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PROPOSED INCOME TAX TREATY BETWEEN THE UNITED STATES AND EGYPT

PREPARED FOR THE USE OF THE

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BY THE STAFF OF THE

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INTRODUCTION

This pamphlet describes the proposed income tax treaty between the United States and Arab Republic of Egypt. The purpose of the proposed treaty is to avoid double taxation of income earned in one country by residents of the other country and to establish procedures for exchanging information, assisting in collection and other administrative matters between the two countries. The proposed treaty was signed on October 28, 1975. There presently exists no tax treaty in force between the United States and Egypt.

This proposed treaty is substantially similar to other recent U.S. income tax treaties and to the model tax treaty of the Organization for Economic Cooperation and Development (OECD). There are, however, several provisions which vary from the basic model.

(1) The proposed treaty provides (article 11) that the United States is to reduce its withholding tax to 15 percent on dividends paid to Egyptian direct investors. However, the treaty does not provide for a parallel reduction in Egyptian taxes. Under its laws Egypt allows a deduction to corporations equal to the amount of any dividends paid out of current earnings.

The treaty consequently does not limit the Egyptian tax imposed under Egyptian law on U.S. corporate shareholders. However, the treaty does limit the tax which Egypt would otherwise impose on U.S. individuals receiving dividends from Egyptian corporations to 20 percent of the net dividend.

(2) The treaty contains specific provisions (in article 11) which establish the eligibility for Egyptian tax holidays of American direct investors in Egyptian corporations. In order to qualify for the tax holiday, the treaty specifies that U.S. direct investments meet the requirement of Egyptian law that the income of the Egyptian corporation be exempt from U.S. income tax. In addition, the treaty provides that when the income from the corporation is subject to U.S. tax under U.S. law (generally, when a dividend is paid to the United States direct investor), the Egyptian Government will tax the Egyptian corporation on income equal to the dividends and the United States will allow a foreign tax credit for the tax paid.

(3) Income from personal services (articles 15 through 18) is treated in a slightly different manner than in many other U.S. treaties. Individuals performing personal services are to be subject to tax in the country where the services are performed if the individual is present in that country for 90 days within the tax year, instead of the longer period generally provided in U.S. treaties. An exception is provided for entertainers and athletes, whose services may be taxed in the country where performed if the gross income from the services exceeds $400 per day that the individual is present in that country.

(4) The treaty (article —) provides for a 15 percent limit on the withholding rates of each country applicable to dividend (article 11), interest (article 12), and royalties (article 13).

(5) The treaty (article 9) provides for an exemption of shipping income which is slighlty broader than the exemption found in many U.S. tax treaties. Under the treaty income from international shipping of a resident of one country is to be exempt in the other country if the ships or aircraft are registered in either country or in a third country with respect to which either country has a tax treaty. Most U.S. treaties limit the exemption to ships or aircraft registered in the other treaty country.

General Explanation

Article 1. Taxes covered

The proposed treaty applies to the U.S. Federal income taxes imposed under the Internal Revenue Code (other than the Social Security Tax and the self-employment tax.) It also applies to the following taxes of the Arab Republic of Egypt: the tax on income derived from immovable property, the tax on income from movable capital, the tax on commercial and industrial profits, the tax on wages, salaries, indemnities, and pensions, the tax on profits from noncommercial professions, the General Income Tax, the Defense Tax, the National Security Tax, the War Tax, and any supplementary taxes imposed as a percentage of any of the above taxes.

The proposed treaty also contains a provision generally found in U.S. income tax treaties which applies the treaty to substantially similar taxes which either country may subsequently impose.

Additionally, the Article provides that the nondiscrimination provisions (Article 26) of the treaty apply to all taxes at the national level by the United States or Egypt. The Exchange of Information provisions (Article 28) of the proposed treaty will also apply to taxes of every kind imposed by the two countries at the national level.

Article 2. General definitions

The standard definitions found in most of our income tax treaties are contained in the proposed treaty, including the definition of the term "United States", which incorporates the territorial sea of the United States and the continental shelf of the United States insofar as the exploration and exploitation of natural resources on the continental shelf is concerned. A similar definition of Egypt contained in the proposed treaty.

The proposed treaty also contains the standard provision that undefined terms are to have the meaning which they have under the applicable tax laws of the country applying the treaty. Where a term is defined in a different manner by the two countries or where its meaning under the laws of either country is not readily determinable, the competent authorities of the two countries may establish a common meaning for the term in order to prevent double taxation or to further any other purpose of the treaty.

Article 3. Fiscal residence

The benefits of the proposed treaty generally are available only to residents of the two countries. The proposed treaty defines "resident of Egypt" and "resident of the United States," and in addition provides a set of rules to determine residence in the case of an individual with dual residence. This provision of the proposed treaty is based on the fiscal domicile article of the OECD model tax treaty and is similar to the provisions found in other U.S. tax treaties.

An individual whom both countries consider to be a resident according to their general rules for determining residence will be deemed for all purposes of the treaty to be a resident of the country in which he has his permanent home (where an individual dwells with his family), his center of vital interests (his closest economic and personal relations), his habitual abode, or his citizenship. If the residence of an individual cannot be determined by these tests, applied in the order stated, the competent authorities of the countries will settle the question by mutual agreement.

Article 4. Source of income

The source of income rules establish the framework for the basic provision in the treaty (Article 4) that one country may tax residents and corporations of the other country only on income from sources within the taxing country (provided, with certain exceptions, that the resident is not a citizen of the taxing country). The rules are also important because the U.S. foreign tax credit is limited to the U.S. tax on income from sources outside the United States. Several of the source rules contained in the proposed treaty differ in some degree from the source rules provided in the Internal Revenue Code. Since the general rules of taxation contained in the proposed treaty (Article 6) provide that it will not be applied increase a person's tax, a taxpayer is not bound to apply the rules decribed below where the treaty rules would increase his U.S. tax liability.

The proposed treaty provides that dividends will be treated as income from sources within a country if paid by a corporation of that country. However, the treaty provides two exceptions to this general rule. First, dividends paid by U.S. corporations whose activities take place solely or mainly in Egypt are to be treated as Egyptian source income. This rule is basically similar to exceptions provided in the Internal Revenue Code. Second, dividends paid by an Egyptian corporation are to be treated as U.S. source income if for the prior three years at least 50 percent of that corporation's gross income constituted industrial or commercial profits attributable to a permanent establishment in the United States. This rule differs from the comparable Internal Revenue Code provision in that all of the dividend is treated as U.S. source income rather than the pro rata portion of gross income.

Under the proposed treaty, interest will be treated as income from sources within a country only if paid by that country, a political subdivision or a local authority thereof, or by a resident of that country. However, interest paid on an indebtedness incurred in connection with a permanent establishment will be sourced in the country where the permanent establishment is situated. This exception permits one country, under the proper circumstances, to tax interest paid by a permanent establishment maintained in that country by a resident of the other country or by a resident of a third country. For example, if a resident of France has a permanent establishment in Egypt which borrows money from a resident of the United States, the interest paid by the Egyptian permanent establishment will be deemed to be from Egyptian sources and Egypt may therefore tax the interest payments. The United States will not under the Code (sec. 861) impose its withholding tax on interest paid to nonresident alien individuals or foreign corporations by a foreign corporation having a permanent establish-

ment in the United States unless the majority of the foreign corporation's gross income from all sources for the 3-year period preceding the payment of the interest was effectively connected with the conduct of a U.S. trade or business.

In addition, the source rule for interest paid by permanent establishments will operate to exempt interest from tax in the country of the taxpayor's residence if the interest is paid to a resident of the other country by a permanent establishment situated in a third country (and the indebtedness was incurred in connection with the third country permanent establishment). This results from the restriction in Article 6 (General rules of taxation) that a resident of one country who is not a citizen of the other country may be taxed by the other country only on income from sources within that other country.

The proposed treaty provides that royalties for the use of, or the right to use, property or rights will be treated as income from sources within a country only to the extent that such royalties are for the use of, or the right to use, the property or rights within that country.

Income (including mineral royalties) to which the provision relating to income from real property (Article 7) applies will be treated as income from sources within a country only if the real property (or, in the case of a mineral royalty, the underlying real property) is situated in that country.

Income from the rental of tangible personal (movable) property will be treated as income from sources within a country only to the extent that the income is for the use of such property in that country.

Income from the purchase and sale, exchange, or other disposition of intangible or tangible personal property (other than contingent gains described in paragraph (2) of Article 13 (Royalties)) will be treated as income from sources within a country only if such sale, exchange, or other disposition is within that country.

Income received by an individual for his performance of labor or personal services, whether as an employee or in an independent capacity, will be treated as income from sources within a country only to the extent that such services are performed in that country. Income from personal services performed aboard ships or aircraft operated by a resident of one country in international traffic will be treated as income from sources within that country if performed by a member of the regular complement of the ship or aircraft. However, compensation described in Article 21 (Governmental functions) and social security payments (Article 20) will be treated as income from sources within the country making the payments.

Industrial or commercial profits attributable to a permanent establishment will be considered to be from sources within the country in which the permanent establishment is located. This rule also applies to passive income of the types described above in situations where the passive income is treated as industrial and commercial profits because it is effectively connected with the permanent establishment.

The source of any item of income not specified in this article will be determined by each country in accordance with its own law. However, if the source of any item of income under the laws of one country is different from its source under the laws of the other country, or if its source is not readily determinable under the laws of either, the com-

petent authorities of the two countries may, in order to prevent double taxation or further any other purpose of the proposed treaty, establish a common source of the item of income for purposes of the proposed treaty.

Article 5. Definition of permanent establishment

The proposed treaty contains a definition of permanent establishment which generally follows the pattern of other recent U.S. income tax treaties and the OECD model tax treaty. The permanent establishment concept is one of the basic devices used in income tax treaties to avoid double taxation. Generally, a resident of one country is not taxable on its business profits by the other country unless those profits are attributable to a permanent establishment of the resident in the other country. In addition, the permanent establishment concept is used to determine whether the reduced rates of, or exemptions from, tax provided for dividends, interest, and royalties are applicable.

In general, a fixed place of business through which a resident of one country engages in industrial or commercial activities in the other country is considered a permanent establishment. The treaty specifies that a fixed place of business includes a seat of management; a mine or quarry, or other place of extraction of other natural resources; and any building site or construction or assembly project (or supervision activity connected therewith and conducted within the country where a site or project is located) which was maintained for more than 6 months.

This general rule is modified to provide that a fixed place of business which is used for any or all of a number of specified activities will not constitute a permanent establishment. These activities include the use of facilities for storing, displaying, or delivering merchandise belonging to the resident; the maintenance of a stock of goods belonging to the resident for purposes of storage, display, delivery, or processing by another person; and the purchase of goods, collection of information, advertising, scientific research, or other auxiliary activities, for the resident. A resident shall not be deemed to have a permanent establishment in the other country merely because the resident sells goods which were displayed at trade fairs or conventions in that other country. The trade fair exception is not intended to apply with respect to goods in the resident's inventory.

A resident of one country will be deemed to have a permanent establishment in the other country if it maintains an agent in the other country who has, and habitually exercises, a general contracting authority (other than for the purchase of merchandise) in that other country. The proposed treaty contains the usual provision that the agency rule will not apply if the agent is a broker, general commission agent or other agent of independent status acting in the ordinary course of its business.

The determination of whether a resident of one country has a permanent establishment in the other country is to be made without regard to the fact that the resident may be related to a resident of the other country or to a person who engages in business to that other country.

Article 6. General rules of taxation

The proposed treaty contains the basic general rules of taxation which are found in most of our other tax treaties. A resident of one

country may be taxed by the other country only on income from sources within that other country (which includes business profits only to the extent they are attributable to a permanent establishment in that other country). For this purpose, the source rules of Article 4 are to be applied. The proposed treaty also contains the customary rule that it may not be applied to increase the tax burden of either country beyond what it would be in the absence of the treaty—that is, the treaty only applies in those situations where it benefits taxpayers.

Additionally, the proposed treaty provides that, with certain exceptions, the treaty is not to affect the taxation by the United States or Egypt of their citizens or residents. However, this savings clause does not apply in several cases where its application would nullify specific policies contained in the proposed treaty which are designed to benefit residents and citizens. The principal exceptions involve social security payments, the foreign tax credit, and nondiscrimination provision. The savings clause also does not affect the benefits provided to resident aliens under the provisions relating to diplomatic or consular officers or other governmental employees, teachers, and students, provided they do not have immigrant status in the country imposing the tax.

Similar to certain other U.S. tax treaties, the proposed treaty limits to some degree the right of the United States to impose its personal holding company tax and accumulated earnings tax with respect to Egyptian corporations. Under the proposed treaty, an Egyptian corporation will be exempt from the personal holding company tax in any taxable year in which Egyptian residents who are not U.S. citizens own all of the stock of the corporation. In addition, an Egyptian corporation will be exempt from the accumulated earnings tax in any taxable year unless it is engaged in trade or business in the United States through a permanent establishment at any time during such year. In the event an Egyptian corporation does not satisfy the requirements for exemption under the proposed treaty, it may be subjected to the accumulated earnings tax only with respect to income from sources within the United States (Treas. Reg. § 1.532–1(c)).

Article 7. Income from real property

The proposed treaty provides that income from real property may be taxed in the country where the real property is located. Income from real property includes income from the direct use or renting of the property and gains on the sale, exchange, or other disposition of the property. It also includes royalties and other payments in respect of the exploitation of natural resources (e.g., oil wells) and gains on the sale, exchange or other disposition of the royalty rights on the underlying natural resource.

Article 8. Business profits

Under the proposed treaty, industrial and commercial profits of a resident of one country are taxable in the other country only to the extent they are attributable to a permanent establishment which the resident has in the other country.

In computing the taxable industrial and commercial profits, the deduction of all expenses, wherever incurred, which are reasonably connected with the business profits are allowed. Deductible expenses include executive and general administrative expenses, wherever in-

curred. However, in determining the amount of the deduction for head office expenses, the deduction may be limited to the expenses actually incurred by the head office without including a profit element.

The profits of a permanent establishment are determined on an arm's-length basis. Thus, there is to be attributed to it the industrial and commercial profits which would reasonably be expected to have been derived if it were an independent entity engaged in the same or similar activities under the same or similar conditions and dealing at arm's-length with the resident of which it is a permanent establishment.

Industrial and commercial profits will not be attributed to a permanent establishment merely by reason of the purchase of merchandise by the permanent establishment (or by the resident of which it is a permanent establishment) for the account of that resident. Thus, where a permanent establishment purchases goods for its head office, the industrial and commercial profits attributed to the permanent establishment with respect to its other activities will not be increased by any profit element on its purchasing activities.

For purposes of the proposed treaty, the term "industrial or commercial profits" includes income derived from manufacturing, mercantile, banking, insurance, agricultural, fishing or mining activities, the operation of ships or aircraft, the furnishing of services, the rental of tangible personal (movable) property and the rental or licensing of motion picture films or films or tapes used for radio or television broadcasting. The term does not include income from the performance of personal services derived by an individual either as an employee or in an independent capacity. The proposed treaty follows the approach of our other recent tax treaties and the Internal Revenue Code by including within "industrial and commercial profits" investment income (income from dividends, interest, certain royalties, capital gains, and income derived from property and natural resources) where the income is effectively connected with a permanent establishment.

The proposed treaty also contains criteria for determining whether income is effectively connected with a permanent establishment. Factors to be taken into account include whether the rights or property giving rise to such income are used in (or held for use in) carrying on an activity giving rise to industrial or commercial profits through a permanent establishment and whether the activities carried on through such permanent establishment are a material factor in the realization of the income. This effectively connected concept in this paragraph is substantially similar to the effectively connected concept applied to all taxpayers in the Code (sec. 864(c)).

Article 9. Shipping and air transport

The proposed treaty exempts from tax in one country income which is derived by a resident of the other country from the operation of ships and aircraft in international traffic and gains which are derived from the sale, exchange or other disposition of such ships or aircraft. However, the exemption only applies if the ships or aircraft are registered in the United States, Egypt, or a third country which, pursuant to a tax treaty with the U.S., exempts the income in question. This

exemption is somewhat broader than that previously provided in most U.S. tax treaties under which shipping and air transport income of a resident of one country is exempt by the other only if the ships or aircraft are registered in the first country.

Income from the operation in international traffic of ships or aircraft includes the rental income of ships or aircraft operated in international traffic if the rental income is incidental to income of the resident from the actual operation of ships or aircraft which would qualify for the exemption. For example, this rule permits an airline which is a resident of one country and which has excess equipment during certain periods to lease that excess equipment during those periods to an airline which is a resident of the other country. In such a case the rental income of the lessor is exempt from tax in the other country, whether or not the other airline uses the aircraft in international traffic.

The proposed treaty also makes clear that income derived from the use, maintenance, and lease of containers, trailers for the inland transport of containers, and other related container equipment in connection with the operation in international traffic of ships or aircraft is to be included within the scope of the shipping and air transport provision.

The treaty also provides that the Decree of the Egyptian Council of Ministers (of November 23, 1955), which provides a limited exemption for U.S. air transport enterprises, is to cease to have effect upon entry into force of this convention, since the treaty contains a broader exemption provision.

Article 10. Related persons

The proposed treaty, like most other U.S. tax treaties, contains a provision similar to section 482 of the Internal Revenue Code which recognizes the right of each country to make an allocation of income in the case of transactions between related persons, if an allocation is necessary to reflect the conditions and arrangements which would have been made between unrelated persons.

It is anticipated that when a redetermination has been made by one country with respect to the income of a related person, the other country will attempt to reach an agreement with the first country in connection with the redetermination and, if it agrees with the redetermination, it will make a corresponding adjustment to the income of the other person.

Article 11. Dividends.

The proposed treaty limits the rate of withholding tax imposed by the United States to 15 percent on dividends to Egyptian residents generally and to 5 percent on dividends paid to corporations which have at least a 10-percent ownership interest in the paying corporation. The 5-percent withholding rate is not to apply where more than 25 percent of the paying corporation's gross income consists of interest and dividends (i.e., where the corporation is an investment company).

The treaty contains no comparable reduction of Egyptian tax on dividends paid by Egyptian corporations to residents of the United States. Under the treaty, dividends are subject to the tax on movable

capital plus the defense tax, the national security tax, the war tax, the supplementary tax on any of the above taxes and any substantially similar taxes enacted after the treaty enters into force. To the extent dividends are paid out of current earnings, the paying corporation must be allowed a deduction from taxable income equal to the amount of the dividend in order for the dividend to be taxable in Egypt. No deduction is required with respect to distributions out of accumulated earnings. These treaty provisions thus do not alter the rules of Egyptian law which would be applied in the absence of a treaty.

In the case of dividends paid by Egyptian corporations to individuals the treaty provides that the general income tax imposed under Egyptian law may be levied. But under the treaty the average amount of tax imposed cannot exceed 20 percent of the net dividend for any year.

As other treaties have provided, dividends which constitute industrial or commercial profits of a resident in one country attributable to a permanent establishment in the other country are to be treated as business profits (and taxed under Article 8) rather than as dividends.

The treaty contains special rules for branches of U.S. corporations which constitute permanent establishments in Egypt and for U.S. corporations which operate solely or mainly in Egypt. Under the treaty, dividends paid by these U.S. corporations and dividends deemed to be paid (under Egyptian law) by branches of U.S. corporations are also to be fully subject to the Egyptian tax on movable capital and the special purpose taxes described above in connection with dividends paid to Egyptian corporations. These rules are also to apply only if an Egyptian corporate tax deduction is allowed to the U.S. corporation or branch for the amount of the dividend or deemed dividend paid.

Finally, the treaty specifies the treatment of U.S. direct investors so that they are eligible to receive benefits from Egyptian investment incentive laws Egyptian law (Article 16 of Egyptian Law No. 43 of 1974) provides tax exemptions for certain types of direct investors, but the exemption does not apply to the extent that the profits are subject to tax in another country. The treaty verifies that income of an Egyptian corporation which is 10 percent or more owned by U.S. residents is not subject to tax in the United States unless it derives profits which are from sources within the United States or are effectively connected with a U.S. trade or business or unless it makes a dividend distribution to its shareholders. The treaty states that Egypt will treat profits of 10-percent U.S. owned Egyptian corporations as exempt from U.S. tax as long as they are not taxed as described above, thereby qualifying them for tax exemption under Article 16 of Egyptian Law No. 43 of 1974. However, the treaty also provides that any dividends paid which are subject to tax in the United States shall be subject to the Egyptian tax from which exemption was given to the extent of the dividend and shall be entitled to a tax credit by the United States. It is understood that in the absence of the treaty the U.S.-owned Egyptian corporations would not be eligible to receive the tax exemption (and thus the dividends would be treated under the normal rules described above).

Article 12. Interest

The proposed treaty generally limits the withholding tax in the source country on interest derived by a resident of one country from sources within the other country to 15 percent of the gross amount of interest paid.

The reduced rates of withholding tax on interest will apply unless the recipient has a permanent establishment in the source country and the interest is effectively connected with the permanent establishment. If the interest is effectively connected with a permanent establishment then it will be taxed under the business profits provisions (Article 8) of the proposed treaty. This treatment generally conforms to that provided by other recent U.S. tax treaties and the OECD model tax treaty.

Interest paid by a resident of one country to a person other than a resident of the other country (and, in the case of interest paid by a resident of Egypt, to a person other than a U.S. citizen) will be exempt from tax by the other country. However, this rule is inapplicable (1) if the interest is treated as income from sources within the other country under the proposed treaty's source of income rules or (2) if the recipient of the interest has a permanent establishment in the other country and the interest is effectively connected with the permanent establishment.

The proposed treaty also provides that interest derived beneficially by either country, or by a tax-exempt instrumentality of either country, will be exempt from tax by the other country. Under this rule income derived by the Export-Import Bank of the United States and the Overseas Private Investment Corporation (OPIC) on loans made to Egyptian residents will be exempt from tax by Egypt. This exemption also applies where a resident of one country receives interest income on debt obligation guaranteed or insured by that country or an instrumentality of that country.

The proposed treaty defines interest as income from money lent. In situations where the payor and recipient are related, the interest provision of the proposed treaty only applies to the amount of interest to that which would have been paid had they not been related.

Article 13. Royalties

Under the proposed treaty, the withholding tax on royalties derived by a resident of one country from sources within the other is limited to 15 percent of the gross amount of the royalty.

Royalties are defined in the proposed treaty as payments of any kind made as consideration for the use of, or the right to use, copyrights of literary, artistic, or scientific works, and payments of any kind made as consideration for the use of, or the right to use, patents, designs, models, plans, secret processes or formulas, trademarks, or other like property or rights. Payments made on copyrights of motion picture films or films or tapes used for radio or television broadcasting are not treated as royalties to the extent they are commercial and industrial profits under Article 8. Royalties include gains derived from the sale, exchange, or other disposition of such property or rights to the extent the amounts received are contingent on the productivity,

use, or disposition of the property or rights. If the amounts realized are not contingent, the provisions of Article 14 (Capital gains) may apply.

The reduced withholding rates do not apply where the recipient has a permanent establishment in the source country and the royalties are effectively connected with the permanent establishment. If the royalty is effectively connected with a permanent establishment, then it will be taxed under the business profits provisions (Article 8).

As in the case of the interest provision, the royalty provision does not apply to that part of a royalty paid to a related person which is considered excessive. In addition, the provision does not apply to dividends on stock issued under Egyptian law as consideration for royalty rights.

Article 14. Capital gains

The proposed treaty generally provides that capital gains derived by a resident of one country will be exempt from tax by the source country. The exemption does not apply where an individual resident of one country is present in the source country for 183 days or more during the taxable year. In addition, this provision does not apply to gains which are subject to the provisions relating to business profits (Article 8), income from real property (Article 7), royalties (Article 13), or shipping and air transport income (Article 9).

Article 15. Independent personal services

Under the proposed treaty, income from the performance of independent personal services (i.e., services performed as an independent contractor, not as an employee) in one country by a resident of the other country is exempt from tax in the country where the services are performed, unless the person performing the personal service is present in the source country for 90 or more days during the taxable year. This provision does not apply to income derived by public entertainers (theater, motion picture, radio and television artists, musicians, and athletes) which is governed by Article 17.

Article 16. Dependent personal services

Under the proposed treaty, income from services performed as an employee in one country (the source country) by a resident of the other country will not be taxable in the source country if four requirements are met: (1) the individual is present in the source country for less than 90 days during the taxable year; (2) the individual is an employee of a resident of or a permanent establishment in, his country of residence; (3) the compensation is not borne by a permanent establishment of the employer in the source country; and (4) the income is subject to tax in the country of residence. Income of a U.S. citizen which is excluded from income under the section 911 exclusion for income earned abroad thus does not qualify for the exemption from Egyptian tax.

Compsenation derived by an employee aboard a ship or aircraft operated by a resident of one country in international traffic is exempt from tax by the other country, provided that the employee is a member of the regular complement of the ship or aircraft.

Article 17. Public entertainers

This proposed treaty provides that, notwithstanding Articles 15 (Independent personal services) and 16 (Dependent personal services), income derived by an individual resident of one country from his performance of personal services in the other country as a public entertainer, such as a theater, motion picture, radio or television artist, a musician or an athlete, may be taxed by the other country, but only if the gross amount of such income exceeds $400 for each day the individual is present in the other country for the purpose of performing such services therein.

Article 18. Amounts received for furnishing personal services

The proposed treaty contains a provision which allows the country where personal services are furnished to tax the income from the furnishing of the services under situations which have been viewed as an abuse of tax treaties. The purpose of this provision is to prevent individuals (generally residents of a third country) from using an entity of one country (for example, a corporation) to furnish services in the other country and thereby avoid the payment of tax in either country.

Under the proposed treaty, amounts received by a resident of one country for furnishing in the other country the services of one or more individuals may be taxed by the country where the services are performed where the resident directly or indirectly compensates the person or persons who actually performed the services. This provision is to apply if the person for whom the services were rendered had the right (whether or not legally enforceable) to designate the person or persons who would render the services, or did in fact designate the person or persons, and the person performing the services is not a resident of either country who is subject to tax on the compensation. This provision is not to apply if it is established to the satisfaction of the competent authority of the source country that the organization furnishing the services was neither formed nor used in a manner which results in a substantial reduction on the income taxes from the furnishing of the services.

Article 19. Private pensions and annuities

Under the proposed treaty, private pensions and other similar remuneration, alimony, and annuities derived from one country by residents of the other country are exempt from tax in the source country. Child support payments paid by a resident of one country to a resident of the other are exempt in the recipient's country.

Article 20. Social security payments

Under the proposed treaty, social security payments and other public pensions paid by one country to residents of the other are to be exempt from tax in both countries. The article relating to termination of the treaty generally contains a special provision (Article 32(2)) allowing this Article to be terminated by either country at any time after the proposed treaty enters into force.

Article 21. Governmental functions

Under the proposed treaty, wages, including pensions or similar benefits, paid by one country to an individual for labor or personal

services performed for that country in the discharge of governmental functions is exempt from tax by the other country. This exemption does not apply if the individual performing the services is a citizen of, or acquires immigrant status in, the country where the services are performed. However, any services performed in connection with a trade or business carried on by one of the countries are to be treated the same as services provided for private employers (for which Articles 16 and 19 apply).

Article 22. Teachers

The proposed treaty provides that a teacher or researcher who is a resident of one country will be exempt from tax in the other country on income from teaching or engaging in research in the host country if he is present in that country for a period not expected to exceed two years. The exemption only applies if the individual comes to the other country primarily for the purpose of teaching or engaging in research pursuant to an invitation of the host country or a recognized educational institution of the host country. It is not to apply with respect to income from research which is undertaken primarily for the benefit of a specific person or persons. If the teacher or researcher remains in the other country for a period exceeding two years, the exemption only applies to income earned during the 2-year period.

Article 23. Students and trainees

Under the proposed treaty, residents of one country who become students in the other country will be exempt from tax in the host country on gifts from abroad used for maintenance or study and on any grant, allowance or award. In addition, a $3,000 annual exemption from tax by the host country is provided for personal service income (such as income from a part-time job) derived from sources within the country in which the individual is studying.

These exemptions and the visiting teachers' exemption (Article 22) may only be utilized for a period of 5 years plus any additional period of time necessary to complete educational requirements as a candidate for a post-graduate or professional degree from a recognized institution. In addition, the benefits under the teacher's article are not available to an individual if, during the immediately preceding period, the individual received the benefit of the student provision.

In addition to the exemption regarding students, the proposed treaty follows the approach of other recent U.S. tax treaties and provides a limited exemption for personal service income of residents of one country who are employees of a resident of that country and who are temporarily present in the other country to study at an educational institution or to acquire technical, professional, or business experience. This exemption is available for a period of 12 consecutive months and is limited to $7,500. The proposed treaty also provides an exemption for income from personal services performed in connection with training, research, or study by residents of one country who are temporarily present in the other country as participants in Government-sponsored training programs. This exemption is limited to $10,000.

If an individual qualifies for the benefits of more than one of the provisions of this article and Article 22 (the visiting teachers exemption), the individual may choose the most favorable provision but may

not claim the benefits of more than one provision in any taxable year. This provision does not apply to students or trainees who are citizens of, or who have acquired immigrant status in, the host country.

Article 24. Investment or holding companies

The proposed treaty contains a provision which denies the benefits of the dividends, interest, royalties, and capital gains articles to a corporation which is entitled in its country of residence to special tax benefits resulting in a substantially lower tax on those types of income than the tax generally imposed on corporate profits by that country. This provision only applies if more than 25 percent of the capital of the corporation is owned by nonresidents of that country. A similar provision is contained in several recent U.S. tax treaties.

The purpose of this provision is to prevent residents of third countries from using a corporation in one treaty country, which is preferentially taxed in that country, to obtain the tax benefits in the other treaty country which the proposed treaty provides for dividends, interest, royalties, and capital gains derived from that other country. This accords with the purpose of an income tax treaty between two countries to lessen or eliminate the amount of double taxation of income derived from sources within one country by a resident of the other country.

Article 25. Relief from double taxation

Under the proposed treaty, each country agrees to provide its citizens and residents with a foreign tax credit for the appropriate amount of income taxes paid to the other country. The credit allowed for U.S. tax purposes under this provision is subject to the provisions of U.S. law applicable to the year in question. The credit allowed by Egypt is limited to the amount of Egyptian tax attributable to income from sources within the United States.

The proposed treaty also provides that a deemed-paid foreign tax credit will be made available to a United States corporation with respect to dividends from an Egyptian corporation in which it has at least a 10-percent ownership interest. In this case, a credit will be allowed for the Egyptian corporate tax paid by the Egyptian corporation on the earnings out of which the dividend is paid. A deemed-paid foreign tax credit satisfying the treaty requirements is presently provided under the Internal Revenue Code. Similarly, the proposed treaty provides that Egypt is to provide a deemed-paid foreign tax credit for U.S. tax attributable to dividends received by Egyptian corporations from U.S. corporations in which they are 10-percent shareholders.

For the purpose of applying the U.S. foreign tax credit in relation to taxes paid to Egypt, the rules set forth under Article 4 will be applied to determine the source of income. The Egyptian taxes which the proposed treaty provides are creditable for U.S. tax purposes are the various taxes listed as those covered by the treaty in Article 1.

Article 27. Nondiscrimination

The proposed treaty contains a comprehensive nondiscrimination provision relating to taxes imposed at the national level similar to provisions which have been embodied in other recent U.S. income tax treaties. One country cannot discriminate by imposing more burden-

some taxes on its residents who are citizens of the other country, or on permanent establishments of residents of the other country, than it imposes on comparable taxpayers. This provision does not, however, require either country to grant to residents of the other country the personal allowances, reliefs, or deductions for taxation purposes on account of personal status or family responsibilities which it grants to its own residents. The nondiscrimination provision also applies to corporations of one country which are owned by residents of the other country.

The treaty contains two exceptions, however. Egypt is not required to give to U.S. corporations the exemptions from Egyptian tax provided under Egyptian law for income earned outside of Egypt as insurance reserves of an Egyptian corporation and with respect to certain exempt distributions from Egyptian corporations (necessary to avoid double taxation within that country). In addition, an exception is provided for the provisions of Article 11 allowing Egypt to tax dividends from U.S. corporations operating solely or mainly in Egypt and to tax deemed dividends from Egyptian permanent establishments of U.S. corporations.

Articles 27 and 28. Administrative provisions

The proposed treaty contains various administrative provisions generally along the lines of the provisions contained in other U.S. tax treaties. In general, the proposed treaty provides for—

(1) consultation and negotiation between the two countries to resolve differences arising in the application of the proposed treaty and also to resolve claims by taxpayers that they are being subjected to taxation contrary to the terms of proposed treaty; and

(2) the exchange between the countries of information pertinent to carrying out the provisions of the proposed treaty and of the domestic laws of the countries concerning taxes covered by the proposed treaty.

Article 29. Assistance in collection

The provision requires that each country aid in collecting the taxes of the other country to the extent necessary to insure that treaty benefits are not enjoyed by persons not entitled to their benefit.

Article 30. Diplomatic and consular officials

The proposed treaty contains the rule found in other U.S. tax treaties that its provisions are not to affect the fiscal privileges of diplomatic and consular officials under the general rules of international law or the provisions of special agreements.

Article 31. Entry into force

The proposed treaty will enter into force 30 days following the exchange of the instruments of ratification. It will become effective with respect to withholding tax rates on the first day of the second month following the date on which the proposed treaty enters into force. With respect to all other taxes, it will become effective for taxable years beginning on or after January 1st of the year following the date on which the proposed treaty comes into force.

Article 32. Termination

The proposed treaty will continue in force indefinitely, but either country may terminate it at any time after 5 years from its entry into force by giving at least 6 month's prior notice through diplomatic channels. If terminated, the termination will be effective with respect to income of taxable years beginning (or, in the case of withholding taxes, payments made) on or after April 1 next following the expiration of the 6-month period. The provisions of Article 20 (social security payments) may be terminated by either country at any time after the proposed treaty enters into force by prior notice given through diplomatic channels.

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