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Object and Purpose in Tax Treaty Law - Importance and Limits
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1 Introduction

It is safe to say that laws are enacted with an aim, function, objective, purpose, goal or intention in mind. This is true for domestic laws, EU law and international law. This is also true for international tax law. We may think of the aim of avoiding international juridical double taxation or, more recently, the aim of preventing tax treaty abuse. We hear vague proclamations of ensuring that profits should be taxed where value is created. We are confronted with new rules that intend to achieve different purposes at the same time, such as the GloBE rules, which aim to comprehensively address the remaining BEPS challenges and, at the same time, harmful tax competition. Whenever we introduce, change, interpret or apply the law, the object and purpose is there. It is relevant, and will remain relevant, for all existing and future rules in international tax law.
Today’s lecture is about the object and purpose in tax treaty law. While the object and purpose has been a relevant means of interpretation under the Vienna Convention on the Law of Treaties for a long time, since the introduction of the principal purposes test rule or PPT rule it has arguably become more important in recent years. The PPT rule specifically refers to the object and purpose of the relevant provisions of a tax treaty. It may deny tax treaty benefits in cases where these benefits are not in accordance with that object and purpose.

I am going to begin with the role of the object and purpose under the Vienna Convention on the Law of Treaties to better understand the framework that is relevant for the interpretation and application of tax treaties.

- What is the meaning of the object and purpose?
- How can we determine the object and purpose?
- What is the relevance of the object and purpose?

Afterwards, I am going to discuss the object and purpose under the PPT rule. Has nothing changed compared to situations without the PPT rule? Has the object and purpose become more relevant in tax treaty law? Is the PPT rule able to go beyond the wording of a tax treaty? What are the limits of the wording that are relevant in this context?

Finally, I will end with some conclusions.
2 Vienna Convention

2.1 Schools of Interpretation

It is possible to distinguish between three different schools of treaty interpretation, which existed already prior to the conclusion of Vienna Convention on the Law of Treaties. We can call them the teleological school, the subjective school and the objective school. What is the purpose of treaty interpretation?

According to the teleological school, the aim is to determine the object and purpose of a treaty and to give effect to that object and purpose, even where the terms of the treaty fail to be as comprehensive as they should be.

According to the subjective school, the goal is to determine the intentions of the Contracting States and to give effect to those intentions, even where the States did not properly reflect their intentions in the text of the treaty.

According to the objective school, the text must be presumed to be the authentic expression of the intentions of the Contracting States. Thus, the primary goal of interpretation is to determine the meaning of the text of the treaty.

While the rules of the Vienna Convention on the Law of Treaties reflect a compromise between these three different schools, they require treaty interpretation to rely on the text of a treaty. This textual approach does not mean, however, that the object and purpose of a treaty is irrelevant. On the contrary, the general rule of interpretation in Article 31 paragraph 1 of the Vienna Convention on the Law of Treaties explicitly refers to the object and purpose: “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.”

There is no definition of “object and purpose” in the Vienna Convention on the Law of Treaties. Consequently, the meaning of the term “object and purpose” is far from clear. I will address four questions that may come up in this context:

1. First, how many objects and purposes may a treaty have, only one single overarching object and purpose or multiple objects and purposes?

2. Second, as the Vienna Convention refers to its, the treaty’s, object and purpose, what about the object and purpose of specific provisions?

3. Third, how can the object and purpose of a treaty or rule be determined?

4. And finally, how important is the object and purpose for interpretation?

2.2 How Many Objects and Purposes?

It is unclear whether a treaty may only have one single overarching object and purpose or multiple, even conflicting objects and purposes. This may be surprising. Why should a treaty not have multiple objects and purposes? This is less surprising when we look at other provisions of the Vienna Convention. According to Article 19 letter c) of the Vienna Convention, for instance, a State may formulate a reservation unless the reservation is incompatible with the object and purpose of the
treaty. If a treaty would have multiple objects and purposes, a reservation could be compatible with one object and purpose but incompatible with another object and purpose. This would mean that a treaty modification through a reservation could be both acceptable and unacceptable. This does not seem like a reasonable conclusion. A single object and purpose ensures that a reservation can be either acceptable or unacceptable based on its compatibility with that object and purpose, not both at the same time.

However, I believe that the term “object and purpose” may have different meanings in different contexts, so that the meaning for purposes of interpretation under Article 31 paragraph 1 of the Vienna Convention may differ from that in other provisions of the Vienna Convention. In addition, for purposes of interpretation, it does not appear important whether we group the different goals of a treaty into one single overarching object and purpose or accept multiple objects and purposes of a treaty. If the identified goals are helpful for the interpretation, their relevance for the interpretation should not depend on their status of being part of a single object and purpose or multiple objects and purposes.

2.3 Object and Purpose of Specific Provisions

Article 31 paragraph 1 of the Vienna Conventions refers to “its”, the treaty’s, object and purpose, not to the object and purpose of the specific treaty provisions. While this distinction is important – the PPT rule does the opposite and refers to the object and purpose of the specific treaty provisions, not to the object and purpose of the treaty as a whole – there is a
strong connection. The treaty achieves its object and purpose through the specific treaty provisions and the specific treaty provisions contribute to the achievement of the treaty’s general goals. Usually, therefore, the specific provisions incorporate and reflect the more general goals of the treaty. As I will discuss in a moment, the determination of the object and purpose of the treaty as a whole includes an analysis of the structure and scope of the specific provisions. Thus, the specific provisions influence the determination of the object and purpose of the treaty as a whole.

In addition, the object and purpose of specific provisions has to be derived from the available means of interpretation. It therefore automatically becomes part of the interpretation process based on those means of interpretation. It must be considered – together with the object and purpose of the treaty as a whole – when interpreting the specific treaty provisions.

2.4 Determination of the Object and Purpose

While Article 31 paragraph 1 of the Vienna Convention instructs to interpret a treaty in the light of its object and purpose, the Vienna Convention is silent about how the object and purpose of a treaty should be determined.

Initially, the title and the preamble may assist in determining the object and purpose of a treaty. However, the object and purpose of a treaty may be described in general or vague terms, thereby lacking the required clarity. In any case, an initial understanding of the treaty’s object and purpose should be confirmed or revised based on the text of the treaty as a whole, including its specific provisions as well as its structure.
and logic. Finally, it is possible to go beyond the treaty itself to take account of other circumstances, such as those surrounding a treaty’s creation, or other external and supplementary materials.

As each treaty is unique, there is no mechanical approach to identifying the object and purpose. All the available means of interpretation pursuant to Articles 31 and 32 of the Vienna Convention may prove to be helpful in determining the object and purpose of a treaty, or of its specific provisions.

To some extent, the determination of the object and purpose is a circular exercise. In order to interpret the terms of the treaty, it is necessary to take account of the object and purpose, but the object and purpose must also be derived from the terms of the treaty itself. This means that the object and purpose is both: (i) the result of interpretation of the treaty as a whole; and (ii) a means of interpretation to shed light on the ordinary meaning of the terms of the treaty in their context.

2.5 Importance of the Object and Purpose

Article 31 paragraph 1 of the Vienna Convention is also silent about when the object and purpose should be considered and how much weight it should have compared to other means of interpretation. Yet, the Vienna Convention envisions the process of interpretation as “a single combined operation”. All the various elements, as they are present in any given case, interact with each other to give the legally relevant interpretation. This implies that the means of interpretation do not have a predetermined hierarchy or weight, except for a certain distinction between primary and supplementary means of in-
terpretation. Since the process of interpretation is a holistic exercise, the Vienna Convention does not require giving the object and purpose of a treaty or its specific provisions more or less weight than other means of interpretation. Rather, the relevance and weight of each available means of interpretation, including the object and purpose, depends on the facts and circumstances of each particular case.

At the same time, the object and purpose finds its limits in the ordinary (or special) meaning of the terms of the treaty. The object and purpose, whether determined from the title, the preamble, the whole text, structure and logic of the treaty or from other means of interpretation, may shed more or less light on the ordinary meaning of the terms of the treaty in a particular case. It cannot create an independent reading that is not expressed with the words of the text. As the text of the treaty must be presumed to be the authentic expression of the States’ intentions, under the Vienna Convention, it is not possible to rely on an object and purpose that does not manifest itself in the terms of the treaty.

2.6 Objects and Purposes of a Tax Treaty

At this point, I could address in detail which objects and purposes a tax treaty may pursue and what relevance these objects and purposes may have. Today, however, I can only summarize some – by no means exhaustive – conclusions:

First, it is impossible to determine the objects and purposes of a tax treaty without analyzing the structure, logic and substance of specific provisions. If available at all, the title and the preamble are too vague to provide clear directions, such as
what kinds of double taxation are actually addressed by a tax treaty and its provisions. Clearly, the objects and purposes of a tax treaty must be derived by interpreting its substantive rules.

Second, the general desire to achieve a certain goal does not imply that a tax treaty must always achieve that goal. Following the textual approach of the Vienna Convention, interpretation is about determining the meaning of the terms of the treaty and not about giving greatest effect to some identified object and purpose. For instance, the objective of not creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance does not imply that such opportunities will never be created. Such opportunities may only be limited within the boundaries of the specific terms of a tax treaty, including its various anti-abuse provisions.

Third, while we have established models, every tax treaty is somewhat different, including the circumstances surrounding a treaty’s conclusion. Thus, the objects and purposes may differ. What may be true for a tax treaty following the newest version of the OECD or UN Model need not be true for an older tax treaty. For instance, tax avoidance has not been at the forefront of older models and some tax treaties may have even been designed to permit some forms of tax planning or treaty shopping.

Last, but not least, tax treaty provisions may pursue specific objects and purposes which usually advance the general goals of a tax treaty. For example, a certain allocation of taxing rights may pursue the objective of avoiding excessive administrative burdens for taxpayers and tax administrations. This
more specific purpose encourages cross-border exchange and helps developing the economic relationship of the States, contributing to the general goals of the tax treaty. Yet, objects and purposes may also conflict with each other, requiring difficult decisions about which object and purpose should prevail in a particular case. In case of conflicting objects and purposes, treaty benefits may be in accordance with one object and purpose but not in accordance with another object and purpose.

3 PPT Rule

3.1 Overview

It is impossible to discuss the role of the object and purpose in tax treaty law without discussing the PPT rule. This rule has been introduced as a result of BEPS Action 6 through the Multilateral Instrument and is now incorporated in the newest versions of the OECD Model and the UN Model. It consists of two tests:

1. The first test requires an assessment whether obtaining a tax treaty benefit was one of the principal purposes of any arrangement or transaction.

   2. The second test considers whether granting that benefit would be in accordance with the object and purpose of the relevant tax treaty rules.

If it is reasonable to conclude that a tax treaty benefit was one of the principal purposes of an arrangement or transaction, the tax treaty benefit is denied, unless it is established that
granting that benefit would be in accordance with the object and purpose of the relevant tax treaty provisions.

### 3.2 Different Approaches

The PPT rule raises many issues, most of which I cannot address today. However, one important question connected to the specific role of the object and purpose under the PPT rule is the question of the role of the PPT rule as such.

On the one hand, the PPT rule can be understood as relying on the object and purpose of the relevant tax treaty provisions even beyond their wording. We can call this the “beyond the wording approach”.

Where the taxpayer has no principal tax motive, he or she can trust the wording of the provisions. In contrast, where the taxpayer pursues a principal tax motive, he or she cannot be sure that the treaty benefits will be granted. Instead, the benefits are denied if they violate the object and purpose of the relevant tax treaty provisions. This means that the object and purpose may take precedence over the wording. The PPT rule arguably leads to a result that would not be possible by merely interpreting the relevant tax treaty provisions in accordance with the Vienna Convention.

On the other hand, the PPT rule can be seen as a mere reminder that the object and purpose is a relevant means of interpretation under the Vienna Convention. Thus, it should be considered when interpreting and applying a tax treaty. We can call this the “signaling function approach”.

Under the Vienna Convention, the interpretation does not end
with a literal reading of the relevant treaty provisions. Instead, it is necessary to consider the context, the object and purpose and other relevant means of interpretation. This is true regardless of whether the tax treaty includes the PPT rule. As a consequence, the PPT rule merely signals the importance of the object and purpose. If the tax treaty benefits are not in accordance with the object and purpose of the relevant tax treaty provisions, they may be denied with and without the PPT rule.

While this approach limits the practical relevance of the PPT rule and raises the question “why did the Contracting States decide to include an unnecessary rule?”, the OECD Commentary itself believes that very similar results as those under the PPT rule may be reached without it under a “guiding principle” of tax treaty interpretation.

The different approaches raise two important questions:

1. First, what are the limits of the wording? Do we really need to cross these limits to respect the object and purpose of the relevant rules?

2. Second, how can the object and purpose of a relevant tax treaty provision conflict with the same wording from which it was derived?

3.3 Limits of the Wording

Let me start with the first question, the limits of the wording:

Based on a mere literal reading of the terms, the wording may initially seem clear and become quite quickly a limit that may
be difficult to bring in line with the object and purpose of the relevant tax treaty provisions. However, Article 31 paragraph 1 of the Vienna Convention refers to the ordinary meaning of the terms in their context and in the light of the object and purpose. This means that even though the text is the authentic expression of the States’ intentions, the ordinary meaning expressing those intentions includes meanings that may become apparent only after taking the object and purpose of the treaty, or of the relevant provisions, into account. An initially clear meaning of the terms may become less clear if the investigation of the object and purpose reveals an incompatibility and new potential ordinary meanings. In many situations, therefore, the potential ordinary meanings of the terms provide enough flexibility to consider the object and purpose beyond a strict reading of the same terms.

For example, the second sentence of Article 4 paragraph 1 of the OECD Model states that the term “resident of a Contracting State” “does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.”

At first, the literal meaning of these terms provides for a clear outcome. If a person is liable only to source or territorial taxation, he or she is not a tax treaty resident. When looking at the literal meaning of the terms, the provision does not distinguish between, on the one hand, States that tax residents on a worldwide basis and non-residents on a territorial basis, and, on the other hand, States that tax all persons on a territorial basis. The second sentence of Article 4 paragraph 1 would indiscriminately deny treaty residence in all cases of territorial
taxation. This would be the case even if a State adopts a territorial principle, taxing both residents and non-residents in respect only of income from sources in that State.

Pursuant to the OECD Commentary, however, it is not necessary to adhere to this strict understanding of the treaty terms. The second sentence of Article 4 paragraph 1 “has to be interpreted in the light of its object and purpose, which is to exclude persons who are not subjected to comprehensive taxation […] in a State”, not to exclude all residents of jurisdictions adopting a territorial principle in their taxation. This interpretation advocated by the OECD Commentary goes beyond a strict reading of the text and puts great emphasis on the object and purpose while remaining within the broad limits set by the ordinary meaning of the terms.

Before assuming a mismatch between the wording and the object and purpose of a tax treaty provision, we should therefore ask ourselves: Is it really not possible to interpret the terms of the tax treaty in accordance with the identified object and purpose?

3.4 Conflict with the Wording

Let me now turn to the second question, how can the object and purpose of a relevant rule conflict with the same wording from which it was derived?

As already discussed, the object and purpose does not appear out of thin air. It must be derived from the text of the treaty, including the treaty’s substantive provisions, and from other available means of interpretation. Under the Vienna Conven-
tion, the object and purpose must further be reflected in the terms of the treaty from which it is derived. There is no “independent” object and purpose that can be given effect regardless of the text of the treaty. By going beyond the ordinary meaning of the terms in their context and in the light of the object and purpose, the PPT rule would arguably require establishing the object and purpose of the relevant tax treaty provisions from the text of the treaty and other available means of interpretation to go beyond the result of interpretation derived from exactly the same text and the same means of interpretation. This approach would therefore deviate from the established principles of interpretation under the rules of the Vienna Convention.

Is it theoretically possible that the Contracting States, through the PPT rule, intended to deviate from the general rule of interpretation in Article 31 of the Vienna Convention? Yes, the Contracting States are free to deviate from the principles of the Vienna Convention. Nevertheless, I have doubts whether the available means of interpretation, including the OECD Commentary, are sufficient to conclude that the Contracting States intended to disregard the established principles of interpretation in favour of potentially unpredictable consequences.

The danger of the beyond the wording approach is that the PPT rule would potentially introduce an element of interpretation that could rely on what the Contracting States should have agreed to, not what they have actually agreed to. Thus, the object and purpose could become an “independent” means of interpretation that could prevail over the authentic expression of the States’ intentions. It could override what the Con-
Contracting States have objectively intended to achieve with what the Contracting States should have intended to achieve.

Before assuming a mismatch between the wording and the object and purpose of a tax treaty provision, we should therefore ask ourselves: Is the identified object and purpose really pursued without any limitations or should its identified scope rather be revised?

If the identified object and purpose is not reflected in the text of the treaty, the Contracting States may not have agreed to pursue it, or not to the full extent.

### 3.5 Example of the 183-Day Rule

While most examples on the PPT rule relate to business profits or passive income, the scope of the rule goes beyond that. Let me therefore illustrate the difficulties of the “beyond the wording” approach with an example on the 183-day rule. Imagine that an employee is present and works in a State for 360 days. A presence of 360 days in the fiscal year concerned is not a short-term employment for purposes of the 183-day rule and, thus, the rule does not apply.

Imagine now that the employee intentionally decides to work from July to December of one year for 180 days and from January to June of the following year for another 180 days, reaching 360 days of continuous presence. Under the pre-1992 wording of the 183-day rule still used in some tax treaties today, “the fiscal year concerned” constitutes the relevant period for calculating the days of presence. A presence of 180 days in the fiscal year concerned can generally benefit from the 183-
day rule. Now, by changing the work period, the 183-day rule applies and our employee may benefit from no taxation in the State of work and a potentially lower taxation in the State of residence.

Is this conduct in accordance with the object and purpose of the 183-day rule under the pre-1992 wording to cover only short-term employments or should the PPT rule deny treaty benefits by following the “beyond the wording approach”? Let me mention some arguments that can be found in the OECD Commentary and in the literature in similar contexts: Arguably, granting the benefit of the 183-day rule in these circumstances would be contrary to the object and purpose of the rule as the time limitation of 183 days would otherwise be meaningless if employees could avoid taxation in the State of work by merely changing their work period. A confirmation that the object and purpose of the 183-day rule would be defeated also flows from the fact that the newer versions of the OECD Model include a different wording to deal with this problem. Thus, the PPT rule could deny the benefit of no taxation in the State of work by going beyond the wording of the 183-day rule.

For me it seems more reasonable to bring the different means of interpretation closer together. If the interpretation of the 183-day rule is incompatible with the identified object and purpose, it may well be wrong. If it is not wrong and the wording is indeed a limit to an interpretation in accordance with the identified object and purpose, then the object and purpose should be reconsidered.

Through the explicit wording of the 183-day rule, the Con-
tracting States may have accepted some forms of tax planning in favour of a simplified application of the rule. In addition, the threshold can be seen as an arbitrary threshold. If the taxpayer meets this arbitrary formal requirement of the 183-day rule, this should be in accordance with its object and purpose.

In the case of the 183-day rule, the precise wording should inform about the object and purpose rather than leading to the assumption that the identified object and purpose cannot be brought in line with the same wording from which it was derived. To put it differently, the PPT rule should not go beyond the wording of the 183-day rule to implement what the Contracting States should have agreed to – arguably, the new wording of the 183-day rule – instead of what they have actually agreed to – the old pre-1992 wording.

3.6 Priority Approach

Yet, even if we abandon the “beyond the wording” approach, the PPT rule is, in my view, more than just a reminder of the fact that the object and purpose is a relevant means of interpretation under the Vienna Convention. Interpretation under the Vienna Convention is not only about the wording and the object and purpose. Various other means of interpretation, including supplementary means of interpretation, influence the interpretation of tax treaty provisions.

Interpretation is a complex legal exercise, where some means of interpretation may point in one direction, and other means of interpretation may point in a different direction. While the object and purpose plays a role in shedding light on the ordinary meaning of the terms of a tax treaty, it has no predetermined
relevance or weight. Under a holistic approach, therefore, the result of interpretation need not fully align with the identified object and purpose of the relevant rules. Before reaching this conclusion, one should of course reconsider the interpretation and the identified object and purpose. Nevertheless, as long as the result of interpretation stays within the limits of the wording, one may conclude that based on certain means of interpretation, an interpretation that does not fully align with the object and purpose is still more convincing than one that would fully align. In fact, if we encounter multiple conflicting objects and purposes, the result of interpretation by definition cannot fully align with all objects and purposes at the same time; a conflict with an object and purpose will remain.

What is the meaning of the term “beneficial owner”, for example? The term “beneficial owner” does not seem to have a clear ordinary meaning that would impose relevant limits to achieving the object and purpose of the relevant tax treaty provisions, including the object and purpose of not creating opportunities for non-taxation or reduced taxation through treaty-shopping arrangements. In addition, according to the OECD Commentary, the interpretation of the term “beneficial owner” is influenced by the object and purpose of the tax treaty, including the purpose of preventing fiscal evasion and avoidance.

Nevertheless, the OECD Commentary believes that the PPT rule may be necessary to deny tax treaty benefits that would otherwise be granted to the beneficial owner because those benefits would not be in accordance with the object and purpose of the relevant tax treaty provisions. Why do we need the PPT rule to reach this apparently intended result instead of
interpreting the term “beneficial owner” in accordance with the identified object and purpose?

Instead of applying the PPT rule, the condition of beneficial ownership could easily be understood in accordance with the object and purpose of not granting treaty benefits in various treaty-shopping situations. Despite that, other means of interpretation, notably, the historical development of the concept and the explanations in the OECD Commentary, speak in favour of a more narrow understanding of the term “beneficial owner” by covering only agents, nominees, and similar persons who have a contractual or legal obligation to pass on the payment received to another person. The limits that the PPT rule needs to cross do not lie in the wording or in the term “beneficial owner”. The limits come from other means of interpretation. The PPT rule is needed to go beyond the traditional (narrow) understanding of the term “beneficial owner” derived from those other means of interpretation. It shifts priority to the object and purpose.

In my view, the PPT rule should always remain within the limits of the wording of the relevant tax treaty provisions while being more than just a reminder to consider the object and purpose in accordance with the general rule of interpretation. This approach would continue to follow the well-established rules and limits of interpretation pursuant to the Vienna Convention. If the Contracting States were not able to reflect their intentions in the wording of the relevant tax treaty provisions, they have not agreed to pursue those intentions through those provisions. At the same time, where the relevant tax treaty provisions can be interpreted fully in line with the object and
purpose as established by relevant means of interpretation, the PPT rule would require giving priority to this object and purpose even if other relevant means for interpretation speak for a different result. In such situations, the PPT rule could therefore disregard a traditional understanding and interpretation in favour of an interpretation that fully aligns with the identified object and purpose. It would require giving priority to the object and purpose over other relevant means of interpretation while remaining within the objective limits set by the terms of a tax treaty.

4 Conclusions

Whereas the concept of object and purpose “might bring clarity and insight, it might equally generate only conflict and irresolution.” To me, this quotation about the object and purpose from Prof. Dino Kritsiotis is quite accurate for the area of tax treaty law, where we encounter vague statements about general goals and many different, sometimes even conflicting, objects and purposes.

By elevating the object and purpose of specific treaty provisions to the forefront, in particular if a taxpayer intends to receive a tax treaty benefit, the question of “what is the object and purpose?” becomes even more pressing. While this is a topic for another day, this question about the object and purpose is a legal question that has to be interpreted, argued, contested and, in the end, decided by courts. It is not an issue of the burden of proof lying with the taxpayer. In my view, we should not leave the established principles of interpretation pursuant to the rules of the Vienna Convention on the Law
of Treaties by going beyond, or even ignoring, the wording of the relevant tax treaty provisions. The PPT rule should shift priority to the object and purpose but within the limits set by the wording – and those limits are often broader than initially appears.

Where the object and purpose remains in the dark, it is not able to shed light on the ordinary meaning of the terms of a tax treaty. Thus, where the object and purpose remains in the dark, the application of the PPT rule must fail. The PPT rule should not deny treaty benefits due to a lack of legal clarity about the object and purpose. It is therefore more important than ever to enlighten the object and purpose of tax treaty provisions, and I am at the beginning rather than at the end of my journey into the many complexities of the object and purpose.