Tax Treaty — BEAT Connection: Challenge Accepted

To the Editor:

In the article "The Debate on Treaty Application to Section 965, GILTI, and BEAT" (*Tax Notes Int'l*, May 20, 2019, p. 733), Paul Tadros and Marc Schwartz wrote, "More importantly, we would love to be enlightened as to the treaty connections to the tax imposed under the BEAT." As they say, challenge accepted.

The nondiscrimination article (generally article 24) of U.S. tax treaties includes multiple obligations. The one most relevant to the base erosion and antiabuse tax is paragraph 4:

> 4. Except where the provisions of paragraph 1 of Article 9 (Associated Enterprises), paragraph 8 of Article 11 (Interest), or paragraph 7 of Article 12 (Royalties) apply,[1] interest, royalties, and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned Contracting State. Similarly, any debts of an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable capital of the first-mentioned resident, be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned Contracting State.

The authors' A and B scenarios involve royalty payments to foreign persons subject to the BEAT in circumstances in which a payment to a U.S. person would not be — a clear violation of paragraph 4. The authors seem to think that because the BEAT does not violate paragraphs 1 or 5, it does not violate paragraph 4. That's like asking a police officer not to give you a ticket for running a red light because you were not also speeding.

Let's be clear: There is a conflict between the BEAT and the nondiscrimination obligations of (at least) U.S. tax treaties. The issue is how the later-in-time rule will apply with respect to the hastily written provisions of the 2017 tax law. I have some views on that, but to avoid muddying the waters further will leave the argument to those who have more recently done the reading. ■

Very truly yours,

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[1] This does not mean that the paragraph does not apply in every case in which there is a related-party transaction, only when those related-party transactions are not arm's-length.