The text and examples below are being cited only for illustrative purposes to provide capacity-building support to developing countries and are not necessarily being endorsed by the PCT, the four partner organizations, their respective managements, or the organizations' member countries, unless specifically indicated otherwise within the materials themselves.

PRESERVATION OF BENEFITS PROVISIONS: BRIEF DESCRIPTION AND EXAMPLES

Preservation of benefits provisions may appear in a new tax treaty that replaces an existing tax treaty between the Contracting States. They are used when the new treaty would eliminate or reduce benefits with respect to specific types of income and/or particular persons. In those cases, it may be viewed as inequitable to upset the reasonable expectations of taxpayers who have made economic decisions in reliance on the existing provisions in the old tax treaty. For this reason, the provisions are found most frequently in articles dealing with the taxation of individuals, as individuals may be less capable of absorbing additional unexpected taxation.

For example, Article 32, paragraph 4 of the 2010 Germany-United Kingdom tax convention included the following rule, which allowed a professor or teacher to qualify for an exemption from host State taxation under the more generous rules of the 1964 convention between the two States (even if he or she would have been denied benefits under the more restrictive rules of the 2010 convention):

> Notwithstanding the provisions of paragraphs 2 and 3 an individual who is entitled to the benefits of Article XIII of the 1964 Convention at the time of entry into force of this Convention shall continue to be entitled to such benefits as if the 1964 Convention had remained in force.

The following paragraph in the same article (paragraph 5 of Article 32 of the 2010 Germany-United Kingdom tax convention) allows a pensioner to continue to be taxed exclusively in the residence State despite a change in the treaty that allows source State taxation in certain circumstances.

> Notwithstanding the provisions of paragraphs 2 and 3 and the provisions of Article 17, where, immediately before the entry into force of this Convention, an individual was in receipt of payments falling within Article X of the 1964 Convention, that individual may elect that the provisions of Article X shall continue to apply to those payments, and not the provisions of Article 17.

Note, this provision does not protect the expectations of individuals who have not yet begun receiving pension benefits. That is, if an individual had participated in a pension plan for many years, and had planned for his retirement on the assumption that he would be taxable only in one State, but a new treaty changes that rule, a too-narrow preservation of benefits rule can frustrate decades of expectations and planning for retirement.[1]

1 See, e.g., Hoge Raad der Nederlanden, 18/04850 (27 Sept. 2019), where it was found that a taxpayer did not qualify for the preservation of benefits provision because he had retired and been found to qualify for pension benefits before the new treaty entered into force, but did not start receiving those benefits until four years after retirement, when the new treaty was in force.

A more generous provision is found in Article I of the 2014 Protocol to the 2012 Canada-New Zealand tax convention. The provision is intended to preserve exclusive taxation by New Zealand of pensions paid to former New Zealand government employees residing in Canada (as under the 1980 treaty between the two States), rather than allowing taxation by both States, as provided in the 2012 convention.

> It is understood that pensions paid by, or out of funds created by, the Government of New Zealand, or a political subdivision thereof to any individual in respect of services rendered to the Government of New Zealand or subdivision thereof, shall be taxable only in New Zealand. This paragraph only applies to pensions paid under a Government Superannuation Fund scheme or a National Provident Fund scheme to individuals who became members of one of these schemes prior to 1996.

Part of the stated justification for the rule is that the amount of those government pensions had been reduced at the same time that they were made tax exempt in 1991. Taxation of those pensions by Canada therefore “would not be consistent with the policy intent for those pensions”. The rule does not apply to persons who have joined the pension scheme relatively recently, presumably because those persons have not relied to the same extent on the tax treatment provided in the prior treaty.

It is difficult to provide specific drafting advice with respect to these provisions because they depend very much on notions of “equity”, which may not be universally held.