated in Australian cases. The majority of which are immigration decisions and simply consider whether a treaty obligation has been breached, and the consequences of the breach. Rather than whether the breach was a result of a lack of good faith. In CWY20, for instance, the question was whether a decision might be said to be "in the national interest" even though it amounted to a breach. And the conclusion was that it could. The court took the view that the legislation there, in requiring the minister to make a determination of what was "in the national interest", required consideration to be given to the consequences of a breach of treaty obligations. Although it was accepted that "the effect of Australia not complying with a treaty or convention is ordinarily a matter of sensitive judgment for the executive branch of government and not for the Courts"[31]. The court accepted from the legislative context that this was a case where a judgement of what was in the national interest may involve a decision that breached a treaty obligation. But that, even where such a step was contemplated and authorised by the legislature, it was still necessary that the minister explicitly address this issue in the decision making process.

82. So the question in Australian taxation disputes may often simply turn on whether a domestic provision was in breach of a tax treaty, and whether as a result an assessment can be put aside, because for instance there was no clear expression of a legislative intent to override a treaty..

[30] Acting Minister for Immigration, Citizenship, Migrant Services and Multicultural Affairs v CWY20 (2021) 288 FCR 565
[31] At para 163

83. The role of the concept of "good faith" in relation to "performance" in this context may be more about whether the Australian Parliament failed to perform its tax treaty obligations in good faith when it passed inconsistent domestic legislation, since performance in this context is an act of the legislature, not the executive. This would be a question about the legislative behavior of Parliament. Such an argument seems unlikely to be a successful basis for challenging a domestic provision[32].

84. Firstly, the inconsistency itself may result in the tax treaty provision overriding the domestic one[33] unless there is a clear intention that the treaty be overridden giving a taxpayer a basis of appeal under the domestic rules, and secondly it is unlikely that a court would conclude that the inconsistency was, alone, sufficient evidence of a lack of good faith. There may need to be some specific evidence of dishonesty, improper or ulterior motive or deliberate impropriety[34]. For instance, legislation which was contrived in form, as part of an attempt to skirt treaty obligations. It also seems likely that generally a foreign taxpayer will lack standing to bring its own action (outside of the Part IVC tax appeal provisions) against Australia for a breach of a tax treaty since tax treaties do not themselves give taxpayers a right to do so. The best approach open to taxpayers seems to remain an appeal within the domestic tax system, arguing that the tax treaty provision governs their situation. It is possible that Article 26 gives rise to an argument that the Parliament should be presumed to intend to honor its treaties, unless it expressly overrides them. So that "apparent" override will not be sufficient to remove a taxpayer's treaty rights..

85. Separately, it is possible that an argument may be made in a suitable case that the actions of the ATO were inconsistent with an obligation to "perform in good faith" Australia's obligations under a tax treaty. This argument may arise, for example, in the context of provisions of tax treaties which relate to behaviour of a tax authority, rather than taxing rights. In the Australia/United States tax treaty, for instance, article 25 authorises exchange of information in certain circumstances. As discussed above, however, courts in Australia have not yet been presented with a case where the evidence justified a conclusion that the tax authority had acted in bad faith. Taxpayers are likely to face difficulty obtaining evidence regarding internal decision making in the ATO which would support such a matter. As noted above, there is the possibility that a taxpayer may argue that there was a legitimate expectation that the treaty would be complied with[35].

## Could OECD commentary import good faith requirements into domestic law ?

86. It remains to consider whether the OECD Model Convention and Commentaries contain expressions of the principle of good faith that would be imported into Australian tax law under the principles discussed above.

87. The concept is discussed in the Model Tax Convention on Income and on Capital, Condensed version, 21 November 2017 in a number of places.

88. At para 16.2 the role of Article 31(1) of the Vienna Convention is acknowledged. This is consistent with Australia's existing law.

89. In paragraphs 57 to 65 of the Commentary on Article 1 there is a discussion of the role of good faith in preventing treaty abuse. The commentary recognises that if a treaty lacks an "anti-abuse" clause, a state may still take a view that abuse of the treaty is a breach of the requirement to interpret the treaty with recognition of the object and purpose of the treaty, interpreted in good faith. Australia has adopted the MLI principal purpose test in Article 7, and noted that a number of its agreements already contain anti-abuse provisions. The effect of Article 7(1) of the MLI is to prevent benefits where one of the principles purposes was the obtaining of the benefit. But this denial of benefit does not occur where "it is established that granting the benefit…would be in accordance with the object and purpose" of the agreement. The OECD Model commentary, read with the MLI provision suggest that the object and purpose here must be determined "in good faith". Thus perhaps importing the concept into this aspect

[32] Polites v The Cth [1945] 70 CLR 60

[33] International Tax Agreements Act 1953 (Cth), section 4(2); noting that Article 27 and 46 of the Vienna Convention have the effect that inconsistent domestic provisions are not assumed to prevail.

[34] DC of T v Widdup [2022] FCA 1403, at para 9.

[35] Minister for Immigration and Ethnic Affairs v Teoh (1995) 128 ALR 353..

of Australian treaty interpretation. Although it must be remembered that Australian treaties are generally subject to the operation of our GAAR, which does not contain a good faith element.

90. The term is used again in the Commentary on Article 7, at paragraph 59.1 to describe a quality of a type of taxpayer initiated adjustment to their tax position which justify a corresponding adjustment to the tax position in other other state. A similar situation is discussed in paragraph 61 of the Article 9 commentary.

91. These are the extent of the references to good faith in the Commentary. But it seems clear that if there was an emerging international consensus on the role of the concept of good faith, and clarity around its operation then embedding that into the MLI, or the OECD Model agreement and commentary would likely result in it being relevant to the Australian interpretation of its tax treaties.

## Have we seen performance that was not in good faith?

92. There have been several recent measures that raised questions about whether Australia was performing its treaty obligations in good faith. In other words whether Australia's actions unilaterally and improperly overrode its treaty obligations. Because of the discussion above, it is not clear that taxpayers would be successful in arguing that the circumstances support a conclusion that Australia has not performed a treaty in good faith, in the manner contemplated by Article 26 of the Vienna Convention.

93. One arose in relation to the Indian/Australian tax treaty[36]. Although not involving an argument of good faith, the decision dealt with an argument that the ATO interpretation of a treaty (an act of the executive) was overly literal and ignored the "object and purpose" of the provision. The taxpayer argued that the ATO interpretation would result in a taxation outcome in Australia which was different to that arising in India. The court held that, if so, this was a result of differences in Australia's domestic law, not in treaty interpretation. The court accepted evidence of the position under Indian law. India went on to quickly negotiate a new treaty with Australia that reversed the effect of the court decision.

94. It has, sadly, also become a feature of the Australian tax landscape that retrospective legislation can be described as a "clarification" of the law rather by an admission that the Government has decided to retrospectively affect taxpayers rights. One such recent example in fact involves domestic legislation which expressly overrides apparent treaty rights, raising the question whether it could be said to represent a failure by Australia to perform its treaties in good faith. The example in question is the recently enacted *Treasury Laws Amendment (Foreign Investment) Act 2024* (Cth) (**Foreign Investment Act**) which is said to amend the *International Agreements Act 1953* (Cth) (**Agreements Act**) to "clarify the relationship between the Agreements Act and Acts that impose tax other than 'Australian tax". A number of taxpayers were in the process of challenging Foreign Purchaser Surchagre Duty (FPS) and Land Tax Surcharge (LTS) imposed by Australian States on the basis that these were in breach of treaty obligations in relation to the taxation of foreigners, where "tax" in some treaties extended to State taxes and imposts.The Act seeks to prevent such challenges. It is to be expected that the validity of this amending legislation will be challenged. .

95. Taxation Laws Amendment Act (no 4) 2000, amended the International Agreements Act to prevent our treaties operating in the manner that the Full Federal Court found they did in Lamesa[37]. The court had found that the real property alienation provisions in our treaties did not result in taxation of gains on disposal of the shares in a top company of a group where Australian real property was held by underlying entities.

96. Another example involved a personal tax measure which imposed a different effective rate of personal tax on individuals who were in Australia on a "working holiday" visa. The taxpayer argued that the anti-discrimination language in Article 25 of the UK/Australian tax treaty operated to prevent Australia taxing her at the higher rate. The High Court held in her favour[38].

[36] Satyam Computer Services Limited v Commissioner of Taxation [23018] FCAFC 172
[37] Commissioner of Taxatioon v Lamesa Holdings BV [1997] FCA 785
[38] FC of T v Addy [2021] HCA 34

97. A significant exampleinvolved the introduction of certain anti-avoidance provisions. These were the Multinational Anti-Avoidance Law[39] ("MAAL") and Diverted Profits Tax[40] ("DPT"). Both of these measures had the potential effect of imposing a new tax liability on certain corporations, including some who might be resident in jurisdictions Australia had a tax treaty with. And who would likely have faced a lesser Australian tax burden under the tax treaties alone.

98. The Parliament, however, introduced the MAAL and DPT by inserting them into our GAAR, Part IVA. Australia's tax treaties expressly provide that they are "subject to" the operation of our GAAR. So it is argued that the extension in scope of our GAAR is not inconsistent with the object and purpose of our tax treaties. The MAAL was introduced with the express aim of having foreign taxpayers create or increase their taxable presence in Australia. Most did so fairly simply, complying with the Parliamentary intent and avoiding being subject to the MAAL. It is therefore unlikely the question of whether the MAAL is an action which is inconsistent with a good faith execution of our tax treaty obligations, will ever arise in practice.

99. The same question could, however, arise in relation to the operation of the DPT. The ATO has considered the application of the provisions to a significant number of taxpayers and the first such matter was the subject of an appeal recently in the Federal Court.[41]

100. Another setset of provisions which raised concern were those in relation to intangibles and royalties announced by the Government in the Federal Budget of October 2022, but now withdrawn[42]. These provisions targeted payments, directly or indirectly, to low or no-tax jurisdictions, for use of intangibles. Although the details were never finally settled, it is possible that the provisions may have impacted certain payments to treaty residents, which would be royalties or payments for services. The normal treaty outcomes for such payments would be, respectively, withholding tax, or no withholding tax. Subject to the operation of other measures such as our anti-hybrid rules. The proposed consequence of the new measures was loss of Australian tax deductions for the amounts. The result may have been an adverse tax outcome under domestic law that alters the outcome which would otherwise arise under a tax treaty.

101. The Australian Government generally refers to such provisions as "integrity measures". The expression has no accepted domestic or international definition, and appears to be variously used for both measures designed to counter tax evasion[43] and measures addressing what one state considers "unfair" behaviour[44]. Or perhaps behaviour that is not felt to be in good faith.

[39] Section 177DA Income Tax Assessment Act 1936 (Cth)
[40] Section 177J Income Tax Assessment Act 1936 (Cth)
[41] PepsiCo, Inc v Commissioner of Taxation [2023] FCA 1490; appeal heard 8 – 10 May 2024 in Melbourne.
[42] Originally Budget Paper No. 2, page 15; see now page 11 of Part1: Receipt Measures in Budget Paper No.2 Budget 2024-25 .
[43] see for instance the ATO Tax Integrity Centre, to which individuals can report suspicions of illegal behavior
[44] See for example "Government election commitments: Multinational tax integrity and enhanced tax transparency"; Australian Treasury Consultation Paper August 2022