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THE EXTENSION OF U.S. TAX TREATIES TO U.S. TERRITORIES, AS ILLUSTRATED BY THE EXAMPLE OF GUAM

Samuel J. Cohen†

In 1901, Justice Brown, writing for a majority of the U.S. Supreme Court in *Downes v. Bidwell* concluded that to apply the U.S. internal revenue system to U.S. territories¹ “would prove an intolerable burden.”² Nevertheless, in 1951, the U.S. Congress imposed a mirror image of the Internal Revenue Code (the “Code”) upon the territory of Guam.³ Congress not only burdened Guam with a precise replicate of the Code, but it also excluded Guam from benefits of U.S. tax treaties with foreign nations.⁴ Thus, while foreign investment within the U.S. receives favorable tax treatment, comparable investment in Guam faces a far greater tax burden.⁵ Because Congress burdens territories such as Guam with tax systems similar to the Code, it should alleviate this onus by allowing those territories to profit from U.S. tax treaties.

This Article analyzes existing U.S. tax treaties with foreign nations and the application of those treaties to Guam. First, the legal status and the tax systems of U.S. territories are examined. Second,

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1. See *infra* note 6 and accompanying text.

2. *Downes v. Bidwell*, 182 U.S. 244, 284 (1901).

3. See *infra* notes 25-28, 108 and accompanying text. According to history, Ferdinand Magellan discovered Guam on March 6, 1521. PAUL CARANO & PEDRO C. SANCHEZ, COMPLETE HISTORY OF GUAM 41 (1964). However, doubt exists as to whether Magellan sighted Guam or the nearby island of Rota. *Id.* Guam, approximately 225 square miles in area, is about 30 miles long and four to nine miles wide. *Id.* at 2. Guam lies 1,353 miles south of Yokohama, Japan; 1,506 miles east of Manila, Philippines; and 3,337 miles west of Honolulu, Hawaii. LAURA THOMPSON, GUAM AND ITS PEOPLE 20 (chart paraphrase) (3d ed. 1947).

4. See *infra* notes 72-100 and accompanying text.

5. See *infra* notes 62-133, 135 and accompanying text.

the application of U.S. tax treaties to territories is analyzed. Third, the rationales for excluding territories from the geographic scope of U.S. tax treaties are presented. Fourth, tax planning and political solutions are offered. Finally, the Article concludes that Guam fall within the scope of U.S. tax treaties.

I. THE LEGAL STATUS OF UNITED STATES TERRITORIES

Territories are defined as "all lands acquired by the United States by treaty or purchase which have not become an integral part of the United States."⁶ To fully understand how tax treaties between the U.S. and foreign nations impact on territories, the legal status and tax systems of the territories must first be explained.

A. THE LEGAL STATUS OF TERRITORIAL GOVERNMENTS

The island of Guam was captured during the Spanish-American War, and was ceded to the U.S. on December 10, 1898, in accordance with the Treaty of Paris between the U.S. and Spain.⁷ The U.S. Constitution provides for the acquisition of territory either by conquest or by treaty.⁸ Article IV of the Constitution empowers Congress with the authority "to dispose of and make all needful Rules and Regulations respecting the Territory and other Property belonging to the United States."⁹ Thus Congress has "plenary power"¹⁰ in the territories, and may directly legislate the local af-

6. 72 AM. JUR. 2D *States, Territories, and Dependencies* § 129 (1974). "Territorial possessions may be defined as all lands acquired by the United States by treaty or purchase which have not become an integral part of the United States, or, as sometimes stated, territory that has not become incorporated into the United States."

"[U]nder [U.S.] law, the terms 'territory' and 'dependency' have, for all practical purposes, become synonymous." *Id.* § 130. In addition, the word "possession," as used in an act of Congress, has been held not to be a word of art, descriptive of a recognized geographical or governmental entity, but rather a term which should be construed, if reasonably possible, to effectuate the intent of the lawmakers. *Id.* § 131.

In this article, the terms "dependency" or "possession" will not be used, instead the term "territory" will be substituted wherever possible.

7. 48 U.S.C. § 142 (1988). As a Spanish colony, Guam was so cloistered from world events that its residents were unaware of the Spanish-American War until a convoy of American warships sailed into Guam's Apra Harbor on June 20, 1898. CARANO & SANCHEZ, *supra* note 3, at 171. It is rumored that the salvo of warning fire from the U.S. warships was misinterpreted by the Spaniards as a friendly greeting, and that the Spaniards thereupon announced that they could not return such a greeting because they lacked ammunition. CHARLES BEARDSLEY, *GUAM PAST AND PRESENT* 192 (1964). This made the capture of Guam "about the quickest victory the United States Navy has had in the Pacific area, and it was the first territorial conquest outside the continental limits of the United States." *Id.* at 191.

8. *United States v. Huckabee*, 83 U.S. 414, 434 (1873).

9. U.S. CONST. art. IV, § 3, cl. 2.

10. *Binns v. United States*, 194 U.S. 486, 491 (1904). As part of its plenary power in the territories, "Congress has the entire dominion and sovereignty, national and lo-

fairs of territories.¹¹ Congress may also abrogate any pre-existing law in effect prior to the area becoming a U.S. territory and any law enacted thereafter by a territorial legislature to which Congress has delegated a portion of its legislative power.¹² Furthermore, constitutional provisions such as the Bill of Rights do not limit the exercise of this congressional power.¹³ The Constitution only applies to a territory if Congress passes legislation to that effect.¹⁴

Although a territory is not a distinct sovereignty,¹⁵ Congress may delegate power to a local territorial government¹⁶ through legislation termed an organic act, which enumerates and limits the powers of this territorial government.¹⁷ Congress passed an organic act for Guam in 1950,¹⁸ which declared Guam to be an unincorpor-

cal, Federal and state, and has full legislative power over all subjects upon which the legislature of a state might legislate within the State; and may, at its discretion, intrust that power to the legislative assembly of a Territory." *Sims v. Sims*, 175 U.S. 162, 168 (1899). "As an unincorporated territory of the United States, Guam is subject to the plenary authority of Congress to provide for its government under article IV, section 3, of the United States Constitution." *Agana Bay Dev. Co. v. Guam*, 529 F.2d 952, 954 (9th Cir. 1976).

11. *Binns*, 194 U.S. at 492.

12. *Inter-Island Steam Navigation Co. v. Territory of Hawaii*, 305 U.S. 306, 314 (1938) (quoting *The Late Corp. of the Church of Jesus Christ of Latter-Day Saints, L.D.S. v. United States*, 136 U.S. 1, 43 (1890)).

13. *Hooven & Allison Co. v. Evatt*, 324 U.S. 652, 674 (1945); *Downes*, 182 U.S. at 277. There are, however, two other constitutional limits upon congressional action. First, limitations in the Constitution "go to the very root of the power of Congress to act at all, irrespective of time or place." For example, Article I, Section 9, Clause 3 provides that "[N]o Bill of Attainder or *ex post facto* Law should be passed." *Downes*, 182 U.S. at 277. The second constitutional limitation is that "'fundamental' constitutional rights apply in the territor[ies]." *Wabol v. Villacrusis*, 898 F.2d 1381, 1390 (9th Cir. 1990); *Downes*, 182 U.S. at 283 (people are entitled to be "protected in life, liberty, and property").

14. *Hooven & Allison Co.*, 324 U.S. at 674; *Downes*, 182 U.S. at 279.

15. *Talbot v. Silver Bow County*, 139 U.S. 438, 446 (1891); *In re Lane*, 135 U.S. 443, 447 (1890) (territories "are not in any sense independent governments").

16. *Cincinnati Soap Co. v. United States*, 301 U.S. 308, 317 (1937). "A dependency has no government but that of the United States, except so far as the United States may permit." *Id.* "[Congress] may legislate directly in respect to the local affairs of a territory, or transfer the power of such legislation to a legislature elected by the citizens of the territory." *Binns*, 194 U.S. at 491.

17. *National Bank v. County of Yankton*, 101 U.S. 129, 133 (1880) ("The organic law of a Territory takes the place of a constitution, as the fundamental law of the local government."). After Congress establishes an organic act for a civil government, the territory is considered to be "organized." *United States v. Standard Oil*, 404 U.S. 558, 559 n.2 (1972).

18. *Ngiraingas v. Sanchez*, 495 U.S. 182, 185 (1990) ("[The Organic Act of Guam] has functioned as a constitution for Guam, outlining the scope of the territorial government's authority. And the territorial government of Guam can act only to the limits of the Organic Act, just as the national government must observe the limits of the Constitution.") *Agana Bay Dev. Co. v. Guam*, 529 F.2d 952, 954 (9th Cir. 1976); *People v. Okada*, 694 F.2d 565, 568 (9th Cir. 1982) ("The provisions of the Organic Act . . . set the outer limits of the Guam Legislature's authority.").

rated territory of the United States.¹⁹

In many respects the government of Guam resembles that of the United States. The Guam government is organized into three branches: executive, legislative, and judicial.²⁰ A nonvoting delegate also represents Guam in the U.S. House of Representatives.²¹ Furthermore, the Bill of Rights of Guam, passed by Congress in 1968, affords Guam residents with most of the protection granted by the U.S. Constitution.²²

B. TERRITORIAL TAX SYSTEMS

The United States gives its territories the authority to levy taxes.²³ Article I of the U.S. Constitution provides that “[t]he Congress shall have Power to lay and collect Taxes, Duties, Imposts, and Excises. . . .”²⁴ Instead of delegating this taxation power to Guam, Congress has provided that the income tax laws in force in the U.S. likewise are applicable in Guam.²⁵

The income tax law in effect in Guam is referred to as the “Guam Territorial income tax”²⁶ (the “Guam Tax”). It is also termed the “mirror system”²⁷ because in applying the Guam Tax, the applicable provisions of the Code are read to substitute “Guam” for “United States,” along with other changes in language where necessary.²⁸

The treatment of foreign individual and corporate taxpayers in Guam illustrates how the Guam Tax operates. Section 871 of the

19. 48 U.S.C. § 1421(a) (1988). Incorporation means making the U.S. Constitution applicable to the territory. See *Dorr v. United States*, 195 U.S. 138, 141-42 (1904). Because incorporation has always been an important step leading to statehood, Congress “has been careful to bestow incorporation only when it has already been determined that the territory is destined for statehood.” *Smith v. Government of the Virgin Islands*, 375 F.2d 714, 718 (3d Cir. 1967).

20. 48 U.S.C. § 1421(a) (1988).

21. *Id.*

22. ARNOLD H. LIEBOWITZ, *DEFINING STATUS: A COMPREHENSIVE ANALYSIS OF THE UNITED STATES TERRITORIAL RELATIONS* 343 (1989).

23. *Domenech v. National City Bank*, 294 U.S. 199, 204-05 (1935).

24. U.S. CONST. art. I, § 8, cl. 1.

25. 48 U.S.C. § 1421i(a) (1988). The statute applying the U.S. income tax laws in Guam also provides for a separate tax by the legislature of Guam in an amount not to exceed 10 percent of a taxpayer's tax obligation. *Id.*

26. *Id.* § 1421i(b).

27. *Sayre & Co. v. Riddell*, 395 F.2d 407, 410 (9th Cir. 1968). The Tax Reform Act of 1986 defines the “mirror system” as “the provisions of law (in effect on the day before the date of the enactment of this Act) which make the provisions of the income tax laws of the United States (as in effect from time to time) in effect in a possession of the United States.” Tax Reform Act of 1986, Pub. L. No. 99-514, § 1271(f)(2), 100 Stat. 2085, 2592, *reprinted in* 1 TAX REFORM 1986: A LEGISLATIVE HISTORY OF THE TAX REFORM ACT OF 1986: THE LAW, REPORTS, HEARINGS, DEBATES AND RELATED DOCUMENTS, (Bernard D. Reams, Jr. & Margaret H. McDermott, eds., 1988).

28. 48 U.S.C. § 1421i(e) (1988).

Code imposes a 30% gross receipts tax on fixed or determinable annual or periodical ("FDAP")²⁹ gains, profits, and income from U.S. sources³⁰ by a nonresident alien individual.³¹ In comparison, the Guam Tax imposes on a nonresident alien individual an identical 30% gross receipts tax on the amount received as FDAP gains, profits, and income from Guam sources.³² For foreign corporations,³³ Code Section 881 imposes a 30% gross receipts tax on the amount received by the foreign corporation as FDAP gains, profits, and income from U.S. sources. Similarly, under the Guam Tax, the tax on foreign corporations would be modified to apply only to income derived from Guam sources.³⁴

The mirror system, however, may not be appropriate for Guam's social and economic situation.³⁵ Thus, in the Tax Reform Act of 1986, Congress provided that Guam may enact a new income tax law in lieu of the mirror system.³⁶ Any new Guam income tax law, however, must still conform to the guidelines set by Congress. The income tax law must raise an amount of revenue equivalent to the amount raised by the mirror system.³⁷ Also, a reformed Guam tax code may not discriminate against any U.S. person or resident (corporate or otherwise) of any other territory or possession.³⁸ Moreover, before enacting any new income tax law,

29. See *infra* note 50 and accompanying text detailing some of the types of income included in FDAP.

30. Detailed rules for determining whether an income item is from a U.S. source are provided in Sections 861-865 of the Code.

31. I.R.C. §§ 871(a), 871(a)(1)(A) (1992). This 30% gross receipts tax does not apply to any income that is effectively connected with the conduct of a trade or business within the U.S. *Id.* § 871(a).

32. The operation of 48 U.S.C. § 1421i(e) would substitute "Guam" for "United States" in Section 871 of the Code. See *supra* notes 26-28 and accompanying text.

33. The Code defines a foreign corporation as any corporation that is not a domestic corporation. I.R.C. § 7701(a)(5) (1992). A domestic corporation is one that is organized in the U.S. or under the laws of the U.S. or of any state. *Id.* § 7701(a)(4) (1992). A domestic corporation under the Guam Tax would be a corporation organized under the law of Guam. See *supra* notes 26-28 and accompanying text.

34. The operation of 48 U.S.C. § 1421i(e) would substitute "Guam" for "United States" in Section 881 of the U.S. Internal Revenue Code. See *supra* notes 26-28 and accompanying text.

35. *Guam Commonwealth: Hearing Before the Subcomm. on Insular and International Affairs of the House Comm. on Interior and Insular Affairs on H.R. 98, 101st Cong., 1st Sess. 242 (Dec. 11, 1989) [hereinafter Guam Commonwealth Hearings]* (statement of Rufo C. Taitano, Member, Guam Commission on Self-Determination) (The mirror code "has always placed Guam in a precarious position of uncertainty with regard to the potential for changes in the U.S. law."). For example, "[I]t was projected that changes in the I.R.C. engendered in the 1986 Act would reduce Guam's personal income tax revenues by \$18 million and corporate income taxes by another \$5 million." *Id.* "Fortunately, the strength of Guam's economy during the transition to the new tax provisions was such that the projected tax loss were never materialized." *Id.* at 243.

36. Pub. L. No. 99-514, § 1271(a).

37. *Id.* § 1271(c).

38. *Id.* § 1271(d).

Guam must enter into an implementing agreement with the U.S. that satisfactorily addresses the following four concerns:

- (1) the elimination of double taxation involving taxation by such possession and taxation by the United States,
- (2) the establishment of rules under which the evasion or avoidance of United States income tax shall not be permitted or facilitated by such possession,
- (3) the exchange of information between such possession and the United States for purposes of tax administration, and
- (4) the resolution of other problems arising in connection with the administration of the tax laws of such possession or the United States.³⁹

On April 5, 1989, Guam entered into an implementation agreement with the U.S.⁴⁰ However, the agreement was amended on December 27, 1990, delaying its effective date indefinitely.⁴¹ The delay was requested to give Guam the opportunity to plan, enact, and implement a new tax law.⁴²

The double taxation concern of the U.S. poses a potential problem for individuals in Guam who are both Guam residents⁴³ and U.S. citizens, since Congress gave U.S. citizenship to persons born on Guam after it became a U.S. territory in 1899.⁴⁴ Generally, the Code taxes U.S. citizens on their worldwide income.⁴⁵ Therefore, residents of Guam appear to be subject to both the U.S. income tax as U.S. citizens and the Guam Tax as Guam residents. However, Section 931 of the Code specifically exempts from taxation any income derived from, or effectively connected with the conduct of a trade or business within Guam by a bona fide resident of Guam.⁴⁶ In effect, then, a double taxation problem does not exist for Guam individuals.

39. *Id.* § 1271(b).

40. Tax Convention 1989-1 C.B. 342, 345.

41. Treas. Rel. (Dec. 27, 1990).

42. 9 BENDER, BENDER'S FEDERAL TAX SERVICE [MB] § M:15.80, at 15-18 (1992).

43. The definition of residency for individuals is provided in Treasury Regulations. Treasury Regulation 1.871-2(b) provides:

(b) *Residence defined.* An alien actually present in the United States who is not a mere transient or sojourner is a resident of the United States for purposes of the income tax. Whether he is a transient is determined by his intentions with regard to the length and nature of his stay. A mere floating intention, indefinite as to time, to return to another country is not sufficient to constitute him a transient. If he lives in the United States and has no definite intention as to his stay, he is a resident.

Treas. Reg. § 1.871-2(b) (1992). This regulation, however, does not apply to nonresident alien individuals. See *supra* note 31 and accompanying text.

44. 8 U.S.C. § 1407 (1988).

45. I.R.C. § 61; *Cook v. Tait*, 265 U.S. 47, 56 (1924).

46. I.R.C. § 931(a). The converse of the Section 931 exception is that income *not* derived from or effectively connected with the conduct of a bona fide trade or business within Guam by a bona fide resident of Guam will be taxed by both the U.S. and Guam.

In contrast to the U.S. tax treatment of Guam individuals, Guam corporations are considered to be foreign corporations under U.S. law.⁴⁷ The Code taxes foreign corporations on certain types of U.S. source income.⁴⁸ Under Section 881, which parallels in part the Section 871 provisions applied to foreign individuals, the tax constitutes 30% of the amount received from sources in the U.S. as profits, income, and FDAP gain.⁴⁹ Such FDAP gain includes interest other than original issue discounts, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, and emoluments.⁵⁰ The 30% gross receipts tax, however, does not apply to any amount received that is effectively connected with the conduct of a trade or business in the U.S.⁵¹

Under the mirror system, the Guam Tax treats U.S. corporations as foreign. It imposes a 30% gross receipts tax on U.S. corporations in the same manner as U.S. tax law imposes a 30% gross receipts tax on Guam corporations.⁵²

Section 881(b) of the Code, however, enables Guam corporations to avoid the 30% gross receipts tax on U.S. source income. Section 881(b) treats a Guam corporation as not foreign if it meets three requirements:

- (1) at all times during such tax year less than 25% in value of the stock of such corporation is beneficially owned (directly or indirectly) by foreign persons,⁵³

47. *Sayre & Co. v. Riddell*, 395 F.2d 407, 408 (9th Cir. 1968).

48. I.R.C. § 881(a). Similar rules also apply to nonresident alien individuals under both the U.S. and Guam tax laws. *Id.* § 871(a).

49. *Id.* § 881(a).

50. *Id.* § 881(a)(1).

51. *Id.* § 881(a). Such effectively connected income, instead of being subject to the 30% gross receipts tax, is taxed like a domestic corporation pursuant to Code Sections 11, 55, 59A, or 1201(a). *Id.* § 882(a).

52. Under both U.S. and Guam law, income of foreign corporations effectively connected to trade or business in the area imposing the tax will be taxed under the tax rates for domestic corporations in Section 11. *Id.* § 882.

53. For the purposes of Section 881(b)(1), the Code defines "foreign person" to mean any person other than "(i) a United States person, or (ii) a person who would be a United States person if references to the United States in Section 7701 included references to a possession of the United States." *Id.* § 881(b)(2)(A).

A United States person is "(A) a citizen or resident of the United States, (B) a domestic partnership, (C) a domestic corporation, and (D) any estate or trust (other than a foreign estate or trust, within the meaning of Section 7701(a)(31))." *Id.* § 7701(a)(30). "Domestic" when applied to a corporation or partnership means "created or organized in the United States or under the law of the United States or of any State." *Id.* § 7701(a)(4). In contrast, "foreign" when applied to a corporation or partnership means "a corporation or partnership which is not domestic." *Id.* § 7701(a)(5).

In applying Section 881(b) under U.S. law, owners of Guam corporate stock who are defined as not foreign persons are U.S. citizens, Guamanians who are U.S. citizens, U.S. corporations, U.S. partnerships, and U.S. non-foreign estates or trusts. In addition, because Section 881(b)(2)(A)(ii) applies the definition of U.S. persons as if references to the U.S. persons in Section 7701 include a possession of the U.S., owners that

- (2) at least 65% of the gross income of such corporation is shown to the satisfaction of the Secretary to be effectively connected with the conduct of a trade or business in such a possession of the United States for the three-year period ending with the close of the taxable year of such corporation (or for such part of such period as the corporation or any predecessor had been in existence), and
- (3) no substantial part of the income of such corporation is used (directly or indirectly) to satisfy obligations to persons who are not bona fide residents of such a possession or the United States.⁵⁴

Under Guam's mirror system, the same Section 881(b) exception to the 30% gross receipts tax applies to U.S. corporations.

The Section 881(b) exception from the 30% gross receipts tax is of little use however, because most foreign investment in Guam does not come from the U.S.⁵⁵ In 1984, the devaluation of the dollar strengthened the Japanese yen, which led to prodigious growth in the Japanese tourist industry in Guam.⁵⁶ In 1989, roughly 500,000 Japanese tourists visited Guam; this number is predicted to increase.⁵⁷ This growth in tourism has stimulated a construction

are defined as not foreign persons would also include Guam residents, Guam partnerships, Guam corporations and any Guam non-foreign estates or trusts.

54. *Id.* § 881(b)(1). For purposes of determining ownership, the rules of Section 318(a)(2) apply to Section 881(b), except that "5 percent" is substituted for "50 Percent" in Section 318(a)(2)(C). *Id.* § 881(b)(2)(B).

This version of Section 881(b) will become effective only after the implementing agreement between Guam and the U.S. goes into effect. The effective date of the current implementing agreement was delayed indefinitely. *See supra* notes 40-42 and accompanying text. Thus, the version of Section 881(b) of the Internal Revenue Code of 1954 is currently effective.

The 1954 Code version of Section 881(b) provides:

- (1) At all times during the year less than 25% of the value of the corporation's stock was owned by foreign persons; and
- (2) At least 20 % of the corporation's gross income was from Guam sources for the three-year period ending with the close of the tax year (or since the corporation came into existence if less than three years old).

Id. § 881(b) (1954).

55. *Guam Commonwealth Hearings, supra* note 35, at 92 (statement of Joseph A. Ada, Governor of Guam) ("The investment in Guam does not come from America; it comes from Japan. The hotels in Guam are not filled with Americans, but Asians.").

56. Francis K. Hezel & Thomas B. McGrath, *The Great Flight Northward: FSM Migration to Guam, reprinted in Implementation of the Compact of 1985: Oversight Hearing before the Subcomm. on Insular and Internal Affairs of the House Comm. on Interior and Insular Affairs*, 101st Cong., 1st Sess. 361 (July 18, 1989) ("Then in early 1984 the real boom began. Thanks to the devaluation of the dollar and the resultant strength of the yen, the Japanese tourist industry on Guam began to show prodigious growth. This in turn helped to power a new construction boom and rapid growth in island business.").

57. *Hearings on National Defense Authorization Act for Fiscal Year 1991 and Oversight of Previously Authorized Programs before the House Comm. on Armed Services*, 101st Cong., 2nd Sess. 189 (Feb. 1, 1990) (statement of Admiral Huntington Hardisty) ("There were almost 500,000 Japanese tourists in Guam last year and that is going to

boom and rapid growth in local business.⁵⁸ In addition to increased Japanese tourism, Japan has also become the major source of investment capitalization in Guam.⁵⁹

Japanese corporations that invest in either the U.S. or Guam are subject to the 30% gross receipts tax under Section 881 on corporate income derived from either U.S. or Guam sources,⁶⁰ in addition to being taxed in Japan. The burden of this double taxation creates disincentives to invest. The U.S. and Japan, however, have negotiated a tax treaty that lowers the tax rates on various types of corporate income, such as a maximum tax on corporate dividends of 15% of the gross amount actually distributed.⁶¹ This 50% reduction in the tax rate demonstrates the significant incentives to foreign investment in the U.S. created by tax treaties.⁶² Whether any of the U.S. tax treaties applies to and benefits U.S. territories such as Guam, however, will be analyzed in section II of this Article.

II. THE APPLICATION OF U.S. TAX TREATIES TO U.S. TERRITORIES

A. SUPRANATIONAL TAX TREATY MODELS

A number of model tax treaties have been proposed to alleviate the problem of double taxation.⁶³ The Organization for Economic

increase. The Japanese are funding eight new golf courses there and there is hardly any property.”).

58. Hezel & McGrath, *supra* note 56, at 361.

59. *Guam Commonwealth Hearings*, *supra* note 35, at 243 (statement of Rufo C. Taitano) (“Japan is the major source of investment monies into Guam; U.S. firms seem to have no interest in the strategic commercial location that the island occupies.”).

60. Under Section 881 of the Code the gross receipts of a Japanese corporation are subject to the 30% tax if (1) that Japanese corporation is not incorporated under U.S. law and therefore is defined as a foreign corporation, and (2) the gross receipts are from U.S. or Guam sources and are classified as FDAP. In addition, those same gross receipts cannot be effectively connected with the conduct of a trade or business in the U.S. or Guam.

61. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, Mar. 8, 1971, U.S.-Japan, art. 12(2)(a), *reprinted in* RICHARD L. DOERNBERG & KEES VAN RAAD, *U.S. TAX TREATIES* 246 (1991).

62. *Guam Commonwealth Hearings*, *supra* note 35, at 243-44 (statement of Rufo C. Taitano). Taitano stated:

[i]n a tax treaty with Japan, though, this [30%] withholding rate [on foreign distributions of U.S. source income] has been reduced to ten percent, but Guam is not included in the treaty, it being excluded from coverage by the U.S. . . . The result is that Hawaii and other states that compete with Guam for Japanese investment funds are given a distinct advantage, to the detriment of Guam's economic development.

Id.

63. Work on model tax conventions dates back to the League of Nations and draft conventions in 1928, 1943, and 1946. Robert J. Patrick, Jr., *United States Negotiating Objectives and Model Treaties*, 5 N.Y.U. INT'L INST. ON TAX AND BUS. PLANNING 5 (Virginia di Francesco & Nicolas Liakas eds., 1978). Although the U.S. was not a

Cooperation and Development ("OECD"), for example, published the leading model tax treaty, the OECD Draft Double Taxation Convention on Income and Capital. This model treaty was published in 1963, with a revised version published in 1977.⁶⁴

The 1963 and 1977 OECD Treaties apply to "persons who are residents of one or both of the contracting states."⁶⁵ In addition, they define the existing taxes to which the particular tax treaty shall apply for each country.⁶⁶ However, the OECD models do not expressly define the geographic scope which they cover.⁶⁷

Article 3 is the definition section of the OECD 1977 Treaty.⁶⁸ Article 3(2) provides that any term not defined "shall, unless context otherwise requires, have the meaning which it has under the law of that State concerning taxes to which the Convention applies."⁶⁹ Article 3(2) of the OECD 1963 Treaty contains substantially the same language.⁷⁰

Resorting to the law of one of the contracting states, however, has been criticized because definitions under local law may not be interpreted uniformly or may be unclear.⁷¹ Furthermore, contracting states could potentially unilaterally change the nature of agreements by interpreting treaty definitions after the treaty has been signed.

B. U.S. TREASURY MODEL AND U.S. TREATIES IN FORCE

1. *The Definition of "United States" in U.S. Tax Treaties*

The U.S. Treasury Department published its model tax treaty (the "U.S. Treasury Model Treaty") in 1977 and revised it on June

member of the League of Nations, U.S. tax scholars participated in some of the drafting of that model treaty. This treaty has been largely supplanted by the OECD Draft Double Taxation Convention on Income and Capital in 1963.

The United Nations has drafted a model tax treaty for use in negotiations between developed and developing countries. The United Nations Model Double Taxation Convention Between Developed and Developing Countries was published in 1980.

64. OECD Draft Double Taxation Convention on Income and Capital (1963)(revised 1977), *reprinted in* DOERNBERG & VAN RAAD, *supra* note 61, at 438 (1991) [hereinafter OECD Convention].

65. OECD Convention, *supra* note 64, art. 1 ("Personal Scope").

66. *Id.* art. 2(3) ("Taxes Covered").

67. DOERNBERG & VAN RAAD, *supra* note 61, at 537 (quoting Selections from the 1977 OECD Commentary).

68. OECD Convention, *supra* note 64, art. 3 ("General Definitions").

69. *Id.* art. 3(2).

70. The 1963 OECD Treaty provides in part: "As regards the application of the Convention by a Contracting State any term not *otherwise* defined shall, unless the context otherwise requires, have the meaning which it has under the *laws* of that *Contracting State relating to the taxes which are the subject of the Convention.*" *Id.* (emphasis added to show the differences between the 1963 and 1977 OECD Treaties).

71. U.S. Treasury Dept.'s Proposed New Model Income Tax Treaty, June 16, 1981, *reprinted in* DOERNBERG & VAN RAAD, *supra* note 61, at 439 (1991) [hereinafter the U.S. Treasury Model Treaty].

16, 1981.⁷² The geographic scope of both versions of the U.S. Treasury Model Treaty excludes U.S. territories from coverage. Specifically, the U.S. Treasury Model Treaty defines "United States" as "the United States of America, but [not including] Puerto Rico, the Virgin Islands, Guam or any other United States possession or territory."⁷³ Nine of the forty-seven U.S. tax treaties currently use this definition.⁷⁴

Not all existing U.S. treaties contain a geographic scope that excludes U.S. territories. Some of the earliest U.S. treaties define "United States" as "the United States, the territories of Alaska and Hawaii, and the District of Columbia."⁷⁵ Today, only four treaties still define "United States" as including the territories of Alaska and Hawaii.⁷⁶

After Alaska and Hawaii achieved statehood, subsequent treaties and treaty amendments omitted the phrase "the territories of Alaska and Hawaii."⁷⁷ The "United States" is now most commonly defined as "the States thereof and the District of Columbia."⁷⁸ Twenty-two existing tax treaties currently use this definition.⁷⁹

While the U.S. Treasury Model Treaty expressly excludes territories such as Guam from its scope, the definition of the "United States" does not mention the applicability of the model tax treaty to territories. It appears in nontax law that "states" and "territories" are separate and distinct entities.⁸⁰ However, similar to Article 3(2)

72. *Id.* art. 3(1)(f).

73. U.S. Treasury Dept.'s Proposed New Model Income Tax Treaty, June 16, 1981, reprinted in DOERNBERG & VAN RAAD, *supra* note 61, at 439 (1991) [hereinafter the U.S. Treasury Model Treaty].

74. *See infra* Appendix B.

75. *See infra* Appendix D.

76. *Id.*

77. The territories of Alaska and Hawaii were removed from the definition of "United States" in the Code by 1959 and 1960. The definition of "United States" was amended to mean in a geographic sense "the States and the District of Columbia." 26 U.S.C. § 7701(a)(9) (1988).

78. *See infra* Appendix A.

79. *Id.*

80. *See, e.g.,* *Hooven & Allison Co. v. Evatt*, 324 U.S. 652, 673 (1945); *see also* *Hepburn & Dundas v. Ellzey*, 6 U.S. 445 (1805), in which the Court stated,

[T]he term "states" . . . is a vague expression. It will sometimes mean an extent of country within certain limits, within which the authority of the neighboring country cannot be lawfully exercised. It sometimes means the government which is established in separate parts of a territory occupied by a political society. It may also be said to be a society by which a multitude of people unite together under the dependence of a superior power for protection. And sometimes it means a multitude of people united by a communion of interest and by common laws. This is the definition given by Cicero.

Id. at 445-46.

Ordinarily, the term "States" is held to apply to those political communities, exer-

of the OECD Model Treaty, all U.S. tax treaties contain a default provision which provides that any term not defined in the convention "shall, unless the context otherwise requires, . . . have the meaning which it has under the laws of that State concerning the taxes to which the Convention applies."⁸¹ Therefore, the definitions of "states" and "territories" must be provided either by U.S. tax law for treaty purposes or by the context of those terms within a particular treaty.

As for U.S. treaties which define "United States" as the "States thereof and the District of Columbia," there are indications that the definition "United States" does not include territories. For example, instead of defining "United States" as only the "States thereof," the definition provides that the United States consists of both "States" and the "District of Columbia." To the extent that the term "States" includes all U.S. territories, the District of Columbia need not be separately defined. Thus, the inclusion of the term "District of Columbia" emphasizes that the term "States" in the definition does not include all U.S. territories. However, such an inference is inconclusive on whether the definition of the "United States" includes specific U.S. territories such as Guam.

As part of U.S. tax law, the Code also contains a definition of "United States." The Code defines "United States" as the "States and the District of Columbia."⁸² In addition, "State" includes "the District of Columbia when such construction is necessary."⁸³ Therefore, the definition of "United States," as a combination of the "States" and the "District of Columbia," demonstrates that the term "States" does not include all U.S. territories. However, like

cising various attributes of sovereignty, which compose the United States, as distinguished from the organized municipalities known as Territories and the District of Columbia. *Talbott v. Silver Bow County*, 139 U.S. 438, 445 (1891)(citations omitted). However, it is established that the District of Columbia and the Territories are "states" as that word is used in treaties with foreign powers, with respect to the ownership, disposition and inheritance of property. *Downes v. Bidwell*, 182 U.S. 244, 270 (1901).

That our dependencies, acquired by cession as the result of our war with Spain, are territories belonging to, but not a part of the union of states under the Constitution, was long since established by a series of decisions of the U.S. Supreme Court beginning with *The Insular Tax Cases* in 1901. *Hooven & Allison Co.*, 324 U.S. at 673 (citations omitted).

81. See U.S. Treasury Model Tax Treaty, *supra* note 72, art. 3(2); William L. Burke, *Report on Proposed United States Model Income Tax Treaty*, 23 HARV. INT'L L.J. 219, 237 n.16a (1983) ("Generally treaties contain a provision similar to article 3(2), stating that when a term is not defined it shall take its meaning from the law of the state applying the treaty. Interpretation of the term "United States" will thus typically lead to a consideration of U.S. domestic law when the U.S. is applying the treaty.").

Article 3(2) also provides that the competent authorities of the Contracting States may agree to a common meaning pursuant to the Mutual Agreement Procedure under Article 25. U.S. Treasury Model Tax Treaty, *supra* note 72, art. 3(2).

82. I.R.C. § 7701(a)(9) (1988).

83. *Id.* § 7701(a)(10).

the contextual definition of "States" in U.S. treaties, this inference is also inconclusive on whether the definition of "United States" includes specific U.S. territories.

Prior to 1959, the Code definition of "States" included the "Territories and the District of Columbia."⁸⁴ The Code definition of "United States" at that time included the territories of Alaska and Hawaii.⁸⁵ Because both Alaska and Hawaii achieved statehood in 1959, reference to them as territories was omitted in the definition of "United States" and reference to "territories" was also omitted in the definition of "State."⁸⁶

The inclusion of the territories of Alaska and Hawaii in the definition of "United States" prior to 1959 provides some evidence that "United States" as defined in the Code does not include U.S. territories. Instead of including all U.S. territories in the definition of "United States," the definition prior to 1959 only included Alaska and Hawaii. If other territories were intended to be included in the term "United States," they would have been included in the definition of "United States" in the same way as were the territories of Alaska and Hawaii.

While the historical changes in the definition of "United States" may be ambiguous, removing the term "territories" from the definition of "State" in 1959 clearly demonstrates that under current U.S. tax law, territories are not included in the definition of "States." To the extent that the definition of "United States" consists solely of the "States thereof and the District of Columbia," and territories are not included in the definition of "States," then territories would not be included in this definition of "United States." Therefore, the definitions "United States" and "States" under U.S. tax law indicate that the definition "United States" as the "States thereof and the District of Columbia" in some U.S. treaties does not include U.S. territories.

2. *The Definition of "United States" in U.S. Tax Treaties with China and India*

The U.S. tax conventions with China and India provide a dif-

84. The Internal Revenue Code of 1954 defines "State" as "the Territories and the District of Columbia, where such construction is necessary to carry out provisions of this title." I.R.C. § 7701(a)(10) (1954).

85. The definition of "United States" in the Internal Revenue Code of 1954, when used in a geographical sense, was "only the States, the Territories of Alaska and Hawaii, and the District of Columbia." *Id.* § 7701(a)(9).

86. Hawaii Omnibus Act, Pub. L. No. 86-624, § 18(j), 74 Stat. 422 (1960) (amended the 1954 Code Section 7701(a)(10) by striking out "the Territory of Hawaii and" following the words "to include", effective as of August 21, 1959); Alaska Omnibus Act, Pub. L. No. 86-70, § 22(g), 73 Stat. 146 (1960) (amended the 1954 Code Section 7701(a)(9) by replacing "the Territory of Hawaii" for "the Territories of Alaska and Hawaii", effective January 3, 1959).

ferent definition of geographic scope.⁸⁷ In the U.S. tax conventions with China⁸⁸ and India,⁸⁹ the term "United States of America" is defined as "all the territory of the United States of America, including its territorial sea, in which the laws relating to United States tax law are in force."⁹⁰ The treaties with China and India define "United States tax" as the federal income taxes imposed by the Code.⁹¹

The phrase "in which the laws relating to United States tax law are in force" in the tax treaties with China and India can be interpreted narrowly or broadly. Interpreted narrowly, the phrase indicates that the treaties only apply to areas where the Code is in force. However, this restricted reading does not give effect to the treaties' broader language, which merely requires that the territory be one where laws "relating" to United States tax are in force. Thus, territories such as Guam with tax systems that mirror the Code should be covered under the U.S. tax treaties with China and India if Guam's tax laws are deemed to "relate to United States tax."⁹²

Because there is no definition in these treaties regarding which laws "relate to United States tax," the definition under the domestic

87. Both China and India are considered less developed countries, and tax treaties with less developed countries are often negotiated with greater flexibility. Thomas D. Koch, *Current United States Tax Treaty Policy with Developing Countries—The Need for a United States-Developing Country Model Income Tax Treaty*, 7 ASILS INT'L L.J. 125, 157 (1983) ("Each treaty as approved by the Senate Foreign Relations Committee, contains provisions specifically designed to reflect the individual country's status as a developing nation; thus, the treaties represent purposeful departures from previous United States tax treaty policy.").

88. Agreement between the Government of the United States of America and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income, art. 3(1)(b) (Apr. 30, 1984), *as amended by Protocol* (May 10, 1986), *reprinted in* DOERNBERG & VAN RAAD, *supra* note 61, at 76 [hereinafter U.S.-China Treaty].

89. Convention between the Government of the United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, art. 3(1)(b) (Sept. 12, 1989), *reprinted in* DOERNBERG & VAN RAAD, *supra* note 61, at 180 [hereinafter U.S.-India Treaty].

90. *See supra* notes 88-89.

91. U.S.-China Treaty, *supra* note 88, art. 2(b); U.S.-India Treaty, *supra* note 89, art. 2(1)(a).

92. Congress has considered a related issue in regard to the continued vitality of the U.S. tax treaty with Hong Kong after Hong Kong reverts to Chinese control in 1997. The Senate Foreign Relations Committee has demonstrated concern about "the significant potential for treaty abuse by third country residents who establish residence in Hong Kong to derive Agreement benefits." David A. Kelly, *A Comparative Analysis of the United States-People's Republic of China Tax Treaty: United States Tax Treaty Policy Concerning Developing Countries*, 13 SYRACUSE J. INT'L L. & COM. 83, 93 (1986). "The Senate Foreign Relations committee recommended ratification based on the understanding that Hong Kong is excluded from Agreement coverage." *Id.*

law of the contracting state concerning taxes must be used.⁹³ While absent from the Code, provisions for the Guam mirror tax system are codified in Title 48 of the U.S. Code.⁹⁴ Also, the U.S. imposes the tax law in Guam as either a present mandate or a delegation of congressional power, possibly revocable in the future.⁹⁵ In addition, as U.S. citizens, residents of Guam would be subject to the Code without the effect of the Section 931 exception.⁹⁶ Therefore, to say that Guam tax law is not related to U.S. tax law improperly focuses more on labels and less on the source of the taxing power involved.⁹⁷

Under the U.S. Treasury Model Treaty, the exclusion of tax treaty benefits to all territories is express and clear.⁹⁸ Most U.S. tax treaties in force, in contrast, exclude the U.S. territories by omission.⁹⁹ Only the U.S. tax treaties with China and India may apply to U.S. territories.¹⁰⁰

III. RATIONALES FOR EXCLUDING U.S. TERRITORIES FROM U.S. TAX TREATIES

There are two possible rationales for excluding territories from the scope of U.S. tax treaties. First, the definition of taxes covered by the U.S. tax treaties may not include territorial tax systems. Second, the U.S. needs to exclude its territories from tax treaties in order to preserve U.S. tax revenues.

A. THE DEFINITION OF TAXES COVERED BY U.S. TAX TREATIES

Typically, a U.S. tax treaty defines the taxes covered under the treaty. The U.S. Treasury Model Treaty is illustrative. Article 2(1)(a) of the Treasury Model defines the existing taxes to which the convention shall apply as "in the United States: the Federal income taxes imposed by the Internal Revenue Code."¹⁰¹ To the extent that the Code is only in effect in the states of the United States, the geographic scope of the treaty should be no broader than those states.¹⁰² In fact, to extend treaty benefits to territories under those

93. U.S.-China Treaty, *supra* note 88, art. 3(2); U.S.-India Treaty, *supra* note 89, art. 3(2).

94. 48 U.S.C. § 1421i (1988).

95. See *supra* notes 10-17, 23 and accompanying text.

96. See *supra* notes 44-46 and accompanying text.

97. The doctrine that substance and not form is to be determinative in tax law is established in Section 931 of the Code, and therefore would be part of the laws of the state concerning taxes used to define terms not defined in a U.S. tax treaty.

98. See *supra* notes 73-74 and accompanying text.

99. See *supra* notes 75-79 and accompanying text.

100. See *supra* notes 87-97 and accompanying text.

101. U.S. Treasury Model Treaty, *supra* note 72, art. 2(1)(a).

102. Burke, *supra* note 81, at 235.

circumstances would result in the provision of tax treaty benefits for taxes imposed by the Code, and Guam residents and Guam corporations are already exempted from U.S. income tax and U.S. gross receipts tax under the Code.¹⁰³

The definition of taxes under the U.S. Treasury Model Treaty has two parts: (1) the federal income taxes (2) imposed by the Code. In the U.S., federal income taxes are easily distinguished from state income taxes. States enact income taxes pursuant to the authority of their laws and collect the proceeds of such taxes.¹⁰⁴

In the case of U.S. territories, however, such a distinction is more difficult. U.S. territories have no authority to impose taxes unless Congress expressly delegates such power.¹⁰⁵ In the case of the Guam Tax, Congress directly imposed the mirror system.¹⁰⁶

The government of Guam, rather than the U.S. federal government, collects the Guam Tax.¹⁰⁷ Prior to 1951, Guam had no income tax law, and Congress directly financed all government expenditures in Guam. Congress later enacted the Guam Tax to make Guam more financially self-sufficient.¹⁰⁸

The fact that Congress has the power to enact tax legislation in Guam and also decide to what level of government such tax proceeds are paid demonstrates the true nature of the Guam Tax as a federal income tax.¹⁰⁹ Only the tax collection mechanism of the Guam Tax distinguishes it as a separate income tax system.¹¹⁰

The second relevant element in determining the scope of taxes

Paragraph 1(f) [of the United States Model Income Tax Treaty] defines the term, United States as the United States of America, excluding Puerto Rico, the Virgin Islands, Guam and any other United States possession or territory. The main function of the definition is its geographic reference. For this purpose it is the Committee's view that the use of the term United States ought to be co-extensive with the jurisdictional reach of the federal income and other taxes to which the Model Treaty applies.

Id. (Report of the New York State Bar Association, Tax Section's Committee on United States Activities of Foreign Taxpayers).

103. Guam residents are exempted from U.S. taxes by Section 931, *see supra* note 46 and accompanying text, and Guam corporations are exempted from the 30% gross receipts tax under Section 881(b), *see supra* notes 53-54 and accompanying text.

104. *See* 84 C.J.S. *Taxation* § 350 (1954) ("The power of a state legislature to levy taxes is general and unlimited with respect to the amount or rate of taxation except insofar as it is restrained or limited by constitutional provisions.").

105. *See supra* note 23 and accompanying text.

106. *See supra* notes 25-28 and accompanying text.

107. *Laguana v. Ansell*, 102 F. Supp. 919, 922 (D. Guam 1952) (Section 31 of the Organic Act of Guam imposes a territorial tax to be collected by officials of the Government of Guam), *aff'd* 212 F.2d 207 (9th Cir. 1954).

108. *Sayre & Co. v. Riddell*, 395 F.2d 407, 409 (9th Cir. 1968).

109. *Laguana*, 102 F. Supp. at 921 (through Section 31 of the Organic Act of Guam, Congress meant to "impose the full burden of income taxation, measured by the federal tax, in this unincorporated territory").

110. Rev. Rul. 70-229, 1970-1 C.B. 164, 165 ("The effect of section 31 of the Organic Act of Guam was to set up a separate income tax system for Guam which is a

covered is whether taxes in Guam are imposed by the Code.¹¹¹ Section 31 of the Organic Act of Guam provides that "[t]he income-tax laws in force in the United States of America and those which may hereinafter be enacted shall be held to be likewise in force in Guam."¹¹² The tax laws in force in Guam have been further defined by the Organic Act to be the Internal Revenue Code.¹¹³

The mirror system currently in force in Guam seems to meet the requirement of being "imposed by the Internal Revenue Code." However, once Guam enacts its own tax laws pursuant to the Tax Reform Act of 1986, this characterization may no longer be valid.

Any efforts to extend U.S. tax treaty benefits to territories such as Guam also should expressly extend the scope of the taxes covered by the tax treaty. Doing so would clarify whether Guam's mirror system is included in the scope of taxes covered by U.S. treaties, and include within tax treaty coverage any new Guam income tax law that deviates from the mirror system.

B. THE PRESERVATION OF U.S. TAX REVENUES

Many Pacific islands, such as Nauru¹¹⁴ and Vanuatu,¹¹⁵ have begun to market themselves as tax havens to the international financial community.¹¹⁶ In addition, Hong Kong¹¹⁷ and Singapore,¹¹⁸ while not tax free, do not tax foreign income.

Guam has also attempted to provide tax incentives to foreign investors. In the early 1980s, Guam's efforts to issue tax-free Eurobonds were stifled by the U.S. Treasury Department.¹¹⁹ How-

duplicate of the Federal income tax system."), *modified* Rev. Rul. 73-523, 1973-2 C.B. 295, 295.

111. The Code defines the term "Internal Revenue Code of 1986" as title 26 of the U.S. Code. I.R.C. § 7701(a)(29) (West 1989).

112. 48 U.S.C. § 1421i(a) (1988).

113. *Id.* § 1421i(d)(1). This section expressly mentions the Internal Revenue Code of 1954. However, the 1954 Internal Revenue Code was redesignated as the Internal Revenue Code of 1986 in a note preceding section 1 of title 26. Internal Revenue Code of 1986, Pub. L. No. 99-514, § 2, 100 Stat. 2095 (Oct. 22, 1986).

114. MARSHALL J. LANGER, PRACTICAL INTERNATIONAL TAX PLANNING 86-6 (3d ed. 1991). "Naurans dislike taxes and they have none. Nauru enacted corporation and trust laws in 1972 that were specifically designed to attract tax-haven business. Nauru does not offer guarantees against possible future taxes, and it has no tax treaties."

115. *Id.* at 87-7.

116. Tax havens have been grouped into a number of categories. No-tax havens impose no taxes on certain classes of companies that do business there. Minimal tax havens impose taxes on companies doing business there, but do not tax certain types of income such as foreign earnings income. Tax treaty havens enable companies engaged in business there to enjoy certain tax treaty benefits.

117. LANGER, *supra* note 114, at 84-6.

118. *Id.* at 85-6.

119. LIEBOWITZ, *supra* note 22, at 378-79 ("[The U.S.] Treasury [Department] acted to stop the issuance of Guam Eurobonds by promulgating a Revenue Ruling stating,

ever, currently the Code permits the establishment of Foreign Sales Corporations ("FSCs") in Guam.¹²⁰ If Guam can provide a favorable environment for FSCs, it can generate more financial service revenues from foreign investment.¹²¹

The application of U.S. tax treaties to Guam, however, prevents Guam from becoming a tax haven for two reasons. The first reason is that any new Guam income tax law must raise the same amount of revenue as the mirror system.¹²² Turning Guam into a no-tax haven would be difficult to reconcile with this requirement of revenue neutrality.¹²³

The second reason preventing Guam from becoming a tax haven is that the U.S. can condition the use of any U.S. treaty benefits extended to a U.S. territory such as Guam. A precondition that the U.S. can require would be that any Guam individual or corporation claiming treaty benefits¹²⁴ must meet the requirements of the anti-treaty-shopping clause of the U.S. Treasury Model Treaty. An anti-treaty-shopping clause denies treaty benefits to an entity (other than an individual) unless (1) more than 75% of the beneficial interest in the entity is owned, directly or indirectly, by individual residents of the entity's contracting state, and (2) the income of the entity is not

that the Guam territorial income tax will apply to interest received by foreigners from Guam corporations.").

120. *Guam Commonwealth: Hearing Before the Subcomm. on Insular and International Affairs of the House Comm. on Interior and Insular Affairs on H.R. 98*, 101st Cong., 1st Sess. 128 (Dec. 12, 1989) (statement of Eduardo A. Calvo).

The location of Foreign Sales Corporations (FSCs) in Guam has been a major step forward in Guam's pursuits to assume such a role as a conduit for U.S. exports with markets in Asia. Since the enactment of the Foreign Sales Corporation Act in 1984, of the over 3,000 FSCs which have established worldwide, more than 300 have [been] incorporated in Guam.

Id.

121. LANGER, *supra* note 114, at 57-12. "Guam is a U.S. territory that is actively seeking to provide tax haven facilities to U.S. businesses. The U.S. Treasury blocked its efforts to serve as a base for international finance subsidiaries. It is now trying to serve as a base for FSCs." (emphasis in original).

122. See *supra* note 37 and accompanying text.

123. Arguably, Guam could both maintain its tax revenues and still be a tax haven by creating some class of tax-free foreign holding corporations. However, to the extent that companies doing business in Guam could avail themselves of this status, tax revenues would decrease. If such foreign holding corporations did not conduct a trade or business in Guam, the Section 881(b) exception to the 30% gross receipts tax would not apply and any investment into the U.S. by such corporations would be the same as any other foreign investment into the U.S.

124. Article 1(1) of the U.S. Treasury Model Treaty provides "[t]his Convention shall apply to persons who are residents of one or both of the Contracting States." A "person" includes a "company." *Id.* art. 3(1). A "resident of a Contracting State" is determined under State law definitions of place of management and place of incorporation. To the extent that a corporation is a resident of both Contracting States, such as where it is a U.S. resident because of its place of incorporation and a resident of another Contracting State because of its place of management, then residency will be determined by which Contracting State (or subdivision thereof) it is created under. *Id.* art. 4(3).

substantially used to meet liabilities to persons who are residents of a state not a party to the treaty and who are not citizens of the U.S.¹²⁵ In addition, the entity's principal purpose cannot be to obtain benefits under the tax convention.¹²⁶

U.S. tax treaties have begun to include anti-treaty-shopping clauses to reduce the use of shell corporations to obtain treaty benefits.¹²⁷ An example of such a shell corporation would consist of (1) a parent corporation incorporated in a no-tax haven, (2) a subsidiary in a U.S. territory such as Guam, and (3) an intermediary shell subsidiary in a country which is a U.S. tax treaty partner. The intermediary shell subsidiary would receive Guam dividend and interest payments at tax treaty rates.

Traditionally, anti-treaty-shopping clauses seek to deny tax treaty benefits to shell corporations located in countries which are U.S. tax treaty partners. The treaty protocol extending a particular U.S. tax treaty to Guam could provide that the anti-treaty-shopping clause be a precondition for eligibility for treaty benefits.

Using the anti-treaty-shopping clause as a precondition for tax treaty eligibility in Guam would be no more onerous than the present Section 881(b) requirements to avoid the 30% gross receipts tax on the receipt of U.S. source income by Guam corporations. For example, in the case of a Guam corporation, the anti-treaty-shopping clause requires that more than 75% of that corporation be beneficially owned by one or more residents of Guam.¹²⁸ Likewise, Section 881(b) requires that less than 25% of a Guam corporation be beneficially owned by foreign persons.¹²⁹ Moreover, both the anti-treaty-shopping clause and Section 881(b) prohibit the use of substantial amounts of income to meet liabilities (anti-treaty-shopping clause¹³⁰) or obligations (Section 881¹³¹) to persons who are

125. *Id.* art. 16(1).

126. *Id.* art. 16(2).

127. ANTHONY SANFIELD GINSBERG, *TAX HAVENS* 211 (1991) ("The slow spread of anti-treaty-shopping clauses in the treaty network of the United States has also narrowed the range of [tax-haven] alternatives."). *Id.* at 221.

As the high-tax countries continue to mount pressure against the users of tax-haven countries, it is evident that the revision of double taxation treaties in that respect will be directed toward eliminating treaty shopping. . . . In many, if not most, treaties now being negotiated or renegotiated, the United States is inserting anti-treaty-shopping provisions. These provisions, among other things, generally limit the use of the treaty by corporations of a country to cases where a prescribed minimum percentage of shares is owned by citizens or residents of that country.

MICHAEL W.E. GLAUTIER & FREDERICK W. BASSINGER, *A REFERENCE GUIDE TO INTERNATIONAL TAXATION* 274 (1987).

128. *See supra* note 125 and accompanying text.

129. *See supra* note 54 and accompanying text.

130. *See supra* note 125 and accompanying text.

131. *See supra* note 54 and accompanying text.

not residents of Guam.¹³²

IV. TAX PLANNING AND POLITICAL SOLUTIONS

A. TAX PLANNING INCORPORATING U.S. TAX TREATIES THAT APPLY TO TERRITORIES

The example of the U.S.-China tax treaty best illustrates how a territory like Guam can benefit from a tax treaty.¹³³ If the U.S.-China tax treaty does not apply to Guam, and a China corporation earns dividend income from a Guam source, the mirror system version of Section 881 will impose a 30% tax on that income.¹³⁴ However, if the U.S.-China tax treaty does apply to Guam, Article 9(2) of the treaty limits the taxation of the Guam source dividend to 10% of its gross amount.¹³⁵ The application of the tax treaty, therefore, decreased the Guam tax rate from 30% to 10% of the gross amount of the dividend.

1. *The Effect of Applying U.S. Tax Treaties to Guam*

If the U.S.-China treaty is applied to Guam, other countries could use Guam as a conduit to channel income.¹³⁶ For example, a Japanese parent corporation might set up a Chinese subsidiary to repatriate profits to the parent under the U.S.-China tax treaty from a Guam subsidiary of the parent. However, even without an anti-treaty-shopping clause in the U.S.-China treaty,¹³⁷ this strategy is ineffective if all profits are repatriated through dividends.

For instance, assume that dividend income from Guam sources is distributed to a Chinese holding company. Such a dividend would be taxed at the 10% treaty rate for dividends.¹³⁸ China would then tax the Chinese holding company. Assuming that the holding company is a joint venture, the tax rate in China on joint ventures is a 30% tax on joint venture income.¹³⁹ Even without considering any possible Chinese taxes on dividends from China sources to foreign corporations, the cumulative tax rate in this sce-

132. Section 881(b) adds the requirement that at least 65% of a Guam corporation's gross income must be connected with the conduct of a business in Guam for the three-year period ending with that taxable year. See *supra* note 54 and accompanying text.

133. See *supra* note 88 and accompanying text.

134. See *supra* notes 48-51 and accompanying text.

135. U.S.-China Treaty, *supra* note 88, art. IX(2).

136. See generally GINSBERG, *supra* note 127, at 211 ("A corporation may establish operations abroad solely to benefit from tax treaties that may reduce foreign taxes.").

137. See *infra* notes 143-145 and accompanying text.

138. See *supra* note 135 and accompanying text.

139. The Income Tax Law of the People's Republic of China Concerning Chinese-Foreign Joint Ventures art. III (1980), reprinted in 1 CHINA'S FOREIGN ECONOMIC LEGISLATION 36 (1982).

nario is 37%.¹⁴⁰ Because Guam source dividends distributed to a nontreaty country are taxed at 30%,¹⁴¹ the use of Guam as an investment conduit appears unprofitable.

To avoid Chinese taxes in the above example, instead of remitting the Guam income of the Chinese subsidiary to the Japanese parent corporation in the form of a dividend, the parent corporation could extend a loan to the Chinese subsidiary at an interest rate set to approximate the value of the dividends from the Guam subsidiary. Because the sole income source of the Chinese subsidiary is the Guam source dividends, the gross income reduction achieved by the interest expense paid to the Japanese parent corporation would decrease the taxable income of the Chinese subsidiary to zero.¹⁴²

In this revised example it is assumed that the U.S.-China tax treaty applies to Guam and that Guam dividends to the Chinese subsidiary are taxed at the treaty rate of 10%. Because its interest expense equalled its Guam dividend income, the Chinese subsidiary would have no income and therefore pay no Chinese income tax. The interest payments from the Chinese subsidiary to the Japanese parent corporation would be taxed at a 10% treaty rate according to the interest provisions of the China-Japan tax treaty.¹⁴³ The 10% U.S.-China treaty rate combined with the 10% China-Japan treaty rate result in an aggregate tax rate of 19%.¹⁴⁴ This 19% tax rate, not taking into account the administrative costs of maintaining the Chinese subsidiary, reflects a reduction in the 30% tax rate im-

140. If the amount of taxable income (TI) under U.S. and Chinese law is assumed to be equal, the formula would be: $(10\% \text{ TI}) + 30\%(\text{TI} - 10\% \text{ TI})$.

141. See *supra* notes 48-51 and accompanying text.

142. This example does not account for the effect of Guam taxes under the mirror system. Instead of the Guam subsidiary distributing earnings to the Chinese subsidiary through dividends, the Chinese subsidiary could make a loan to the Guam subsidiary with interest payments in an amount that equals its earnings. The resulting interest payments would decrease the Guam subsidiary's taxable income to zero or near zero depending on how closely the interest expense approximated the amount of taxable income.

143. John Darcy, Comment, *The Effect of Tax-Sparing on United States Business in China*, 21 U.S.F. L. REV. 393, 398 (1987) ("The tax treaty entered into on September 6, 1983, between Japan and China . . . was substantially similar to the U.S.-China Tax Treaty except that the Japanese Government agreed to the inclusion of a tax-sparing measure in the provision for the avoidance of double taxation."). If such tax treaty were not in effect, "[d]ividends, interest, rents, royalties and other income with a source in China earned by a foreign enterprise, and not attributable to an establishment in China of that enterprise, are taxed at a flat rate of 20 percent under the FEIT [Foreign Enterprise Income Tax] Law, tax being withheld by the paying unit from the amount of each payment." A.J. EASSON & LI JINYAN, *TAXATION OF FOREIGN INVESTMENT IN THE PEOPLE'S REPUBLIC OF CHINA* 97 (1989), quoting Income Tax Law of the People's Republic of China Concerning Foreign Enterprises, adopted by the Third Session of the Fifth National People's Congress and promulgated on December 13, 1982, art. 11.

144. If the amount of taxable income (TI) under U.S. and Chinese law is assumed to be equal, the formula would be: $(10\% \text{ TI}) + 10\%(\text{TI} - 10\% \text{ TI})$.

posed by Section 881 on dividend income from Guam to Japan by more than one-third.

2. *The Effect of the Anti-Treaty-Shopping Clause on Tax Rates*

The U.S.-China tax treaty anti-treaty-shopping clause, however, may deny tax treaty benefits for foreign corporations. The U.S.-China tax treaty anti-treaty-shopping clause modifies the U.S. Treasury Model Treaty anti-treaty-shopping clause in three respects. First, 50% of the beneficial interest of a Chinese corporation must be owned by residents of China.¹⁴⁵ Second, not more than 50% of the gross income of a Chinese corporation can be used to make interest payments to non-Chinese residents.¹⁴⁶ Third, the anti-treaty-shopping clause is unnecessary to thwart tax evaders if obtaining benefits under the treaty was the parties' principal purpose.¹⁴⁷

To avoid the application of the anti-treaty-shopping clause, therefore, the ownership of the Chinese subsidiary may be adjusted so that China residents hold at least a 50% beneficial interest. A joint venture corporation held equally by a Japanese parent corporation and a China resident would meet the anti-treaty-shopping clause's ownership requirements, and the joint venture contract could provide payment of a small fee to the Chinese owner to assign his or her rights to manage the company to the Japanese parent.

However, the fact that the entire income of the Chinese subsidiary is used for interest payments to the Japanese parent corporation clearly violates the anti-treaty-shopping clause requirement that no more than 50% of gross income be used to make interest payments to non-Chinese residents. It may be possible to relabel a portion of these interest payments as fees that are not interest, such as fees for management services, licenses, or royalties paid. To the extent that such recharacterization cannot reduce interest payments to the Japanese parent corporation to at least 50% of the Chinese subsidiary's gross income, the parent corporation can defeat application of the anti-treaty-shopping clause only by arguing that the Chinese subsidiary was not established for the principal purpose of obtaining treaty benefits.

145. U.S.-China Treaty, *supra* note 88, protocol II(1)(a). The differences in the anti-treaty-shopping clause in the U.S.-China Treaty are (1) the reduction to 50% of the beneficial interest that must be owned by individual residents of the Contracting States, their citizens, or resident corporations; and (2) not more than 50% of gross income may be used to make payments of interest to persons other than those same residents, citizens, or corporations. *Id.* However, the above provisions shall not apply if the principal purpose was not to obtain benefits under the treaty, *id.* protocol II(2), or if there is substantial and regular trading of the principal class of company shares on a recognized stock exchange. *Id.* protocol II(1)(b).

146. *Id.* protocol II(1)(a).

147. *Id.* protocol II(2).

Through a strategy of combining Japanese parent corporation loan interest, joint ownership of the Chinese subsidiary, and characterizing Guam income as management fees, licenses, or royalties, it may be possible to meet the technical requirements of the anti-treaty-shopping clause of the U.S.-China treaty. Should the Chinese subsidiary fail to meet the requirements of the anti-treaty-shopping clause, the Guam dividend will be taxed at the Section 881 30% rate. The 30% rate combined with the 10% tax treaty rate under the China-Japan tax treaty would result in an aggregate tax rate of 37%.¹⁴⁸ Therefore, the applicability of the anti-treaty-shopping clause will determine whether there is a cumulative decrease or increase in the tax rate of 18%.¹⁴⁹

B. TAX PLANNING THROUGH NO-TAX HAVENS

A foreign parent corporation with a Guam subsidiary would derive no tax benefits by establishing an intermediary holding corporation in a no-tax haven such as Nauru or Vanuatu. If a Guam subsidiary distributed dividends to a Vanuatu subsidiary and the Vanuatu subsidiary paid the dividends to the parent corporation, the Vanuatu subsidiary would be receiving dividend income from a Guam source and thus would be subject to the 30% gross receipts tax.

Vanuatu would not tax the receipt of the Guam dividend by the Vanuatu subsidiary, nor would Vanuatu tax the distribution of the dividend to the parent corporation.¹⁵⁰ However, the costs of establishing the Vanuatu subsidiary and the increase in other transaction costs seem unjustified because the 30% tax rate would also apply if the Guam subsidiary distributed the dividend directly to the parent corporation.¹⁵¹

C. EXTENDING U.S. TAX TREATIES TO U.S. TERRITORIES

Language in the OECD Model Tax Treaties of 1963 and 1977 provide for the possibility of extending U.S. tax treaties to territories.¹⁵² Two older U.S. tax treaties with Pakistan and France incor-

148. If the amount of taxable income (TI) under U.S. and Chinese law is assumed to be equal, the formula would be: $(30\% \text{ TI}) + 10\%(\text{TI} - 30\% \text{ TI})$.

149. If the amount of taxable income under U.S. and Chinese law is assumed to be equal, the formula would be the difference between the cumulative tax rate of 37%, see *supra* note 148 and accompanying text, and the cumulative tax rate of 19%, see *supra* note 144 and accompanying text.

150. See *supra* notes 114-15 and accompanying text.

151. For example, in Nauru "[i]t costs about A[Australian dollar]\$1,100 to incorporate a company, and slightly less each year to maintain it in good standing," LANGER, *supra* note 117, at 86-8, and in Vanuatu "[i]t costs about US \$2,000 to form an exempted company and about US \$1,200 per year to maintain it." *Id.* at 87-9.

152. See Appendix E.

porate the same language.¹⁵³ Also, the U.S.-Netherlands tax treaty contains substantially similar language that may permit a treaty extension.¹⁵⁴ In addition, five other countries whose treaties with the U.S. became effective after 1970 provide for the extension of the treaties to territories.¹⁵⁵ The U.S. Treasury Model Treaty, however, does not contain any provisions for treaty extension.

1. *The U.S.-U.K. Tax Treaty*

The provisions for extending a U.S. tax treaty to territories were exercised when the U.S.-U.K. tax treaty covered former British colonies as part of the British Commonwealth. The first tax treaty between the U.S. and the United Kingdom, signed on April 16, 1945 (the "1945 Treaty"), did not contain a provision for extending the treaty to U.S. territories or U.K. colonies.¹⁵⁶ Thereafter, the 1945 Treaty was amended to permit its extension to territories or colonies by either party by the Supplementary Protocol to British Tax Convention, ratified on January 19, 1955.¹⁵⁷ After the ratification of the Supplementary Protocol, the British Ambassador requested that the 1945 Treaty be extended to twenty

153. *Id.*

154. *See* Appendix F.

155. *See* Appendix G.

156. 3 Federal Tax Treaties (P-H) ¶ 89,102, at 89,103 (1991).

157. 3 Federal Tax Treaties (P-H) ¶ 89,128, at 89,153. The Supplementary Protocol to British Tax Convention provides in pertinent part:

Paragraph (1) of Article XXII of the Convention of the 16th April, 1945, for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income is hereby amended to read as follows:

(1) Either of the Contracting Parties may, at any time while the present Convention continues in force, by a written notification given to the other Contracting Party through the diplomatic channel, declare its desire that the operation of the present Convention, either in whole or in part or with such modifications as may be found necessary for special application in a particular case, shall extend to all or any of its territories for whose international relations it is responsible, which impose taxes substantially similar in character to those which are the subject of the present Convention. When the other Contracting Party has, by a written communication through the diplomatic channel, signified to the first Contracting Party that such notification is accepted in respect of such territory and territories, the present Convention, in whole or in part or with such modifications as may be found necessary for special application in a particular case, as specified in the notification, shall apply to the territory or territories named in the notification on or after the date or dates specified therein. None of the provisions of the present Convention shall apply to any such territory in the absence of such acceptance in respect of that territory.

Id.

This treaty extension clause is substantially similar to the clauses in post-1970 U.S. treaties that include territorial extension provisions listed herein in Appendix G.

countries as former U.K. colonies.¹⁵⁸

Even though the U.S. and the U.K. signed a new tax treaty on December 31, 1975, and ratified it as amended on June 27, 1978 (the "1978 Treaty"), the 1978 Treaty does not affect the extension of the 1945 Treaty to U.K. colonies.¹⁵⁹ The extension of the 1945 Treaty to U.K. colonies was terminated by the U.S. on January 1, 1984.¹⁶⁰ Prior to that time, the extension of the 1945 Treaty to U.K. colonies was terminated for Trinidad and Tobago as of January 1, 1966,¹⁶¹ Cyprus as of December 31, 1967,¹⁶² the Cayman Islands (as part of Jamaica) as of January 1, 1969,¹⁶³ and the British Virgin Islands as of January 1, 1983.¹⁶⁴

2. *The U.S.-Netherlands Tax Treaty*

The provisions for extending a U.S. tax treaty to a territory were also exercised when the U.S.-Netherlands treaty was extended to the Netherlands Antilles.¹⁶⁵ The Netherlands Antilles is a group of six islands in the Caribbean.¹⁶⁶ The Netherlands Antilles taxes

158. 3 Federal Tax Treaties (P-H) ¶ 89,132-A, at 89,156 (Note with enclosure, from the British Ambassador to the Secretary of State, August 19, 1957). The U.K. Colonies specified in the request were Aden (now Yemen); Antigua; Barbados; British Honduras (Belize); Cyprus; Dominica; Falkland Islands; Gambia; Grenada; Jamaica; Montserrat; Federation of Nigeria; Federation of Rhodesia and Nyasaland (now Zambia, Malawi and Zimbabwe); St. Christopher, Nevis and Anguilla; St. Lucia; St. Vincent; Seychelles and Sierra Leone; Trinidad and Tobago; and British Virgin Islands. *Id.*

159. Convention Between the Government of the United States of America and the Government of the United Kingdom of Great Britain and Northern Ireland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains art. XXVIII(6) (Dec. 31, 1975) ("This Convention shall not affect any Agreement in force extending the 1945 Convention in accordance with Article XXII thereof.") amended Aug. 26, 1976, March 31, 1977, & March 15, 1979, reprinted in DOERNBERG & VAN RAAD, *supra* note 61, at 439.

160. Treas. Dep't. Release R-2222 (July 1, 1983), quoted in 3 Federal Tax Treaties (P-H) ¶ 89,001, at ¶ 89,004.

161. Treas. Dep't. Release F-330 (July 1, 1983), quoted in 3 Federal Tax Treaties (P-H) ¶ 89,001, at ¶ 89,004.

162. Treas. Dep't. Release F-1068 (July 1, 1983), quoted in 3 Federal Tax Treaties (P-H) ¶ 89,001, at ¶ 89,004.

163. Treas. Dep't. Release F-1368 (July 1, 1983), quoted in 3 Federal Tax Treaties (P-H) ¶ 89,001, at ¶ 89,004.

164. 3 Federal Tax Treaties (P-H) ¶ 89,001, at ¶ 89,005. See generally GLAUTIER & BASSINGER, *supra* note 127, at 273.

[D]eveloped countries rarely negotiate tax treaties with tax havens, but in some cases, the extension of an existing treaty to former colonies has resulted in the application of a treaty to a tax haven. Such was the case, for example, of the (since rescinded) extension of the U.S.-U.K. treaty to the British Virgin Islands. So also was the case of the extension of the U.S.-Netherlands treaty to the Netherlands Antilles.

Id.

165. LANGER, *supra* note 114, at 58-10.

166. BURTON W. KANTER, THE NETHERLANDS ANTILLES, FOREIGN TAX HAVENS 179-80 (PLI Tax Law & Transcript Series No. 13, Marshall J. Langer & Roy A. Povell eds., 1973).

foreign earned income at very low rates. Because of the combination of low tax rates and tax treaty benefits, the Netherlands Antilles became a significant tax haven.¹⁶⁷ However, the U.S. responded to this loss of tax revenues by terminating the protocol extending the U.S.-Netherlands tax treaty to the Netherlands Antilles on January 1, 1988.¹⁶⁸ The U.S., though, subsequently modified the termination to mitigate adverse effects upon the European market.¹⁶⁹

Extending U.S. tax treaties to Guam will not result in the same revenue loss as did the extension of the U.S.-Netherlands tax treaty to the Netherlands-Antilles. First, the Tax Reform Act of 1986 requires that any change in Guam's tax laws must raise the same amount of revenue, preventing Guam from becoming a tax haven.¹⁷⁰ Second, anti-treaty-shopping clauses in U.S. tax treaties make it increasingly difficult to establish subsidiaries solely to obtain tax treaty benefits.¹⁷¹ Ultimately, the extension of U.S. tax treaties to Guam merely would equalize the tax rates applied to foreign investment in Guam with similar foreign investment in the U.S.

V. CONCLUSION

As U.S. territories such as Guam develop economically, double taxation problems with foreign countries follow. Such double taxation is usually lessened by tax treaties. However, U.S. tax treaties generally exclude territories from their geographic scope, thus discouraging foreign investment in U.S. territories.

To rectify this problem, U.S. tax treaty benefits should be extended to U.S. territories. Territorial extension provisions already exist in some treaties and should be added to others. Such territorial extension provisions should be exercised so that U.S. tax treaties can be applied to U.S. territories in the same manner that U.S. tax treaties apply to any state in the United States.

167. LANGER, *supra* note 114, at 58-1.

168. 3 Federal Tax Treaties (P-H) ¶ 65,001, at ¶ 65,003 (1991).

169. *Id.*

170. *See supra* note 37 and accompanying text.

171. *See supra* notes 122-24 and accompanying text. There is some question, however, as to Guam's incentive to enforce any anti-treaty-shopping clause. A possible solution may be a system of dual tax returns filed in both Guam and the U.S. for corporations or individuals located in Guam who take advantage of a U.S. tax treaty.

APPENDIX A¹⁷²

Treaty Definition of "United States":

"[W]hen used in a geographic sense, the term 'United States' means the states thereof and the District of Columbia . . ."

Other contracting state:	Year treaty concluded:	Year(s) of amendment(s):	Treaty provision:
Australia	8/6/82		III(1)(j)(ii)
Belgium	7/9/70	12/31/87	III(1)(a)(ii)
Egypt	8/24/80		II(1)(a)(ii)
France	7/28/67	10/12/70, 11/24/78, 1/17/84 & 6/16/88	II(1)(a)
Korea	6/4/76		II(1)(a)(ii)
Luxembourg	12/18/62		II(1)(a)
Netherlands	4/29/48	12/30/65	II(1)(a)
Philippines	10/1/76		II(1)(a)(ii)
Spain	2/22/90		III(1)(b)
U.S.S.R. (CIS)	6/20/73		II(2)
U.K.	12/31/75	8/26/76, 3/31/77 & 3/15/79	III(1)(g)(ii)
Trinidad & Tobago	1/1/70		II(1)(a)(ii)
Norway	11/29/72	12/15/81	II(1)(a)(ii)
Romania	2/26/76		II(1)(b)(ii)
Poland	7/23/76		III(1)(b)
Iceland	12/26/75		II(1)(a)(ii)
Morocco	12/30/81		II(1)(a)(ii)
Jamaica	12/29/81		III(1)(f)
Indonesia	12/30/90		III(1)(b)
Tunisia	12/26/90		III(1)(e)
Barbados	2/28/86		III(1)(a)(i)
Cyprus	12/31/85		II(1)(a)

Note: (1) Netherlands Treaty of 4/29/48 uses the same language as that which appears in Appendix D. Netherlands Treaty of 12/30/65 uses the same language as that which appears in Appendix A.

172. Information in appendices taken from 1-3 PRENTICE HALL FEDERAL TAXES, TAX TREATIES. Information regarding U.S.-Greece Treaty taken from 2 COMMERCE CLEARING HOUSE TOPICAL LAW REPORTS, TAX TREATIES.

APPENDIX B

Treaty Definition of "United States":

"[T]he term 'United States' means: the United States of America, but does not include Puerto Rico, the Virgin Islands, Guam or any other United States possession or territory"

Other contracting state:	Year treaty concluded:	Year(s) of amendment(s):	Treaty provision:
Canada	9/26/80	6/14/83 & 3/28/84	III(1)(b)(i)
Germany	8/29/89		III(1)(b)
Italy	4/17/84		III(1)(f)
Hungary	9/18/79		III(1)(g)(ii)
Malta	5/18/82		III(1)(g)(i)
Greece	1/1/53		II(1)(a)
New Zealand	11/2/83		III(1)(g)
Bermuda	12/2/88		I(1)(a)(i)
Finland	12/30/90		III(1)(b)

APPENDIX C

Treaty Definition of "United States":

"[T]he term 'United States of America', when used in a geographic sense, means all the territory of the United States of America, including its territorial sea, in which the laws relating to United States tax are in force"

Other contracting state:	Year treaty concluded:	Year(s) of amendment(s):	Treaty provision:
China	4/30/84	5/10/86	III(1)(b)
India	9/12/89		III(1)(b)

APPENDIX D

Treaty Definition of "United States":

"The term 'United States' means the United States of America, and when used in a geographical sense means the United States, the Territories of Alaska and Hawaii, and the District of Columbia."

Other contracting state:	Year treaty concluded:	Year(s) of amendment(s):	Treaty provision:
Ireland	9/13/49		II(1)(a)
Switzerland	5/24/51		II(1)(a)
Austria	1/1/57		II(1)(a)
Pakistan	1/1/59		II(1)(a)

APPENDIX E

US Treaties that include the Territorial Extension Provision (Article 28) of the OECD Model Income Tax Treaty:

1. This Convention may be extended, either in its entirety or with any necessary modifications [to any part of the territory of (State A) or of (State B) which is specifically excluded from the application of the Convention or], to any State or territory for whose international relation (State A) or (State B) is responsible, which imposes taxes substantially similar in character to those to which the Convention applies. Any such extension shall take effect from such date and subject to such modifications and conditions, including conditions as to termination, as may be specified and agreed between the Contracting States in notes to be exchanged through diplomatic channels or in any other manner in accordance with their constitution procedures.
2. Unless otherwise agreed by both Contracting States, the termination of the Convention by one of them under Article 30 shall also terminate, in the manner provided for in that Article, the application of the Convention [to any part of the territory of (State A) or of (State B) or] to any State or territory to which it has been extended under this Article.

Other contracting state:	Year treaty concluded:	Year(s) of amendment(s):	Treaty provision:
Pakistan	1/1/59		Art. XVIII
France	7/28/67	10/12/70, 11/24/78, 1/17/84 & 6/14/88	Art. XXIX

- Notes: (1) Pakistan treaty has some slight grammatical changes.
- (2) France treaty only applies to territorial extensions to the Overseas Territories of the French Republic, and does not mention U.S. territories or possessions. France treaty Termination Article (art. 32) makes the treaty effective until the end of 1969. After that time the treaty may be terminated by six months notice after the end of the calendar year. Termination of treaty extensions are separately governed by Article 29(2):
- (2) At any time after the expiration of a period of 1 year from the effective date of an extension made by virtue of paragraph (1) either of the Contracting States may by a written notice of termination given to the other Contracting State through diplomatic channels, terminate the application of the provisions in respect to any territory to which such application has been extended, in which case the provisions shall cease to be applicable to such territory on and after the first day of January following the date of such notice; provided, however, that this shall not affect the continued application of such provision to the United States, to France, or to any other territory to which such provisions apply and which is not named in the notice of termination.

APPENDIX F

US-NETHERLANDS TREATY
[EXTENSION TO TERRITORIES]

ARTICLE 27

(1) Either of the Contracting States may, at the time of exchange of instruments of ratification or thereafter while the present Convention continues in force, by a written notification of extension given to the other Contracting State through diplomatic channels, declare the desire of the government of any overseas part of the Kingdom (in the case of the Netherlands) or overseas territory (in the case of the United States), which imposes taxes substantially similar in character to those which are the subject of the present Convention, that the operation of the present Convention, either in whole or as to such provisions thereof as may be deemed to have special application, shall extend to such part or territory.

(2) In the event that a notification is given by one of the Contracting States in accordance with paragraph (1) of this Article, the present Convention, or such provisions thereof as may be specified in this notification, shall apply to any part or territory named in such notification on and after the first day of January following the date of a written communication through diplomatic channels addressed to such Contracting States by the other Contracting State, after such action in the latter States as may be necessary in accordance with its own procedures, stating that such notification is accepted in respect of such part or territory. In the absence of such acceptance, none of the provisions of the present Convention shall apply to such part or territory.

(3) At any time after the expiration of one year from the effective date of an extension made by virtue of paragraphs (1) and (2) of this Article, either of the Contracting States may, by a written notice of termination given to the other Contracting State through diplomatic channels, terminate the application of the present Convention to any part or territory to which the Convention, or any of its provisions, has been extended. In that case, the present Convention, or the provisions thereof specified in the notice of termination, shall cease to be applicable to that part or territory named in such notice of termination on and after the first day of January following the expiration of a period of six months after the date of such notice; provided, however, that this shall not affect the continued application of the Convention, or any provisions thereof, to the United States, to the Netherlands, or to any other territory

(not named in the notice of termination) to which the Convention, or such provision thereof, applies.

(4) For the application of the present Convention in relation to any part of territory to which it is extended by notification given by the United States or the Netherlands, references to "the United States" or to "the Netherlands" or to one or the other Contracting State, as the case may be, shall be construed to refer to such part or territory.

Notes: (1) Netherlands treaty became effective on 4/29/48 and was amended on 12/30/65.

(2) Netherlands treaty is effective for five years after ratification and may be terminated on the January following the giving of six months prior notice of termination. Article 28(2). In contrast, termination of any territorial extension may be made by following the same procedures one year after such territorial extension becomes effective. Article 27(3).

APPENDIX G

Post-1970 US Treaties that include Territorial Extension Provisions:

Extension to Territories

(1) Either one of the Contracting States may, at any time while this Convention continues in force, by written notification given to the other Contracting State through diplomatic channels, declare its desire that the operation of this Convention, either in whole or in part or with such modifications as may be found necessary for special application in a particular case, shall extend to all or any of the areas (to which this Convention is not otherwise applicable) for whose international relations it is responsible and which impose taxes substantially similar in character to those which are the subject of this Convention. When the other Contracting State has, by a written communication through diplomatic channels, signified to the first-mentioned Contracting State that such notification is accepted in respect of such area or areas, and the notification have been ratified and instruments of ratification exchanged, this Convention, in whole or in part, or with such modifications as may be found necessary for special application in a particular case, as specified in the notification, shall apply to the area or areas named in this notification and shall enter into force and effect on and after the date or dates specified therein. None of the provisions of this Convention shall apply to any such area in the absence of such acceptance and exchange of instruments of ratification in respect of that area.

(2) At any time after the entry into force of an extension under paragraph (1), either of the Contracting States may, by six months prior notice of termination given to the other Contracting State through diplomatic channels, terminate the application of this Convention to any area to which it has been extended under paragraph (1), and in such case this Convention shall cease to apply and have force and effect, beginning on or after the first day of January next following the expiration of the six month period, to the area or areas named therein, but without affecting its continued application to the United States, to . . . [State B], or to any other area to which it has been extended under paragraph (1).

(3) In the application of this Convention in relation to any area to which it is extended by notification by the United States or . . . [State B], reference to the "United States" or ". . . [State B]" as the case may be, shall be construed as referring to that area.

(4) The termination in respect to the United States or . . .

[State B] of this Convention under Article 29 (Termination) shall, unless otherwise expressly agreed by both Contracting States, terminate the application of this Convention to any area to which the Convention has been extended under this article by the United States or . . . [State B].

Other contracting state:	Year treaty concluded:	Year(s) of amendment(s):	Treaty provision:
Belgium	7/9/70	12/31/87	Art. XXIX
Norway	11/29/72	12/15/81	Art. XXX
Iceland	12/26/75		Art. XXXIII
Korea	6/6/76		Art. XXIX
Morocco	12/30/81		Art. XXVII

- Notes: (1) Belgium Treaty only applies to U.S. territories.
 (2) Norway Treaty has slight grammatical changes.
 (3) All the above treaties are effective for five years after ratification and may be terminated on the January following the giving of six months prior notice of termination. In contrast, termination of any territorial extension may be made by giving six months prior notice of termination any time one year after such territorial extension becomes effective.