After numerous years in treaty limbo, the US Senate recently provided its advice
and consent for ratification of four protocols with Luxembourg, Switzerland,
Japan and Spain, setting the stage for the protocols to enter into force after an
exchange of ratification instruments with the relevant jurisdictions. Each of the
protocols had been “held” in the Senate Foreign Relations Committee for several
years because of objections by Senator Rand Paul, a Republican Senator from
Kentucky, over questions about the privacy of taxpayer information.

The Senate Foreign Relations Committee still has not acted on new income tax
treaties with Hungary, Chile and Poland. Action is delayed on these treaties due
to concerns about the interaction of these treaties with the recently enacted
§ 59A of the Internal Revenue Code, “base erosion anti-abuse tax.” Legislators
want to ensure that the treaties will not override the application of § 59A.

The material provisions of each of the protocols is summarized below:

- Luxembourg
- Switzerland
- Japan
- Spain

LUXEMBOURG

The Protocol Amending the Convention between the Government of the United
States of America and the Government of the Grand Duchy of Luxembourg for
the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with
Respect to Taxes on Income and Capital (the Luxembourg Protocol) was signed
on May 20, 2009. For the full text of the protocol, please see the following link:
Luxembourg Protocol.

The Luxembourg Protocol makes various changes to the convention, but
particularly broadens the scope of the information sharing provisions. The
specific provisions are discussed more fully below.

Exchange of Information (Article 28)

The Luxembourg Protocol replaces Article 28 with a new exchange of
information article that allows for easier exchange of information by the United
States and Luxembourg for purposes of carrying out the convention or each of
such country’s domestic law.
Under the new Article 28, the tax authorities of each country are allowed to exchange information that is foreseeably relevant in carrying out the provisions of the convention or the domestic tax laws of either country, including information that would otherwise be protected by bank secrecy laws. Specifically, each of the United States and Luxembourg commits to providing information to the other, regardless of whether the non-requesting state needs or wants the information, and explicitly states that information requests cannot be denied solely because a bank, other financial institution, agent, nominee or fiduciary holds the requested information. Moreover, the exchange of information provision is not restricted to taxes covered under the convention.

Significantly, the information exchange provision in the protocol also covers non-US or non-Luxembourg persons if there is a connection to the applicable jurisdiction (e.g., a bank account, permanent establishment).

**Eversheds Sutherland Observation:** The Luxembourg Protocol continues what has been over a decade-long push by the United States, and more recently the Organization for Economic Cooperation and Development (OECD), to increase information sharing among treaty partners. The change to the information exchange provision is a response to private banking scandals, where US taxpayers were shielded by domestic bank secrecy laws that may have helped certain US taxpayers evade US tax obligations. The updated provisions reflect the United States’ attempt to ensure that the exchange of information is not hindered due to domestic bank secrecy laws and to expand the US exchange of information network.

In years since the 2009 signature date of the Luxembourg Protocol, information sharing has become a common fact-of-life for many multinational taxpayers, meaning that transactions involving multiple jurisdictions are likely to be scrutinized by several taxing authorities. The new Article 28 incorporates the standard OECD language, which in turn is substantially similar to Article 26 of the 2006 Model Treaty. The language is also consistent with the standard codified in § 7602 of the Internal Revenue Code.

The Luxembourg Protocol also provides the legal basis of the Intergovernmental Agreement (IGA) between the United States and Luxembourg for purposes of the Foreign Account Tax Compliance Act (FATCA). The IGA specifically referenced the Luxembourg Protocol, but since the Luxembourg Protocol was not in force, the Luxembourg tax authorities have been providing information to the Internal Revenue Service based on the OECD multilateral convention on mutual administrative assistance, which raised legal questions due to bank secrecy rules. Thus, even though exchange of information in light of
FATCA was already occurring, the Luxembourg Protocol clarifies the legal basis for this exchange of information.

**Effective Date**

The Luxembourg Protocol entered into force on September 9, 2019. After September 9, 2019, requests can be made for tax years beginning on or after January 1, 2009.

**Eversheds Sutherland Observation:** The effective date of the information exchange provision is retroactive and may be used by authorities to obtain information, including bank information, from as far back as tax years beginning on or after January 1, 2009.

**SWITZERLAND**

The Protocol Amending the 1996 Convention between the United States of America and the Swiss Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income (the Switzerland Protocol) was signed on September 23, 2009. For the full text of the protocol, please see the following link: [Switzerland Protocol](#).

The Switzerland Protocol makes various changes to the convention:

- Broadens the scope of the information sharing provisions;
- Implements mandatory arbitration procedures for certain cases; and
- Provides a 0% withholding rate for dividends paid to certain individual retirement accounts.

These and other items are discussed more fully below.

**Mutual Agreement Procedure (Article 25)**

The Switzerland Protocol incorporates a mutual agreement procedure under Article 25.

The mandatory arbitration procedure under the Switzerland Protocol applies to certain cases that the US and Swiss competent authorities have been unable to resolve after a reasonable period of time. The arbitration panel's determination for a case is binding on both the United States and Switzerland, unless any concerned person does not accept the determination. Unresolved cases are not eligible for arbitration if the decision has been rendered by a US or Swiss court or administrative tribunal. This arbitration procedure is similar to the procedures outlined in the US income tax conventions with Belgium, Canada, France and Germany, as well as the Japan Protocol and the Spain Protocol.

**Eversheds Sutherland Observation:** The new mutual agreement
procedure provisions are generally helpful to taxpayers. Oftentimes, taxpayers that submit disputes to competent authority are left in a state of limbo waiting for the competent authorities of the contracting states to reach a resolution. Under the arbitration procedures, if the competent authorities are unable to reach a conclusion within two years or other such time period agreed upon by the competent authorities, the new mutual agreement procedure provisions require the competent authorities to allow taxpayers to submit such disputes to an arbitration panel that will then reach a resolution with respect to the taxpayer’s issue. Additionally, the arbitration procedures are binding on the contracting states only if the taxpayer accepts the decision of the arbitration panel. A taxpayer continues to have other avenues to resolve the dispute should the arbitration panel reach a result that is unfavorable to the taxpayer.

Exchange of Information (Article 26)

The Switzerland Protocol modifies the exchange of information provisions of Article 26 and the 1996 protocol that was executed and ratified with the current version of the convention. Conforming with the standard codified in § 7602 of the Internal Revenue Code, the Switzerland Protocol allows the tax authorities of each country to exchange information that may be relevant in carrying out the provisions of the convention or the domestic tax laws of either country, including information that would otherwise be protected by bank secrecy laws. The exchange of information is not restricted by the taxes covered under the convention. The information exchange provisions also cover certain non-US or non-Switzerland residents to the extent there is a connection to either jurisdiction (e.g., a bank account, permanent establishment). The Switzerland Protocol expands the current convention exchange of information provisions. Absent the provisions in the Switzerland Protocol, only information that is necessary to prevent tax fraud or related fraudulent activities with respect to taxes covered under the convention is permitted to be exchanged.

Eversheds Sutherland Observation: The Switzerland Protocol continues what has been over a decade-long push by the United States, and more recently the OECD, to increase information sharing among treaty partners. The change to the information exchange provision is a response to private banking scandals, where US taxpayers were shielded by domestic bank secrecy laws that may have helped certain US taxpayers evade US tax obligations. The updated provisions reflect the United States’ attempt to ensure that the exchange of information is not hindered due to domestic bank secrecy laws and to expand the US exchange of information network. Also, the Switzerland Protocol provides a lower threshold as information can be exchanged if such information may be relevant to carrying out the domestic tax laws and it does not require fraud. As noted above, the lower threshold for information exchange was the stated reason that this and the other protocols were being held up in the Senate Foreign
Relations Committee.

Since the 2009 signature date of the Switzerland Protocol, information sharing has become common for many multinational taxpayers, meaning that transactions involving multiple jurisdictions are likely to be scrutinized by multiple taxing authorities.

**Dividends (Article 10)**

The Switzerland Protocol revises Article 10 to exempt dividends paid to pensions, retirement arrangements and individual retirement accounts from withholding unless the payor is a company that is controlled by the payee. Previously, individual retirement accounts did not qualify for the exemption. However, this provision is not self-executing. To qualify for the exemption, the Swiss and US competent authorities are required to agree that such payee’s classification generally corresponds to a pension, retirement arrangement or individual retirement account that is respected for tax purposes in the other country. Also, the payee must satisfy the limitation of benefits provision in paragraph 2 of Article 22.

**Eversheds Sutherland Observation:** As this provision is not self-executing with respect to the status of the payee, a memorandum of understanding is required to be entered by the Swiss and US competent authorities for this provision to be effective and to allow payees to obtain these benefits.

**Effective Dates**

The Switzerland Protocol will enter into force once the United States and Switzerland exchange instruments of ratification.

Specific provisions have different effective dates once the Switzerland Protocol is entered into force. Amounts paid or credited are eligible for the withholding exemption under the Switzerland Protocol if such amounts are paid or credited on or after January 1 of the year following the date the Switzerland Protocol is entered into force. The arbitration provisions apply to cases that are under consideration by the competent authorities starting on the date the Switzerland Protocol is entered into force.

The exchange of information provisions apply to requests made on or after the date the Switzerland Protocol is entered into force. However, information obtained under these provisions may relate to prior years. The exchange of information provisions regarding information held by banks and financial institutions applies to information relating to any date beginning on or after the Switzerland Protocol’s September 23, 2009, signature date. The other exchange of information provisions are effective with respect to information that relates to taxable periods beginning on or after January 1, 2010.

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Legal Alert: Following the protocols – US Senate approves tax treaty protocols with Luxembourg, Switzerland, Japan and Spain continued
The effective date of the information exchange provisions are retroactive and may be used by authorities to obtain information, including bank information, from as far back as September 23, 2009.

JAPAN

The Protocol Amending the Convention between the Government of the United States of America and the Government of Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Protocol (the Japan Protocol) was signed on January 24, 2013. For the full text of the protocol, please see the following link: Japan Protocol.

The Japan Protocol makes various changes to the convention:

• Broadens availability of 0% withholding rates on interest and dividends;

• Implements mandatory arbitration procedures for certain cases; and

• Incorporates provisions that require the contracting states to assist each other in the collection of certain revenue claims.

These and other items are discussed more fully below.

*Interest (Article 11) and Dividends (Article 10)*

The Japan Protocol generally liberalizes who can claim 0% withholding on interest under Article 11. As described below, 0% withholding on interest was previously reserved for a set group of persons, with all others eligible for (in a best-case scenario) 10% withholding on interest paid by a resident of one jurisdiction to a resident in the other jurisdiction. The Japan Protocol retains 10% withholding for “contingent” interest and excess inclusions with respect to residual interests from real estate mortgage investment conduits, consistent with the 2006 US Model Treaty.

Eversheds Sutherland Observation: The Japan Protocol dramatically expands the payees eligible to claim withholding exemptions with respect to interest payments, bringing the convention in line with most of the United States’ major trading partners. The existing provisions of Article 11 essentially limit the available interest withholding exemption to the US or Japanese governments (and instruments guaranteed insured, or financed by such governments), banks, insurance companies, registered securities dealers, enterprises primarily engaged in lending or deposit activities, certain pension funds, and certain trade receivables. All other payees are eligible for a reduced 10% withholding rate on interest, but not an exemption.

The Japan Protocol reduces the ownership and holding requirements to claim an
exemption from withholding on dividends. Specifically, the current treaty requires ownership of “more than 50% of the voting stock of the corporation paying the dividend.” The Japan Protocol changes this threshold to “at least 50%.” The Japan Protocol also reduces the stock holding period to be eligible for the exemption from 12 months to 6 months.

**Eversheds Sutherland Observation:** The existing provision of the Japanese treaty was already very favorable with respect to the requirements of 0% withholding for dividends, and the Japan Protocol is even more so. Most US income tax treaties with a dividend withholding exemption, in addition to other specific requirements, require a holding of at least 80% of the stock of the payor for 12 months before the applicable dividend.

**Mutual Agreement Procedure (Article 25)**

The Japan Protocol adds new paragraphs 5 through 7 to Article 25. These paragraphs implement a mutual agreement procedure.

The mandatory Japanese procedure under the Japan Protocol applies to certain cases that the US and Japanese competent authorities have been unable to resolve. The arbitration panel will deliver its determination in writing. Notably, a person presenting the case is not required to accept the resolution of the arbitration panel. However, if the presenter does accept the resolution, such resolution is treated as constituting a resolution by mutual agreement under Article 25, which has the effect of binding the contracting states.

This arbitration procedure is similar to the procedures outlined in the US income tax conventions with Belgium, Canada, France and Germany, as well as the Switzerland Protocol and the Spain Protocol.

**Eversheds Sutherland Observation:** The new mutual agreement procedure provisions are generally helpful to taxpayers. Oftentimes, taxpayers that submit disputes to competent authority are left in a state of limbo waiting for the competent authorities of the contracting states to reach a resolution. Under the arbitration procedures, if the competent authorities are unable to reach a conclusion within two years or other such time period agreed upon by the competent authorities, the new mutual agreement procedure provisions require the competent authorities to allow taxpayers to submit such disputes to an arbitration panel that will then reach a resolution with respect to the taxpayer’s issue. Additionally, the arbitration procedures are binding on the contracting states only if the taxpayer accepts the decision of the arbitration panel. A taxpayer continues to have other avenues to resolve the dispute should the arbitration panel reach a result that is unfavorable to the taxpayer.
Because the arbitration panel’s decision must be one of the resolutions proposed by the contracting states, these changes put pressure on competent authorities to settle claims, as the panel has no ability to reach a decision that lies between those competing resolutions.

**Assistance in the Collection of Certain Revenue Claims (Article 27)**

The Japan Protocol amends Article 27 to require the contracting states to assist each other in collecting taxes, interest, costs of collection, and related penalties with respect to taxes covered by the convention and certain listed taxes upon request. The request for information must be withdrawn if the requesting contracting state loses its right under domestic law to collect the revenue or suspends collection of the revenue according to its domestic law.

However, this assistance is limited. With respect to a company, the assistance is available only where: (1) a claim is not eligible to be resolved through mutual agreement procedure; (2) a claim has been agreed to through mutual agreement procedure; or (3) a claim involves a company that has terminated the mutual agreement procedure.

**Exchange of Information (Article 26)**

The Japan Protocol expands the information that a contracting state is required to exchange with the other contracting state. Article 26 of the Japan Protocol requires disclosure of information that is “foreseeably relevant” for certain administrative or enforcement purposes, including information from a bank. Before this amendment, the Article had only required disclosure of “relevant” information. The language is also consistent with the standard codified in § 7602 of the Internal Revenue Code. The exchange of information is not restricted by the taxes covered under the convention. However, under the amended provision, a contracting state is not required to reveal certain confidential communications between a client and an attorney.

**Japanese Foreign Tax Credit and Dividend Provisions (Article 23)**

The Japan Protocol amends Article 23(1)(a) to include a re-sourcing rule, which is intended to ensure that a Japanese resident can obtain Japanese foreign tax credits for US taxes paid in cases where the United States has the primary taxing rights over an item of income. Specifically under the re-sourcing rule, if the United States can tax an item of income beneficially owned by a resident of Japan, that income will be deemed to arise from sources within the United States for Japanese foreign tax credit purposes.

**Eversheds Sutherland Observation:** If, but for the resourcing provision, a payment to a Japanese person would be considered US source income, the income is treated as Japan source income under the resourcing provision, and foreign tax credits are available with respect to such
Income. However, the resourced income is treated as arising from a separate category of income (the treaty category), meaning that a separate foreign tax credit limitation applies to the resourced income.

The Japan Protocol also amends Article 23(b). Under the amended provision, dividends paid by a US company to a Japanese company are excluded from the basis upon which Japanese tax is imposed, so long as the Japanese company that received the dividend owned at least 10% of the shares of the US company paying the dividend for a period of six months before the date the obligation to pay the dividend arose.

**Teachers and Researchers (Article 20)**

The Japan Protocol deletes Article 20 in its entirety, which had previously allowed for individuals who were a resident of either country immediately before coming to the other country for the purpose of teaching or performing research at an educational institution to be exempt on the income from that teaching or researching for two years. Persons who currently enjoy this benefit will be “grandfathered” after the Japan Protocol goes into force for the period that they otherwise would be entitled, had the Japan Protocol not entered into force. The provision was deleted to bring the Japanese treaty into “conformity” with the current treaty policies of the United States and Japan.

**Eversheds Sutherland Observation:** This provision provided a benefit for US and Japanese academics, but was not limited to teachers in colleges and universities. Although the US treaty policy does not include a special teachers/researchers article because the Dependent Personal Services article would apply, similar provisions are included in many US treaties when the treaty partner requests such a provision. Since there is a grandfather provision, it may be advisable for taxpayers to claim this benefit before the Japan Protocol is entered into force.

**Effective Dates**

On August 30, 2019 the Japan Protocol entered into force. With respect to withholding taxes, the Japan Protocol is effective for amounts that are paid or credited on or after November 1, 2019. With respect to other taxes, the Japan Protocol is effective from January 1, 2020. Additionally, the information exchange and collection provisions are effective with respect to outstanding claims beginning on August 30, 2019.

**SPAIN**

The Protocol Amending the Convention between the United States of America and the Kingdom of Spain for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (Spain Protocol) was signed on January 14, 2013. For the full text of the protocol, please see the following link: [Spain Protocol](#).
The Spain Protocol makes various changes to the convention:

- Modifies withholding rates on certain dividends, royalties and interest;
- Updates the limitation on benefits and exchange of information provisions; and
- Implements mandatory arbitration procedures for certain cases.

These and other items are discussed more fully below.

**Dividends (Article 10), Interest (Article 11) and Royalties (Article 12)**

The Spain Protocol reduces withholding taxes on dividends to 0% and 15% depending on the applicable payee. The 15% rate applies in most cases. However, withholding taxes on dividends are reduced to 5% if the dividend's beneficial owner is a company that owns 10% (previously 25%) of the voting stock of the company paying the dividends. Moreover, if the dividend's beneficial owner is a company that owns at least 80% of the voting stock (directly or indirectly) of the company paying the dividends for at least 12 months and meets certain tests of Article 17’s Limitation on Benefits provision, a 0% rate applies. In addition, pension funds that are exempt from tax or subject to a 0% rate of tax are also eligible for 0% withholding on dividends to the extent that the applicable dividends are not derived from the carrying on of a trade or business by the pension fund or an associated enterprise.

**Eversheds Sutherland Observation:** The dividends article of the Spain Protocol is a substantial modernization and brings that provision in line with most of the European Union (EU) treaties. Before the Spain Protocol’s effective date of this provision, the convention reduces dividend withholding taxes to at least 10%, while the new provision under the Spain Protocol allows for 0% or 5% withholding to the extent that additional requirements are met.

Generally, under the Spain Protocol, most beneficial owners of interest of the United States or Spain are eligible for 0% withholding taxes. Previously, a 10% rate applied except in certain limited instances. The Spain Protocol retains only 10% withholding for “contingent” interest and excess inclusions with respect to residual interests from real estate mortgage investment conduits that are similarly carved out of 0% witholding under the 2006 US Model Treaty.

**Eversheds Sutherland Observation:** The new interest article of the Spain Protocol is also a substantial modernization and likewise brings that provision in line with most of the EU treaties. The 0% withholding tax rate was previously available only to the US or Spanish governments (and instruments guaranteed insured, or financed by governments), banks, or financing companies providing loans of five years or more and interest
paid in connection with the sale on credit of industrial, commercial or scientific equipment.

Like the new interest provisions, United States and Spanish beneficial owners of royalties are also generally eligible for 0% withholding under the Spain Protocol.

**Eversheds Sutherland Observation:** Again, the 0% rate for royalties is a significant modification and is consistent with the 2006 Model Treaty and most of the US income tax treaties with EU members. This change has particular benefits for media companies, most significantly for the licensees of sporting rights and broadcasts. Before the date the Spain Protocol is entered into force and the effective date of this provision, rates of 5%, 8% and 10% are applicable based upon the rights granted. A 5% rate is applicable for royalties received for copyrights of literacy, dramatic, musical or artistic works. The 8% rate is applicable for royalties paid with respect to cinematographic, films, tapes or other means of transmission of image or sound; royalties for the right to use industrial commercial or scientific equipment; and royalties for the copyright of scientific work. The 10% rate is applicable for all other cases.

**Limitation on Benefits Provision (Article 17)**

The Spain Protocol replaces the limitation of benefits article with provisions that generally align with the 2006 Model Treaty, but also includes several additional tests. The Spain Protocol adopts most of the “qualified persons” identified by the 2006 Model Treaty (i.e., individuals, government entities, publicly traded companies and certain of their subsidiaries, tax-exempt entities, companies that meet the ownership and base erosion tests, companies that meet the active trade or business test, and competent authority relief). However, the Spain Protocol also extends treaty benefits to entities that perform headquarter functions and companies that can satisfy a derivative benefits and base erosion test.

The more novel headquarters test, which is substantially similar to the test in the 2016 Model US tax treaty (the 2016 Model Treaty), allows for a company that is a resident of a contracting state to qualify for treaty benefits if it is the headquarters company of a multinational corporate group that supervises other members of the group. Supervisory activities are the material consideration, and ownership of the group is not required. In addition, such headquarters company and/or its group must also meet the following requirements and threshold: (1) provide substantial portion of the overall supervision of the group (which cannot be principally group financing); (2) the corporate group consists of corporations resident and actively engaged in a business in at least five countries (or five groupings of companies) that generate 10% of the gross income of the group; (3) business activities in any one country (other than the headquarters company’s residence state) is less than 50% of the group’s gross income; (4) no more than 25% of the headquarters company's gross income is derived from the other contracting state; (5) such headquarters company has and exercises
independent discretionary authority to carry out its supervisory and administrative functions; (6) the headquarters company must be subject to tax in its residency state like any other company engaged in an active trade or business (i.e., it cannot benefit from a special tax rate or artificially low tax base because it is a headquarters company); and (7) the income in the other contracting state is derived in connection with, or incidental to, the larger corporate group’s active trade or business described in (2) above.

As indicated above, a taxpayer that fails to qualify for full treaty benefits may still be entitled to treaty benefits for certain items of income under the active trade of business test. Moreover, competent authorities can also grant treaty benefits where other tests cannot be met.

The Spain Protocol also contains an anti-abuse rule for certain triangular structures. If an entity derives income from the non-resident country, and that income is attributable to a permanent establishment the entity has in a third state, the non-resident country may impose a withholding tax of up to 15% on payments. However, to impose the withholding tax, the combined tax actually paid on the income in resident country and the third state must be less than 60% of the general rate of company tax applicable in the resident country.

**Eversheds Sutherland Observation:** The Spain Protocol’s limitation on benefits provision is modernization of the prior article and is consistent with many of the US treaties with other EU countries. Nonetheless, there are several interesting features of the above tests:

- The publicly traded test allows in certain circumstances for a company to be traded on an established exchange in Toronto, Mexico City and Buenos Aires.
- Consistent with the 2006 Model Treaty but inconsistent with some other treaties with close trading partners (g., the United Kingdom), the ownership base erosion test requires that a resident of a contracting state be owned at least 50%, directly or indirectly, by residents of *that same* contracting state and that each applicable intermediate owner be that *same state*. By way of example, for a Spanish company claiming benefits for royalties paid by its US Subsidiary, that Spanish company would need to be owned at least 50% by Spanish individuals, the Spanish government (and its political subdivisions and instrumentalities), Spanish tax-exempt entities or Spanish publicly traded entities to meet the ownership prong of the ownership base erosion test. Any intermediate entities between such beneficial owners and the Spanish company would also need to be Spanish. The Spain Protocol includes a similar rule for intermediate entities with respect to the ownership prong of the derivative benefits test (i.e., each intermediate owner has to be an
EU or NAFTA entity).

- Also with respect to the derivative benefits test, the Spain Protocol takes into account 0% withholding on dividends, interest and royalties under the EU’s applicable directives regardless of whether the applicable income tax treaties between EU members have been updated to reflect a 0% withholding rate on such income.
- The addition of the headquarters provision is interesting as this provision was not in the 2006 Model Treaty and its inclusion hints at Spain’s efforts to be a holding company jurisdiction. As indicated above, it is substantially similar to a comparable provision in the 2016 Model Treaty and provides that treaty benefits are available for companies resident in the United States or Spain that administer or supervise a larger multinational group. With respect to the applicable numerical ratios found in the headquarters test and like the 2016 Model Treaty, the Spain Protocol makes clear that such ratios can be met by averaging the applicable gross income of the preceding four years.

**Exchange of Information (Article 27)**

The Spain Protocol also replaces the exchange of information article with one similar to the 2006 Model Treaty. Article 27 of the Spain Protocol requires disclosure of information that is “foreseeably relevant” for certain administrative or enforcement purposes. Before this amendment, the Article had required disclosure only of “necessary” information. The language is also consistent with the standard codified in § 7602 of the Internal Revenue Code. The exchange of information is not restricted by the taxes covered under the convention. The information exchange provisions also cover certain non-US or non-Spain residents to the extent there is a connection to jurisdiction (e.g., a bank account, permanent establishment).

**Mutual Agreement Procedure (Article 26)**

The Spain Protocol adds rules for arbitration when the competent authorities cannot reach a negotiated agreement. The arbitration panel’s determination for a case is binding on both the United States and Spain, unless the presenter of the case does not accept the determination. The panel is required to select one of the proposed resolutions provided by the competent authorities. The procedure is similar to the procedures outlined in the US income tax conventions with Belgium, Canada, France and Germany, as well as the Japan Protocol and the Switzerland Protocol.

**Eversheds Sutherland Observation:** The new mutual agreement procedure provisions are generally helpful to taxpayers. Oftentimes, taxpayers that submit disputes to competent authority are left in a state of limbo waiting for the competent authorities of the contracting states to
reach a resolution. Under the arbitration procedures, if the competent authorities are unable to reach a conclusion within two years or other such time period agreed upon by the competent authorities, the new mutual agreement procedure provisions require the competent authorities to allow taxpayers to submit such disputes to an arbitration panel that will then reach a resolution with respect to the taxpayer’s issue. Additionally, the arbitration procedures are binding on the contracting states only if the taxpayer accepts the decision of the arbitration panel. A taxpayer continues to have other avenues to resolve the dispute should the arbitration panel reach a result that is unfavorable to the taxpayer.

Because the arbitration panel’s decision must be one of the resolutions proposed by the contracting states, these changes put pressure on competent authorities to settle claims, as the panel has no ability to reach a decision that lies between those competing resolutions.

**Fiscally Transparent Entities (Article 3)**

The Spain Protocol adds a new provision on the treatment of an item of income derived through a fiscally transparent entity organized either in: (1) Spain or the United States; or (2) another country that has an agreement with the source state containing an exchange of information on tax matters provision when the item of income is derived by a resident of a Contracting State and is treated as the income item of that resident by that Contracting State. Consistent with many treaties, the US 2006 Model Income Tax Treaty and US income tax policy, a resident may claim treaty benefits for an item of income paid to a fiscally transparent entity only if either the United States or Spain treats the entity as fiscally transparent. The characterization by the third-party country is irrelevant for purposes of this provision. In addition, to be eligible for the benefits of the treaty, such resident must still satisfy the other requirements of the convention.

**Eversheds Sutherland Observation:** Before the addition of this provision, the regulations under § 894(c) of the Internal Revenue Code applied and potentially limited the availability of treaty benefits in the case of transactions with fiscally transparent entities. Those regulations can be a trap for the unwary, so the addition of this provision is positive for taxpayers. For this provision to apply, an entity must be treated as fiscally transparent under the laws of either the United States or Spain, even if the entity is not organized in either country. The characterization of an entity by a third country is irrelevant even if the entity is organized in that third country. Third-party residents may claim a benefit under a third-party treaty with either the United States or Spain if either the United States or Spain characterizes an entity as fiscally transparent.

**Effective Dates**

The Spain Protocol will enter into force on November 27, 2019.
Protocol withholding rates will apply to income paid or credited on or after November 27, 2019. The Spain Protocol will have effect with respect to taxes determined with reference to a taxable period beginning on or after November 27, 2019.

With respect to certain provisions of the Spain Protocol’s arbitration article, certain procedures are not effective for cases that are under consideration by the competent authorities as of November 27, 2019. For existing cases, certain provisions shall have effect only on the date on which the competent authorities agree in writing on their applicability. Similarly, the commencement date for cases that are under consideration by the competent authorities as of November 27, 2019, but before such provisions have effect, is the date on which the competent authorities have agreed in writing on their applicability.

If you have any questions about this legal alert, please feel free to contact any of the attorneys listed under ‘Related People/Contributors’ or the Eversheds Sutherland attorney with whom you regularly work.