A brave new post-BEPS world: new Double Tax Treaty between Germany and Australia implements BEPS measures

On 12 November 2015, Germany and Australia signed a new Double Tax Treaty ("Treaty") replacing the existing Treaty between both countries signed in 1972. The new Treaty is one of the first double tax treaties to be concluded globally since the finalization of the OECD’s BEPS Action Plan and therefore represents a significant landmark on the global tax landscape that may indicate the trajectory of post-BEPS double tax treaties.

Implementing BEPS measures of the Treaty

The Treaty implements a number of recommendations made in the final BEPS reports:

- **Preventing treaty abuse**: as recommended by the BEPS Action 6 report, the title of the Treaty and its preamble have been changed to expressly refer to the prevention of tax avoidance as a purpose of the Treaty and to clarify that the Treaty shall not create opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping). Furthermore, the new Treaty provides that dual resident entities can not benefit under the Treaty if the state of the dual resident’s place of effective management either (i) cannot be determined or (ii) is in neither state and has not been determined by mutual agreement between the competent authorities of both states. Another BEPS measure to prevent treaty abuse is the inclusion of a Limitation of Benefits (LoB) Article that (i) disallows the relief for individuals exempt from tax in another state by reason only of his/her status as a temporary resident, (ii) disallows the benefits of the Treaty if obtaining of that benefit was one of the principal purposes unless it is in accordance with the object and purpose of the Treaty and (iii) allows the application of domestic anti-avoidance rules in addition to the Treaty LoB.

- **Preventing the artificial avoidance of permanent establishments**: as recommended by the BEPS Action 7 report, the PE definition has been extended. Under the new Treaty, the specific activity exemptions of the PE definition will only apply if the activities listed are themselves "preparatory or auxiliary". In addition, the specific activity exemptions are also subject to an anti-fragmentation rule whereby the exemptions will not be available if either (i) "complementary functions" are carried on by closely related enterprises at either a PE of that other enterprise or (ii) if the activities of the offshore entity and the closely related enterprise in combination are not
preparatory or auxiliary. Furthermore, the new Treaty expressly states that
the dependent agent PE rule also applies with respect to persons who
"habitually play the principal role leading to the conclusions of contracts
that are routinely concluded without material modification". Commissionaires and contract manufacturers may also constitute a
deemed PE under the new Treaty unless they act as independent agents.
The constitution of a deemed PE by a contract manufacturer goes beyond
the BEPS Action 7 recommendation and has its origins already in the
Treaty from 1972. An agent does not qualify as independent if this agent
acts exclusively or almost exclusively on behalf of one or more enterprises
to which that person is closely related. The new Article 5 of the Treaty
provides for a broad definition of "closely related" person whereby the
decisive criterion is being under the control of another enterprise based on
all the relevant facts and circumstances and, in any case, if more than 50
per cent of the beneficial interest or vote and value are (directly or
indirectly) held by another person.

- **Dispute resolution:** as recommended in the **BEPS Action 14** report, the
  Treaty makes dispute resolution mechanisms more effective by generally
  limiting the time period in which a state can make an adjustment to profits
  attributable to a PE or in relation to a transfer pricing adjustment to a
  period of 10 years and limiting mutual agreement procedures to cases
  presented within three years from the first notification of the relevant
  action.

**Other significant changes**

- **Reduced withholding tax rates:** the Treaty provides for a nil tax rate
  applicable for intercorporate dividends paid to publicly listed
  companies (or their subsidiaries) and certain unlisted companies that
  hold 80 per cent or more of the shares in the paying company, but at
  the same time sets forth certain minimum holding periods. If the nil
dividend withholding tax rate is not available a rate of between 5 to 15
  % applies. The general withholding tax rate on interest remains at 10
  per cent however exemptions are available for certain financial and
government institutions. The royalty withholding tax rate has been
  reduced from 10 to 5 per cent.

- **Greater cooperation between tax authorities:** the new Treaty also
  contains a new Non-discrimination and Assistance in Collection of
  Taxes Articles and provides for more comprehensive Mutual
  Agreement Procedure and Exchange of Information Articles.

- **Hybrid entities:** the Treaty contains several provisions to address
  hybrid entity mismatches, inter alia in Article 1 (2) and in the protocol to
  the Treaty. In the event that a hybrid entity mismatch results in double
taxation, the protocol requires the competent authorities to consult
each other to find an appropriate solution.
Commencement

According to information provided by German Federal Ministry of Finance, the ratification of the new Treaty shall be done as soon as possible, but is not expected prior to the second half of 2016 due to procedural requirements. Australia has similarly stated that it will seek to pass legislation to implement the treaty as soon as possible, however given the limited number of parliamentary sitting days left in 2015 it would be unlikely that this would occur before February 2016. If the new Treaty should be ratified by both countries in the course of 2016, it will become applicable on 1 January 2017 for Germany and on 1 January (withholding tax), 1 April (fringe benefits tax) and 1 July (other Australian taxes) respectively for Australia.

Interaction with Australian Multinational Anti-Avoidance Law ("MAAL")

Pursuant to the recommendations under BEPS Action 6, the new Treaty provides for the application of domestic anti-avoidance rules under paragraph 3 of the LoB Article. The Australian MAAL (which forms part of Australia’s general anti-avoidance rule) is likely to be the type of domestic anti-avoidance rule contemplated by this paragraph and to this extent should therefore not offend Australia’s treaty obligations. In any case, as from an Australian perspective Australia’s general anti-avoidance rule applies in priority to its treaty obligations, the Australia MAAL may apply despite any protections afforded by the new Treaty. The Australian MAAL may therefore still apply to effectively deem a notional PE of a German entity (and attribute Australian taxable income and royalty/interest payments to that PE) despite no PE existing under the Treaty definition.

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