Tax Treaties and How They Affect You the Individual

Common OECD Model Convention Treaty Articles in Plain English

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The goal of this article is to provide a comprehensive checklist of information for the individual to consider prior to filing a tax return. This article is not designed to teach you the technical competence required to perform self compliance; however it will certainly arm you with the technical knowledge to determine if your U.S. tax preparer knows all that they should know to provide you with technically competent professional services.

Income Tax Treaties:

The U.S. and various other countries have negotiated income tax treaties based upon preset international models, one being the OECD Model Tax Convention. One purpose of the tax treaties is to avoid double taxation when the tax laws of two or more countries create a double tax situation.

For the purposes of U.S. nonresident and U.S. resident aliens alike Form 8833, Treaty-Based Return position Disclosure Under Section 6114 or 7701(b) may need to be completed.

Special attention must be paid to the Exceptions from Reporting of Form 8833 found in IRC Sec 301.6114-1(c) most notably dealing with individuals: and in part include the reduction or modification of the taxation of income derived from dependent personal services, pensions, annuities, social security and other public pensions, or income derived from artists, athletes, students, trainees or teachers, income from an individual relating to treaty resourcing for the foreign tax credit, and where a Social Security Totalization Agreement or a Diplomatic or Consular Agreement reduce or modify the taxation of income derived by a taxpayer.

However regardless of the exceptions from reporting on Form 8833 under IRC Sec 301.6114-1(c), this will not affect reporting requirements on Schedule OI (Form 1040-NR)- Other Information- L, which is not subject to such exceptions.

Further as noted below under Other General Facts to Consider, U.S. persons must always remember that buried in all OECD US negotiated treaties are Limitation on Benefit or Savings Clauses prohibiting the application of most Treaty Articles to U.S. persons.

The following income tax treaty articles related to individuals have been highlighted as relevant to possibly providing you relief:

- Article IV- Residence: will seek to determine where persons are tax resident if they are found to be tax residents of two or more countries under the domestic tax laws of those respective countries, commonly referred to as the “treaty tie-breaker rules”.

- Article VI- Income from Real Property: typically, real property is real-estate, this article would cover in part rental income or losses. As below since the country of source maintains the first right of taxation. Most income tax treaties under Article VI will not avoid this matter, so the application of the catch-all article XXIV is required. Or use of a foreign tax credit to avoid double taxation.

- Article X- Dividends: seeks to reduce the U.S. 30 percent flat tax or lower as per specific treaty country.

- Article XI- Interest: seeks to reduce the U.S. 30 percent flat tax or lower as per specific treaty country.

- Article XIII- Gains: covering capital gains from the disposition of assets this article seeks to reduce the U.S. 30 percent flat tax or lower as per specific treaty country. In many cases there is a catch-all provision that capital gains remain taxable *only* in the alienator's state of residence.

- Article XIV- Independent Personal Services: seeks to address the taxation of income from self-employed persons.

- Article XV- Dependent Personal Services: seeks to address the taxation of income of employees. In many treaties if the compensation is paid and borne by a foreign employer and the employee is not physically present in the U.S. for more than 183 days, the compensation shall only be taxable in the employees' state (country) of residence. In the case of foreign nationals here in the U.S., taxation would not be in the U.S.

- Article XVI- Artistes and Athletes: seeks to address the taxation of income from such persons.

- Article XXII- Other Income: seeks to address the taxation of all other income not addressed elsewhere.

- Article XXIV- Elimination of Double Taxation: seeks to invoke what is sometimes already incorporated in to pre-existing domestic tax law, the foreign tax credit. This article is a catch-all that prevents double taxation with respect to income not addressed above.

- Article XXVII- Exchange of Information: is an agreement in principle to allow the respective taxation authorities of all treaty countries to share information to help avoid tax evasion and to allow for the smooth application of domestic tax laws.

Other Income Tax Matters:

- A general tax presumption is that the country of income source retains the first right of taxation. However, treaties usually seek to have that income taxed in the country of residence and not the country of source to avoid a double filing compliance obligation.

- The U.S. has conveniently slipped into most income treaties, a provision to prevent U.S. citizens and Green card holders from accessing treaty benefits. That is, they file U.S. income tax returns as if the income tax treaty did not exist. This is typically referred to as a "Savings Clause" or "Limitation on Benefits Clause".

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