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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

INCOME TAX (INTERNATIONAL AGREEMENTS) AMENDMENT BILL (NO. 2) 1980

EXPLANATORY MEMORANDUM

(Circulated by authority of the Treasurer, the Hon. John Howard, M.P.)

Introductory note

The main purpose of this Bill is to give the force of law in Australia to a revised comprehensive double taxation convention (agreement) between Australia and Canada that was signed in Canberra on 21 May 1980.

The new convention, which replaces an agreement concluded in 1957, became necessary because of changes in the tax laws of both countries, particularly in Canada, where major reforms of the tax system came into effect in 1976. On entering into force the revised convention will have effect, in broad terms, in Australia from 1 July 1975 and in Canada from 1 January 1976. However, under transitional provisions, the old agreement will continue to apply generally, in Australia, in respect of the 1979-80 and earlier income years and, in Canada, in respect of the 1980 and earlier calendar years, in cases where it would give greater relief from tax of either country than the new convention does.

The Bill specifies that interest and royalties, and income attributable to interest and royalties, derived from Canada by residents of Australia, and in respect of which the Canadian tax is limited by the terms of the convention to 15 per cent or 10 per cent, will not, by reason of the payment of that limited tax, be exempt from Australian tax. Australia will instead allow credit for the limited tax against the Australian tax on this income. As a transitional measure, because the convention is expressed to have effect from a date prior to its signature, provision is made to the effect that Australian residents deriving interest or royalties from Canada will not be disadvantaged by the changed arrangements in relation to such income derived up to and including the date of signature of the revised convention.

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The convention sets out the basis on which, and the extent to which, income derived in one country by residents of the other, is to be taxed in each country and the basis on which relief from double taxation is to be effected where income may be taxed by both countries. The main features of the revised arrangements with Canada are as follows:

- Business profits, if they are derived by a resident of one country from a branch or other "permanent establishment" in the other country, may be taxed in the latter country, otherwise they are to be taxed only in the country of residence.

- Dividends, interest and royalties will be subject to tax in the country of source, but there is a general limit on the tax that that country may charge of 15 per cent for dividends and interest and 10 per cent for royalties.

- Income from real property is taxable in full in the country in which the property is situated.

- Profits from international operations of ships and aircraft will be taxed only in the country of residence of the operator.

- Income from independent personal services will be taxed only in the country of residence of the recipient unless the income is attributable to a fixed base of the recipient in the other country.

- Income from dependent personal services, i.e., employees' remuneration, will generally be taxable in the country where the services are performed. However, where the services are performed during a short visit to one country by a resident of the other country and either the remuneration does not exceed the greater of $CAN3000 and $AUS2600, or the employer is not a resident of or a permanent establishment in the country visited, the income will be taxed only in the country of residence of the recipient.

- Government officials are to be taxed by their home country.

- Directors' fees will generally be taxed in the country of residence of the paying company.

- Income derived by public entertainers from their activities as such are to be taxed by the country in which the activities take place.

- Pensions and annuities may be taxed in the country of source, subject to a limitation of the amount of tax that may be charged.

- Professors and teachers are not the subject of a special rule, and their remuneration is to be dealt with according to the generally-applicable rules of the convention.

- A student from one country who is temporarily present in the other country solely for the purpose of receiving an education will be exempt from tax in the latter country in respect of payments made from abroad for the purposes of his or her maintenance or education.

- Dual residents of both countries are, according to specified criteria, to be treated for the purposes of the convention as being residents of only one country.

- Associated enterprises may be taxed on the basis of dealings at arm's length.

- Exchange of information and consultation between the taxation authorities of each country is authorised.

- Double taxation relief to be allowed by the country of residence in respect of income taxed in the other country will be:

  - in Australia, by allowance of credit against Australian tax for the Canadian tax on interest and royalties, where that tax is limited by the convention, and on dividends received by individuals - dividends received by Australian companies from Canada and all other categories of income received by Australian residents from Canada being freed from Australian tax by Australian tax law;

  - in Canada, broadly, by allowance of credit against Canadian tax for the Australian tax on income derived by residents of Canada from sources in Australia.

Notes on the clauses of the Bill are given below and these are followed by explanations of the articles of the convention.

Income Tax (International Agreements) Amendment Bill (No. 2) 1980

Clause 1 : Short title, etc.

This clause formally provides for the short title of the amending Act and refers to the Income Tax (International Agreements) Act 1953 as the Principal Act.

Clause 2 : Commencement

Under section 5(1A) of the Acts Interpretation Act 1901, unless the contrary intention appears, every Act is to come into operation on the twenty-eighth day after the day on which it receives the Royal Assent. By this clause the amending Act will come into operation on the day on which it receives the Royal Assent, thus enabling early implementation of the convention.

Clause 3 : Interpretation

Section 3 of the Principal Act contains a number of definitions for the more convenient interpretation of the Act. Paragraph (a) of clause 3 will effect a purely formal amendment of section 3 and paragraph (b) will ensure that the previous agreement with Canada will, to the extent that it continues to have any force, be an "agreement" to which the Act refers. Paragraphs (c) and (d) of clause 3 will insert in section 3 definitions of the new convention with Canada (which by clause 6 is being incorporated as Schedule 3 to the Principal Act, in substitution for the previous Canadian agreement) and of the 1957 agreement with Canada which it replaces.

Clause 4 : Convention with Canada

This clause provides for the force of law in Australia to be given to the new Canadian convention, and for the previous Canadian agreement to cease to have the force of law in Australia. Section 6A of the Principal Act (which gave the force of law to the previous Canadian agreement) is to be repealed by sub-clause (1) of clause 4 and a new section 6A inserted in its place. The new convention will be given the force of law with effect from the dates indicated in the agreement itself (see explanation of article 27).

By sub-section (1) of the proposed new section 6A the Canadian convention will, when the convention enters into force, have effect as regards Australian tax -

(a) in respect of dividends and interest subject to withholding tax that are derived on or after 1 July 1975;

(b) in respect of other income, for any year of income beginning on or after 1 July 1975.

Sub-section (2) of proposed new section 6A provides for the date on which the convention enters into force to be notified in the Gazette as soon as practicable thereafter. The purpose of this is to provide a readily available and authoritative source from which persons may ascertain the fact and date of entry into force of the convention. Because, under the terms of the convention, the convention will enter into force on the exchange of diplomatic notes advising that everything has been done to give the convention the force of law in Australia and in Canada, it is not possible to indicate in this Bill the date of entry into force.

Sub-section (3) of proposed new section 6A relates to paragraphs (2) and (3) of Article 27 of the new convention, which make provision for the previous Canadian agreement to continue to have the force of law in certain circumstances. Those circumstances are explained in the notes on Article 27.

Australia's double taxation agreements customarily provide that income which, under those agreements, Australia may tax in the hands of a resident of the other country, is to be deemed to have a source in Australia. No provision in such terms was included in the Canadian convention, but Article 22(2) of the convention indicates that Australia may legislate to give income derived by Canadian residents that, under the various articles of the convention, may be taxed in Australia, a source in Australia for purposes of Australia's domestic income tax law. Sub-section (4) of new section 6A will give effect to this arrangement.

Sub-clause (2) of clause 4 of the Bill will empower the Commissioner of Taxation to amend assessments for the purpose of giving effect to the new convention with Canada. It is necessary to give the Commissioner this power because, although the convention will not enter into force until an exchange of diplomatic notes has been made, its provisions will have effect - pursuant to proposed section 6A(1) - in relation to income in respect of which assessments may have already been made.

Clause 5 : Provisions relating to certain income derived from sources in certain countries

The primary purpose of this clause is to apply the credit method of relief of double taxation to interest and royalties that are derived by residents of Australia from Canada and in respect of which, under the convention, Canadian tax is limited. Section 12 of the Principal Act, which is to be amended by this clause, already achieves a corresponding result for interest and royalties derived by residents of Australia from countries with which Australia has concluded comprehensive double taxation agreements which limit the foreign tax on such income.

Section 23(q) of the Income Tax Assessment Act 1936 confers relief from double taxation in the form of an exemption from Australian tax for foreign source income (other than dividends) of Australian residents that is taxed (not exempt from tax) in the country of source. Section 12 of the Principal Act gives effect to a policy that this exemption method of relief is not to apply to interest or royalties derived (either directly or through a trustee) from another country where the double taxation agreement with that country limits the tax it may charge. Once the exempting provision is, by section 12, made inapplicable, interest and royalties that are taxed in the other country become assessable income for the general purposes of the Income Tax Assessment Act, but the agreement in each case requires Australia to credit against its tax the limited tax of the other country. Sections 14 and 15 of the Principal Act govern the allowance of the credit.

Clause 5 will apply this policy to interest and royalties derived by Australian residents from Canada after the commencement of the year of income to which the convention is to apply. Article 23 is the relevant credit article in the convention. Paragraph (a) of clause 5(1) will effect a formal drafting amendment consequent upon the addition to section 12(1) of the Principal Act of new paragraph (aj).

Paragraph (b) of the sub-clause will insert the new paragraph in section 12(1) of the Principal Act. This section formally sets out classes of income to which the exemption under section 23(q) of the Income Tax Assessment Act is not to apply.

The new paragraph (aj) will ensure that interest or royalties derived from Canada by a resident of Australia, the Canadian tax on which is limited under the convention to 15 or 10 per cent, will not be exempt from Australian tax.

Paragraph (aj) will apply to income derived in years of income commencing on or after 1 July 1975. Where a Canadian trust estate derives income such as interest or royalties, Canada treats a non-resident beneficially entitled to a share of that income as having derived income from the trust estate rather than as having derived a share of the interest or royalties derived by the trust estate. Under Article 21(3) of the convention, Canada will limit its tax to 15 per cent of the gross amount of such income derived by a resident of Australia provided the income is subject to tax in Australia. The reference in new paragraph (aj) to paragraph (3) of Article 21 of the Canadian convention will thus mean that income derived by an Australian beneficiary that is attributable to interest or royalties derived by a Canadian trust estate will, like such income attributable to interest or royalties derived from trust estates in other countries

with which Australia has double taxation agreements limiting the source country tax on interest and royalties, be taxed in Australia (and so subject to limited Canadian tax) with credit being allowed against the Australian tax for the limited Canadian tax on the income.

Sub-clause (2) of clause 5 is designed to avoid any retrospective increase in overall tax liability that might result from the application of the credit method of double taxation relief to interest or royalty income derived from Canada by Australian residents after the commencement of the 1975-76 income year, but on or before the date of announcement of signature of the convention on 21 May 1980. When signature of this convention was announced, it was indicated that the credit method of relief was to be applied to this income. This sub-clause will mean, in effect, that any increase in the Australian tax payable in respect of such interest or royalty income, resulting from the change from the exemption system to the credit system, is not to exceed the amount by which Canadian tax on the income is reduced by reason of the convention.

Sub-clause (3) of clause 5 has a similar purpose to that of clause 4(2) of the Bill. It will empower the Commissioner to amend assessments that have already issued, to apply the credit method of double taxation relief in accordance with sub-clauses (1) and (2) as regards interest and royalties from Canada.

Clause 6 : Schedule 3

This clause will replace the present Schedule 3 to the Principal Act (a copy of the 1957 agreement with Canada) by a new Schedule 3 (a copy of the new convention with Canada).

Convention with Canada

This convention corresponds closely with other modern comprehensive double taxation agreements to which Australia is a party. The country of source is generally allocated the right to tax income arising there (sometimes at limited rates) while in particular situations the country of residence of the recipient of income is given the sole right to tax. The relief from double taxation of classes of income taxable in both countries is assured by provisions in the convention which require the country of residence to give credit against its own tax for the tax of the country of source, or other comparable relief.

Article 1 : Personal Scope

The convention will apply to persons (which term includes companies) who are residents of Australia or Canada.

The situation of persons who are residents of both countries (i.e., dual residents) is dealt with in Article 4.

Article 2 : Taxes Covered

This article specifies the existing (Federal) income taxes of each country to which the convention is to apply. The article will automatically extend the application of the convention to any identical or substantially similar taxes that are later imposed by either country.

Article 3 : General Definitions

This article defines a number of the terms used in the convention. Definitions of some other terms are contained in the articles to which they relate and terms not defined in the convention are to have the meaning which they have under the taxation law of the country applying the convention.

As with Australia's other modern double taxation agreements, "Australia" is defined as including external territories and areas of the continental shelf. "Australia" as defined in the previous Canadian agreement did not include the continental shelf, the area of which had not been specified when that agreement was made. By virtue of this definition, Australia retains taxing rights in relation to mineral exploration and mining activities on its continental shelf. The definition also has relevance to Australian taxation of shipping and airline profits under Article 8 of the convention.

Article 4 : Residence

This article sets out the basis on which the residential status of a person is to be determined for the purpose of the convention. Residential status is one of the

criteria for determining taxing rights, and the provision of relief under the convention. As in the previous Canadian agreement, residence according to each country's taxation law provides the basic test. The article provides rules for determining how residency is to be allocated to one or other of the countries for the purposes of the convention where a taxpayer - whether an individual, a company or other entity - is regarded as a resident under both countries' domestic laws. Such rules were not provided in the previous Canadian agreement with the result that dual residents were denied the benefits of the agreement.

Article 5 : Permanent Establishment

The application of various provisions of the convention (principally Article 7) is dependent upon whether a resident of one country has a "permanent establishment" in the other, and if so, whether income the person derives in the other country is attributable to the "permanent establishment". The definition of the term "permanent establishment" which this article embodies corresponds closely with definitions of the term in Australia's other double taxation agreements.

The primary meaning of the defined term is stated in paragraph (1) as being a fixed place of business through which the business of an enterprise is wholly or partly carried on. Other paragraphs of the article are concerned with giving examples of what constitutes a permanent establishment - such as an office, a factory or a mine - and defining the circumstances in which a resident of one country shall, or shall not, be deemed to have a "permanent establishment" in the other country.

Article 6 : Income from Real Property

By this article, provisions equivalent to which were not included in the previous Canadian agreement, income from real property, including royalties and other payments in respect of the operation of mines or quarries or the exploitation of any natural resources, may be taxed in the country in which the property is situated.

The scope of what is meant by "income from real property" is extended by paragraph (2) of the article to include income from any direct interest in or over land, the interest in effect being deemed to be situated in the country in which the land to which the interest relates is situated.

Income to which this article applies is specifically excluded from the scope of Article 7 (by paragraph (6) of that article) and is therefore taxable in the country of source, regardless of whether or not the recipient has a "permanent establishment" in that country.

Article 7 : Business Profits

This article sets out the general basis of taxation of business profits derived from sources in one country by a resident of the other. Broadly, the country of source will be able to tax the profits of an enterprise resident in the other country only if they are attributable to a permanent establishment through which that enterprise carries on business in the country of source. If they are not, the profits will be taxed only in the country of residence of the taxpayer.

Article 7 has practical effect comparable with the corresponding article in the previous Canadian agreement and those in Australia's other double taxation agreements. As under those agreements, the article provides for an arm's length basis to be applied in ascertaining the amount of profits fairly attributable to a permanent establishment.

Paragraph (5) of the article allows the application of provisions of the source country's domestic law where there is insufficient information available to determine the profits of a permanent establishment on the basis of arm's length dealing, while paragraph (7) preserves the application of the special provisions in each country's domestic law relating to the taxation of income from a business of any form of insurance.

Article 8 : Shipping and Air Transport

Under this article the right to tax profits from the operation of ships or aircraft in international traffic, including profits received through participation in a pool service, in a joint transport operating organisation or in an international operating agency, is reserved to the country of residence of the operator. This is broadly comparable with the provisions of the previous Canadian agreement.

Any profits derived by a resident of one country from internal traffic in the other country may be taxed in that other country. By reason of the definition of "Australia" in Article 3 and the terms of paragraph (4) of Article 8, any shipments by air or sea from a place in Australia to another place in Australia, its continental shelf or external territories are to be treated as forming part of internal traffic.

Article 9 : Associated Enterprises

This article, like the corresponding article in the previous Canadian agreement, authorises the re-allocation, on an arm's length basis, of profits between associated enterprises where the commercial or financial arrangements between them are different from those that might be expected to exist between independent enterprises.

If a re-allocation of profits were effected in one of the countries and the profits of an enterprise of that country were adjusted upwards, a form of double taxation would arise if the profits so re-allocated remained subject to tax in the hands of an associated enterprise in the other country. Paragraph (3) requires the other country concerned to make an appropriate adjustment in these circumstances with a view to relieving any such double taxation. The previous Canadian agreement did not provide for such an adjustment. Paragraph (4) limits the period within which the other country is required to make an adjustment in accordance with paragraph (3) to six years from the end of the year of income or taxation year in respect of which the profits to which the adjustment would relate have been charged to tax.

Article 10 : Dividends

The broad scheme of this article, which is basically to the same effect as the corresponding provisions in the previous Canadian agreement, is to generally limit to 15 per cent of the gross amount of dividends the tax that the country of source may impose on dividends payable to shareholders resident in the other country. Under this article Australia will limit its rate of withholding tax on dividends paid to residents of Canada to 15 per cent (instead of the 30 per cent applicable under domestic law), while Canada will limit its withholding tax on dividends paid to Australian residents to 15 per cent (25 per cent under Canadian domestic law).

Paragraph (3) is a provision which ensures, broadly, that one country will not tax dividends paid by a company resident solely in the other country unless the person deriving the dividend is a resident of the first country or the holding giving rise to the dividends is effectively connected with a "permanent establishment" or "fixed base" in that country.

Paragraph (5) of Article 10 ensures that the country of source will remain free to impose its normal rate of tax where the holding giving rise to the dividends is effectively connected with a "permanent establishment" or "fixed base" that the recipient has in that country. In such a case the dividends will be treated as business profits subject to the provisions of Article 7 or taxable in accordance with Article 14 (Independent Personal Services).

Paragraphs (6) and (7) preserve the right of each country to impose the "branch profits" taxes provided for under their domestic laws.

Article 11 : Interest

This article, provisions equivalent to which were not included in the previous Canadian agreement, requires the country of source generally to limit its tax on interest income derived by residents of the other country to 15 per cent of the gross amount of the interest. This rate limitation will not affect the Australian withholding tax rate of 10 per cent which will continue to be imposed in respect of interest payments to Canadian residents.

By paragraph (4), the 15 per cent limitation does not apply where the person deriving the interest has in the country of source a "permanent establishment" or "fixed base" with which the indebtedness giving rise to the interest is effectively connected. In such a case the provisions of Articles 7 or 14 apply. A general safeguard is contained in paragraph (6) against payments of excessive interest - in cases where there is a special relationship between the persons associated with a loan transaction - which restricts the 15 per cent limitation in such cases to an amount of interest which might be expected to have been agreed upon by persons dealing at arm's length.

Article 12 : Royalties

In Australia, gross royalties (other than film and video tape royalties) paid to non-residents, as reduced by allowable expenses, are, in the absence of provisions to the contrary in a double taxation agreement, taxed by assessment at ordinary rates of tax. In Canada the basic rate of a withholding tax on royalties paid to non-residents is 25 per cent of the gross royalties. The previous Canadian agreement exempted, in specified circumstances, certain cultural royalties from source country taxation but did not include any specific provisions relating to other royalties.

This article requires the country of source generally to limit its tax on royalties derived by residents of the other country to 10 per cent of the gross royalties. The 10 per cent limitation is not to apply to natural resource royalties, which, in accordance with Article 6, are to remain taxable in the country of source without limitation of the tax that may be imposed.

As in the case of dividends and interest, it is specified in paragraph (4) that the 10 per cent limitation of tax in the country of source is not to apply to royalties effectively connected with a "permanent establishment" or "fixed base" in that country.

Where royalties are paid by a person not independent of the payee, paragraph (6) requires that the 10 per cent limitation on the source country's tax will not apply to any amount of the royalty that is in excess of what might be expected to have been agreed upon by independent persons acting at arm's length.

Article 13 : Alienation of Property

This article is to the effect that income from the alienation of real property or of a direct interest in or over land, or of a right to exploit or to explore for a natural resource may be taxed in the country in which the real property, land or natural resource is situated. In Australia it will only apply to amounts that are income for taxation purposes, e.g., profits from the sale of Australian real estate purchased for the purpose of re-sale at a profit.

Article 14 : Independent Personal Services

A provision corresponding to this article was not included in the previous Canadian agreement, which treated independent personal services in the same way as dependent personal services.

The article, which is the same in effect as corresponding provisions in Australia's modern agreements, provides that an individual resident in Australia or in Canada will be subject to tax only in the country of residence on remuneration derived from the performance in the other country of professional services or other similar independent activities unless the person has a "fixed base" regularly available in the other country for the purpose of performing his or her activities. If the person has such a fixed base and the remuneration is attributable to activities exercised from it, the remuneration may be taxed in the other country.

Article 15 : Dependent Personal Services

This article sets out the basis for taxing remuneration derived by visiting employees. As in the previous Canadian agreement and in Australia's agreements with other countries, a resident of one country will generally be taxed in the other country on wages and other similar remuneration from an employment where the services are rendered during a visit to the other country but, subject to specified conditions, there is an exemption from this rule for short-term visitors which, when it applies, provides an exemption from the tax of the country being visited. The conditions for exemption correspond with those in Australia's other agreements, that is, in broad terms, that the visit not exceed 183 days in the year of income and the remuneration not be paid by a resident of or permanent establishment in the country visited. Unlike Australia's other agreements, however, this article provides for exemption of earnings during a short-term visit even if they are paid by a resident of or permanent establishment in the country visited, provided they do not exceed $CAN3,000 or $AUS2,600 (or those amounts as varied by agreement between the Australian Treasurer and the Canadian Minister of National Revenue) in the year of income.

The article also permits income from an employment exercised aboard a ship or aircraft operated in international traffic to be taxed in the country of residence of the operator.

Article 16 : Directors' Fees

This article relates to remuneration received by a resident of one country from a company resident in the other country in his capacity as a director of that company. To avoid difficulties in such cases in ascertaining in which country a director's services are performed, and the remuneration is to be taxed, the article indicates that the remuneration may be taxed in the country of residence of the company.

Article 17 : Entertainers

By this article income derived by visiting entertainers (including athletes) from their personal activities as such are to be taxed in the country in which the activities are exercised, no matter how short their visit to that country. This is the same as the result achieved by the provisions of the previous Canadian agreement.

The new article also contains a safeguard against attempts by entertainers to circumvent its general purpose by, e.g., having fees paid to a separate enterprise which the performer controls, and which formally provides his or her services. In such a case, the profits of the enterprise from the provision of the services of the entertainer may be taxed in the country in which the entertainer performs, whether or not that enterprise has a "permanent establishment" in that country, but only if the entertainer or persons related to the entertainer participate directly or indirectly in the profits of the enterprise.

Article 18 : Pensions and Annuities

Unlike the corresponding provisions in the previous Canadian agreement and those in Australia's agreements with other countries - which are to the effect, broadly, that pensions and annuities are to be taxed only in the country of residence of the recipient - this article provides for limited taxation rights for the country of source in respect of pensions paid to residents of the other country. The source country may levy tax of up to 15 per cent of the pension or annuity received in a year, but the pensioner is not to pay more tax on the pension than would have been payable if he or she had been a resident of the country in which the pension or annuity arose.

In order to avoid a form of double taxation arising from the different bases of taxing alimony and maintenance payments in the two countries, paragraph (3) of the article

introduces a new rule that such payments arising in one country and paid to a resident of the other are to be taxed only in the country in which they arise.

Article 19 : Government Service

By this article, which is the same in practical effect as the corresponding provisions of the previous Canadian agreement, remuneration, other than a pension or annuity, in respect of services rendered to a government (including a State or local government) of one of the countries will be taxed only by that country, unless the remuneration is paid in respect of services rendered in the other country and the recipient is, in broad terms, a citizen of, or ordinarily resident in, that country. In that case it will be taxed only by the other country. These provisions do not apply, however, where the services are rendered in connection with a trade or business carried on by a government.

Article 20 : Students

This article, provisions corresponding to which were not included in the previous Canadian agreement, applies to students resident in one of the countries who are temporarily present in the other country solely for the purpose of their education. In these circumstances, a student will be exempt from the tax of the country visited in respect of payments made from abroad for the purposes of his or her maintenance or education.

Article 21 : Income Not Expressly Mentioned

This article provides rules for the allocation between the two countries of taxing rights in relation to items of income not expressly mentioned in the preceding articles of the convention, for example, income arising in a third country.

The general rule is that any such income is to be taxed only by the country of residence of the recipient. Where a resident of one country derives such income from sources in the other country the country of source may also tax the income.

Where a non-resident of Canada is beneficially entitled to a share of, e.g., interest income derived by a Canadian trust estate, Canada taxes the non-resident beneficiary on the income as income from the trust estate rather than as a share of the interest income derived by the trust estate. Accordingly, in the case of income derived from a trust resident in Canada by a resident of Australia, this article, rather than the articles that apply to specific classes of income, provides for the Canadian tax to be limited to 15 per cent of the gross income, provided it is subject to tax in Australia. Paragraph (4) ensures that Canada will remain free

to impose its normal rate of tax where the right or interest in the trust in respect of which the income is paid is effectively connected with a "permanent establishment" or "fixed base" that the Australian recipient has in that country.

Article 22 : Source of Income

This article specifies that Australia may for the purpose of ensuring that it is empowered to exercise the taxing rights assigned to it by the convention over income derived by residents of Canada, provide in its domestic law that the income concerned is to be deemed to have a source in Australia. (See also the notes on clause 4(1).). It eliminates any question of income not having, by domestic law rules, a source in Australia where Australia is, by the convention, entitled to tax that income in the hands of a resident of Canada. It also ensures that the country of residence will, as the convention intends, give double taxation relief in respect of tax levied by the country of source pursuant to the rights assigned to it by the convention.

Article 23 : Elimination of Double Taxation

Double taxation does not arise in respect of income flowing between the two countries where the terms of the convention provide for the income to be taxed only in one country or the other, or where the domestic taxation law of one of the countries frees the income from its tax. It is necessary, however, to prescribe a method for relieving double taxation in respect of other classes of income subject to tax in both countries. Australia's other double taxation agreements provide for a credit basis for the relief of double taxation to be applied by Australia and, usually, the other country. In these cases the country of residence is required to give credit against its tax for tax of the country of source. This approach was adopted in the previous Canadian agreement and has been adopted in this convention.

When the Income Tax Assessment Act and the Income Tax (International Agreements) Act (as amended by the present Bill) are read together, the measures that will operate to relieve double taxation of income derived from Canada by Australian residents are as follows. Australia will allow credit for the Canadian tax on dividends derived by individuals from Canada and on interest and royalties derived by individuals and companies in respect of which the tax of Canada is limited by Articles 11 and 12 or, where the income is attributable to interest or royalties derived by a Canadian trust estate to which a resident of Australia is beneficially entitled, by Article 21. Section 46 of the Income Tax Assessment Act will continue to free from Australian tax dividends that are derived from Canada by Australian resident companies.

For its part Canada will, broadly, allow a credit to Canadian residents, in respect of taxes paid in Australia on

their Australian source income, against the Canadian tax payable on that income. A Canadian company with an affiliated Australian subsidiary will be allowed a deduction against its income of any dividend received by it out of what, under Canadian tax law, is the exempt surplus of the affiliated Australian subsidiary.

Article 24 : Mutual Agreement Procedure

One of the purposes of this article is to provide for the taxation authorities of the two countries to consult with a view to reaching a satisfactory solution where a taxpayer is able to demonstrate actual or potential subjection to taxation contrary to the provisions of the convention.

The other main object of the article is to authorise consultation between the taxation authorities of the two countries for the purpose of resolving any difficulties regarding the application of the convention and to give effect to it.

Article 25 : Exchange of Information

This article, which is along the lines of provisions in Australia's other modern agreements, authorises the exchange, between the two taxation authorities, of information necessary for the carrying out of the convention or of domestic laws concerning the taxes to which the convention applies. This will permit a wider exchange of information than the corresponding provision in the previous Canadian agreement. The restrictions which the article contains in relation to the purposes for which this information may be used and the persons to whom it may be disclosed are along lines usual in double taxation agreements. The article does not permit the exchange of information that would disclose any trade, business, industrial, commercial or professional secret or trade process or which would be contrary to public policy.

Article 26 : Diplomatic and Consular Officials

The purpose of this article is to ensure that members of diplomatic and consular posts will, under the provisions of the convention, receive no less favourable treatment than that to which they are entitled in accordance with international law. In Australia, fiscal privileges are conferred on such persons by the Diplomatic (Privileges and Immunities) Act and the Consular (Privileges and Immunities) Act.

The article also includes a safeguard to ensure that the benefits of the convention shall not apply to international organisations, to organisations or officials thereof, or the diplomatic or consular staff of a third country who, although present in one of the countries, are not treated for income tax purposes in the same manner as residents of either country.

Article 27 : Entry into Force

This article provides for the entry into force of the convention. This will be on the date on which notes are exchanged through the diplomatic channel notifying that the last of all such things has been done in Australia and Canada as is necessary to give the convention the force of law in both countries.

Once the convention enters into force it will have effect in Australia, for purposes of withholding tax, as from 1 July 1975. In respect of tax other than withholding tax, it will have effect in Australia as from 1 July 1975, although where a taxpayer has adopted an accounting period ending on a date other than 30 June, the beginning of the accounting period that has been substituted for the year which began on 1 July 1975 will be the date from which the convention takes effect. In Canada, the convention will have effect, in respect of tax withheld at the source, in relation to income paid or credited as from 1 January 1976. In respect of other Canadian tax it will have effect in Canada for taxation years beginning on or after 1 January 1976.

The article also makes provision for the previous Canadian agreement to cease to have effect in relation to taxes in respect of which the convention comes into effect. However, under transitional provisions in paragraph (3), the previous Canadian agreement will continue to have effect in Australia, in respect of the 1979-80 and earlier income years and, in Canada, in respect of the 1980 and earlier calendar years, in cases where it would give a greater relief from tax of either country than the convention does.

An example of circumstances in which Article 27(3) will apply is provided by the effect of the previous agreement and of this convention on cultural royalties. Under the 1957 agreement (Article IX) a taxpayer resident in one country is exempt from tax in the other country on certain cultural royalties having a source there. By contrast, the convention allows the country of source to tax the royalties, its tax being limited to 10 per cent. Another example relates to the taxation of teachers resident in one country who visit the other country for the purpose of teaching there. Under Article XII of the 1957 agreement, this income was not subject to tax in the country visited, but there is no equivalent article in the convention and taxation of the remuneration of visiting teachers will be governed by the other articles of the convention. But for Article 27(3) the provisions of the convention would have effect from the dates specified in paragraph (1) even though the provisions of the previous agreement would, in relation to the tax of the country concerned, have been more beneficial to the taxpayer.

Article 28 : Termination

This article declares that the convention is to continue in effect indefinitely but either country may give notice of termination on or before 30 June in any calendar year after the year 1983. In that event, the convention would cease to be effective in Australia, for withholding tax purposes, as from 1 July in the calendar year following the year in which notice of termination is given. In respect of tax other than withholding tax, it would cease to be effective in Australia from the beginning of the income year commencing in that next calendar year.

In Canada, the convention would cease to be effective, in respect of tax withheld at the source, as from 1 January in the second calendar year next following the year in which notice of termination is given. In respect of other Canadian tax, it would cease to be effective for any taxation year beginning on or after 1 January in the second calendar year next following that in which notice of termination is given.

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