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Concept of “Beneficial Ownership” in OECD and Chinese Tax Law

similarity and difference

by

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Contents

Abstract

The term of Beneficial Ownership is a widely recognized term in international double tax treaties for the purpose of preventing tax evasion and avoidance regarding the cross-border payments of dividends, interests and royalties. OECD model is the most commonly used tax model for countries negotiating and conclusion the tax treaties. However, over the past half decades of OECD model's progress, there is no clear definition of Beneficial Ownership and countries have developed various interpretation based on their own judicial practice. In 2017, the latest OECD tax model has been released by taking into consideration of BEPS Action Plan.

China has been developed this concept since 2009 in the context of domestic law and in 2018, the Announcement 9 was released and be valid till today.

In this paper, a briefly overview of the development of the Beneficial Ownership concept under the context of both OCED model and China domestic law will be conducted, to compare the similarities and differences under the two models. Besides, some recommendations will also be made based on the observation of the comparison.

Keywords: Beneficial Ownership, tax treaty, tax benefit, OECD, BEPS, China

Preface

I would like to express my sincerest gratitude to my supervisor Sigrid Hemels for her support and guidance through each stage of my master thesis. Further, I am deeply grateful to Cécile Brokelind for her inspirational and innovative insights brought to me during this whole master programme. I am also thankful to all the professors, lecturers and fellow students that make my academic journey in Lund University memorable and meaningful.

Lastly, I'd wish to thank my parents for their unconditional love and support, and my friends for the continuous encouragement.

Abbreviations

BEPS	Base Erosion and Profit Shifting
BO	Beneficial Owner / Beneficial Ownership
DTT	Double Taxation Treaty
GAAR	General Anti-Avoidance Rules
LOB	Limitation on Benefit
MLI	Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting
OECD	Organization for Economic Co-operation and Development
OECD MTC	OECD Model Tax Convention on Income and on Capital
PPT	Principal Purpose Test
SAAR	Specific Anti-Avoidance Rules
SAT	State Administration of Taxation, People's Republic of China
SPV	Special Purpose Vehicle
UK	United Kingdom
UN	United Nations
WHT	Withholding Tax
WTO	World Trade Organisation

1 . Introduction

1.1 Background

The concept of "Beneficial Ownership" ("BO") nowadays is a term widely adopted in international tax law, which is used to determine the actual beneficiaries of passive income such as dividends, interest, royalties, e.g. the source state agrees to enjoy treaty benefit and offer reduced withholding tax ("WHT") rate on those income if the recipient of certain income is qualified as the BO of the captioned income. But ever since its first introduction to Organization for Economic Cooperation and Development ("OECD") Model Tax Convention ("MTC") in 1977, there is no clear definition of the term being offered in the different versions of OECD MTC and Commentaries, which leads to a continuously discussion topic over the past 50 years.

OECD Commentaries link the BO with anti-double taxation and prevention of tax evasion and avoidance and the concept of BO has been used to prevent the misuse of preferential tax treaty.

Treaty abuse refers to person's indirectly taking advantage of treaty benefits between the two jurisdictions without being a resident of one of these jurisdictions. According to OECD website,[1] the issue of treaty abuse is increasing over the past years and cause significant loss of tax revenue.

Since 2013, OECD has started the BEPS project and set out 15 Action Plans in 2015, aiming to dealing with the issue of double non-taxation and tax avoidance. To facilitate the implementation of these BEPS outcome, a multilateral agreement ("MLI") which includes Action 6 (rule of treaty abuse) was issued.

By end of December 2023, China had formally concluded 111 double taxation treaties, two double taxation arrangements with Hong Kong and Macau, one strengthen tax cooperation agreement with Taiwan, and ten tax information exchange agreements.[2] Using OECD MTC as guidance and reference, the term of BO has been widely recognized and be used in the article of dividends, interests and royalties of double taxation treaties concluded between China and other tax jurisdictions. In some tax treaties, a lower WHT rates on dividends, interests and royalties are entitled to the qualified BO.

With no clear definition provided by OECD, over the last 15 years, Chinese central tax authority has issued a series of domestic circulars and rules, to define and interpret the concept of BO. In the same time, China has also been an active participate in BEPS project and signed the MLI in 2017.

[1] OECD website, http://www.oecd.org/tax/beps/about/

[2] SAT statistics, available at https://www.chinatax.gov.cn/chinatax/n810341/n810770/index.html

1.2 Purpose and research questions

This master thesis briefly reviews the evolution of BO concept in the context of OECD MTC, Commentary and implementation of BEPS project as well as the interpretation of BO concept under Chinese tax law framework and in the post-BEPS era.

By comparison the latest BO concept under two legal contexts (OECD and China), it aims to discuss the similarities, difference and impacts that OECD/BEPS have brought to China's BO concept. What is more, through comparison, we understand the concerns and question that still lie in the concept of BO and possible solutions to it.

1.3 Delimitations

There shall not be a comprehensive go through of the historical development of BO concept under OECD model as there are plenty of literatures available in this field.

Besides OECD MTC, there is another tax model, namely United Nations ("UN") MTC, also being commonly used as a guidance for countries negotiating double tax treaties. Since China started its very first tax treaty negotiations with several OECD member states, naturally the OECD MTC was used as a reference and China nowadays still work closely with OECD. For China, the OECD model is more relevant rather than UN model. Therefore, the UN MTC shall not be discussed in this thesis.

1.4 Methods and materials

This thesis use doctrine in law legal research method.

An introduction in the evolution in the OECD MTC are presented by studying the sources of law. Besides, the commentaries to the OECD MTC are also addressed when interpreting the relevant articles in the OECD MTC. The aim is to have an analysis of the concept's definition and content. In the context of the implementation of BEPS Action 6, MLI and the principal purposes rule and its interaction with beneficial ownership are explored.

Literature research and cases analysis are also used to sort out the way of China's identification of BO under existence of unique Chinese institutional system, by comparing with the latest OECD MTC and BEPS principle in same context. BO in China domestic law context are discussed briefly as this contribution is centred on BO in tax treaties.

The methods include studying the legal material (including historical and latest OECD MTC and Commentaries, double taxation treaties, domestic tax laws and circulars, case-laws, authorities and organization websites, etc.) and its argumentation and reasoning, when applicable.

China domestic laws and circulars and cases are published by authorities in Chinese language only. The English translation quoted in this thesis may contain certain level of deviation from the original intention. In this regard, based on its original intention, I will try to use similar legal and tax language to explain the laws and cases as much as possible, to avoid ambiguity or misunderstanding.

1.5 Outline

In Section 2, I present an overview of the progress of BO concept in OECD model through literature review and case-law analysis. In Section 3, the origin, development and present status of BO concept in China are discussed. In Section 4, there is a comparison between the concept under OECD model and China tax context by showing the major similarities and differences. Further in Section 5, with the comparison of OECD framework, the shortfalls of the application of certain concept in the prevailing China tax law system are discussed and some suggestions for improvements are provided as well. Last but not least in Section 6, is the conclusion of this thesis.

2 . Overview of BO concept under OECD / BEPS

2.1 BO concept under OECD MTC and Commentaries

When dealing with international trade or investment, it is common to have cross-border payments that entity resides in State A ("residence state") receives income originated from State B ("source state") and both states may levy tax on the same income under each's own domestic tax law regime.[3] For example, the recipient is liable to its world-wide income in the residence state based on the universality principle while a WHT on the same income is also levied in the source state based on the territory principle.

To avoid or mitigate such double taxation on same income in different states, many states use a bilateral/multilateral agreement called double taxation treaty for limiting and binding the tax rights between the contracting states.[4] Generally, the state of source offers a limited or reduced WHT rate to be levied on certain income, which is also known as treaty benefit.

However, such treaty benefit has been abused as a tax planning method, i.e. an intermediate company in the third state is used for receiving the income from source state in form of dividend, interest or royalty, to enjoy the lower WHT rate of the tax treaty between the source state and third state. This obviously violates the original purpose and objects of tax treaty.

The concept of BO in tax treaty was firstly referred in a 1966 supplementary treaty protocol of United Kingdom - United States tax treaty (1945),[5] which emphasized that the tax relief in the country of source shall be determined based on whether income of dividends, interests and royalties were beneficially owned by a resident in other country.[6]

Later on, to cope with the situation of obtaining improper tax benefits, the term "beneficial owner", was introduced into the Article 10 (dividend), Article 11 (interest) and Article 12 (royalty) of OECD MTC in 1977, as a result of several rounds of discussions by OECD Working Parties, to limit the scope of entitlement of treaty benefit. Referring to those historical OECD materials, the term of BO was used for denying the reduced WHT rate to intermediate who had a minimal legal right to certain income such as agents and nominees.[7] The 1980 UN MTC also introduce the concept of BO for the same intention. However, instead of offering a

[3] M. Lang, Introduction to the Law of Double Taxation Conventions (3rd edition), 2021, chapter 1.1.

[4] M. Lang, Introduction to the Law of Double Taxation Conventions (3rd edition), 2021, chapter 3.1.

[5] J. Avery Jones, The United Kingdom's Influence on the OECD Model Tax Convention, 2011, p678.

[6] C. Du Toit, The Evolution of the Term "Beneficial Ownership" in Relation to International Taxation over the Past 45 Years, 2010, Sec. 3.2.1.

[7] J.J.M. Janssen & M.Sada Garibay, What Should Be the Scope of the Beneficial Owner, 2020, p.1089.

clear definition or some criteria of BO, the OECD Commentaries only provided a list of examples (i.e. agent and nominee) which were NOT be considered as BO.

The 2003 OECD MTC Commentaries to Article 10, Article 11 and Article 12 has adopted ideas from "The Double Taxation Convention and The Use of Conduit Companies Report" issued by OECD in 1986, i.e. conduit structures "as a practical matter" with "very narrow powers" became an example being excluded from getting treaty benefits. Different from legal approach, it was the first time that the substance-over-form / economic substance principle be introduced in OECD MTC and later versions. Besides, the concept of BO has also been substantially expanded under this version of OECD MTC Commentaries, i.e., the BO should not just be explained from technical perspective, but in light of the object and purposes of the convention (that is anti-double taxation and prevention of tax evasion and avoidance).[8] Here, the article of BO is used to reject the treaty benefits (i.e. the elimination or reduction of the WHT on sourced income) that non-treaty benefits country tax payer intends to obtain through certain intentionally arranged legal structure.[9]

Since the introduction of BO concept into OECD MTC, OECD continuously revising the relevant provisions to provide better interpretation. In 2011 and 2012, OECD further released public draft discussion report for receiving comments and proposals from different parties regarding the meaning of BO,[10] which eventually leads to the updates of 2014 OECD MTC / Amendment.

Followed by the 2003 OECD MTC Commentaries specifying that BO is "not used in a narrow technical sense",[11] the 2014 Amendment further clarifies that such narrow technical sense refers to "the meaning that it has under the trust law of many common law countries".[12] Besides, the 2014 Amendment for the first time offered a definition of BO. Referring to para.12.4 of Article 10, the key characteristic of BO therefore is that the person that receives the payment and has the "right to use and enjoy it", is "not be obliged to pass on the income item to another person under any contractual or legal form". The payment received may not be designated to transfer to another person stipulated in legal form.[13] However, the word of "control" or "ownership" is not discussed. The language of the Commentaries leaves some open discussion to what kind of circumstance should this requirement applicable. For instance, a first criticism arises from the fact that the Commentaries still starts by providing a negative definition of the term of BO.[14]

In 2017, the OECD introduced the Principal Purpose Test ("PPT") as a General Anti-Avoidance Rules ("GAAR") in Article 29.9 as well as Limitation on Benefit ("LOB") in Article 29.1- Article 29.7 of 2017 OECD MTC,[15] that allows reviewing the specific facts and circumstances to determine whether treaty benefit should be

[8] OECD MTC (2003): Commentaries on Art.10 para.12, Art.11 para.8, Art.12 para.4.

[9] S. Yoon, Comparative Study on Anti-Treaty Shopping - Focused on Beneficial Ownership Theory, 2016, p.231.

[10] OECD Public Discussion Draft on the Meaning of Beneficial Ownership (29 Apr. 2011); Revised Public Discussion Draft on the Meaning of Beneficial Ownership (19 Oct. 2012).

[11] OECD MTC (2003): Commentaries on Art.10 para.12, Art.11 para.8, Art.12 para.4.

[12] OECD MTC (2014): Commentaries on Art.10 para.12.1, Art.11 para.9.1, Art.12 para.4.

[13] OECD MTC (2014): Commentaries on Art.10 para.12.4, Art.11 para.10.2, Art.12 para.4.3.

[14] B. Da Silva, Evolution of the Beneficial Ownership Concept: More Than Half of Century and History Can Tell Us, 2017, p.521.

[15] OECD MTC (2017), Art.29 para.9.

denied. This article mirrors the outcome of BEPS Action 6. The 2017 Commentaries also stated that even though the concept of BO deals with tax avoidance (through the interposition of a recipient who has an on-payment obligation), it does not deal with other cases of abuses.[16] In other word, the concept of BO is not a general anti-avoidance rule.

Over the past half century, the concept of BO has been discussed and modified many times in OECD MTC and Commentaries, combining the practices, tax administrations / courts decisions and concerns by members states and scholars.

Autonomous meaning or domestic interpretation

Referring to Article 3.2 (General Definitions) of the OECD MTC,[17] where there is any undefined term, a definition under applicable domestic tax law prevails unless the context otherwise requires. Thus, there had been some arguments on whether the domestic law or an autonomous treaty meaning should be applied in identifying the concept of BO.[18]

The idea that the BO should be interpreted autonomously and be independent of domestic law was reflected in the Indofood Case (discussed in Section 2.2.2).[19] Later, the relevant issues had also been raised during the 2011/2012 public discussion regarding the meaning of BO[20] and eventually the idea of autonomous approach has been incorporated into OECD MTC 2014 version.[21]

Legal approach or economic substance approach

OECD MTC and Commentaries does not indicate if a legal interpretation or economic substance interpretation should be preferred when determining the scope of BO. Some argues that that the BO concept should be determined using legal approach while some others prefer the economic substance approach. For example, Danon is of the opinion that "beneficial ownership looks at the intensity of the ownership attributes enjoyed by the recipient over the item of income".[22]

Of course, both approaches have their advantages and supporters as well as shortfalls. Adopting legalistic doctrine can offer certain extent of legal certainty to the taxpayers and limit the discretion of tax authorities, which helps to facilitate the cross-border transactions. The assessment of BO and entitlement of tax treaty benefits should be made based on the clear legal and contractual obligations between the counterparties. However, it is also easy to manipulate the transactions for illegal tax avoidance purpose. On the other hand, economic substance approach focuses on the nature of the transaction and the flow of the economic benefits for determining

[16] OECD MTC (2017): Commentaries on Art.10 para.12.5, Art.11 para.10.3, Art.12 para.4.4.

[17] OECD MTC (2017), Art.3 para.2.

[18] C. Du Toit, Beneficial Ownership of Royalties in Bilateral Tax Treaties, 1999, p.173-p.174.

[19] Indofood International Finance Ltd v. JP Morgan Chase NA London Branch, High Court of Justice Chancery Division [2006] EWCA Civ. 158

[20] OECD Public Discussion Draft on the Meaning of Beneficial Ownership (29 Apr. 2011), para.12.1 of the Commentaries on Art.10; Revised Public Discussion Draft on the Meaning of Beneficial Ownership (19 Oct. 2012), para.12.1 of the Commentaries on Art.10.

[21] OECD MTC (2014): Commentaries on Art.10 para.12.1.

[22] R. Danon, Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention – Comment on the April 2011 Discussion Draft, 2011, p.82.

the real owner and controller of the economic benefits. It helps to lift the veil of the conduit companies and against the treaty shopping. However, such interpretation method would no doubt increase the difficulty of assessment for tax authorities and reduce legal certainty for tax payers.

Given that there is no convincing argument that one approach could completely replace another one, there are also some authors suggesting using "targeted hybrid approach" in determination of BO.[23]

2.2 Case law

Due to the ambiguity of the definition of BO under OECD MTC context, there have always been differences and inconsistencies in international tax law theory and judicial practice.

In order to facilitate the determination and application of BO, countries have continuously improved their concepts of BO in their respective judicial practices and case systems, and formed their own judgements and decisions. Among these practices, the following judgements made by different countries' courts are significant and representative in nature.

2.2.1 Royal Dutch Shell case (Netherlands 1994)[24]

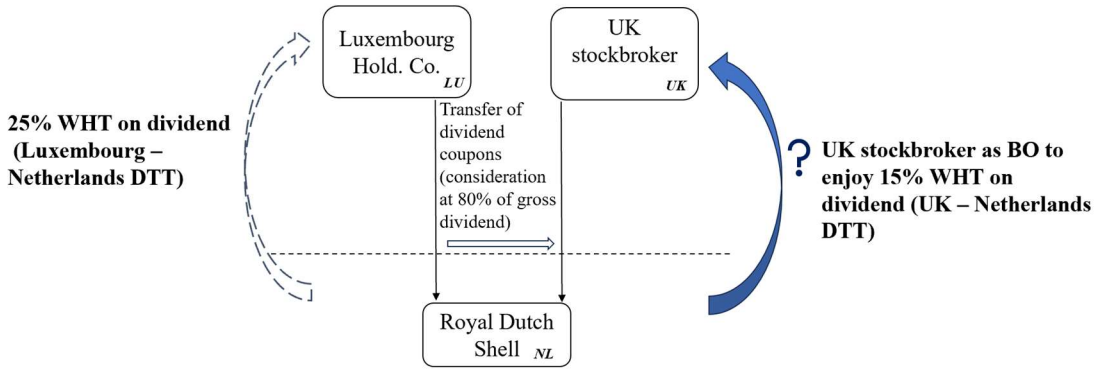
A Luxembourg holding company ("Luxembourg Hold. Co.") owned shares in Royal Dutch Shell, a company resided in Netherland. Luxembourg Hold. Co. could not claim the treaty benefits on the dividend it received from Royal Dutch Shell and hence had to pay a WHT at rate of 25% pursuant to Luxembourg – Netherlands DTT. Therefore, upon the declaration of the dividends, but before they were made payable, a UK stockbroker acquired dividend coupons on the shares from Luxembourg Hold. Co. Such arrangement aimed to get a 10% WHT reduction by UK stockbroker's entitlement of treaty benefit of 15% WHT under UK– Netherlands DTT. This case is illustrated in Diagram 1.

In its judgement, the Dutch Supreme Court held the view that the UK stockbroker was a BO given that: the UK stockbroker was the owner of the dividend coupons upon acquisition and it can freely dispose of these coupons as well as the monies distributed. The UK stockbroker did not act as any agent or nominee.[25]

In this case, it is clear that the ownership of the shares was not a factor to be considered when Dutch Supreme Court assessing the BO. Instead, according to Dutch Supreme Court's judgement, a BO should be the owner of the legal title on which its dividend distribution rights (dividend votes) are based.

[23] A. Wardzynski, The 2014 Update to the OECD Commentary: A Targeted Hybrid, 2015, p.188.
[24] Royal Dutch Shell Case no 28 638, BNB 1994/217 (the Hoge Raad, the Netherlands)
[25] Royal Dutch Shell Case no 28 638, BNB 1994/217 (the Hoge Raad, the Netherlands), sec. 3.2.

Diagram 1
Royal Dutch Shell case



2.2.2 The Indofood case (UK 2004)[26]

Although the Indofood case was a private law case rather than a tax case, it is still an important case in the field of tax and BO for several reasons. It is the first time that the English court to give interpretation on the term of BO in respect the tax treaty, since the concept of BO was originated from UK common law.[27] What's even more interesting is that the decision made by the UK High Court and the Court of Appeal were under different interpretation doctrines (i.e., legal approach and economic substance approach).[28] Besides, the captioned transactions of this case was a typical back-to-back loan arrangement which was arguable.

To simplify the case background, the focus of the dispute between the loan borrower in Indonesian (Indofood) and the noteholders' trustee in UK (JP Morgan) was that whether a new Dutch SPV which to be interposed between Indofood and a Mauritian SPV (the note issuer), holding the back-to-back loan with same amount of principal and same amount of receipts and payment of interest, could be treated as a BO by Indonesian tax authority under the prevailing Indonesian-Netherland DTT. The UK courts were asked to provide prediction on this issue. This case is illustrated in Diagram 2.

In its judgement, based on the OECD MTC and Commentaries, the Court of Appeal stated that the term of BO was "to be given an international fiscal meaning not derived from the domestic laws of contracting states."[29] It also confirmed that the concept of BO shall not merely be interpreted in legal way while the substance-over-form doctrine was also necessary.[30] Given that the Dutch SPV was requested to pay the same income within short deadlines, the Court of Appeal said that the Dutch SPV did not get any "direct benefit" from such income but rather be an "administrator of

[26] Indofood International Finance Ltd v. JP Morgan Chase NA London Branch, High Court of Justice Chancery Division [2006] EWCA Civ 158.

[27] C. Du Toit, The Evolution of the Term "Beneficial Ownership" in Relation to International Taxation over the Past 45 Years, 2010, p.6; P. Baker, Beneficial Ownership: After Indofood, 2007, p.21.

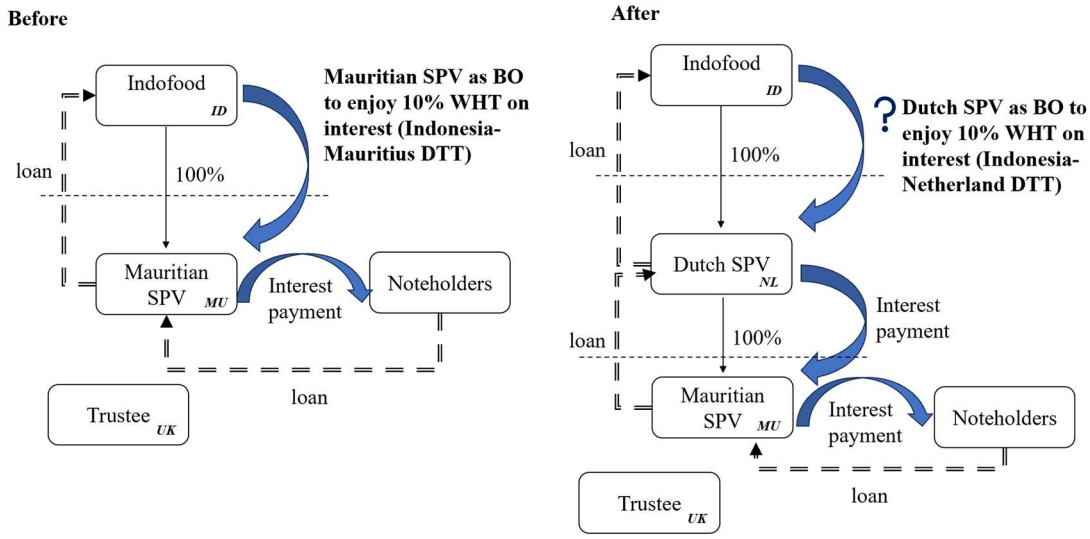
[28] P. Laroma Jezzi, The Concept of Beneficial Ownership in the Indofood and Prévost Car Decisions, 2010, p.254.

[29] Indofood International Finance Ltd v. JP Morgan Chase NA London Branch, High Court of Justice Chancery Division [2006] EWCA Civ 158, para.42.

[30] Indofood International Finance Ltd v. JP Morgan Chase NA London Branch, High Court of Justice Chancery Division [2006] EWCA Civ 158, para.44.

the income".[31] Therefore, the Dutch SPV is not qualified as being a BO, regardless its legal relationship, title or liability set by the loan agreement..

Diagram 2
The Indofood case



2.2.3 The Prévost Car case (Canada 2007)[32]

The Prévost Car case is of great importance with the following reasons. Firstly, Canada is a satisfied tax jurisdiction to interpret the concept of BO because of its prevalence of both the common law and civil law, plus two official languages namely English and French (are also the official languages of the OECD Model).[33] Secondly, the judgement of this case was made based on legalistic approach and rejected an economic interpretation.[34]

Prévost Car Inc. was a Canadian tax resident wholly owned by Prévost Holding B.V. ("PHB.V.") in Netherland. PHB.V. was owned by a Swedish Company, Volvo (51%) and a UK Company, Henlys (49%). As admitted during the trial, one of the reasons for having such holding structure was for tax purpose, that a reduced WHT of 5% on dividend distributed from Canada to Netherland was applicable under Canada-Netherland DTT. However, dividend directly paid back from Canada to Sweden and to UK shall be levied WHT at rate of 15% and 10% respectively under the corresponding DTT. PHB.V. had very limited substance with no premise or employee. As aligned in the agreement between the two ultimate shareholders, an amount of no less than 80% of PHB.V.'s profits should be paid to the two shareholders in the form of "dividends, return of capital or loans". The key issue in

[31] Indofood International Finance Ltd v. JP Morgan Chase NA London Branch, High Court of Justice Chancery Division [2006] EWCA Civ 158, para.44.

[32] Prévost Car Inc. v. Her Majesty the Queen [2008] TCC 231.

[33] C. Du Toit, The Evolution of the Term "Beneficial Ownership" in Relation to International Taxation over the Past 45 Years, 2010, p.8.

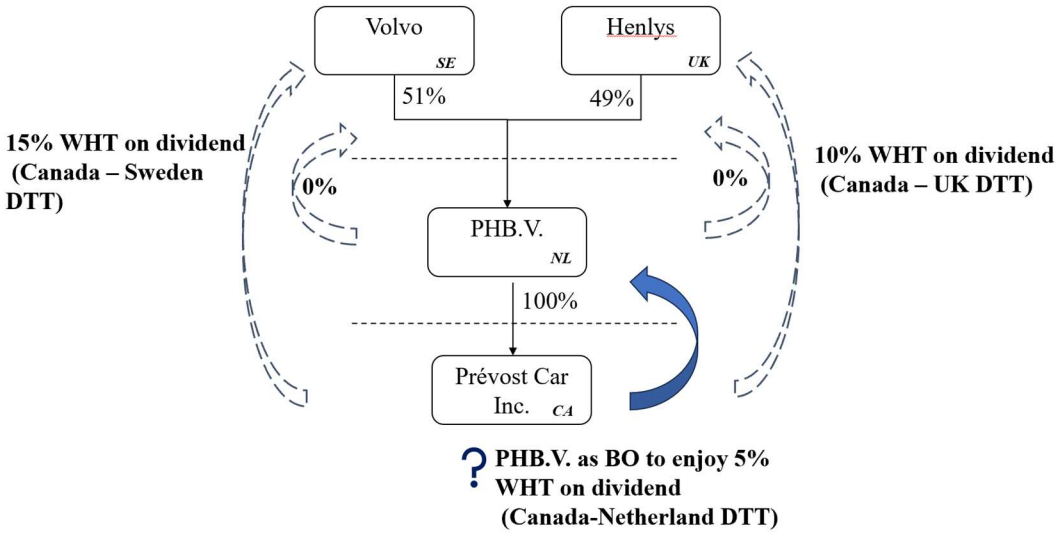
[34] A. Martin Jimenez, Beneficial Ownership: Current Trends, 2010, p.48.

this case is that whether PHB.V. could be a BO of the dividend from Prévost Car Inc. under Canada-Netherland DTT. This case is illustrated in Diagram 3.

In this case, Tax Court strictly reviewed the wording meaning of BO from different legal sources with the reference of OECD MTC and Commentaries. According to the court, PHB.V. did not have the legal (contractual) obligation for distribution its profits received from Prévost Car Inc. to its shareholders in Sweden and UK. It can freely use and enjoy the funds until PHB.V.'s declaration of dividend to its shareholders. There was no predetermined or automatic flow of funds and PHB.V. was not a conduit company. Besides, there were commercial reasons for setting up an intermediary holding structure in Netherland. It reflects the legalistic doctrine that Tax Court of Canada adopt in contrast to the economic substance doctrine.

According to the judgement of the Tax Court, there was no evident that PHB.V. being a conduit for Volvo and Henlys.

Diagram 3
The Prévost Car case



2.3 BO concept under BEPS Action Plans and MLI

2.3.1 Development of BEPS Action Plans and MLI

In the context of economic globalization, the issue of Prevent Base Erosion and Profit Shifting ("BEPS") is becoming more and more severe. Companies in particular those multinational groups tend to minimize or avoid its overall tax costs by taking advantage of the international tax rules and exploiting the differences and mismatches among various countries' tax systems. Referring to OECD website, the total amount of BEPS practice is around 100 to 240 billion US dollar annually, which

greatly jeopardizing the international tax order and leading to the economic imbalance among countries.[35]

To cope with this situation, in 2015, based on the context of OECD/G20 BEPS Project, BEPS Action Plans were designed. The 15 Action Plans are expected to be implemented in over 140 countries and jurisdictions (including both developed and developing countries). Considering that for certain low-capacity countries, it will be difficult to implement the whole package due to its complexity, OECD has listed four minimum standards for all countries' transforming into domestic legislations. One of this four minimum standard is Action 6, prevention of tax treaty abuse.[36]

Multilateral Convention on the Implementation of Measures Related to Tax Agreements to BEPS ("MLI"), agreed in June 2017, is a multilateral instrument to accelerate the process of the implementation of BEPS outcome as well as the update of the existing over 3000 bilateral tax treaties. It incorporates Action 6 (prevention of tax treaty abuse) and another three Actions, to make sure that the implementation of BESP final report would be rapidly and harmonized.[37]

It can be seen that BEPS Action Plan 6 (prevention of tax treaty abuse) appears as a minimum standard not only in the Final Report of BEPS Action Plan, but also in the BEPS MLI. It has become a general consensus to revise the description of bilateral tax treaties and domestic laws of various countries to achieve the purpose of BEPS Action 6 and prevent the improper entitlement of preferential treatment in tax treaties. Countries will converge on their principles for dealing with this issue.

2.3.2 Impact of BEPS Action Plans and MLI on the concept of BO

As recognized by OECD as well as supported by academia, the concept of BO could only deal with some forms of tax avoidance but not all cases of treaty shopping.[38] Thus pursuant to BEPS Action 6's recommendation, the minimum standard of MLI in respect treaty abuse are:

- Following the recommendation of BEPS Action 6 (page 10), "a reformulation of the title and preamble of the Model Tax Convention that will clearly state that the joint intention of the parties to a tax treaty is to eliminate double taxation without creating opportunities for tax evasion and avoidance, in particular through treaty shopping arrangements."[39]

- Following the recommendation of BEPS Action 6 (para 22, page 19), "states that countries, at a minimum, should implement: (i) a PPT only; (ii) a PPT and either a simplified or detailed LOB provision; or (iii) a detailed LOB provision,

[35] OECD website, http://www.oecd.org/tax/beps/about/

[36] OECD/G20 BEPS Project Explanatory Statement - 2015 Final Reports, para.11.

[37] OECD/G20 BEPS Project Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15 2015 Final Report, para.8.

[38] J.J.M. Janssen & M.S. Garibay, What Should Be the Scope of the Beneficial Owner, 2020, p.1091; A.V. Demin & A.V. Nikolaev, Beneficial Owner Concept in the Context of BEPS: Problems and Prospects, 2019, p.5; OECD MTC (2017): Commentaries on Art.10 para.12.5, Art.11 para.10.3, Art.12 para.4.4.

[39] OECD/G20 BEPS Project Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 2015 Final Report, p.10.

supplemented by a mechanism that would deal with conduit arrangements not already dealt with in tax treaties."[40]

Pursuant to MLI, PPT is described as: "Notwithstanding any provisions of a Covered Tax Agreement, a benefit under the Covered Tax Agreement shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the Covered Tax Agreement."[41]

The purpose of LOB is to increase the threshold and constraints for taxpayers being granted treaty benefit through different tests, including the qualified persons' test, or the active business test, or the derivative test and the residual bona fide test.[42]

The provision of PPT and simplified version of LOB has been introduced into the Article 29.9 & Article 29.1-7 of the latest 2017 OECD MTC, being complement to each other. I.e., even if the Specific Anti-Avoidance Rules ("SAAR") of Article 29.1-7 are not applicable to certain arrangement, it shall still fall in the scope of Article 29.9.[43] In addition, the Commentaries also contain a detailed explanation and examples highlighting the functions and scope of this article.

2.4 An overview of BO concept under the latest OCED MTC and Commentaries

Followings are the most important features of BO concept under OECD:

Clarification on "paid… to a resident"	Demonstrate that the source state is not obliged to provide treaty benefits to the receiver of the dividends only because he/it is a resident of the other contracting state.
The concept should have an independent international fiscal meaning	The term BO is therefore not used in a narrow technical sense (such as the meaning that it has under the trust law of many common law countries), rather, it should be understood in its context, in particular in relation to the words "paid… to a resident", and in light of the object and purpose of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance.[44]

[40] OECD/G20 BEPS Project Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 2015 Final Report, p.19, para.22.

[41] Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, Art.7 para.1.

[42] B. Kuźniacki, The Limitation on Benefits (LOB) Provision in BEPS Action 6 /MLI: Ineffective Overreaction of Mind-Numbing Complexity-Part 1, 2018, p.71.

[43] A.V. Demin & A.V. Nikolaev, Beneficial Owner Concept in the Context of BEPS: Problems and Prospects. 2019, p.6-p.7.

[44] OECD MTC (2017): Commentaries on Art.10 para.12.1, Art.11 para.9.1, Art.12 para.4.

Exclusion of conduit	… a conduit company cannot normally be regarded as the beneficial owner if, though the formal owner, it has, as a practical matter, very narrow powers which render it, in relation to the income concerned, a mere fiduciary or administrator acting on account of the interested parties.[45]
The test of "use and enjoy"	Where the recipient of a dividend does have the right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass on the payment received to another person, the recipient is the "beneficial owner" of that dividend. Both the legal form and substance should be considered.[46]
Control over the income	Only the income, but not the assets or property that generate such income
Relationship between anti- tax avoidance	The provision restricting treaty benefits to a resident of a Contracting State who is a "qualified person".[47] The BO concept only deal with some forms of tax avoidance (i.e., the interposition of a recipient who is obligated to pass on dividend to someone else). It does not deal with other cases of abuse that are addressed in other provisions of the 2017 update of the OECD MTC.[48]

[45] OECD MTC (2017): Commentaries on Art.10 para.12.3, Art.11 para.10.1, Art.12 para.4.2

[46] OECD MTC (2017): Commentaries on Art.10 para.12.4.

[47] OECD MTC (2017), Art.29 para.1.

[48] OECD MTC (2017): Commentaries on Art.10 para.12.5, Art.11 para.10.3, Art.12 para.4.4.

3 . Overview of BO concept under Chinese tax law

3.1 BO concept under double taxation treaty

3.1.1 Development of double taxation treaty in China

Since China's launch of reform and opening-up program in 1978, many foreign investments had their presence in China. To further facilitate the economic development and attract more foreign capital, in 1980s, China began negotiating and signing tax treaties with other countries / jurisdictions, in particular with the OECD member countries. The first income tax treaty, China-Japan DTT, was signed on 1983. Over the following two years, China had concluded tax treaties with another five OECD member countries, that is United States (1984), France (1984), United Kingdom (1984), Belgium (1985), Germany (1985), etc. By 1988, 11 more tax treaties were concluded with the OECD member countries.

Back to that time, China didn't have a mature understanding of the international tax or a modern income tax system, it was necessary for China to learn from the other contracting states' relevant advanced theories and practical experiences. Given that Japan and the following contracting states were OECD member countries, those earliest treaties based on OECD MTC had well served as guidance and reference for the following double taxation treaties concluded between China and other countries / jurisdictions. Naturally, the concept of BO based on OECD MTC was initially included in the article 10, 11 and 12 of the China-Japan DTT, with respect the dividend, interest and royalty income. The concept then had been widely recognized and retained in the following double taxation treaties concluded by China. In general, the WHT rate on the income of dividends, interests and royalties is 10% under China's tax treaties. But in some tax treaties, China entitles a reduced WHT rate on certain income to the "beneficial owner" who are resident of the other contracting state.

However, as already discussed in Section 2, OECD MTC does not offer a clear definition of BO. Since China use the OECD MTC as guidance, the double taxation treaties concluded by China do not contain such definition as well. In this regard, referring to Article 3.2 (General Definitions) of the OECD MTC,[49] where there is any undefined term, a definition under applicable domestic tax law prevails unless the context otherwise requires.

3.1.2 China's involvement in BEPS initiative

Though China is not an OCED member, it has been actively participated in BEPS Action Plans and holds a positive view towards the whole project and thereby

[49] OECD MTC (2017): Commentaries on Art.3 para.2.

strengthening its role and status in international tax affairs.[50] It is also because that China itself has been suffered from BEPS and has lost tax revenue especially in the field of transfer pricing and treaty abuse for a long time period.[51] It is quite common for those foreign investors of Chinese subsidiaries using intermediary company(s) in certain jurisdiction(s) as holding vehicles for obtaining the treaty benefit under double taxation treaties between China and that jurisdiction so that a lower WHT shall be levied on the income paid to the foreign investors from China subsidiaries. Therefore, Chinese tax authority is keen to look into this issue.

By the signing of the OECD MLI in June 2017, China includes its 105 formally singed tax agreements be covered by the MLI and China choose to implement the preamble statement as well as PPT provisions.[52] As of 31st May 2023, 60 of these agreements are complied with the minimum standard.[53]

From double taxation treaty perspective, in the recently concluded China - Chile DTT (2015), for the first time, it is stated in the preamble of tax treaty that the intention of the treaty is to prevent "non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangement)",[54] which follows the recommendation of BEPS Action 6. However, since most of the China's DTT were concluded before the launch of BEPS project, there aren't be many DTT which reflect the outcome of BEPS Action 6.

3.2 BO concept under Chinese tax law

From domestic tax law perspective, to combat the treaty abuse, China has launched a series of circulars for the guidance and criteria of qualified BO since 2009. In particular the launch of Announcement 9 [2018] (details discussed in Section 3.2.4) further improves China's BO concept combining the consideration of BEPS initiative and its latest development.

3.2.1 Background of Chinese tax law regime

As discussed in Section 3.1.1, the normal WHT rate on dividend, interest and royalty is 10% under China's tax treaties.

Before 2008, China ran a dual enterprise income tax system for domestic funded enterprises and foreign related companies (including foreign enterprises, wholly foreign owned enterprises, joint ventures), where the latter were in a preferential tax regime for encouraging the foreign direct investment. One of the favourable tax treatments was that "the profit derived by a foreign investor from a foreign invested Chinese enterprise shall be exempted from income tax", i.e. WHT on dividends (or

[50] D. Xu, The Convergence and Divergence between China's Implementation and OECD/G20 BEPS Minimum Standards, 2018, p.473.
[51] J. Li, China and BEPS: From Norm-Taker to Norm-Shaker, 2015, p.356.
[52] Explained by STA, the major outcomes of MLI that China has adopted in its tax treaties, available https://www.chinatax.gov.cn/chinatax/n810341/n810760/c5178627/content.html
[53] OECD website, the progress of the implementation of minimum standard for China, available at https://www.oecd-ilibrary.org/sites/36cebf8e-en/index.html?itemId=/content/publication/36cebf8e-en
[54] China – Chile Double Taxation Treaty (2015), Preamble.

profit distribution) was waived pursuant to the prevailing tax law by that time.[55] There weren't be many tax planning for mitigating the tax costs in this aspect.[56] (see Diagram 4)

As China's reform and opening up entered a new stage as well as its joining WTO in the beginning of 21st century with its commitment, the dual income tax system was seen as an unfair treatment to domestic capital investment. Besides, it was also no longer adaptable to China's more sophisticated economy environment or its integration into international tax system. Therefore, on 1st of January, 2008, the dual income tax systems were unified into one and a new domestic Enterprise Income Tax Law was implemented which is applicable to both domestic and foreign related companies.[57] Under the new tax law regime, resident enterprises are subject to tax on their worldwide income while non-resident enterprises are subject to tax on the Chinese sourced income only. Thus a 20 % WHT is imposed on the income (including dividends, interests and royalties) derived by non-residents from Chinese sources and China's tax treaties usually offer a 10% WHT rate on the said income.[58] (see Diagram 5)

As a result, the tax burden of those foreign investors holding Chinese subsidiaries under the new tax regime (at 10%) were likely to be higher than those under the old regime (exempted) when receiving China sourced income, which become those investors' concern and lead to many tax planning.[59] To enjoy the treaty benefit and lowering the tax costs, foreign direct holding companies in non-treaty jurisdiction then considering to transfer their shares in Chinese subsidiaries to intermediate holding companies which locate in the tax jurisdiction that have a favourable DTA with China.[60] One common choice was using holding vehicle in Hong Kong, of which a reduced WHT rate on dividends (5%), interest (7%) and royalties (7%) is applicable for qualified BO under China-Hong Kong DTA.[61] (see Diagram 6)

[55] China Enterprise Income Tax Law for Foreign Investment (1991), Art.19

[56] J. Eichelberger & B. Kelly, Tax Planning Strategies in Response to China's Changing Tax Landscape: Issues and Structures To Be Considered in a Post Tax Unification China, 2008, p.224.

[57] For an overview of the unification of the two income tax systems, pls see J. Li, Fundamental Enterprise Income Tax Reform in China: Motivations and Major Changes, 2007.

[58] China Enterprise Income Tax Law (2008), Art. 3.3, Art. 27; Implementation Regulation for China Enterprise Income Tax Law, Art. 91.

[59] D. Qiu, The Concept of "Beneficial Ownership" in China's Tax Treaties – The Current State of Play, 2013, p.98-p.99.

[60] J. Eichelberger & B. Kelly, Tax Planning Strategies in Response to China's Changing Tax Landscape: Issues and Structures To Be Considered in a Post Tax Unification China, 2008, p.224.

[61] D. Qiu, The Concept of "Beneficial Ownership" in China's Tax Treaties – The Current State of Play, 2013, p.99.

Diagram 4
Old tax regime before 2008

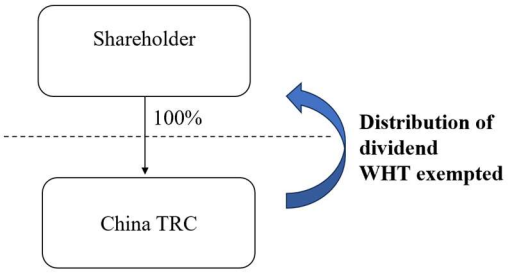


Diagram 5
New tax regime since 2008

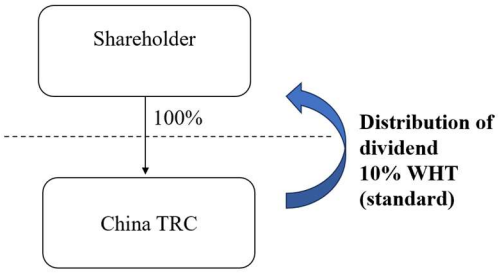
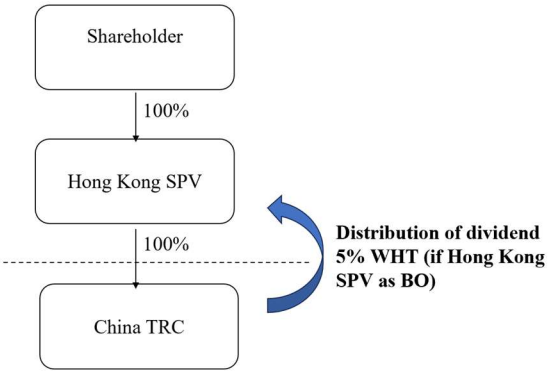


Diagram 6
Insert a Hong Kong SPV



On a separate matter, Article 47 of Enterprise Income Tax law is China's GAAR provision, "where the taxable income or amount of income of an enterprise is reduced as a result of arrangements with no reasonable commercial objectives implemented by the enterprise, the tax authorities have a right to make adjustments according to a reasonable method."[62]

Under such background, one year later, China has launched its first circular guiding the determination of BO (details refers to Section 3.2.2 – Section 3.2.4) to against such treaty abuse.

3.2.2 Circular 601 [2009] (repealed)

Though China's first double taxation treaty and concept of BO was concluded in 1983 as discussed in Section 3.1.1, it was until October 2009 that China's central tax authority, State Administration of Taxation ("SAT") issued Circular 601 [2009],[63] to provide a guidance on the qualification of a BO of China sourced income for applying treaty benefit. It basically gives the position of the China domestic law, that is, (1) the principle of economic substance; (2) exclusion the agent and conduit; (3) ownership and control rights on the income or the properties/rights over the income; (4) be generally engaged in substantial business activities.

[62] China Enterprise Income Tax Law (2008), Art.47.

[63] SAT, Circular on Interpretation and Determination of "Beneficial Owner" in Tax Treaties (Circular 601 [2009]), effective from 27 October 2009.

In Article 1 of Circular 601 [2009], BO of China source income is defined as "a person or an entity which has the ownership and right to control the income or the properties / rights generating income and a BO shall generally engage in substantial business activities". Agents or conduit companies will not be treated as BO as specified in this circular. It further defines the conduit companies as "the companies incorporated for the purpose of evading or reducing taxes, transferring or accumulation of profits. Such companies do not engage in substantial activities such as manufacturing, trading or management but merely meet the incorporation requirements in the country where they register".

In Article 2, it emphasizes that when determining the BO status, it should not only be considered from the technical level or the perspective of domestic law, but should also be based on the purpose of the tax treaty (that is, the avoidance of double taxation and prevention of tax evasion). Chinese tax authorities shall use the "substance-over-form" principle in determining the status of BO on a case-by-case basis. Seven "unfavourable factors" were innovated as a benchmark for Chinese tax authorities identifying the applicant's status of BO:

1) has obligation to pass on all or majority of the income (e.g., more than 60%) to a resident of a third country (region) within a short period (within 12 months);
2) has no or very little business activities other than holding the properties / rights that generates income
3) has little amount of assets, scale of operation and staffing, which is hardly compatible to the amount of income
4) has no or very little control or disposition right on the properties / rights that generates income, and bears no or little risk
5) locates in the country (jurisdiction) that has no or exempted tax levy, or levy at a very low tax rate
6) there exists a back-to-back loan arrangement with third party with similar amount, interest rate and date of execution
7) there exists a back-to-back royalty arrangement with third party

Different from OECD MTC and Commentaries which does not indicate if a legal interpretation or economic substance approach is used for justifying BO, the interpretation of BO in Circular 601 [2009] can be seen as a combination of legal approach and economic substance approach. On one hand, it indicates that the concept of BO is based on the ownership and control right on certain income. On the other hand, it in particular emphasized the adoption of substance-over-form principle. Unfavourable factors #2, #3, #5, #6 & #7 were the reflection of substance-over-form principle.

Due to the institutional system in China, the decisions of BO status are made by the tax officials at lower level of the hierarchy who may not fully aware of the international tax and BO concepts and their interpretation and enforcement tend to

follow this circular in a mechanical way.[64] In addition, sometimes the ownership or control right is unclear and legal relationship is hard to identify. To avoid such vagueness, some local tax authorities are inclined to assess if there exit any substantial business activities which are tangible and identifiable.[65] Besides, in view of the assessment of the seven unfavourable factors, some local tax authorities adopt a stricter way of assessment and deny the BO status whenever there is only one unfavourable factor had been met. But other tax authorities use a more comprehensive way by going through the seven factors and ticking the boxes. Some unfavourable factors are too flexible to interpretate and assess. For example, unfavourable factor #3, is highly up to local tax authorities' discretion in judging whether the amount of assets, the business scale or the staffing can properly match the amount of certain income. The decision is therefore made based on local tax officials' subjective judgement and personal experiences without objective criteria.

3.2.3 Announcement 30 [2012] (repealed)

In June 2012, by summarizing the problems and experiences in the past two years since the implementation of Circular 601 [2009], SAT further issued Announcement 30 [2012][66] for clarification of the status of BO.

Article 1 of Announcement 30 [2012] reaffirmed that the decision of BO should comprehensively consider all seven unfavourable factors listed in Article 2 of Circular 601 [2009]. The unrecognition or recognition decision shall not be made just because of the existence of certain one single unfavourable factor or just because "the purposes of evading or reducing taxes, transferring or accumulating of profits" specified in Article 1 of Circular 601 [2009] does not exist. To facilitate the tax authorities' analysis of BO status, various kinds of documents shall be submitted, including but not limit to article of association, financial statements, board meeting minutes, board resolutions, function and risk analysis, relevant contracts, etc. (Article 2 of Announcement 30 [2012]). SAT intends to guide the local tax authorities to adopt a more comprehensive and objective approach to determine the BO status, rather than simply make a subjective judgement based on one single unfavourable factor. However, it still leaves plenty of room for interpretation and discretion to local tax authorities.

Besides, in Article 3 of Announcement 30 [2012], it is the first time that a "listed company safe-harbour rule" is introduced, where treaty benefit could be automatically entitled to the dividend recipient that meets the safe-harbour rule criteria without an assessment of the seven "unfavourable factors" pursuant to Circular 601 [2009]. Under this rule, the immediate recipient of the dividends which is also a listed company in the tax treaty jurisdiction, or is directly or indirectly wholly-owned by a listed company in the tax treaty jurisdiction, is automatically be recognized as a BO.

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[64] N. Sharkey, China's Tax Treaties and Beneficial Ownership Innovative Control of Treaty Shopping or Inferior Law Making Damaging to International Law, 2011, p.656 – p.657.

[65] D. Qiu, The Concept of "Beneficial Ownership" in China's Tax Treaties – The Current State of Play, 2013, p.100.

[66] SAT, Announcement of State Administration of Taxation on Recognition of "Beneficial Owner" in Tax Treaties (Announcement 30 [2012]), effective from 29 June 2012.

3.2.4 Announcement 9 [2018] (valid)

In February 2018, the SAT issued the long-time expected Announcement 9 [2018],[67] which repeals Circular 601 [2009] and Announcement 30 [2012]. This new Announcement, according to SAT, aims to allowing cases that do not for the treaty abuse purpose to enjoy treaty benefits, increasing such certainty and reducing the costs for both the tax payers and the collectors. Besides, it also reflects the outcome of BEPS Action Plans and the enforcement of MLI in China to certain extent. Some provisions of Circular 601 [2009] and Announcement 30 [2012] were retained while other terms were amended or updated accordingly. Main rules and changes of Announcement 9 [2018] include:

Article 1: the concept - BO shall mean a person who has ownership and control over the income and the rights and property from which the income is derived.

Article 2: The **seven** unfavourable factors for identify BO status have been tightened and incorporated into **five** as:

Circular 601 [2009] – Article 2 7 unfavourable factors (old list)	**Announcement 9 [2018] – Article 2** 5 unfavourable factors (new list)
1. has obligation to pass on all or majority of the income (e.g., **more than 60%**) to a resident of a third country (region) within a short period (**for example, 12 months**);	1. has obligation to pay **50%** or more of the income, **within 12 months** from receipt of the income, to a resident of a third country (region). "Obligation to pay" includes both contractual obligations to pay and any payment already made even though there is no contractual obligation to pay.
2. has **no or very little business activities** other than holding the properties / rights that generates income	2. if the applicant **does not conduct substantive business activities** (which shall include manufacturing, sales and marketing and management activities of a substantive nature). The functions performed and the risks undertaken by the applicant shall be assess when determining the BO status Substantive investment management activities can be construed as substantive business activities. Where the applicant carries out both non-substantive investment management activities

[67]SAT, Announcement of the State Administration of Taxation on Issues Relating to "Beneficial Owner" in Tax Treaties (Announcement 9 [2018]), effective from 1 April 2018.

	and other business activities, it will not be considered as having substantive business activities if the other business activities are not significant enough Through a series of interpretations and example cases, SAT provides some relatively clear guidance on how to determine substantive business activities.
3. has little amount of assets, scale of operation and staffing, which is hardly compatible to the amount of income	delete and incorporated into No. 1 & 2 factor of new list
4. has no or very little control or disposition right on the properties / rights that generates income, and bears no or little risk	delete and incorporated into No. 1 & 2 factor of new list
5. locates in the country (jurisdiction) that has no or exempted tax levy, or levy at a very low tax rate	3. maintain in the new list
6. there exists a back-to-back loan arrangement with third party with similar amount, interest rate and date of execution	4. maintain in the new list
7. there exists a back-to-back royalty arrangement with third party	5. maintain in the new list

Article 3: Introduce new "same jurisdiction rule" and "same (better) treaty benefit rule" for multi-layer holding structures. (Examples are provided by SAT for illustration and guidance purpose. Details refer to Appendix I)

Article 4: Expand the scope of "safe-harbour rule":

Announcement 30 [2012] – Article 3	**Announcement 9 [2018] – Article 4**
Where treaty benefit could be automatically entitled to the dividend recipient that meets the safe-harbour rule criteria without an assessment of the seven "unfavourable factors" pursuant to Circular 601 [2009]. The immediate recipient of the dividends which is also a listed company in the tax treaty jurisdiction, or is directly or indirectly 100% owned by a listed company in the	For dividends received by the following recipient(s) from a PRC tax resident enterprise, it/they will be automatically recognized as BO(s) in application for tax treaty benefit without an assessment of five "unfavourable factors": (1) listed companies in the tax treaty jurisdiction;

treaty jurisdiction, is automatically be recognized as a BO.	(2) **governments of the tax treaty jurisdiction**; (3) **individual resident of the tax treaty jurisdiction;** and (4) **company which is 100% directly or indirectly owned by (1), (2) or (3).**

Article 6: Exclusion of agent or designated payees from BO.

Article 10: "Even if a recipient is treated as a BO, the Chinese tax authority can still invoke the main purpose testing clause under the relevant tax treaty or the GAAR in its domestic law to deny the treaty benefits." As discussed in Section 3.1.2, China signed the OECD MLI in June 2017, under which the PPT was introduced to the tax treaty network of China. PPT is similar the main purpose test and its adoption indicates China's commitment to comply with the minimum standard under BEPS Action 6 (prevention of tax treaty abuse) of OECD.

Announcement 9 [2018] remove the term and definition of conduit companies and emphasize the principle of substance-over-form again.

These are the most important features of BO concept under Chinese domestic tax law.

4． The comparison of the latest BO concept under OECD/BEPS and Chinese tax law

4.1 The comparison

Below are some main comparisons of BO concept under latest OECD MTC and Commentaries vs. Announcement 9 [2018]:

	2017 OECD MTC and Commentaries	**Announcement 9 [2018]**
Legal interpretation	The recipient has the right to use and enjoy the *dividend* unconstrained by a contractual or legal obligation to pass on the payment received to another person.[68]	Article 1. BO shall mean a person who has ownership and control rights over the *income* and *the properties/rights from which the income is derived*.
Economic substance	conduit structures "as a practical matter" with "very narrow powers"	Article 2. Unfavourable factor #2 (substantial business activities test); #4 (back-to-back loan arrangement); #5 (back-to-back royalty arrangement)
LOB	Article 29.4 Provision that provides treaty benefits to a person that is not a qualified person if at least more than an agreed proportion of that entity is owned by certain person entitled to equivalent benefits. OECD MTC Commentaries provide more detailed explanations and examples on this provision: "at least half of the days of any twelve- month period that includes that time, persons that are equivalent beneficiaries own,	Article 3. "same jurisdiction rule" and "same (better) treaty benefit rule" (Details refer to Appendix 1) Article 5. The shareholding ratio stipulated in Article 3 of this Announcement shall attain the stipulated ratio at all times during the 12 consecutive months before the dividends are obtained.

[68] OECD MTC (2017): Commentaries on Art.10 para.12.4, Art.11 para.10.2, Art.12 para.4.3.

	directly or indirectly, at least 75 per cent of the shares of the resident."[69]	
	Article 29.2 Definition of situations where a resident is a qualified person, which covers a. an individual; b. Contracting State, its political subdivisions and their agencies and instrumentalities; c. certain publicly-traded companies and entities; d. certain affiliates of publicly-listed companies and entities; e. certain non-profit organisations and recognised pension funds; f. other entities that meet certain ownership and base erosion requirements; g. certain collective investment vehicle. OECD MTC Commentaries provide more detailed explanations and examples on this provision.	Article 4. Safe-harbour-rule For dividends received by the following recipient(s) from a PRC tax resident enterprise, it/they will be automatically recognized as BO(s) in application for tax treaty benefit without an assessment of five "unfavourable factors": (1) listed companies; (2) governments; (3) individuals; and (4) company which is 100% directly or indirectly owned by (1), (2) or (3).
Exclusion of conduit company	… a conduit company cannot normally be regarded as the beneficial owner if, though the formal owner, it has, *as a practical matter, very narrow powers.*	Wording in relation to "conduit company" is removed
Anti-tax avoidance	The BO concept only deal with some forms of tax avoidance (i.e., the interposition of a recipient who is obligated to pass on dividend to someone else). [70] It does not deal with other cases of abuse that are addressed in	Article 10. PPT clause under relevant tax treaty or the GAAR in domestic law could be invoked for denying the treaty benefits, regardless the BO status.

[69] OECD MTC (2017): Commentaries on Art.29 para.82.

[70] OECD MTC (2017): Commentaries on Art.10 para.12.5, Art.11 para.10.3, Art.12 para.4.4.

	other provisions of the latest OECD MTC.	
Autonomous or domestic meaning	…it was intended to be interpreted in this context and not to refer to any technical meaning that it could have had under the domestic law of a specific country…[71]	Unilaterally prevailing, domestic law

Legal interpretation:

This is one major difference. OECD's interpretation covers the income only, but not the properties / rights over certain income. BO doesn't need to own such income, as long as it can freely use or enjoy the income without legal binding.

It seems that the interpretation under Announcement 9 [2018] is stricter. However, in some cases, the beneficial ownership and legal ownership are separated. With the development of new products in the international financial market, it is common for beneficiaries to only have control over the proceeds but not any underlying benefits or rights. If the BO status of the beneficiary is denied, the real beneficiary shall bear additional tax costs, which will impact the tax fairness.

Furthermore, the interpretation under OCED model is relatively clear and unvague, which is more convenient for the identification and operation of the tax authorities and can effectively combat international tax evasion, give more legal certainty to tax payers. If the contracting state adopt OECD model for determining the scope of income while China adopt Announcement 9 [2018], the inconsistency in calibre may lead to additional tax costs for taxpayers.

Economic substance:

Ever since the launch of Circular 601 [2009], China SAT has been emphasized the principle of substance-over-form and set several criteria for testing purpose.

Though the wording of "conduit companies" is removed and the idea of "substantial business activities" are used in the Announcement 9 [2018], it provides a positive list of several kinds of activities (i.e. manufacturing, sales and marketing, management, investment management activities of substantial nature) as qualified ones. With the increase of companies holding passive investment activities, it is not clear whether the activities such asset management and trust funds can fall in the category of "substantial business activities".

[71] OECD MTC (2017): Commentaries on Art.10 para.12.1, Art.11 para.9.1, Art.12 para.4.

LOB

Announcement 9 [2018] has introduced some LOB rules from the latest OECD MTC with stricter criteria in terms of time period and shareholding percentage. However, Announcement 9 [2018] doesn't provide detailed explanation on these rules.

Conduit companies:

OECD model only exclude some qualified conduit companies from BO status. A conduit company which has very limited rights over the proceeds received shall be denied as a BO.

Announcement 9 [2018] removed the term of conduit companies and the definition. Instead, it pays more attention to the substantial facts such as the company's articles of association, financial data, capital flow to the record, the decision of the board of directors, board meeting minutes, human labour and physical resources, the relevant expenditure reports, functions and risk-taking, loan & licensing contract, certificate of patent and copyright, etc.[72] To determine whether it is the case of "receiving income on behalf of an agent" as stipulated in Article 6 of this announcement, analysis shall be made according to the agency contract or the designated collection contract. Announcement 9 [2018] excludes beneficial owners beyond conduit companies and removes the definition of conduit companies, emphasizing the principle of substance over form.

Anti-tax avoidance:

Regarding the concept and definition of BO, the OECD MTC and Commentaries stress that the concept of BO should have an autonomous meaning and be independent of the domestic law of certain contracting states.

But under Announcement 9 [2018], even if the applicant has the BO status, the tax authorities still can deny its tax treaty treatment by using the main purpose test provisions in the tax treaty or the GAAR rules stipulated by domestic tax laws. Invoking domestic GAAR for denial of treaty benefit may lead to double taxation if the treaty contracting party does not agree with China's practice and decision.[73]

This is also in contrast to the OECD MTC and Commentary that the BO concept clause is only a SAAR with limited functions and should not be interpreted or treated as a GAAR concept or rule.

[72] Q. Xu & L. Yuan, Presentation of the Beneficial Owner Rule and Its Application in Intl Anti tax Avoidance, Advances in Economics, Business and Management Research, 2019, p.251.

[73] J. Li, China and BEPS: From Norm-Taker to Norm-Shaker, 2015, p.363.

Autonomous or domestic meaning:

OECD inclines to have the BO concept be interpreted in an international meaning and be independent from domestic law. But China currently use the domestic tax law governing BO concept.

5 . Concerns and recommendation for BO concept in China

5.1 The competence of domestic law regarding the BO concept

Concerns:

OECD MTC and Commentary intends to provide an international interpretation to BO regardless the meaning of domestic law. China, however, has launched the relevant domestic laws for many years.

Given that the relevant domestic circulars and announcements are unilaterally executed by China tax authority and most of the DTT concluded between China and other contracting states were earlier than the issuance date of these domestic rules, those contracting states of the DTT may not be fully aware of these domestic rules or acknowledge their legal effects. It is not appropriate to use these domestic laws to explain the issues caused by tax treaties. When it comes to any dispute between tax payers and Chinese tax authority and the case be brought to court, these domestic rules may not necessarily be served as a basis for court decision.

Recommendation:

Though China is not OECD member country, it has been co-operating with OECD for a long period as one of its key partners. OECD MTC does not have biding force to China, but China has been actively involved in is update work and OECD MTC has been a guidance for China's negotiation and conclusion DTT with other contracting states as well as making up domestic laws.

Therefore, when BO is widely accepted as an international recognized tax term and the OECD model becomes more and more important in guiding the conclusion of international tax treaties, China should actively participate in the updating and revision of the OECD model and propose suggestions from Chinese perspective for the formulation of the concept of BO.

Besides, it is also suggested that China should update the existing tax treaties in respect the determination of BO as well as the implementation of BEPS Action 6. In particular, priority should be given to the contracting states which have large amount of inbound/outbound investment and of which the DTT have treaty benefits.

5.2 The divergence of legal interpretation

Concerns:

As presented in Section 4.1, there are divergence between the legal interpretation under OECD MTC and under China domestic law, which may cause dispute and double taxation or non-taxation issues.

Recommendation:

Same as discussed in Section 5.1, China is suggested to assist with OECD for updating the concept of BO by providing China's concerns and practical considerations, and eventually be aligned with OECD of this issue either in tax treaty aspect and in domestic law aspect.

5.3 Refine the detail testing rules

Concerns:

The rules for testing the substantive are not very clear and are absent of instructive, which still leave discretion to local tax authorities and uncertainty to the tax payers.

Recommendation:

While the latest OECD MTC and Commentaries have included PPT and LOB provisions, China is also suggested to refer to such practice, to respond to the increase and changes in tax avoidance or treaty abuse by making up a series of detailed anti-abuse regulations or refining the relevant testing rules.

China SAT put too much emphasize on the assessment of "substantial business activities" when codifying Announcement 9 [2018] and its predecessor. However, the inclusion of manufacturing, sales and marketing and management activities" is not very practical for determining as "substantial business activities". Instead, PPT concept is suggested to adopted in domestic law, i.e., when assessing the economic substance, the purpose of the transaction shall also to be reviewed. This helps to assess the status of BO from both subjective and objective ways.

Though Announcement 9 [2018] has adopted some LOB provisions, the current articles are quite general without further instruction. This may lead to confusion and uncertainty for both taxpayers and tax officials in practice. It is suggested to use the OECD Commentaries on the relevant articles as a reference for making up more targeted and specific test rules so as to mitigate the discretion by tax authorities.

5.4 International cooperation

BO is usually a company resides in the resident state while China, as the source state, may find difficult to collect the information and even harder to verify the authenticity of the information. Thus, a complete international tax information exchange system is very important and necessary.

6 . Conclusion

The concept of BO is well recognized and has been continuously developed in the international tax field for the past half century. Taxpayers who meet the criteria of domestic laws and tax treaties can be recognized as BO and hence be entitled the treaty benefit. This article has briefly summarized the evolving process of the concept and interpretation of BO under the Article 10, 11 and 12 of OECD framework. With the presentation of certain well-known international cases, it also shows the divergences in doctrines and principles applicable to various countries which further reflect the complexity and uncertainty of this concept. Further, the launch of BEPS project opens a new chapter for tax treaties where the outcome of BEPS has been incorporated into the latest version of OECD MTC and Commentaries (2017).

As for China, the concept of BO has also gone through several phases which are in line with the change of international and domestic tax environment. Both the tax treaties and the domestic laws, in particular the domestic law have ongoingly provide update of BO concept to reflect such changes. However, the comparison of BO concept under latest OED framework / BEPS MLI and China domestic law shows that there is still a lot to improve for BO concept in China. In this post-BEPS ear, it is suggested that China to comprehensively review and renegotiate the tax treaties with other countries for the purpose of reflecting the latest achievements of the BEPS project and reaching the mutual consensus of the convention. Besides, domestic law regarding BO should also be revised to keep consistency with tax treaties and to meet the BEPS initiatives. As an active partner of OECD, it is necessary for China to provide its comments from China perspective for OECD's refining the BO concept.

Appendix A

Introduce “same jurisdiction rule” and “same (better) treaty benefit rule” for multi-tier holding structures under Announcement 9 [2018].

Article 3 of Announcement 9 [2018]:

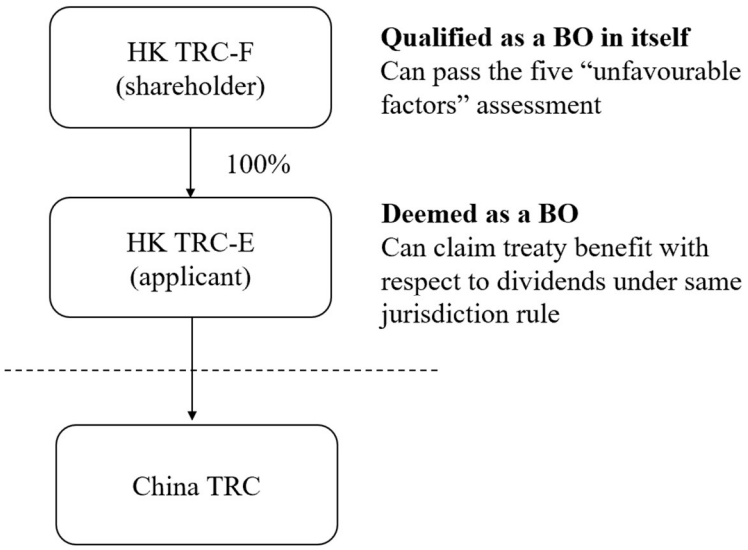
“Where the income derived by the applicant from China is dividend income, if the applicant does not satisfy the criteria for "beneficial owner" but the person who holds 100% of the applicant's shares directly or indirectly satisfies the criteria for "beneficial owner" and the circumstances falls under either of the following scenarios, the applicant shall be deemed as a "beneficial owner":

(1) the aforesaid person who satisfies the criteria for "beneficial owner" is a resident of the country (region) for which the applicant is a resident;

(2) although the aforesaid person who satisfies the criteria for "beneficial owner" is not a resident of the country (region) for which the applicant is a resident, but the said person and the multi-tier holders holding the shares indirectly are persons who satisfy the criteria. "satisfy the criteria for "beneficial owner"" shall mean that it can be determined that the person is a "beneficial owner" upon comprehensive analysis conducted pursuant to the provisions of Article 2 of this Announcement.”

The official interpretation of Announcement 9 [2018] by SAT set several examples to illustrate the above new rule.[74]

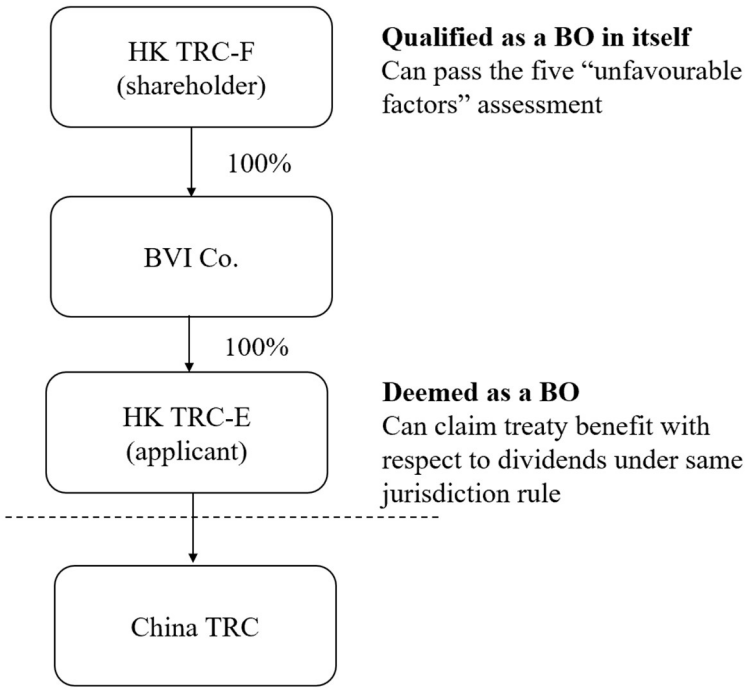
Example 1 – same jurisdiction rule, E & F are both Hong Kong Tax Resident Company (“TRC”)



HK TRC-E is 100% directly owned by another HK TRC-F, both are Hong Kong tax residents (in same jurisdiction). The applicant HK TRC-E is deemed as a BO (though itself is not qualified as a BO), since it is 100% directly owned by the shareholder HK TRC-F which can pass the five “unfavourable factors” assessment and be qualified as a BO itself.

[74] SAT, Interpretation on Announcement 9 [2018], issued on 6 February 2018.

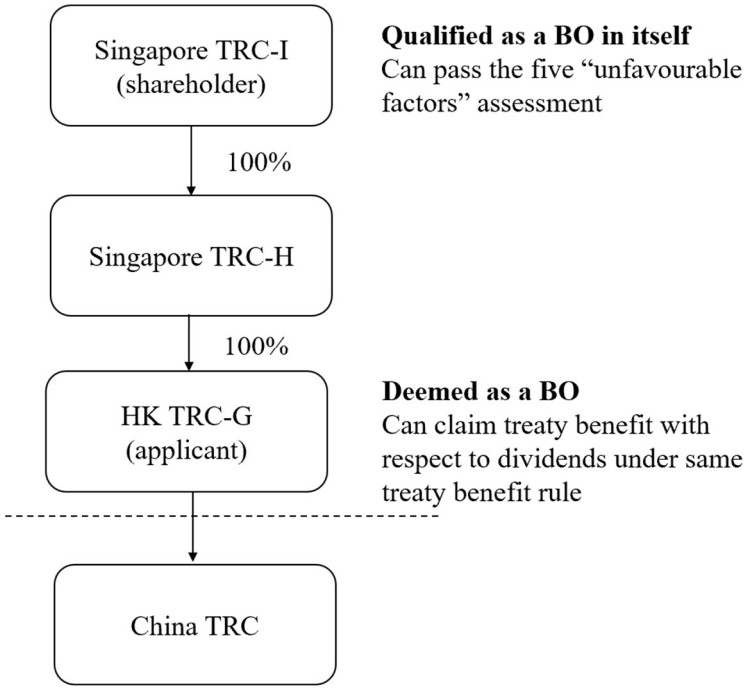
Example 2 – same jurisdiction rule, E & F are both Hong Kong TRC



In a multi-layer holding structure, any intermediate shareholder(s) (e.g. BVI Co.) that is/are not required to be of the same tax residence as the applicant and the shareholder (Hong Kong tax resident in this case). The applicant HK TRC-E is deemed as a BO under this structure, as it is 100% indirectly owned by the shareholder HK TRC-F which can pass the five "unfavourable factors" assessment and be qualified as a BO itself.

These two examples illustrate that under "same jurisdiction rule", there is no difference if any intermediate shareholder(s) exist or if the intermediate shareholder is a tax resident of another jurisdiction for applicant being deemed as a BO, as long as the 100% (in)direct shareholder (qualified as a BO in itself) and applicant are in the same tax jurisdiction.

Example 3 – same treaty benefit rule, Singapore and HK have same treaty benefit on dividend received from China



Singapore TRC-I owns 100% of HK TRC-G indirectly through another Singapore TRC-H. The applicant HK TRC-G is deemed as a BO because the following two conditions under the "same treaty benefit rule" can be met:

(a) Singapore TRC-I (the shareholder) can pass the five "unfavourable factors" assessment and be qualified as a BO itself; and

(b) Singapore TRC-I (the shareholder) and Singapore TRC-H (the intermediate shareholder) are a resident of Singapore (tax treaty jurisdiction) which enjoys the same treaty benefit as HK TRC-G (the HK applicant) with respect to the dividends received from China, namely, 5% withholding tax rate on dividend under both the China-Singapore double tax treaty and the China-HK double tax treaty.

The reason under "same treaty benefit rule", is that since Singapore TRC-I could be granted treaty benefit on dividends if it directly holds PRC TRC (as long as Singapore TRC-I being qualified as a BO), the purpose for Singapore TRC-I's setting up intermediate shareholders (i.e., Singapore TRC-H and HK TRC-G) is not to utilize the preferential treatment under the China-HK double tax treaty.

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