Is the Saving Clause A Wolf in Sheep’s Clothes:
An Interdisciplinary Study from Legal and Economics Aspects on Article 1(3) of the OECD MC 2017

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Abstract
Art. 1(3) OECD MC 2017, the “saving clause”, was initially proposed to safeguard tax treaties from being abused to prevent the application of domestic anti-avoidance rules. However, the provision is drafted in such a general and neutral way, which raises doubts on its efficiency and proportionality. This research investigates the saving clause from legal and economics aspects to explore the mechanism, legal consequences and practical impact on states policy inclination and taxpayers’ welfare and behaviours.

Introduction
● The compatibility of national anti-avoidance rules to tax treaty obligations has been discussed by the OECD as early as 1998 → Lack of Certainty.
● To prevent treaties to be abused to circumvent the application of domestic anti-abuse rules, the OECD incorporated a new Art. 1(3) into its model convention (2017), which reads: “This Convention shall not affect the taxation, by a Contracting State, of its residents except with respect to the benefits granted under paragraph 3 of Article 7, paragraph 2 of Article 9 and Articles 20, 23 [A] [B], 24, 25 and 28.”
● The Art. 11 MLI purports to incorporate the saving clause into existing treaty network, but…

Signatories’ Position to Art. 11 MLI

- Signatories that accept the saving clause
- Signatories that reserve the saving clause (Art. 11(3)a)
- Signatories that apply the saving clause to some of its treaties (Art. 11(3)b)

Research Questions – Legal Study
The first part conducts a standard legal analysis to the provision:

1) Interpretation of the provision: the object and purpose, the scope, legal consequences of its application, and interaction with other treaty provisions.
2) Whether the rule is an effective and efficient tool to achieve its original purpose, namely, to reconcile the application of national anti-avoidance/abuse rules with tax treaty obligations;
3) Whether the saving clause overshoots its target and/or causes disproportionate/ latent unintended consequences:
⇒ Regarding income attribution conflicts, the rule converges the solutions to juridical double taxation and economic double taxation, which is not fully set in the Partnership Report (1999) by OECD:

⇒ The rule opens a backdoor to rules departing from conventional norms to allocate taxing right, e.g., the GLoBE proposal under Pilar II?

4) Whether the provision is coherent with the collective intention of both parties or extra carve-outs to the provision’s ambit is needed so that its application does not go beyond what was agreed by both parties?

Research Questions – Economics Study
(1) How do contracting states react to new policy options provided by the saving clause?
⇒ Necessarily reach the prisoner’s dilemma or not?
Relax assumptions under the 2*2 game, e.g., number of strategies, various distribution of bargaining power.
(2) How do taxpayers react to different policy options of the contracting states in terms of, e.g., decision on location and/or legal forms of business?

Conclusions To Date
● The US saving clause is of very limited value to interpret the OECD saving clause in the light of significant differences in their objects and context.
● In combination with revised Art. 23A/B(1), applying the saving clause to certain extent eliminates legal uncertainties in income attribution conflicts at the price of unrelieved double taxation.
● The saving clause is far from an ideal master key to reconcile rules such as that of the GLoBE proposal to current tax treaty network.

Open for Discussion
- Economic double taxation stems from tax system disparities among jurisdictions, but application of the saving clause is the "last step" before reaching economic double taxation consequence. Whether/to what extent tax treaties should be responsible for this result?
- Solving economic double taxation requires not only restricting taxing right but also (to some extent) harmonising national tax law. Whether it is a proper time now to reconsider the function of tax treaties in such as highly digitalised and globalised era?

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