

**National Interest Analysis [2010] ATNIA 31**

**with attachment on consultation**

**Convention between  
the Government of Australia and the Government of the Republic of Turkey  
for the Avoidance of Double Taxation with Respect to Taxes on Income and  
the Prevention of Fiscal Evasion, and Protocol,  
done at Ankara on 28 April 2010**

**[2010] ATNIF 28**

**Regulation Impact Statement**



## NATIONAL INTEREST ANALYSIS: CATEGORY 2 TREATY

### SUMMARY PAGE

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#### **Nature and timing of proposed treaty action**

1. The proposed treaty action is to bring into force the *Convention between the Government of Australia and the Government of the Republic of Turkey for the Avoidance of Double Taxation with Respect to Taxes on Income and the Prevention of Fiscal Evasion, and Protocol* (the proposed Convention).
2. The proposed Convention was signed on 28 April 2010. The proposed Convention will enter into force, pursuant to Article 28, on the date of the last notification through the diplomatic channel between the Contracting States confirming that each State has completed their domestic requirements to bring the proposed Convention into force.
3. The provisions of the proposed Convention will take effect in Australia in three stages, namely:
  - a) In respect of withholding tax, on income derived on or after 1 January in the calendar year following entry into force;
  - b) In respect of other tax, on income, profits or gains of any year of income beginning on or after 1 July following entry into force; and
  - c) In respect of administrative provisions, on the date of entry into force.

#### **Overview and national interest summary**

4. The key objectives of the proposed Convention are to:
  - a) Promote closer economic cooperation between Australia and Turkey by reducing taxation barriers caused by the double taxation of income derived by residents of either Contracting State; and
  - b) Improve the integrity of the tax system by providing a framework through which the tax administrations of Australia and Turkey can prevent international fiscal evasion.
5. The proposed Convention also aims to improve certainty for Australian businesses looking to expand into Turkey and for other Australian taxpayers by establishing an internationally accepted framework for the taxation of cross-border transactions which is based upon the OECD *Model Tax Convention on Income and on Capital*.

6. In this manner the proposed Convention is expected to promote trade and investment between Australia and Turkey and enhance the taxation arrangements for Australians engaged in cross-border transactions, thereby improving the well-being of the Australian people.

## **Reasons for Australia to take the proposed treaty action**

### *Reducing barriers to bilateral investment and trade*

7. The proposed Convention is expected to reduce barriers to bilateral trade and investment, primarily by reducing withholding taxes on dividend, interest and royalty payments between the two countries. Rather than taking unilateral action to reduce withholding taxes under domestic law, Australia has adopted the approach of agreeing to any such reductions on a bilateral basis. This approach 'locks in' the withholding tax limits in both countries, ensuring a steady financial framework for business between the proposed Convention partner countries.

8. In particular, the proposed Convention reduces the Australian dividend withholding tax rate limit from 30 per cent to 5 per cent on inter-corporate dividends where the recipient directly holds at least 10 per cent of the voting power of the Australian company paying the dividend and reduces Turkish dividend withholding tax from 15 per cent to 5 per cent for intercorporate dividends in respect of direct holdings of at least 25 per cent of capital, where the dividends have been paid out of profits that have been subjected to the full rate of corporation tax in Turkey. A general rate of 15 per cent is to apply in all other cases (Article 10). This will promote direct investment into Australia by reducing tax impediments and thus make Australia a more attractive location for investment by Turkish multinationals. It will also assist in ensuring the competitiveness of Australian investment in Turkey by reducing Turkish withholding tax on dividends received by Australian companies from subsidiaries in Turkey.

9. The proposed Convention reduces interest withholding tax from 15 per cent to 10 per cent on Turkish sourced interest paid to Australian lenders (Article 11). The proposed Convention also exempts interest derived from the investment of official reserve assets by a government, its central bank or a bank performing central banking functions.

10. The proposed Convention reduces Australian royalty withholding tax from 30 per cent to 10 per cent and Turkish royalty withholding tax from 20 per cent to 10 per cent (Article 12). Reduced Turkish withholding taxes on royalty payments are likely to encourage Turkish businesses to source intellectual property from Australia. While the Australian company remains legally liable for tax on royalty income earned in Turkey, contracts will often include provisions (known as 'gross up clauses') requiring the Turkish company to absorb this tax. Consequently, lower withholding taxes on royalties are expected to reduce the costs for Turkish businesses of accessing Australian intellectual property. Likewise the lower royalty withholding tax rate is expected to reduce the costs for Australian businesses of accessing Turkish intellectual property.

11. The proposed Convention also provides an agreed basis for determining the allocation of profits within a multinational company and whether the profits on related Party dealings by members of a multinational group operating in both countries reflect the pricing that would be adopted by independent Parties (Articles 7 and 9). Tax treaties are therefore an important tool in dealing with international profit shifting through transfer pricing.

12. More generally, the proposed Convention will provide important benefits to Australians looking to expand their business activities into Turkey. It will establish an internationally accepted framework for the taxation of cross-border transactions, thus reducing investor risk and providing some degree of legal and fiscal certainty - unlike domestic laws which can be amended unilaterally. It

also includes rules to prevent tax discrimination against nationals of either Contracting State (Article 24).

#### *Establishing a framework to prevent international fiscal evasion*

13. The proposed Convention establishes a framework to prevent international fiscal (tax) evasion through the inclusion of rules to allow the tax administrations to exchange taxpayer information (Article 26). These rules meet the internationally agreed tax standard for exchange of information which was developed by the OECD. This standard has been endorsed by the G20 and the United Nations Committee of Experts on International Cooperation in Tax Matters. This framework will support global action on improving information exchange and transparency.

#### *Compliance and administrative cost reduction benefits*

14. The proposed Convention does not impose any greater compliance obligations on the residents of Australia than Australian domestic tax laws would otherwise and in some cases reduces the obligations of Australians operating or investing in Turkey (for example Article 7 concerning business profits). Given this and the fact that the proposed Convention is broadly consistent with international norms, it is expected to reduce compliance costs for those taxpayers with cross-border dealings between the Contracting States.

### **Obligations**

15. Articles 6 to 21 allocate taxing rights in respect of certain types of income between the two countries. To reduce or eliminate double taxation, Australia and Turkey have agreed in certain situations to limit taxing rights over various types of income dealt with under these Articles. For example Articles 10 to 12 impose limits on the rate of tax which may be imposed by the country of source (ie, the country where the payment arises) on dividends, interest or royalties. In the case of pension income, the proposed Convention provides that most pension and retirement annuities and lump sums paid after the age of 60 in lieu of a right to receive a pension, are to be taxed only in the country of residence of the recipient (Article 18). In respect of other lump sum payments, taxing rights are shared between the country of residence and the country of source (Article 18). The proposed Convention also provides an agreed basis for determining the allocation of profits within a multinational company and whether the profits on related Party dealings by members of a multinational group operating in both countries reflect the pricing that would be adopted by independent Parties (Article 9).

16. Article 23 of the proposed Convention sets out a general obligation for both countries to relieve double taxation on cross-border income by permitting tax paid under the other country's laws and in accordance with the proposed Convention, to be allowed as a credit against tax payable in respect of that income under their own laws.

17. Article 24 contains a general non-discrimination principle, requiring each country to treat nationals of the other country no less favourably than it treats its own nationals regarding taxation and any connected requirements. There are general exceptions to this principle to ensure that certain provisions of the laws of Australia and Turkey continue to operate for their intended purpose. The laws that are specifically exempt are those designed to prevent the avoidance or evasion of taxes or that deny certain tax deferrals and those that provide for the consolidation of group entities or aid

research or development. However, if necessary the Contracting States may also agree (by an exchange of notes), that other laws are to be exempt from the operation of Article 24.

18. Article 25 establishes procedures for dispute resolution, including a mechanism for taxpayers to present complaints to their country of residence, irrespective of the remedies provided by the domestic laws of those States, where they consider that they have been taxed not in accordance with the proposed Convention. The country receiving a complaint that appears to be justified must endeavour to resolve it, either unilaterally or by mutual agreement with the other country. Difficulties or doubts regarding interpretation or application of the proposed Convention shall be resolved by mutual agreement between the Contracting States. A dispute between the Contracting States which may also involve the application of the General Agreement on Trade in Services may be brought before the Council for Trade in Services by consent of both States.

19. Article 26 provides obligations for the exchange of information between both countries, including a specific obligation to gather and provide information upon request. Article 26(2) imposes an obligation on the country receiving any such information to treat it as secret in the same manner as information obtained under its domestic laws. Article 26(3) allows either country to decline to supply information in certain circumstances. Specifically, a request may be denied where: (i) it would require implementation of administrative measures at variance with either Contracting State's domestic law or administrative practice; (ii) the information requested is not obtainable under the laws or in the normal course of administration of either Contracting State; or (iii) it would involve disclosure of a trade, business, industrial, commercial or professional secret or information which would be contrary to public policy (for example, if it would breach human rights obligations). These circumstances, which act as a safeguard to protect Australia's interests and taxpayer's rights, accord with the OECD Model Tax Convention on Income and on Capital.

## **Implementation**

20. Amendments to the *International Tax Agreements Act 1953* will be made prior to the proposed Convention entering into force, to give the proposed Convention the force of law in Australia. No action is required by the States or Territories. There will be no change to the existing roles of the Commonwealth, or the States and Territories, in tax matters as a consequence of implementing the proposed Convention.

## **Costs**

21. Treasury has estimated the impact of the first round effects on forward estimates is unquantifiable but expected to be small (less than \$5 million per annum).

22. No other material costs have been identified as likely to arise from the implementation of the proposed Convention. In contrast, the establishment of a treaty between Australia and Turkey which is broadly consistent with international norms would generally be expected to reduce compliance costs for taxpayers.

23. There would be a small, unquantifiable cost in administering the changes made by the proposed Convention, including minor implementation costs to the Australian Taxation Office (ATO) in educating the taxpaying public and ATO staff concerning the new arrangements. There are also 'maintenance' costs to the ATO and the Department of the Treasury in terms of dealing with inquiries,

rulings and other interpretative decisions and mutual agreement procedures (including advance pricing arrangements). However, these costs will continue to be managed within existing agency resources.

### **Regulation Impact Statement**

24. A Regulation Impact Statement is attached.

### **Future treaty action**

25. The proposed Convention does not provide for the negotiation of future legally binding instruments, although it does require both countries to consult with each other regarding changes to the relevant laws (otherwise than in minor respects), relating to the taxation of income from insurance with non-resident insurers or of dividends, with a view to agreeing to any amendment that may be required to the relevant treaty provisions as a result.

26. The proposed Convention does not contain specific amendment procedures, however it may be amended from time to time by agreement of both countries (Article 39 of the *Vienna Convention on the Law of Treaties*). Any such amendment would be subject to Australia's domestic treaty-making process, including tabling and consideration by the Joint Standing Committee on Treaties.

### **Withdrawal or denunciation**

27. The proposed Convention remains in force indefinitely, unless terminated by one of the Contracting Parties. Either Contracting Party can terminate the proposed Convention by providing written notice of termination through the diplomatic channel at least six months prior to the end of any calendar year beginning after the expiration of five years from the date of its entry into force (Article 29). Termination by Australia would be subject to Australia's domestic treaty-making process. The proposed Convention would then cease to be effective, in the case of Australia, on 1 January in the calendar year next following the date on which the notice of termination notice is given (in respect of withholding tax on income derived by a non-resident), or on 1 July in the calendar year next following the date on which the notice of termination is given (in respect of other Australian tax).

### **Contact details**

Tax Treaties Unit  
International Tax & Treaties Division  
Department of the Treasury.

## ATTACHMENT ON CONSULTATION

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### CONSULTATION

28. Treasury sought comments from the business community through the Tax Treaties Advisory Panel, members of which include:

- Australian Bankers' Association
- Australian Chamber of Commerce and Industry
- Australian Financial Markets Association.
- Business Council of Australia
- CPA Australia
- Corporate Tax Association
- Institute of Chartered Accountants in Australia
- International Fiscal Association
- Investment and Financial Services Association
- Law Council of Australia
- Minerals Council of Australia
- Taxation Institute of Australia
- Property Council of Australia

29. The State and Territory Governments have been consulted through the Commonwealth-State Standing Committee on Treaties.