UNITED STATES TREASURY DEPARTMENT TECHNICAL EXPLANATION OF THE CONVENTION BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF AUSTRALIA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME

GENERAL EFFECTIVE DATE UNDER ARTICLE 28: 1 DECEMBER 1983

This Convention, signed at Sydney, Australia on August 6, 1982, was negotiated on the basis of the U.S. Model Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, published in May 1977, the revised U.S. Model published in draft form in June 1981 (also referred to as the "U.S. Model"), and the Model Double Taxation Convention on Income and Capital published by the Organization for Economic Cooperation and Development (OECD) in January 1977.

The technical explanation is an official guide to the Convention. It reflects policies behind particular Convention provisions, as well as understandings reached with respect to the interpretation and application of the Convention.

TABLE OF ARTICLES

ARTICLE 1
Personal Scope

This Article identifies the persons who come within the scope of the Convention (also referred to as “the Treaty”) and establishes the relationship between it and domestic law.

Paragraph 1 states that, except where the Convention specifically provides otherwise, the Convention applies to residents of the United States and/or Australia. Certain provisions of the Convention may apply to residents of third counties, for example, paragraph 5 of Article 10 (Dividends), paragraph 6 of Article 11 (Interest), and Article 25 (Exchange of Information). The term “resident” is defined in Article 4 (Residence).

Paragraph 2 provides that the Convention may not increase tax above the liability that would result under domestic law or under other agreements between the Contracting States. If domestic law provides a more favorable treatment than the Convention, the taxpayer may apply the provisions of domestic law. For example, if certain interest income derived by nonresidents is exempt from tax by statute, but the Treaty authorizes a tax at source of not more than 10 percent, the statutory exemption will apply. A taxpayer, however, may not make inconsistent choices between the rules of the Internal Revenue Code and the Convention rules.

Paragraph 3 contains the traditional "saving clause" under which each Contracting State reserved the right to tax its residents, as defined in Article 4 (Residence), as if the Convention had not come into effect. The two States also reserve the right so to tax their citizens, individuals electing under their respective domestic laws to be taxed as residents, and in the case of the United States, former citizens whose loss of citizenship had as one of its principal purposes the avoidance of tax. Such former citizens are taxable in accordance with section 877 of the Internal Revenue Code for 10 years following the loss of citizenship.

Paragraph 4 sets forth certain exceptions to the application of the saving clause where other provisions of the Convention present overriding policies. The saving clause does not override the benefits provided under paragraph 2 of Article 9 (Associated Enterprises), relating to correlative adjustments of tax liability, or the benefits of paragraphs 2 or 6 of Article 18 (Pensions, Annuities, Alimony and Child Support), relating to social security payments, alimony and child support. Social security payments and similar public pensions paid by Australia and alimony, child support and similar maintenance payments arising in Australia are taxable only by Australia even though the recipient may be a resident of the United States; similarly, social security payments by Australia to a citizen of the United States, wherever resident, are taxable only in Australia. The benefits provided in Articles 22 (Relief from Double Taxation), 23 (Non-

Discrimination), and 24 (Mutual Agreement Procedure), and the source rules of paragraph 1 of Article 27 (Miscellaneous) are also available to residents and citizens of the Contracting States, notwithstanding the saving clause.

In some cases, the saving clause overrides benefits otherwise conferred by the United States on citizens or persons having immigrant status in the United States and benefits otherwise conferred by Australia on citizens or persons ordinarily resident in Australia, but does not override those benefits when conferred on other residents of the respective States. This second category of exceptions to the saving clause concerns the benefits provided under Article 19 (Governmental Remuneration), 20 (Students) and 26 (Diplomatic and Consular Privileges). The term “immigrant status” means a person admitted to the United States as a permanent resident under U.S. immigration laws (i.e., holding a "green card").

ARTICLE 2
Taxes Covered

Paragraph 1 enumerates the existing taxes to which the Convention applies in each Contracting State.

In the United States these are the Federal income taxes imposed by the Internal Revenue Code, but excluding the accumulated earnings tax and the personal holding company tax. Social security taxes and excise taxes, such as those on private foundations and foreign insurers, are not covered by the Convention.

In Australia the Convention covers the income tax, including the additional tax on undistributed income of private (closely held) companies.

Paragraph 2 provides that taxes enacted after the date of signature of the Convention (August 6, 1982) are also covered if they are substantially similar to the taxes referred to in paragraph 1. The competent authorities agree to notify each other at the end of each calendar year of substantial changes in their income tax laws or in the official interpretation of those laws or of the Convention.

ARTICLE 3
General Definitions

Paragraph 1 defines some of the principal terms used throughout the Convention. Unless the context otherwise requires, the terms defined in this paragraph have a uniform meaning throughout. A number of other important terms are defined in other Treaty articles. For example, the term "resident" is defined in Article 4 (Residence), the term "permanent establishment" is defined in Article 5 (Permanent Establishment), and the term "royalties" is defined in Article 12 (Royalties).

The definitions of the terms "person", "company", "enterprise of a Contracting State", and "international traffic" are similar to the definitions in the U.S. Model.

The "competent authority" for the United States is the Secretary of the Treasury or his delegate, and for Australia the Commissioner of Taxation or his authorized representative.

The definitions of a United States corporation and an Australian corporation, respectively, exclude corporations which under the laws of the Contracting States are residents of both States. A corporation created and organized under the laws of a state of the United States is considered by the United States to be a United States corporation. Such a corporation could also be considered by Australia to be an Australian corporation if it is managed and controlled in Australia or if it does business there and its voting power is controlled by Australian resident shareholders. Typically, a corporation can avoid being a dual resident. If such a situation does arise, the dual resident corporation is not considered a resident of either country for purposes of the Treaty and is therefore not entitled to benefits granted by either State under the Treaty to residents of the other State.

The terms "United States" and "Australia" are defined to include the continental shelf areas of the two countries with respect to exploration and exploitation of their natural resources. For the United States, the definition of the continental shelf is interpreted in accordance with section 638 of the Internal Revenue Code and the regulations thereunder. The term "United States" does not include Puerto Rico, the Virgin Islands, Guam, or any other United States possession. The term "Australia" does include the Territories of Norfolk Island, Christmas Island, the Cocos Islands, Ashmore and Cartier Islands and the Coral Sea Islands; however, see also the discussion of paragraph 1(a)(iii) of Article 4 (Residence).

Definitions are provided for the terms "Contracting State," "State," "United States tax," "Australian tax," and “resident of one of the Contracting States." The covered taxes do not include penalty or interest charges. For example, the ceiling rate of tax at source of 15 percent on dividends under Article 10 (Dividends) does not include any penalty or interest charge for late payment of tax.

Paragraph 2 provides that terms not defined in the Convention shall have the meaning which they have under the laws of the Contracting State concerning the taxes to which the Convention applies, unless the context of the Convention requires a different interpretation. Under the terms of Article 24 (Mutual Agreement Procedure), the competent authorities may agree on a common definition of an otherwise undefined term. The term "context" includes the purpose and background of the provision in which the term appears. An agreement by the competent authorities with respect to the meaning of a term used in the Convention would supersede conflicting meanings in the domestic laws of the Contracting States.

ARTICLE 4
Residence

This Article sets forth rules for determining the residence of individuals, corporations, and other persons for purposes of the Convention. A definition of residence is important because, for the most part, only residents of the Contracting States may claim benefits under the Convention. The Convention definition is of course, exclusively for purposes of the Convention.

Paragraph 1 of this Article describes those persons who, for purposes of the Convention, are residents of Australia or the United States.

Subparagraph (a) provides that a resident of Australia means an Australian corporation and any other person (except a company that is not an Australian corporation) that is resident in Australia for purposes of its tax. However, if such a person is subject to Australian tax on income from Australian sources (but not on income from U.S. sources or other sources outside Australia), that person is not a resident of Australia for purposes of this Convention except to the extent that the income is subject to tax in Australia as the income of a resident or is exempt from Australian tax solely because it is subject to U.S. tax. This provision excludes residents of certain territories included within the definition of Australia in paragraph 1(k) of Article 3 (General Definitions) from claiming any Treaty reductions in United States tax on United States source income under the Treaty; although subject to Australian tax on their Australian source income, such persons are not subject to Australian tax on their United States source income and the reason is not solely because they are subject to U.S. tax. Similarly, a partnership, estate or trust is a resident of Australia for purposes of the Convention only to the extent that the income it derives is subject to Australian tax as the income of a resident either at the level of the partnership, estate or trust or in the hands of a partner or beneficiary, or, if that income is exempt from Australian tax under the Treaty, it is exempt solely because it is subject to U.S. tax. However, an Australian trust will be considered a resident of Australia, notwithstanding that its income is exempt from Australian tax, if the trust qualifies as a tax exempt organization under Australian law because it is established for public charitable purposes or scientific research. Thus, a dividend paid by a U.S. corporation to an Australian partnership comprised equally of an Australian resident partner and an Indonesian resident partner would be treated as paid one half to an Australian resident and that half would enjoy the reduced rate of U.S. tax provided for in Article 10 (Dividends).

Subparagraph (b) provides that a resident of the United States means a U.S. corporation and any other person resident in the United States for purposes of its tax. However, a partnership, estate or trust is a resident of the United States for purposes of the Convention only to the extent that the income it derives either is subject to U.S. tax as the income of a resident (either at the level of the entity or in the hands of a partner or beneficiary), or is exempt from U.S. tax for reasons other than the recipient's not being a U.S. person. Thus, a U.S. person that qualifies as a tax-exempt organization under U.S. law qualifies as a resident, and a recipient of tax-exempt income does not lose its status as a resident with respect to that income. The rule in paragraph 1 that tax-exempt organizations and recipients of tax-exempt income qualify as residents, notwithstanding that the income they derive is not subject to tax, is meant to be a clarification and not to imply that such tax-exempt organizations and other persons are not entitled to Treaty benefits under conventions which do not include this or similar language.

Paragraph 2 provides a series of tie-breakers for assigning a single residence to an individual who, by the criteria of paragraph 1, would be a resident of both countries.

The first test is where the individual has a permanent home. If that test is inconclusive because the individual has a permanent home in both countries or in neither of them, the second test is where he has his habitual abode. If that test also fails to establish a single country of residence, because the individual has a habitual abode in both countries or in neither of them, he is deemed to be a resident of the country with which his personal and economic relations are closer. Citizenship, *per se*, is not recognized by Australia as a tie breaker, but if the individual is a citizen of one of the Contracting States, that factor will be taken into account in determining where his personal and economic relations are closer. If these tests do not establish a single residence, the competent authorities will attempt to settle the question by mutual agreement under Article 24 (Mutual Agreement Procedure). Once an individual is assigned a residence under this paragraph for a taxable year, he is a resident only of that State for all purposes of the Convention for that year.

The residence of persons other than individuals is determined under the respective laws of the Contracting States. A dual resident company is treated as a resident of neither Contracting State for purposes of the convention. (See paragraph 1(g) of Article 3 (General Definitions).)

ARTICLE 5
Permanent Establishment

The rule governing the taxation by a Contracting State of business income derived by a resident of the other State utilize the concept of a "permanent establishment." Paragraph 1 of this Article defines in general terms the "permanent establishment" concept, and the following paragraphs give some specific illustrations of the meaning of the term.

A place of management, branch, office, factory, workshop and a place of extraction of natural resources, such as a well or quarry, are examples of a permanent establishment. Since a place of management would in most cases require an office, which is specifically noted in paragraph 2, the addition of that term will not generally cause a permanent establishment to exist where there would not otherwise be one.

A building site or construction or installation project will only be considered a permanent establishment if it lasts longer than 9 months, and an installation, drilling rig or ship used for dredging or exploring or exploiting offshore natural resources is a permanent establishment only if so used for at least 6 months in any 24-month period. In such a case, the site, project, installation, rig or ship constitutes a permanent establishment from the first day when work physically begins within the territory of a Contracting State. A series of contracts or projects which are interdependent both commercially and geographically are to be treated as a single project for the purpose of applying the 9- month and 6-month tests.

Paragraph 3 enumerates certain activities which may be undertaken singly or in

combination without creating a permanent establishment. Although subparagraph (f) of this paragraph of the U.S. Model was deleted, the same effect is obtained by the insertion of the reference to "one or more" in the introductory language of paragraph 3.

Paragraphs 4(a) and 5 consider the use of agents. A dependent agent who habitually exercises an authority to conclude contracts in the name of an enterprise is deemed to be a permanent establishment of that enterprise except to the extent that his activities are limited to those mentioned in paragraph 3 which would not constitute a permanent establishment under that paragraph. An enterprise of a Contracting State will not be considered to have a permanent establishment in the other State merely because it uses the services of an independent agent acting in the ordinary course of business in that other State.

Subparagraphs (b), (c) and (d) of paragraph 4 specify certain activities which constitute a permanent establishment even if not carried on through a fixed place of business like those enumerated in paragraph 2. Maintaining substantial equipment in a Contracting State for rental or other purposes for longer than 12 months constitutes a permanent establishment unless the equipment is leased under a “hire-purchase” agreement. Under Australian law the lessee under a “hire-purchase” agreement (a lease accompanied by certain lessee purchase options or rights) is treated for tax purposes as the owner of the leased property. The exception for hire-purchase agreements in this Article and elsewhere in the Convention (see Article 12 (Royalties)) was inserted at the request of Australia to distinguish such agreements from leases respected as such for tax purposes. Such a distinction is also made in the Commentary to Article 12 of the OECD Model Convention. Similarly, under the Internal Revenue Code, the terms of a “lease” may be such that for U.S. income tax purposes the lessee is treated as the owner of the property. For purposes of United States tax the exception for “hire-purchase” agreements simply confirms such treatment, which would also apply in the absence of such an explicit exception. See paragraph 2 of Article 3 (General Definitions). Engaging in supervisory activities at a building site or construction, assembly or installation project for more than 9 months in a 24-month period constitutes a permanent establishment. And, an enterprise which maintains goods in the other Contracting State which goods were either purchased there (and not previously processed elsewhere) or produced there by it or in its behalf, and are then substantially processed there by a related enterprise is deemed to have a permanent establishment in that other State. This provision was added at the request of Australia to permit it to tax a portion of the sale profit when goods are produced or purchased in Australia, processed there at cost by a related enterprise, and then sold. It is an alternative approach to allocating part of the profit to the processing operation in such a case, as the United States could do under section 482.

Paragraph 6 provides that control of one company by another does not of itself constitute either company a permanent establishment of the other. The determination as to whether a subsidiary is a permanent establishment of its parent corporation, or the converse, or whether two or more subsidiaries of the same corporation are permanent establishments of the parent or of each other is made by reference to the tests set out in paragraphs 1 through 5.

These same principles apply in determining whether an enterprise of a Contracting State has a permanent establishment in a third State or whether an enterprise of a third State has a

permanent establishment in a Contracting State. Such a determination may be relevant, for example, in deciding the source of interest (paragraph 7 of Article 11 (Interest)) or royalties (paragraph 6 of Article 12 (Royalties)).

ARTICLE 6
Income from Real Property

This Article provides that income from real property may be taxed by the Contracting State where the property is located. This rule does not confer an exclusive right of taxation on the State where the property is located. It simply provides that the situs State has the primary right to tax such income, regardless of whether the income is derived through a permanent establishment in that State or not. The provision in the U.S. Model for a binding election to be taxed on a net basis was deleted. Such an election is available under U.S. law and Australia taxes income from real estate on a net basis. The Article incorporates the rule that a leasehold interest in land and rights to exploit or explore for natural resources constitute real property situated where the land or resources, respectively, are situated. Except for those cases, the definition of real property is governed by the internal law of the Contracting State where the property is situated.

ARTICLE 7
Business Profits

This Article provides rules for the taxation by a Contracting State of income from business activity carried on by a resident of the other State.

Paragraph 1 provides that business profits of an enterprise of one Contracting State shall be taxable only in that State except to the extent that such profits are attributable to a permanent establishment through which the enterprise carries on business in the other Contracting State. (The term "enterprise of one of the Contracting States," used here and elsewhere in this Convention, excludes dual-resident corporations that are treated as residents of neither Contracting State for purposes of the Convention.)

Paragraph 2 provides that the profits to be attributed to a permanent establishment are those which it might be expected to make if it were an independent enterprise engaged in similar activities under similar conditions. The profits must reflect arm’s length prices. The profits so attributed may be from income described in section 864(c)(4)(B) of the Internal Revenue Code which are attributable to a permanent establishment in the United States may be subject to tax by the United States. In addition, the limited "force of attraction" rule in I.R.C. section 864(c)(3) does not apply for U.S. tax purposes under the Convention.

Paragraph 3 provides that deductions shall be allowed for expenses incurred for the purposes of the permanent establishment, including, *inter alia,* executive and general administrative expenses, wherever incurred, if such expenses are reasonably connected with the profits of the permanent establishment and would be deductible if it were an independent entity.

Australia and the United States will each allow an allocation to a permanent establishment of a portion of research and development and interest expenses incurred by the U.S. home office or elsewhere, provided that the expenses are reasonably connected with the profits of the permanent establishment.

Paragraph 4 states that no profits shall be attributed to a permanent establishment by reason of the mere purchase by it of goods or merchandise for the enterprise.

Paragraph 5 provides that, unless there is good and sufficient reason to the contrary, the same method of determining profits attributable to the permanent establishment shall be used each year.

Paragraph 6 provides that, where business profits include items of income dealt within other articles of the Convention, the provisions of those other articles override the provisions of this Article. For example, the taxation of income of international shipping and aircraft operations is governed by Article 8 (Shipping and Air Transport) and not by this Article. Similarly, the taxation of dividends, interest, and royalties is controlled by Articles 10, 11, and 12, respectively; however, the terms of those Articles provide that where dividends, interest, or royalties derived by a resident of a Contracting State are attributable to a permanent establishment in the other Contracting State, the provisions of this Article do apply and the item of income is taxed as business profits.

Paragraph 7 was inserted at the request of Australia to permit the tax authorities of a Contracting State to apply the provisions of internal law in determining tax liability in cases where the information available to the competent authority is not adequate to measure accurately the profits of a permanent establishment. The Internal Revenue Service would have this power even in the absence of such a specific provision. The determination of profits in such cases, based on the available information, must be done consistently with the principles of this Article, i.e., it must seek to reflect arm’s length pricing and appropriate deductions of expenses.

Notwithstanding the other provisions of this Article, paragraph 8 allows each State to apply its domestic law in taxing income from the insurance business, provided that such law remains the same as on the date the Convention was signed or is modified only in minor respects. In the case of a nonresident general insurance company which insures risks in Australia, Australia imposes its ordinary corporate tax rate (now 46 percent) on a deemed profit equal to 10 percent of the gross premiums from such insurance. The company may elect instead to be taxed on a net basis. The United States will apply its excise tax on insurance and reinsurance premiums of Australian insurers or will tax the net income of a U.S. trade or business of an Australian insurer, as appropriate.

Unlike the U.S. Model, this Convention does not provide that business profits include income from the rental of tangible personal property and films. In this Convention those types of rentals are treated as royalties under Article 12 (Royalties). However, the maintenance of substantial equipment in the other Contracting State for more than 12 months (other than equipment leased under a "hire-purchase" agreement) constitutes a permanent establishment

covered by this Article.

ARTICLE 8
Shipping and Air Transport

Paragraph 1 provides that each of the Contracting States shall exempt from tax profits derived by an enterprise of the other Contracting State from the international operation of ships or aircraft, including:

(a) profits from the rental on a full basis of ships and aircraft operated in international traffic by the lessee (provided that the lessor also engages in the international operation of ships or aircraft or in the regular leasing of ships or aircraft on a full basis), and

(b) profits from the rental of ships and aircraft on a bareboat basis and of containers and related equipment operated or used in international traffic by the lessee, provided in each case that the leasing activity is incidental to the operation of ships or aircraft in international traffic by the lessor. Rental on a full or bareboat basis refers to whether the ships or aircraft are leased fully equipped, manned and supplied.

For example, if a U.S. airline which operates internationally leases a plane on a bareboat basis to an Australian airline for use on its international routes, the rental income derived by the U.S. company is exempt from Australian tax under this Article. However, if the U.S. airline operates only within the United States, or if the leased plane is used only within Australia, the rental income is not exempt under this Article. Moreover, if a U.S. bank leases a plane on a bareboat basis to the Australian airline, either for use internationally or within Australia, that rental income is not exempt under this Article.

Income from the rental of ships, aircraft or containers which is not exempt from tax under this Article is taxable in accordance with Article 12 (Royalties). Australian law imposes tax on the net income after deducting expenses, subject to a maximum tax under Article 12 of 10 percent of the gross rental.

Paragraph 2 states that the provisions of this Article apply to the share of an enterprise of a Contracting State in the profits of a pool or joint venture, even though the other participants may be enterprises of third States not covered by this Convention. The profit shares of such third country participants are not affected by this Convention, but are taxable in accordance with internal law or under the provisions of another international agreement, if applicable.

Paragraph 3 merely clarifies that profits from the transport of goods or passengers picked up and discharged within the same Contracting State are not within the definition of international traffic and may be taxed by that State.

ARTICLE 9
Associated Enterprises

This Article provides that, where related persons engage in transactions which are not at arm's length, the Contracting States may make appropriate adjustments to their taxable income and tax liability.

Paragraph 1 states the general rule that where an enterprise of one Contracting State and an enterprise of the other Contracting State are related through management, control, or capital and their commercial or financial relations differ from those which would prevail between independent enterprises, the profits of the enterprises may be adjusted to reflect the profits which would have accrued if the two enterprises had been independent.

Paragraph 2 provides that where one of the Contracting States has increased the profits of an enterprise of that State to reflect the amount that would have accrued to the enterprise had it been independent of an enterprise in the other Contracting State, the second State shall make an appropriate adjustment, decreasing the amount of tax which it has imposed on those profits. In determining such adjustments, due regard is to be had to the other provisions of the Convention. The competent authorities of the two States shall consult each other if necessary in implementing this provision.

Paragraph 3 clarifies that each Contracting State may apply its internal law in determining liability for its tax. For example, although paragraphs 1 and 2 refer to allocations of "profits" and "taxes," it is understood that such terms also include the components of the tax base and of the tax liability, such as income, deductions, credits, and allowances. The United States will apply its rules and procedures under section 482 of the Internal Revenue Code. Australia will apply the provisions of its income tax legislation, particularly with respect to the determination of taxable income in cases where the information available is inadequate to measure net income under the ordinary rules. Such determinations must be consistent in each case with the principles of arm's length transactions.

ARTICLE 10
Dividends

This Article limits the rate of tax which may be imposed by a Contracting State on dividends paid by a company which is a resident of that State for purposes of its tax to a resident of the other Contracting State. A dual resident corporation is a resident of each Contracting State "for purposes of its tax," but is a resident of neither State for purposes of the Convention.

Paragraph 1 states that such dividends may be taxed in the State of residence of the recipient. This provision, which is based on the OECD Model, confirms the provision of paragraph 3 of Article 1 (Personal Scope) that each Contracting State reserves the right to tax its residents.

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Paragraph 2 provides that such dividends may also be taxed in the Contracting State of which the paying company is a resident for the purposes of its tax, but such tax may not exceed

15 percent of the gross amount of the dividends when the beneficial owner is a resident of the other State. This limitation applies to the tax imposed by either State on dividends paid by a dual resident company to a resident of the other Contracting State; but since a dual resident company is not a resident of either State under Article 4 (Residence), it does not apply to dividends received by such a company. In the absence of a Treaty, Australia, like the United States, imposes a tax of 30 percent on gross dividends paid to nonresidents. By Treaty, Australia is willing to reduce that the tax to, but not below, 15 percent. The reciprocal 15 percent limit of taxation at source provided in this paragraph also applied in the 1953 Convention.

Paragraph 3 defines dividends as income from shares and income which under domestic law is assimilated to income from shares.

Paragraph 4 provides that when dividends beneficially owned by a resident of one Contracting State are attributable to a permanent establishment or a fixed base which that resident maintains in the other State, of which the company paying the dividends is a resident, such dividends are not taxable in accordance with this Article, but in accordance with the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services).

Paragraph 5 provides that a Contracting State may not impose tax on dividends paid by a company which is a resident of the other State, with three exceptions:

(a) to the extent that the dividends are paid to a resident of the first State;

(b) to the extent that the dividends are attributable to a permanent establishment or fixed base of the beneficial owner in the first State; or

(c) to the extent that 50 percent or more of the gross income of the company paying the dividends is attributable to one or more of permanent establishments of that company in the first State and the dividends are paid out of the profits of such permanent establishment.

Subparagraph (c) applies only if the taxing State does not impose branch profits tax of the kind described in paragraph 6. For this purpose, the U.S. accumulated earnings and personal holding company taxes are not taxes of the kind described in paragraph 6. If only subparagraph (c) applies, the tax is limited to 15 percent. The United States may also tax dividends received by U.S. citizens under paragraph 3 of Article 1 (Personal Scope).

Paragraph 6 authorizes the imposition of a branch profits tax in addition to the ordinary corporate tax on profits of a permanent establishment of a resident of the other Contracting State. Australia's ordinary corporate income tax rate is 46 percent, but the rate of tax on permanent establishments of nonresident corporations is 51 percent. Dividends distributed by Australian corporations to a U.S. corporation are subject to a tax of 15 percent. Distributions by an Australian branch of a U.S. company are not subject to a further tax. Thus, the additional 5 percentage points of tax on the branch profits serves as a substitute for a withholding tax on distributed profits. Under paragraph 6, Australia's additional tax may not exceed the amount which would result if the 15 percent dividend withholding tax were to be applied to the profits of the permanent establishment net of the corporate tax at the rate applicable to domestic corporations. For example, if a permanent establishment has taxable income of 100 in Australia

and the ordinary corporate income tax rate is 46 percent, the additional tax on the branch profits may not exceed 15 percent of 54, or 8.1; i.e., the total tax on the branch may not exceed 54.1 percent (46 plus 8.1). The Australian tax of 51 percent is within this limit.

Paragraph 6 also provides that, if a nonresident company is liable to a tax on its undistributed profits, the amount of undistributed profits shall be calculated as if that company had paid the corporate income tax applicable to a domestic corporation and had distributed dividends of an amount such that the 15 percent tax on those dividends imposed in accordance with paragraph 2 of this Article would have equaled the additional tax. For example, with an Australian tax on domestic corporations of 46 percent and on permanent establishments of foreign corporations of 51 percent, a permanent establishment of a U.S. corporation would, for purposes of any Australian tax on undistributed profits, be deemed to have distributed profits of 33.33 and undistributed profits of 20.67 for each 100 of taxable income. (Profit of 100 after basic corporate tax of 46 leaves 54 available for distribution. Additional tax of 5 is equivalent to a 15 percent withholding tax on 33.33; 15% x 331/3 = 5. Therefore, distributed profits are deemed to be 33.33 and the remainder of the after-tax profit of 54, or 20.67 is deemed to be undistributed.)

ARTICLE 11
Interest

This Article limits the tax which may be imposed by either Contracting State on interest derived and beneficially owned by a resident of the other Contracting State. There is no corresponding provision in the 1953 Convention.

Paragraph 1 states that such interest may be taxed in the State of residence of the beneficial owner. This provision, which comes from the OECD Model, confirms the provision of paragraph 3 of Article 1 (Personal Scope) that each Contracting State reserves the right to tax its residents.

Paragraph 2 provides that such interest may also be taxed by the State in which it has its source, but the tax is limited to 10 percent of the gross amount of the interest. Australia's statutory rate of tax on interest paid to nonresidents is generally 10 percent.

Paragraph 3 provides that, when interest beneficially owned by a resident of one Contracting State is attributable to a permanent establishment or fixed base which that resident maintains in the other State, that interest is not taxable in accordance with this Article but in accordance with the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services).

Paragraph 4 states that the provisions of this Article shall not apply to interest payments between related persons in excess of the amount which would have been agreed upon at arm’s length. Such excess amount shall be taxed according to the laws of each Contracting State, with regard also to the other provisions of this Convention.

Paragraph 5 defines interest as income assimilated to income from money lent under the tax law of the Contracting State where the income arises.

Paragraph 6 provides that a Contracting State may not tax interest paid by a resident of the other State, with three exceptions:

(1) to the extent that the interest has its source in that State;

(2) to the extent that the beneficial owner of the interest is a resident of that State; or

(3) to the extent that the interest is attributable to a permanent establishment or fixed base of the owner in that State.

Under these rules the United States may tax interest paid by an Australian company if the interest has its source in the United States in accordance with paragraph 7 of this Article, and in accordance with the Internal Revenue Code. Where such interest is beneficially owned by a resident of Australia, the U.S. tax will be reduced to 10 percent, in accordance with paragraph 2 of this Article. The United States may also tax interest received by U.S. citizens, pursuant to paragraph 3 of Article 1 (Personal Scope).

Paragraph 7 defines the source of interest. Interest has its source in a Contracting State if paid by that State, a political subdivision or local authority thereof, or a person who is a resident of that State for purposes of its tax, including a corporation which under the respective internal laws is a resident of both States. (Thus, interest paid by such a dual resident company may be eligible for the reduced rate provided in paragraph 2, although interest beneficially owned by such a company is not.) An exception to this general rule, which looks to the payer of the interest, provides that when the indebtedness is incurred in connection with and the interest is borne (deducted in computing taxable income) by a permanent establishment or fixed base which the payer has in a Contracting State, the interest has its source in that State.

The Convention does not provide for exemption at a source of interest derived and beneficially owned by the Government of the other State or by a government instrumentality. Under Australian law, such interest, e.g., interest derived by the U.S. Government or the Export-Import Bank, is currently exempt from tax in Australia. Similarly, under U.S. law (I.R.C. section 892) interest derived by the Australian government would generally be exempt from U.S. tax.

ARTICLE 12
Royalties

This Article limits the tax which may be imposed by either Contracting State on royalties derived and beneficially owned by a resident of the other Contracting State.

Paragraph 1 states that such royalties may be taxed in the State of residence of the beneficial owner. This provision, which comes from the OECD Model, confirms the provision of paragraph 2 of Article 1 (Personal Scope) that each Contracting State reserves the right to tax its residents.

Paragraph 2 provides that such royalties may also be taxed by the State in which they have their source, but the tax is limited to 10 percent of the gross amount of the royalties. Under the 1953 Convention, copyright royalties (other than those related to films) are exempt from tax at source, but other royalties are taxable at the statutory rates. Australia's statutory tax on royalties paid to nonresidents, other than for films or video tapes, is withheld by the payer at the full corporate or individual tax rate on the gross amount less allowable expenses necessarily incurred in deriving the royalty. The Convention preserves the net basis of taxation by Australia, except that the amount of tax liability may not exceed 10 percent of the gross amount of the royalty paid. Payments for the use of films and video tapes are taxed by Australia at 10 percent of the gross amount. This practice is confirmed by this Article. On the U.S. side the statutory rate of 10 percent will be reduced to 10 percent.

Paragraph 3 provides that when royalties beneficially owned by a resident of one Contracting State are attributable to a permanent establishment or fixed base maintained by that resident in the other State, the royalties will not be taxed in accordance with the provisions of this Article but in accordance with the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services).

Paragraph 4 contains a definition of the term "royalties." The definition is broader than the one in the U.S. Model. For purposes of this Convention, payments for the use of, or right to use, industrial, commercial or scientific equipment are treated as royalties, except when such equipment is leased under a "hire-purchase" agreement. Payments for the use of, or right to use, motion picture films and certain tapes are also taxed as royalties. And royalties, for purposes of this Article, include payments or credits for scientific, technical, industrial or commercial knowledge or information owned by any person, and payments or credits for ancillary assistance furnished to enable the application of any property or right to which this Article applies. The reference to knowledge or information "owned" is meant to indicate that the term "royalties" implies a property right as distinguished from personal services. An engineer or architect who prepares a design for a customer is considered to perform personal services, the remuneration for which is covered under Article 14 (Independent Personal Services) or 15 (Dependent Personal Services).

An engineer or architect who supplies a preexisting design or blueprint is considered to be furnishing knowledge or information, the payment for which constitutes a royalty governed by this Article. The supply of ancillary services does not give rise to a royalty when supplied in connection with the sale of property, but does give rise to a royalty when supplied in connection with the leasing of any of the property or rights covered by this Article.

In some cases, income covered by this Article gives rise to a permanent establishment if the income-producing activity continues long enough. For example, payments for the leasing of industrial, scientific or commercial equipment (other than under a "hire-purchase" agreement) are taxable as royalties, but if the enterprise deriving the royalties maintains the equipment for rental in the other State for longer than 12 months, it is considered to have a permanent establishment in that other State under paragraph 4(b) of Article 5 (Permanent Establishment). In such a case the income is taxable from the beginning in accordance with Article 7 (Business Profits), as

provided in paragraph 3 of this Article. Similarly, payments for the supply of supervisory services could in some cases constitute royalties; but if the services are furnished for more than 9 months in a 24-month period, the enterprise has a permanent establishment under paragraph 4(c) of Article 5 (Permanent Establishment), and the income is taxable in accordance with Article 7 (Business Profits), as provided in paragraph 3 of this Article.

Subparagraph (b)(iii) of paragraph 4 provides a special rule to deal with the situation of a disguised lease of a property right of the type covered by this paragraph. If, for example, an Australian company were to use in Australia a copyright or patent held by a U.S. company without paying a royalty to the U.S. company and the U.S. company were to forebear from selling the protected products in Australia in return for payment, the U.S. company would be treated as having received a royalty from the Australian company.

Subparagraph (c) of paragraph 4 provides that, to the extent that income from the disposition of any property or right described in this paragraph is contingent on the productivity or use or further disposition of such property or right, it is a royalty.

Paragraph 5 states that the provisions of this Article shall not apply to royalty payments between related persons in excess of the amount which would have been agreed upon at arm's length. Such excess amount shall be taxed according to the laws of each Contracting State, with regard also to the other provisions of this Convention.

Paragraph 6 defines the source of royalties. In general, a royalty is considered to have its source in a Contracting State if paid by the Government or a resident of that State or by a company which under internal law is a resident of that State. (Thus, a royalty paid by a dual resident company may be eligible for the reduced rate provided in paragraph 2, although a royalty beneficially owned by such a company is not.) However, if a permanent establishment or fixed base in one of the Contracting States or in a third State incurs the liability to pay the royalties and bear the payment (deducts it in computing taxable income), the royalty is considered to have its source in the State where the permanent establishment or fixed base is located. Moreover, if under these rules a royalty is not considered to have a source in either State but it relates to the use of property or the right to use property in one of them, the royalty is considered to have its source where the property is used or where there is a right to use it. Thus, for example, if an Australian resident were to license a patent to a third country company, which in turn sub-licenses the patent for use in the United States, the United States would tax the sub-license payment by the U.S. user to the third country company in accordance with U.S. law, or with the provisions of a U.S. Treaty with that country, if applicable, and would also tax the license payment by the third country company to the Australian resident, subject to the limitation in paragraph 2. Third country residents cannot obtain the rate reduction provided in paragraph 2, since this Article applies only to royalties derived by residents of a Contracting State.

ARTICLE 13
Alienation of Property

This Article provides rules for the taxation of certain gains derived by a resident of a Contracting State. In general, it provides that:

(1) gains from the alienation of real property may be taxed where the real property is located;

(2) gains derived from the alienation of ships or aircraft or related property may be taxed only by the State of which the enterprise is a resident, except to the extent that the enterprise has been allowed depreciation of the property in computing taxable income in the other State; and

(3) gains from the alienation of property referred to in paragraph 4 (c) of Article 12 (Royalties) are taxable under Article 12.

Gains with respect to any other property are covered by Article 21 (Income Not Expressly Mentioned), which provides that gains effectively connected with a permanent establishment are taxable where the permanent establishment is located, in accordance with Article 7 (Business Profits), and that other gains may be taxed by both the State of source of the gain and the State of residence of the owner. Double taxation is avoided under the provisions of Article 22 (Relief from Double Taxation).

Paragraph 1 of Article 13 states the rule that gains derived from the alienation of real property situated in a Contracting State may be taxed by that State.

Paragraph 2 defines real property in each of the Contracting States. In the case of the United States, paragraph 2(a) explains that the term "real property situated in the other Contracting State" includes a United States real property interest as defined under the Foreign Investment in Real Property Tax Act, as amended. Thus, the United States retains its full taxing right under the law. In the case of Australia, paragraph 2(b) provides that real property has the meaning it has under Australian law and includes an interest in a company, partnership, trust or estate, the assets of which consist wholly or principally of real property situated in Australia.

Paragraph 3 provides that when an enterprise of a Contracting State derives gains with respect to the alienation of ships, aircraft, or containers operated or used by it in international traffic, the gain shall be taxable only in the State of residence of the enterprise, except to the extent that the enterprise has been allowed depreciation on that property in the other Contracting State. To the extent that depreciation deductions have reduced the tax on income from the operation of such ships, aircraft, or containers in the other State, that other State may recapture those depreciation deductions (but not in excess of the gain realized) when the property is disposed of. This paragraph also provides a cross-reference to paragraph 4(c) of Article 12 (Royalties) and states that gain on royalties described in that paragraph (royalties which are contingent on the use or productivity of the right or property) are taxable in accordance with that Article.

Paragraph 4 clarifies that real property consisting of shares in a company or interests in a partnership, estate or trust referred to in paragraph 2(b) is deemed to be situated in Australia.

ARTICLE 14

Independent Personal Services

This Article concerns the taxation of income derived by a resident of one of the Contracting States from independent personal services.

The rule established in this Article is that, if an individual who is a resident of one Contracting State performs independent personal services in the other Contracting State, the income from those services may be taxed by that other State if the individual either is present in that other State for an aggregate of more than 183 days in the taxable year (or income year) or has a fixed base regularly available to him in that other State for the purpose of performing his activities. In the latter case, the other State may tax the income for services performed in that other State which is attributable to that fixed base.

It is understood that the term "fixed base" is analogous to the term "permanent establishment." Independent personal services include all personal services performed by an individual for his own account, including services performed as a partner in a partnership, where he receives the income and bears the losses arising from such services, except that services performed as a director of a company are covered by Article 15 (Dependent Personal Services).

ARTICLE 15
Dependent Personal Services

This Article concerns the taxation of remuneration derived by a resident of one of the Contracting States as an employee or as a director of a company.

Pensions, annuities and remuneration of government employees are covered by Articles 18 and 19. Other remuneration of a resident of one of the Contracting States for employee services or for services performed as a director of a company may be taxed only in the State of residence unless the employment is exercised or the services are performed in the other State, in which case that other State may tax the remuneration for the services performed there, subject to the conditions set forth in paragraph 2.

Paragraph 2 provides that, even where a resident of one Contracting State performs services in the other State, that other State may not tax the income for such services if three conditions are met:

(a) the recipient is present in that State for not more than 183 days in the taxable year (or income year);

(b) the remuneration is paid by or on behalf of an employer, or, in the case of remuneration of directors, a company, that is not a resident of that State; and

(c) the remuneration is not deductible in determining taxable profits of a permanent establishment, fixed base, or a trade or business of the employer or company in that State.

If any one of these conditions is not met, e.g., if the employer is a resident of the State where the

services are performed, the income may be taxed by that State. The insertion of the reference to a trade or business means that if, for example, an Australian resident is employed in the United States by a Bermuda company and his salary is deducted in determining the profits of the U.S. trade or business of that company, the salary is taxable in the United States even if the Bermuda company does not have a permanent establishment in the United States.

Paragraph 3 provides that remuneration derived for employment aboard a ship or aircraft operated in international traffic by a resident of a Contracting State may be taxed by that State. Under this provision, Australia may tax the remuneration of employees for services aboard ships or aircraft operated internationally by Australian residents. Similarly, the United States may tax such remuneration when the operator is a U.S. resident. However, under U.S. law, the United States taxes such income of a nonresident alien only to the extent it is derived from U.S. sources (i.e., within U.S. territorial waters). This paragraph does not confer an exclusive taxing right. Both Contracting States retain the right to tax their residents and citizens under paragraph 3 of Article 1 (Personal Scope).

ARTICLE 16
Limitation on Benefits

This Article limits the benefits of the Convention to bona fide residents of the Contracting States. It is intended to prevent residents of third countries from inappropriately using a company which is a resident of one of the Contracting States as a conduit or similar vehicle to obtain Treaty benefits. Specifically, a person (other than an individual) which is a resident of one of the Contracting States is entitled to relief from taxation from the other Contracting State only if any of three alternative tests is met.

The first two tests are objective tests relating to the entity in question. If more than 75 percent of the beneficial interest in the person receiving the income is owned, directly or indirectly, by any combination of individuals who are residents of the Contracting States, citizens of the United States, the Contracting States themselves, or publicly traded companies which are residents of the Contracting States, the first test is met.

Under the second test a publicly traded company that is a resident of Australia or the United States is considered to have a sufficient nexus with Australia or the United States, respectively, so as to entitle it to Treaty benefits. Under this test, Treaty benefits are not denied if there is substantial and regular trading of the principal class of shares of such a company on a recognized stock exchange in one of the Contracting States. A recognized stock exchange includes the NASDAQ system in the United States.

The third test recognizes that ownership of an entity that is a resident of the United States or Australia by persons resident in third countries is not uncommon. In view of the factors discussed below, granting Treaty benefits to such an entity often is consistent with the goals of the Treaty. Accordingly, under the third test, Treaty benefits are allowed if the establishment, acquisition and maintenance of the person and the conduct of its operations did not have as a

principal purpose the purpose of obtaining Treaty benefits. This test would be met, for example, if an Australian company owned by third country residents conducts business operations in Australia and its U.S. investments are related or incidental to those business activities, or if the Australian tax burden equals or exceeds the tax reduction claimed under the Convention. It could also be met in other situations.

Paragraph 3, inserted at the request of Australia, provides a special rule concerning certain trust situations. The benefits of the Treaty do not apply to income derived by a trustee which under the Convention is treated as income of a resident of one of the Contracting States if a principal purpose of the use of the trust was to obtain a benefit under the Convention. For example, if an Australian resident establishes one or more U.S. accumulation trusts with Australian beneficiaries to receive dividends from Australian corporations in order to reduce the Australian tax on those dividends, the reduced rate provided in paragraph 2 of Article 10 (Dividends) will not apply.

This Article is not meant to impose any added burden on withholding agents, and withholding agents will not be required to verify a person's ownership or purposes.

In applying this Article the normal burden of proof rules apply. For example, under present U.S. procedures an entity that is a resident of Australia and that believes it is entitled, under one of the alternative tests of this Article, to the 10 percent U.S. tax rate on interest provided by Article 11 (Interest) would merely file a U.S. Form 1001 with the appropriate withholding agent to claim the benefit. Of course, the Internal Revenue Service could, on audit, examine the transaction.

In view of a combination of factors - the tax burden imposed by both the United States and Australia; the fact that, even under treaties, Australia imposes source taxation on income of nonresidents of Australia at a level that is not insignificant; the fact that the Treaty's rate reductions on source taxation of passive income are not as great as those accorded by the United States in many other treaties; and the concerns of both countries about tax avoidance and evasion - this Convention is not expected to be the subject of abuse. It is, therefore, anticipated that residents of the Contracting States will typically satisfy at least one of the three exceptions. Consequently, it should rarely be necessary to deny Treaty's benefits under this Article.

ARTICLE 17
Entertainers

This Article provides certain exceptions to the rules otherwise governing income from personal services in the case of income derived by entertainers and athletes.

Paragraph 1 provides that a Contracting State may tax income derived by a resident of the other State from the performance of personal services in the first State as an entertainer or athlete if the gross receipts for such services, including expenses reimbursed or paid on his behalf, exceeds $10,000 (or the equivalent in Australian dollars) for the income year or taxable year

concerned. In that case the full amount may be taxed by the first State, subject to any deductions allowable under its laws. This rule overrides the provisions of Article 14 (Independent Personal Services) and 15 (Dependent Personal Services) by adding another basis for taxation at source. However, if the income does not exceed $10,000, whether the income may be taxed by the State where the services are performed is determined in accordance with Article 14 or 15, as the case may be.

Income derived from services rendered by producers, directors, technicians and others who are not artistes or athletes is taxable in accordance with Article 14 or 15, as appropriate.

Paragraph 2 corresponds to the provisions in the U.S. Model. Where income for services performed by an entertainer or athlete accrues not to the entertainer or athlete but to another person, it may be taxed in the State where the activities are performed, without regard to the provisions of the Convention concerning business profits or income from personal services, unless it is established that neither the entertainer or athlete nor any related person participates in those profits in any manner.

ARTICLE 18
Pensions, Annuities, Alimony and Child Support

This Article deals with the taxation of pensions, social security payments, annuities, alimony and child support derived by individuals who are residents of a Contracting State or citizens of the United States.

Paragraph 1 provides that pensions derived and beneficially owned by a resident of one of the Contracting States in consideration of past employment, other than pensions covered in Article 19 (Governmental Remuneration), shall be taxable only in that State.

Paragraph 2 provides that public pensions, such as social security benefits, paid by one Contracting State to a resident of the other State or to a citizen of the United States are taxable only in the paying State. The reference to U.S. citizens is to ensure that a social security payment by Australia to a U.S. citizen resident in Australia shall be taxable only in Australia and not in the United States. The exemption of such income provided by this paragraph is excepted from the saving clause under paragraph 4 of Article 1 (Personal Scope).

Paragraph 3 provides that annuities paid to a resident of a Contracting State shall be taxable only in that State.

Paragraph 4 defines "pensions and similar remuneration" and paragraph 5 defines "annuities."

Paragraph 6 provides that alimony and other maintenance payments, including child support payments, are taxable only in the State where they arise. The definitions and source rules relating to alimony and child support payments are determined under the internal laws of the

Contracting States. Under Australian law alimony and child support payments are exempt to the recipient and not deductible by the payer. Thus, under this provision, alimony arising in the United States and paid to a resident of Australia will be deductible by the payer but taxed to the recipient by the United States. Alimony arising in Australia and paid to a U.S. resident, and child support payments arising in either State and paid to a resident of the other State, will not be deductible by the payer and will not be taxed to the recipient. These exemptions are available to residents and citizens of the respective States as a result of paragraph 4 of Article 1 (Personal Scope).

ARTICLE 19
Governmental Remuneration

This Article provides that remuneration, including pensions, paid by one of the Contracting States or a political subdivision, local authority or agency thereof to a citizen of that State for the performance of governmental functions is exempt from tax by the other State. If such remuneration is paid to an individual who is a resident, but not a citizen, of the employing State, whether it may be taxed by the other Contracting State is determined in accordance with the provisions of Articles 14 (Independent Personal Services), 15 (Dependent Personal Services), 17 (Entertainers) or 18 (Pensions, Annuities, Alimony and Child Support), as the case may be. If such remuneration is paid by one of the States to an individual who is a resident of the other State (or by Australia to a citizen of the United States), it may be taxed by that other State (or by the United States in the case of U.S. citizens) in accordance with paragraph 3 of Article 1 (Personal Scope). If such remuneration is paid to an individual who is not a resident of either State (and is not a citizen of the United States), it is not covered by this Convention.

Whether functions are of a governmental nature is determined by reference to the concept of a governmental function in the State in which the income arises.

ARTICLE 20
Students

This Article provides that, when a resident of one of the Contracting States goes to the other State for the purpose of full-time education, that other State may not tax payments received by the student for the purpose of his maintenance or education from sources outside that State.

ARTICLE 21
Income Not Expressly Mentioned

This Article provides that items of income derived by a resident of one of the Contracting States and not covered in the preceding articles may be taxed by the country of residence of the recipient. If from sources in the other State, such income may also be taxed by that other State. However, Article 7 (Business Profits) governs the taxation of such income to the extent it is

effectively connected with a permanent establishment in that other State.

Among the items covered by this Article are prizes and income from the insurance business, which is specifically excluded from the provisions of Article 7 (Business Profits) by paragraph 8 of that Article. The source of such items of income is determined under the respective domestic laws of the two countries. Any difficulties or doubts in applying this Article, as in other cases, may be addressed in accordance with the provisions of Article 24 (Mutual Agreement Procedure).

ARTICLE 22
Relief from Double Taxation

Paragraph 1 provides that the United States shall give a foreign tax credit for income taxes paid to Australia, subject to the limitations provided in U.S. law. The credit is allowed for taxes paid directly by or on behalf of the U.S. resident or citizen. In addition, in the case of a U.S. corporation owning at least 10 percent of the voting stock of an Australian corporation, credit is allowed for the underlying Australian corporate tax on the profits of the Australian corporation out of which dividends are paid to the U.S. corporation. The Australian taxes referred to in paragraphs 1(b) and 2 of Article 2 (Taxes Covered) are considered income taxes for purposes of the credit.

This guarantee of a foreign tax credit is independent of the statutory grant of a credit under the Internal Revenue Code, but the amount of the credit to be allowed is determined in accordance with the limitations provided in the Internal Revenue Code. Since the Convention does not provide credit for a tax which is believed not to be creditable under the Internal Revenue Code, no special per-country limitation is contained in the Convention. However, paragraph 1 provides that the Convention source rules may be used only for purposes of determining U.S. foreign tax credits for the Australian taxes covered by the Convention, i.e., not for taxes of other foreign countries.

In paragraph 2, Australia agrees to allow Australian residents a credit against Australian income tax equal to the income tax paid in the United States other than solely by reason of U.S. citizenship (i.e., the amount of tax which the United States is authorized under the Convention to impose at source on residents of Australia who are not U.S. citizens), subject to the limitations in Australian law which limit the credit to the Australian income tax payable on the income or any class thereof or on income from sources outside Australia.

Paragraph 3 confirms that an Australian corporation that owns at least 10 percent of the voting stock of a U.S. corporation is entitled to a rebate in its assessment, at the average rate of Australian tax payable by it, on dividends it receives from the U.S. corporation which are included in its taxable income in Australia. If Australian law providing this relief from tax on intercorporate dividends should change so that the rebate is no longer allowable, Australia agrees to allow credit for the underlying U.S. tax on the profits out of which such dividends are paid (similar to the U.S. credit allowed under section 902 of the Internal Revenue Code) in addition to

the direct credit referred to in paragraph 3.

Paragraph 4 provides a special rule for avoiding double taxation of a U.S. citizen who is a resident of Australia. Both the United States and Australia tax the worldwide income of such a person. The special rule provides that, in such a case, the United States will credit against the U.S. tax the Australian tax paid, net of the Australian foreign tax credit provided for in paragraph 2 (i.e., the Australian foreign tax credit for United States source basin taxation). For purposes of computing the foreign tax credit limitation under this paragraph, the United States will re-characterize enough U.S.- source income as Australian-source income to allow this special credit to be utilized, but without reducing the U.S. tax below the amount the United States may impose under this Convention other than by reason of citizenship (i.e., the amount of U.S. tax that may be imposed on a source basis under this Convention on residents of Australia who are not U.S. citizens). This source rule is provided by paragraph 1(c) of Article 27 (Miscellaneous), subject to the limitation provided in this paragraph.

ARTICLE 23
Non-Discrimination

This Article provides certain criteria of non-discriminatory application of the taxes covered by the Convention.

Paragraph 1 provides, first, that citizens of a Contracting State who are residents of the other State shall not be taxed less favorably in that other State than resident citizens of that other State who are in the same circumstances. It is understood that United States citizens who are not residents of the United States and Australian citizens who are not residents of the United States are not in the same circumstances with respect to the U.S. income tax, which is generally imposed on the worldwide income of U.S. citizens but not of Australian citizens.

Paragraph 1 also provides, in subparagraph (b), that interest, royalties, and other disbursements paid by a resident of a Contracting State to a resident of the other State shall be deductible for determining taxable profits under the same conditions as if they had been paid to a resident of the first-mentioned State. The term "other disbursements" is understood to include a reasonable allocation of executive and administrative expenses, research and development expenses, and other expenses incurred for a group of related enterprises.

Subparagraph (c) is the same as the corresponding paragraph in the U.S. Model. It requires that a Contracting State not impose more burdensome taxation on a subsidiary corporation owned by residents of the other Contracting State than it imposes on similar corporations which are locally owned.

Subparagraph (d) provides that a Contracting State may not impose more burdensome taxes on a permanent establishment of an enterprise of the other State than it imposes on its own enterprises carrying on the same activities in the same circumstances.

Paragraph 2 states that this Article does not affect the taxes of either Contracting State as in force on the date of signature of the Convention or tax laws subsequently enacted which are substantially similar to the existing taxes in purpose or are reasonably designed to prevent avoidance or evasion of tax. However, any subsequent tax measure must treat residents or citizens of the other State no less favorably than residents or citizens of a third State (except where the treatment of residents or citizens of third States is governed by an international agreement rather than by internal law).

Both Australia and the United States allow certain exemptions, deductions or rate reductions to residents taxed on their worldwide income which they do not extend to nonresidents not taxed on their worldwide income. For example, Australia imposes a 5 percent additional corporate tax on the profits of Australian branches of foreign corporations in lieu of a withholding tax on their profit remittances to the home office, denies to such branches the rebate on intercorporate dividends available to Australian corporations, and limits certain exemptions from the withholding tax on interest to funds borrowed abroad by domestic corporations owned and controlled by Australian residents. The United States does not extend to U.S. branches of foreign corporations the same deductions for dividends received from U.S. corporations which is available to U.S. corporations nor does it allow inclusion of income of foreign corporations in a consolidated return. Under this Article, those practices will not be in violation of the Convention; however, paragraph 2 in this regard is merely clarifying as neither Australia nor the United States would consider the foregoing provisions of its respective law to violate to non-discrimination provisions even in the absence of the rule of paragraph 2.

Paragraph 3 states that differentiating in taxation laws between residents and nonresidents does not of itself constitute discrimination contrary to this Article. This is merely an elaboration of the principles contained in paragraph 1, which require equal treatment of residents in the same circumstances. Residents and nonresidents are not in the same circumstances, reflecting the fact that in both countries residents are taxable on their worldwide income whereas nonresidents in general are taxable only on income from sources in that country.

Paragraph 4 provides that the competent authorities will attempt to resolve any instances of discriminatory taxation which might arise as a result of the tax measures of either country. Taxpayers may also take advantage of the provisions of Article 24 (Mutual Agreement Procedure) in such cases.

ARTICLE 24
Mutual Agreement Procedure

This Article provides for cooperation between the competent authorities to resolve problems of double taxation.

Paragraph 1 (a) provides that a taxpayer who considers that the actions of one or both of the Contracting States may result in taxation not in accordance with the Convention may present his case to the competent authority of the State of which he is a resident or citizen. However, he

must present his case within three years from the first notification of the action giving rise to the potential double taxation.

Paragraph 1(b) provides that the competent authority, if it considers the claim to be justified, shall endeavor to resolve the case by mutual agreement with the competent authority of the other Contracting State. Any agreement reached shall be implemented without regard to any statutory time limits of the Contracting States. Thus, for example, if it is agreed that tax liability should be adjusted downward, a refund of the excess tax paid will be made even though the statute of limitations may have expired. However, no additional tax may be imposed if the statute of limitations has expired in the taxing State.

Paragraph 2 provides that the competent authorities shall endeavor by mutual agreement to resolve any difficulties or doubts which may arise in the interpretation or application of the Treaty. For example, the competent authorities may agree on the same allocation of income, deductions, credits or allowances; to the same determination of the source of particular items of income; on a common meaning of a term; and they may decide, for purposes of paragraph 2(c) of Article 4 (Residence) to which State an individual has closer personal and economic relations. They may also discuss the application of the provisions of domestic law regarding penalties, fines and interest in a manner consistent with the purposes of the Convention.

Paragraph 3 provides that the competent authorities may communicate with each other directly for the purpose of reaching agreements in accordance with this Article.

ARTICLE 25
Exchange of Information

This Article provides for the exchange of information between the competent authorities of the Contracting States for the purposes of implementing the provisions of the Convention or administering statutory provisions concerning taxes covered by the Convention. Its terms are substantially similar to the corresponding provisions of the U.S. Model.

Paragraph 1 provides that the competent authorities shall exchange such information as is necessary for carrying out the provisions of the Convention or for administering statutory provisions concerning taxes covered by the Convention provided the information can be obtained under domestic laws and administrative practices with respect to each State's own taxes. Thus, provided that the information could be obtained in administering a domestic tax covered by the Convention, the competent authorities agree to exchange such information without regard to whether there is a domestic liability in the case in question. The information furnished could relate to a tax not covered by the Convention if it is relevant to enforcing a tax which is so covered. For example, it is possible that information relating to sales taxes or estate taxes could be needed to verify an item of income or expense for income tax purposes.

Paragraph 2 provides guarantees that the information exchanged shall be kept secret and may be disclosed only to persons, including a court or administrative body, concerned with the

assessment, collection, administration or enforcement of the taxes covered by the convention or with litigation with respect to those taxes. Persons involved in the administration of taxes covered by the Convention include legislative bodies involved in the administration of taxes and their agents such as, for example, the United States General Accounting Office; therefore, information may be disclosed to them, subject to the limitations of this Article and the internal law of the respective Contracting State.

Paragraph 3 provides that neither State will furnish information to the other State under this Article if it would be contrary to its public policy to do so.

Paragraph 4 states that, when specifically requested by the competent authority of the other Contracting State, and provided that such documents could be obtained in enforcing its own taxes, copies of unedited original documents shall be provided.

In paragraph 5 the competent authorities of the two Contracting States agree to endeavor to collect taxes on behalf of the other State to the extent necessary to ensure that any exemption or reduction in rate of tax provided in the Convention is not enjoyed by persons not entitled to the benefits of the Convention.

ARTICLE 26
Diplomatic and Consular Privileges

This Article corresponds to Article 27 of the U.S. Model. It provides that the Convention shall not affect taxation privileges of diplomatic consular officials under other special agreements of international law.

ARTICLE 27
Miscellaneous

This Article provides certain miscellaneous rules of taxation under the Convention.

Paragraph 1 provides source rules. Income derived by a resident of the United States which, under the Convention, may be taxed by Australia, is deemed to have its source in Australia. Income derived by a resident of Australia which may be taxed by the United States under the Convention, other than solely by reason of citizenship or because the individual elected under U.S. law to be taxed as a resident of the United States, is deemed to have its source in the United States. With respect to U.S. citizens who are residents of Australia, to the extent that income which they derive is taxed by the United States by virtue of paragraph 3 of Article 1 (Personal Scope), such income is deemed to have its source in Australia for purposes of giving affect to paragraph 4 of Article 22 (Relief from Double Taxation).

Paragraph 2 provides that certain exemptions granted with respect to earned income by the source country, in accordance with Articles 14 (Independent Personal Services), 15

(Dependent Personal Services), 17 (Entertainers), or 19 (Governmental Remuneration), will be inapplicable to the extent that such income is not taxed by the residence country. For example, a United States resident who performs services in Australia as a self-employed person and who neither remains in Australia for 183 days nor has a fixed base in Australia, nevertheless may be taxed by Australia on the remuneration for the services performed there, notwithstanding Article 14 (Independent Personal Services), to the extent with such remuneration is exempt from U.S. income tax under section 911 of the Internal Revenue Code. The purpose of the exemption at source provided in the articles listed in this paragraph is to avoid double taxation, not to provide double exemption.

ARTICLE 28
Entry into Force

The Convention is subject to ratification in accordance with the applicable procedures of each Contracting State. The instruments of ratification will be exchanged at Washington, D.C.

The Convention enters into force on the date on which the instruments of ratification are exchanged. Its provisions take effect, with respect to dividends, interest and royalties paid, credited or otherwise derived, on or after the first day of the second month following the exchange of instruments of ratification and, with respect to all other income, for taxable years (or income years) beginning on or after the first day of the second month following the exchange of instruments of ratification.

The 1953 Convention shall cease to have effect with respect to taxes to which this Convention applies in accordance with the above provisions and shall terminate on the expiration of the last date on which it has effect.

ARTICLE 29
Termination

The Convention shall remain in force indefinitely unless terminated by one of the Contracting States. Either State may terminate the Convention after five years from the date on which it enters into force by giving at least six months prior notice through diplomatic channels. In that event, the Convention will cease to have effect with respect to dividends, interest and royalties paid, credited or otherwise derived on or after January 1 following the expiration of the six-month period and, with respect to all other income, for taxable years (or income years) beginning on or after January 1 following the expiration of the six-month period.

As an exception to those general rules, the provisions of the Convention concerning social security benefits and similar public pensions provided in paragraph 2 of Article 18 (Pensions, Annuities, Alimony and Child Support) may be terminated by either Contracting State at any time by giving prior notice to the other State through diplomatic channels.

May 24, 1983