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EXPLANATION OF PROPOSED INCOME TAX TREATY BETWEEN THE UNITED STATES AND THE KINGDOM OF MOROCCO

PREPARED FOR THE USE OF THE

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INTRODUCTION

This pamphlet provides an explanation of the proposed income tax treaty between the United States and the Kingdom of Morocco ("Morocco"). The proposed treaty was signed on August 1, 1977, and was amplified by an Exchange of Notes signed the same day. No similar treaty between the two countries is in force at the present time. The proposed treaty has been scheduled for a public hearing on September 24, 1981, by the Senate Committee on Foreign Relations.

The proposed treaty is similar to other recent U.S. income tax treaties and to the model income tax treaty of the Organization for Economic Cooperation and Development (OECD).

The first part of the pamphlet is a summary of the principal provisions of the proposed tax treaty. The second part provides an overview of U.S. tax rules relating to international trade and investment and U.S. tax treaties in general. This is followed by a detailed, article-by-article explanation of the proposed treaty.

I. SUMMARY

In general

The principal purpose of the proposed income tax treaty between the United States and Morocco is to reduce or eliminate potential double taxation of income earned by citizens and residents of either country from sources within the other country. The proposed treaty is intended to promote closer economic cooperation between the two countries and to eliminate possible barriers to trade caused by overlapping taxing jurisdictions of the two countries.

As in other U.S. tax treaties, these objectives are principally achieved by each country agreeing to limit, in certain specified situations, its right to tax income derived from its territory by residents of the other. For example, the treaty contains the standard tax treaty provision that neither country will tax the business income derived from sources within that country by residents of the other unless the business activities in the taxing country are substantial enough to constitute a branch or other permanent establishment or fixed base (Article 7). Similarly, the treaty contains the standard "commercial visitor" exemptions under which residents of one country performing personal services will not be required to file tax returns and pay tax in the other unless their contacts with the other exceed certain specified minimums (Articles 14 through 18). Also, the proposed treaty provides that interest, dividends, and royalties, received by residents of one country from sources within the other are to be taxed at reduced rates by the country of source (Articles 10, 11, and 12), and that capital gains and certain other income derived by residents of either country from sources within the other are generally to be taxed only by the country of residence and not by the country of source (Articles 13 and 20).

In situations where the country of source retains the right under the proposed treaty to tax income derived by residents of the other country, the treaty generally provides for the relief by the country of residence of the potential double taxation (Article 21) through a foreign tax credit.

The treaty contains the standard provision (the "saving clause") contained in U.S. tax treaties that each country retains the right to tax its citizens and residents as if the treaty had not come into effect (Article 20). In addition, it contains the standard provision that the treaty will not be applied to deny any taxpayer any benefits he would be entitled to under the domestic law of either country or under any other agreement between the two countries (Article 20); that is, the treaty will only be applied to the benefit of taxpayers.

The treaty also contains standard nondiscrimination provisions and provides for exchanges of information and administrative cooperation between the tax authorities of the two countries to avoid double taxation and prevent fiscal evasion with respect to income taxes.

Issues

(1) *Forced loans.*—The proposed treaty would require the United States to treat as income taxes certain loans which a U.S. business operating in Morocco is required to make to the Moroccan government. Thus, the U.S. business would be allowed a foreign tax credit for the amount of the loan. However, a repayment of the loan will be treated as a refund of Moroccan tax to the U.S. business, and thus the taxpayer's creditable foreign taxes would be reduced in the year of repayment. As a practical matter, this amounts to a loan from the U.S. government to Morocco with the taxpayer as the middleman.

(2) *Developing country concessions.*—The proposed treaty contains a number of provisions that permit greater source basis taxation than does the U.S. model and many U.S. income tax treaties. For example, a building site or construction project is a permanent establishment if it lasts for more than six months rather than the 12 months provided in the U.S. model. Also, the limtis on source basis taxation of investment income are higher than those found in the U.S. model, the OECD model, and many U.S. treaties. These provisions raise the question of the desirability of concessions to source basis taxation in treaties with developing countries.

II. OVERVIEW OF UNITED STATES TAXATION OF INTERNATIONAL TRADE AND INVESTMENT AND TAX TREATIES

A. United States Tax Rules

The United States taxes U.S. citizens and residents and U.S. corporations on their worldwide income. The United States generally taxes nonresident alien individuals and foreign corporations only on their U.S. source income.

Income of a nonresident alien or foreign corporation which is effectively connected with the conduct of a trade or business in the United States is subject to tax at the normal graduated rates on the basis of net taxable income. Deductions are allowed in computing effectively connected taxable income, but only if and to the extent they are connected with income which is effectively connected.

U.S. source fixed or determinable, annual or periodical income (e.g. interest, dividends, rents, salaries, wages, premiums, annuities) which is not effectively connected with a U.S. trade or business is subject to tax at a rate of 30 percent of the gross amount paid to the nonresident alien or foreign corporation. This gross tax on fixed or determinable income is often reduced or eliminated in the case of payments to residents of countries with which the U.S. has an income tax treaty. The 30-percent (or lower treaty rate) tax imposed on U.S. source noneffectively connected income paid to foreign persons is collected by means of withholding (hence they are often called withholding taxes).

Certain exemptions from the gross tax are provided. Bank account interest is defined as foreign source interest and, therefore, is exempt. Exemptions are also provided for certain original issue discount and for income of a foreign government from investments in U.S. securities. Our treaties also provide for exemption from tax in certain cases.

Net U.S. source capital gains are also subject to the 30 percent tax but only in the case of a nonresident alien who is present in the United States for at least 183 days during the taxable year. Otherwise foreign corporations and nonresident aliens are only subject to U.S. taxation (at the graduated rates) on those capital gains that are effectively connected with the conduct of a trade or business in the United States.

Prior to June 18, 1980, noneffectively connected capital gains from the sale of U.S. real estate were subject to U.S. taxation only if received by a nonresident alien who was present in the United States for at least 183 days. However, in the Omnibus Reconciliation Act of 1980 a provision was added to the Internal Revenue Code that the sale, exchange or disposition of U.S. real estate by a foreign corporation or a nonresident alien would be taxed as effectively connected income. Also taxable under this legislation are dispositions by foreign investors of their interests in certain U.S. corporations and other entities whose assets include U.S. real property and associated personal property.

The source of income received by nonresident aliens and foreign corporations is determined under special rules contained in the Internal Revenue Code. Under these rules interest and dividends paid by a U.S. citizen or resident or by a U.S. corporation are considered U.S. source income. However, if the U.S. corporation derives more than 80 percent of its gross income from foreign sources, then dividends and interest paid by such corporation will be foreign source rather than U.S. source. Conversely, dividends and interest paid by a foreign corporation, which has at least 50 percent of its income as effectively connected income, are U.S. source to the extent of the ratio of its effectively connected income to total income.

Rents and royalties paid for the use of property in the United States is considered U.S. source income. The property use can be either tangible property or intangible property (e.g., patents, secret processes and formulas, franchises and other like property).

Since it taxes U.S. persons on their worldwide income, double taxation of income can arise because income earned abroad by a U.S. person will be taxed by the country in which the income is earned and also by the United States. The U.S. seeks to mitigate this double taxation by allowing U.S. taxpayers to credit their foreign income taxes against the U.S. tax imposed on their foreign source income. A fundamental premise of the foreign tax credit is that it may not offset the U.S. tax on U.S. source income. Therefore, the foreign tax credit provisions contain a limitation that insures that the foreign tax credit only offset the U.S. tax on foreign source income. This limitation is computed on a world-wide consolidated basis. Hence, all income taxes paid to all foreign countries are combined to offset U.S. taxes on all foreign income. Separate limitations on the foreign tax credit are provided for certain interest, DISC dividends, and oil income.

A U.S. corporation that owns 10 percent or more of the stock of a foreign corporation may credit foreign income taxes paid or deemed paid by that corporation on earnings that are received as dividends. These deemed paid taxes are included in total foreign taxes paid for the year the dividend is received and go into the general pool of taxes to be credited.

B. United States Tax Treaties—In General

The traditional objectives of U.S. tax treaties have been the avoidance of international double taxation and the prevention of tax avoidance and evasion. To a large extent, the treaty provisions designed to carry out these objectives supplement Code provisions having the same objectives, modifying the generally applicable statutory rules with provisions which take into account the particular tax system of the treaty country. Given the diversity of tax systems in the world, it would be virtually impossible to develop in the Code rules which unilaterally would achieve these objectives for all countries.

Notwithstanding the unilateral relief measures of the United States and our treaty partners, double taxation might arise because of differences in source rules between the United States and the other country. Likewise, if both countries consider the same deduction allocable to foreign sources, double taxation can result. Significant problems arise in the determination of whether a foreign tax qualifies for the U.S. foreign tax credit. Also, double taxation may arise in those limited situations where a corporation or individual may be treated as a resident of both countries and be taxed on a worldwide basis by both.

In addition, there may be significant problems involving "excess" taxation—situations where either country taxes income received by nonresidents at rates which exceed the rates imposed on residents. This is most likely to occur in the case of income taxed at a flat rate on a gross income basis. (Most countries, like the United States, generally tax domestic source income on a gross income basis when it is received by nonresidents who are not engaged in business in the country.) In many situations the gross income tax is imposed at a rate which exceeds the tax which would have been paid under the net income tax system applicable to residents.

Another related objective of U.S. tax treaties is the removal of barriers to trade, capital flows, and commercial travel caused by overlapping tax jurisdictions and the burdens of complying with the tax laws of a jurisdiction where the contacts with, and income derived from, that jurisdiction are minimal.

The objective of limiting double taxation is generally accomplished in treaties by the agreement of each country to limit, in certain specified situations, its right to tax income earned from its territory by residents of the other country. For the most part, the various rate reductions and exemptions by the source country provided in the treaties are premised on the assumption that the country of residence will tax the income in any event at levels comparable to those imposed by the source country on its residents. The treaties also provide for the elimination of double taxation by requiring the residence country to allow a credit for taxes which the source country retains the right to impose under the treaty. In some cases, the treaties may provide for exemption by the residence country of income taxed by the source country pursuant to the treaty.

Treaties first seek to eliminate double taxation by defining the term "resident" so that an individual or corporation generally will not be subject to tax as a resident by each of the two countries. The treaty also provides that neither country will tax business income derived from sources within it by residents of the other country unless the business activities in the taxing jurisdiction are substantial enough to constitute a branch or other permanent establishment or fixed base. The treaties contain commercial visitation exemptions under which individual residents of one country performing personal services in the other will not be required to file tax returns and pay tax in that other country unless their contacts exceed certain specified minimums. For example, presence for a set number of days or earnings of over a certain fixed dollar amount.

The treaties deal with passive income such as dividends, interest, or royalties, or capital gains, from sources within one country derived by residents of the other country by either providing that they are taxed only in the country of residence or by providing that the withholding tax generally imposed on those payments is reduced. As described above, the U.S. generally imposes a 30 percent tax and seeks to reduce this tax in some cases on some income to zero in its tax treaties.

In its treaties, the United States, as a matter of policy, retains the right to tax its citizens and residents on their worldwide income as if the treaty had not come into effect, and provides this in the treaties in the so-called "saving clause." Double taxation can therefore still arise. Double taxation can also still arise because most countries will not exempt passive income from tax at source.

This double taxation is further mitigated either by granting a credit for income taxes paid to the other country, or, in the case of some of our treaty partners, by providing that income will be exempt from tax in the country or residence. The United States provides in its treaties that it will allow a credit against United States tax for income taxes paid to the treaty partners, subject to the limitations of U.S. law. An important function of the treaty is to define the taxes to which it applies to provide that they will be considered creditable income taxes for purposes of the treaty.

The treaties also provide for administrative cooperation between the countries. This cooperation includes a competent authority mechanism to resolve double taxation problems arising in individual cases, or more generally, by consultation between tax officials of the two governments.

Administrative cooperation also includes provision for an exchange of tax-related information to help the United States and its treaty partners administer their tax laws. The treaties generally provide for the exchange of information between the tax authorities of the two countries where such information is necessary for carrying out the provisions of the treaty or of their domestic tax laws. The obligation to exchange information under the treaties typically does not require either country to carry out measures contrary to its laws or administrative practices or to supply information not obtainable under its laws or in the normal course of its administration, or to supply information which would disclose trade secrets or other information the disclosure of which would be contrary to public policy.

The provisions generally result in an exchange of routine information, such as the names of U.S. residents receiving investment income. The IRS (and the treaty partner's tax authorities) also can request specific tax information from a treaty partner. This can include information to be used in a criminal investigation or prosecution.

III. EXPLANATION OF PROPOSED TAX TREATY

A detailed, article-by-article explanation of the proposed income tax treaty between the United States and Morocco is presented below.

Article 1. Taxes Covered

The proposed treaty generally applies to income taxes imposed by either country.

In the case of the United States, the proposed treaty applies to the Federal income taxes imposed under the Internal Revenue Code ("United States Tax"). However, it does not generally apply to the accumulated earnings tax or the personal holding company tax. (See Article 20.)

In the case of Morocco, the treaty applies to the agricultural tax; the taxes on urban property; the tax on public and private salaries, emoluments, fees, wages, pensions, and annuities; the complementary tax; the business profits tax; and the compulsory loan for investment by the Moroccon government as provided in Article 37 of Royal Decree No. 1.010–65 of the 8th of Ramadan 1385 (31 December 1965) containing the Finance Law for the year 1966 (collectively referred to as "Moroccan tax"). The United States will permit a foreign tax credit for these taxes. (See Article 21.)

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

Additionally, the nondiscrimination provisions (Article 22) of the treaty apply to all taxes of every kind imposed at the national, state, or local level by the United States or Morocco. The exchange of information provisions (Article 26) of the proposed treaty will also apply to all taxes of every kind imposed by the two countries at the national level.

Article 2. General Definitions

The standard definitions found in most U.S. income tax treaties are contained in the proposed treaty.

Under the proposed treaty, the term "United States" when used in a geographical sense means the States of the United States and the District of Columbia. (Thus, the treaty does not apply to the possessions or territories of the United States.) The term also includes the territorial sea of the United States and, to the extent a party subject to this treaty is exploring or exploiting natural resources, in the area, the seabed and subsoil of the submarine areas adjacent to the coast of the United States (continental shelf).

Under the proposed treaty, the term "Morocco" means the Kingdom of Morocco. When used in the geographical sense, the term "Morocco" also includes the territorial sea of Morocco and, to the extent a party subject to this treaty is exploring or exploiting natural resources in the area, the seabed and subsoil of the submarine areas adjacent to the coast of Morocco (continental shelf).

Under the proposed treaty, the term "person" includes an individual, a partnership, a corporation, an estate, a trust, or any body of person. Consistent with U.S. law, a "United States corporation" is a corporation that is created or organized under the laws of the United States, the States of the United States, or the District of Columbia. It also includes unincorporated entities which are treated as U.S. corporations under the provisions of the Internal Revenue Code.

A "Moroccan corporation" is a corporation, or any other entity that is treated as a corporation under Moroccan law, which is a resident within Morocco for Moroccan tax purposes.

The proposed treaty also contains the standard provision that, unless the context otherwise requires or the competent authorities of the two countries establish a common meaning, any terms are to have the meaning which they have under the applicable tax laws of the country applying the treaty.

Article 3. Fiscal Residence

The benefits of the proposed treaty generally are available only to residents of the two countries (see Article 20(1)) as that term is defined in the proposed treaty. Under the treaty, a United States corporation and a Moroccan corporation (both as defined in Article 2, above) are treated as residents of their respective countries. Also, any person (other than a corporation or an entity treated as a corporation under the laws of either country) which is resident in one of the treaty countries under its domestic law will be treated as a resident of that country for purposes of the treaty. However, a person acting in his capacity as a partner or fiduciary will be considered to be a resident of the United States only to the extent that the income he derives in that capacity is subject to tax as the income of a resident of the United States.

A set of rules is provided to determine residence in the case of an individual who, under the basic treaty definition, would be considered to be a resident of both countries (e.g., a U.S. citizen who is a resident of Morocco). In the case of a dual resident individual, the individual will be deemed for all purposes of the treaty to be a resident only of the country in which he has his permanent home (where an individual dwells with his family), his closest economic and personal relations (center of vital interests), 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. Permanent Establishment

The proposed treaty contains a definition of the term "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 by the other country on its business profits 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 business in the other country is considered a permanent establishment. This includes a seat of management; a branch, an office; a factory; a workshop; a warehouse; a store or other sales outlet; or a mine, quarry, or other place of extraction of natural resources.

The term permanent establishment also includes any building site or construction or installation project which exists for more than six months. This six month period is shorter than the 12 month period provided in the U.S. and OECD models and many U.S. treaties, and reflects Moroccos status as a developing country.

This general rule is modified to provide that a fixed place of business which is used solely 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 or for the maintenance of a stock of goods belonging to the resident for storage, display, or delivery, or for processing by another person. These activities also include the maintenance of a fixed place of business for advertising or scientific research, for the purchase of goods or merchandise, for the collection or supply of information, or for any similar preparatory or auxiliary activities for the resident.

If a resident of one country maintains an agent (other than an independent agent) in the other country who has, and regularly exercises, the authority to enter into contracts in that other country in the name of the resident, then the resident will be deemed to have a permanent establishment in the other country, unless the agent only purchases goods and merchandise for the resident. This rule does not apply where the contracting authority is limited to those activities (described above) such as storage, display, or delivery of merchandise which are excepted from the definition of permanent establishment. The proposed treaty contains the usual provision that a resident of one country will not be deemed to have a permanent establishment in the other country merely because it engages in business in that other country through an agent who is a broker, general commission agent, or other agent of independent status acting in the ordinary course of its business.

The proposed treaty does contain one provision which is not typically found in most U.S. treaties. The treaty provides that a resident of one country will be deemed to have a permanent establishment in the other country if it maintains substantial equipment for rental within that other country for a period of more than six months.

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 in that other country.

Article 5. Source of Income

The source of income rules are important in view of the general rule in the treaty (Article 20) 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). These rules are also important because the limitation on the foreign tax credit is based on the source of income. Several of the source rules contained in the proposed treaty differ in some degree from the source rules provided in the Internal Revenue Code. However, since the general rules of taxation contained in the proposed treaty (Article 20) provide that it will not be applied to increase a person's tax, a taxpayer is not bound to apply the treaty source rules in calculating his U.S. tax liability.

The proposed treaty provides that dividends will be treated as income from sources within a country only if paid by a corporation of that country.

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 borne by a permanent establishment (on an indebtedness incurred in connection with the 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 resident of the other country and borne by a permanent establishment maintained in that first country by a resident of the other country or by a resident of a third country. For example, if a resident of Mexico has a permanent establishment in the United States and borrows money from a resident of Morocco, and the interest is paid out of the income of the permanent establishment the interest paid by the Mexican resident will be deemed to be from United States sources (even though not paid by a resident of the United States) and the United States may therefore tax the interest payments. The United States would not under the Internal Revenue Code (sec. 861) impose its withholding tax on interest paid to nonresident alien individuals or foreign corporations by a foreign corporation having a permanent establishment 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 payor'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). For example, if a resident of the United States has a permanent establishment in Mexico and the U.S. resident borrows money from a resident of Morocco in connection with the permanent establishment and pays the interest on the debt, the interest income received by the Moroccan resident will not be U.S. source (although paid by a U.S. resident) and thus will not be subject to U.S. tax. Under the Internal Revenue Code, the United States would normally impose its withholding tax on interest payments to a nonresident alien or foreign corporation by a foreign permanent establishment of a U.S. corporation unless more than 80 percent of the U.S. corporation's income was from foreign sources for the three preceding taxable years.

The proposed treaty provides that royalties (as defined in Article 12) 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, property or rights described in Article 12, and the performance of accessory services within that country. This rule is generally the same as the rule found in the Code.

Income and gains from real property (including mineral royalties) will be treated as income from sources within a country only if the real property (including, 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 if the property is located in that country.

Income from the purchase and sale of intangible or tangible personal (including movable) property (other than contingent gains described in paragraph (3)(b) of Article 12 (Royalties)) will be treated as income from sources within a country only if sold within that country.

Income received for the performance of labor or personal services by an individual, whether as an employee or in an independent capacity, will be treated as income from sources within a country only to the extent that the 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. For purposes of the source rules, income from personal services includes pensions (as described in Article 19(3)). However, government compensation described in Article 17 (Governmental Functions) will be treated as income from sources within a country only if paid by or from the public funds of that country or a political subdivision or local authority of that country.

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 (e.g. income from real property and natural resources, dividends, interest, royalties, and capital gains) in situations where the passive income is treated as industrial or commercial profits because the underlying asset generating such income 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 one country, the competent 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 6. Income from Real Property

The proposed treaty provides that income from real property, including royalties received on natural resources, may be taxed in the country where the real property or natural resources are located. Income from real property includes income from the usufruct, direct use, letting or other use of real property and gains on the sale, exchange, or other disposition of real property. It also includes royalties and other payments in respect of the operation of mines, quarries, or other natural resources and gains on the sale, exchange or other disposition of the royalty rights or the underlying natural resource. Income from real property does not include interest on obligations secured by real property (e.g., mortgages) or secured by rights in natural resources which give rise to royalties.

Article 7. Business Profits

U.S. Code rules.—United States law separates the business and investment income of a nonresident alien or foreign corporation. A nonresident alien or foreign corporation is subject to a flat 30 percent (or lower treaty rate) rate of tax on its U.S. source income if that income is not effectively connected with the conduct of a trade or business within the United States. The regular individual or corporate rates apply to U.S. source income which is effectively connected with the conduct of a trade or business within the United States.

The taxation of income as business or investment income varies depending upon whether the income is U.S. or foreign. In general, U.S. source periodic income, such as interest, dividends, rents, wages, and capital gains, is effectively connected with the conduct of a trade or business within the United States only if the asset generating the income is used in or held for use in the conduct of the trade or business, or if the activities of the trade or business were a material factor in the realization of the income. All other U.S. source income is treated as effectively connected income.

Foreign source income is effectively connected income only if the foreign person has an office or other fixed place of business in the United States and the income is attributable to that place of business. Only three types of foreign source income can be effectively connected income; rents and royalties derived from the active conduct of a licensing business; dividends, interest, or gain from stock or debt derived in the active conduct of a banking, financing or similar business in the United States; and certain sales income attributable to a United States sales office.

Except in the case of a dealer, the trading in stocks, securities or commodities in the United States for one's own account does not constitute a trade or business in the United States and accordingly income from those activities is not taxed by the U.S. as business income. This concept includes trading through a U.S. based employee, a resident broker, commission agent, custodian or other agent or trading by a foreign person physically present in the United States.

Proposed treaty rules.—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 in the other country through which the resident actively conducts a trade or business.

In computing the taxable industrial and commercial profits, the deduction of expenses, wherever incurred, which are reasonably connected with the business profits are allowed.

The profits of a permanent establishment are determined on an arm's-length basis. Thus, there is to be attributed to it the industrial or commercial profits which would reasonably be expected to have been derived by it 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.

For purposes of the proposed treaty, the term "industrial or commercial profits" includes income derived from industrial commercial, insurance, agricultural, fishing or mining activities, the operation of ships or aircraft, and the rental of tangible personal property. The term does not include income from the performance of services as an employee or in the exercise of an independent profession. 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 drived from real property and natural resources) where the asset giving rise to the income is effectively connected with a permanent establishment.

The proposed treaty contains criteria for determining whether the asset giving rise to the income is effectively connected with a permanent establishment. Factors to be taken into account include whether the rights or property giving rise to the income are used in (or held for use in) carrying on an industrial or commercial activity through a permanent establishment and whether the activities carried on through the permanent establishment are a material factor in the realization of the income. For this purpose, due regard will be given to whether or not the property or rights or the income is accounted for through the permanent establishment. The effectively connected concept in the proposed treaty is substantially similar to the effectively connected concept in the Code (sec. 864(c)).

Where business profits include items which are dealt with separately in other articles of the treaty, those articles will control the treatment of those items of income, except to the extent they relinquish control to this article.

Article 8. Shipping and Air Transport

The proposed treaty provides that income which a resident of one country derives from the operation of ships in international traffic will be exempt from tax in the other country but only if the ship or aircraft is registered in the country of residence. This exemption also applies to the sale or other disposition of such ships.

The proposed treaty also provides that income which a resident of one country derives from the operation of aircraft in international traffic will be exempt from tax in the other country. However, the aircraft must be registered in one of the two countries or in a third country which has a treaty with the other country that also exempts such income from the operation of aircraft. The treaty also exempts income from the sale or other disposition of such aircraft.

The exemption for income from aircraft is somewhat broader than that provided in some U.S. tax treaties under which air transport income of a resident of one country is exempt by the other country only if the aircraft are registered in the country in which the taxpayer is a resident. However, the shipping and air transport provision is narrower than other recent treaties and the U.S. model which provide that a resident is exempt at source regardless of where the ship or aircraft is registered.

Article 9. Related Persons

The proposed treaty provides that, if a resident of one country is related to a resident of the other country and the two parties make arrangements or impose conditions between themselves which are different from those which would be made between independent persons, then both countries can disregard these arrangements or conditions in imposing their tax on either or both parties. Specifically, the treaty provides that any income, deduction, credit, or allowance which would, but for those arrangements or conditions, have been taken into account in computing the income (or loss) of either party or their taxes payable may actually be taken into account in computing their taxable income or their taxes payable.

A person is related to another person if either person directly or indirectly owns or controls the other, or if any third person or persons directly or indirectly own or control both parties. For this purpose, the term "control" includes any kind of control, whether or not legally enforceable, and however exercised or exercisable. Thus, the treaty does not in any way limit the authority of the Internal Revenue Service to allocate or apportion income, deductions, credits, or allowances between related parties under section 482 of the Internal Revenue Code in situations where it determines that the allocation is necessary in order to prevent the evasion of taxes or clearly to reflect the income of the related parties.

Article 10. Dividends

The United States imposes a 30-percent tax on the gross amount of U.S. source dividends paid to nonresident alien individuals and foreign corporations. The 30-percent tax does not apply if the foreign recipient is engaged in a trade or business in the United States and the dividends are effectively connected with that trade or business. U.S. source dividends are dividends paid by a U.S. corporation, and dividends paid by a foreign corporation if at least 50 percent of the gross income of the corporation, in the prior three year period, was effectively connected with a U.S. trade or business of that foreign corporation. The treaty reduces this tax, and also Canadian tax on dividend income.

Under the proposed treaty, each country may tax dividends paid by its corporations to shareholders resident in the other country (i.e., they may impose a dividend withholding tax on shareholders resident in the other country), but the rate of tax may not exceed 15 percent. (In the absence of a treaty limitation, the statutory U.S. withholding tax rate on dividends paid by U.S. corporations to foreign shareholders is 30 percent.) The withholding tax rate is limited to 10 percent in the case of dividends paid to a corporation which owns at least 10 percent of the voting stock of the corporation making the dividend distribution. However, the 10 percent ownership interest in the paying corporation must have been held by the recipient corporation for the entire part of the current taxable year preceding the date of the dividend payment and for the entire preceding taxable year. Moreover, for the prior taxable year the paying corporation may not have had more than 25 percent of its gross income from dividends or interest (except interest from a banking, financing, or insurance business, or dividends or interest from a 50 percent or more owned subsidiary on the date the dividend or interest is received).

The reduced rates of tax on dividends will apply unless the recipient has a permanent establishment in the source country and the shares of stock are effectively connected with the permanent establishment. If the shares of stock are effectively connected with a permanent establishment, the dividends are to be taxed under the business profits provisions (Article 7). This treatment of dividends generally conforms to that provided by the Internal Revenue Code, other recent U.S. income tax treaties, and the OECD model tax treaty.

Dividends paid by a resident of one country to a person who is not a resident of the other country will be exempt from tax in the other country. (This rule does not apply to dividends paid by Moroccan corporations to U.S. citizens who are not residents of the United States.) However, this exemption will not apply if the recipient has a permanent establishment in the other country and the stock with respect to which the dividends were paid is effectively connected with that permanent establishment. Thus, if a Moroccan corporation pays a dividend to a Mexican corporation, the United States could not impose a tax on the dividend unless the Mexican corporation had a permanent establishment in the United States with which the stock on which the dividend was paid was effectively connected and the dividend was otherwise taxable under the provisions of the Internal Revenue Code.

This rule prevents the United States from imposing its so-called second withholding tax on dividends paid by Moroccan corporations.. Under the Internal Revenue Code if in the three preceding taxable years more than 50 percent of the Moroccan corporation's gross income had been effectively connected with the conduct of a trade or business in the United States than that proportion of the dividend would have been subject to the 30 percent U.S. withholding tax.

Article 11. Interest

The U.S. imposes a 30-percent tax on U.S. source interest paid to foreign persons under the same rules that are applicable to dividends. Under the Code, U.S. source interest generally is interest on debt obligations of U.S. persons, but not interest on deposits in banks. U.S. source interest also includes interest paid by a foreign corporation if at least 50 percent of the gross income of the foreign corporation, in the prior three year period, was effectively connected with a U.S. trade or business of that corporation.

Under the proposed treaty, interest may be taxed by a country if the recipient is a resident of that country or if the interest arose in that country. The proposed treaty limits the withholding tax to 15 percent generally and exempts interest payments to governments or exempt governmental organizations of the other country. (In the absence of a treaty limitation, the United States generally imposes a 30-percent withholding tax on interest paid by U.S. debtors to foreign lenders other than on bank deposits.)

The reduction in the withholding tax will not apply if the recipient has a permament establishment in the source country and the indebtedness on which the interest is paid is effectively connected with the permanent establishment or fixed base. In that event, the interest will be taxed by the source country as business profits (Article 7).

The proposed treaty defines interest as income from government securities, bonds or debentures, and debt claims of every kind, whether or not secured by a mortgage and whether or not carrying a right to participate in profits. It also includes income which is assimilated to interest by the tax law of the country in which the interest had its source. The impact of this provision on U.S. domestic rules (section 385) for distinguishing between debt and equity is made clear. The provision is intended to permit the United States to apply its rules with the competent authorities settling disputes if this causes double taxation.

The proposed treaty also addresses the issue of non-arm's-length interest charges between related parties (or parties having an otherwise special relationship) by holding that the amount of interest for purposes of the treaty will be the amount of arm's-length interest. The amount of interest in excess of the arm's length interest will be taxable according to the laws of each country, taking into account the other provisions of this treaty (e.g., excess interest paid to a parent corporation may be treated as a dividend under local law and, thus entitled to the benefits of Article 10 of this treaty).

Article 12. Royalties

Under the same system that applies to dividends and interest, the U.S. imposes a 30-percent tax on all U.S. source royalties paid to foreign persons. Royalties are from U.S. sources if they are from property located in the United States including royalties for the use of or, including moving picture royalties, the right to use intangibles in the United States.

Under the proposed treaty, royalties that arise in one country and are paid to a resident of the other country may be taxed by both countries. However, the withholding tax imposed in the source country may not exceed 10 percent on the gross royalty. (In the absence of a treaty limitation, the United States generally imposes a 30-percent withholding tax on all U.S. source royalties paid to foreigners not engaged in a U.S. trade or business.) Royalties are payments of any kind made as consideration for the use of, or for the right to use, copyrights of literary, artistic, scientific works, copyrights of motion picture films or films or tapes used for radio or television broadcasting, patents, designs or models, plans, secret processes or formulae, trademarks, or other similar property rights, or knowledge, experience, or skill (know-how).

The term also includes the performance of accessory technical assistance for the use of such property or rights to the extent that the assistance is performed in the country where the payment for the property or right has its source. Gain derived from the sale or other disposition of royalty property or rights is considered royalty income to the extent that the amounts realized on the sale or other disposition are contingent on the productivity, use, or disposition of the property or rights. Finally, renumeration for technical and economic studies paid for out of public funds of the Moroccan Government in the discharge of functions of a governmental nature by the Moroccan Government or a political subdivision or a local authority thereof is also royalty income under the proposed treaty.

The reduced withholding tax rate or exemption does not apply where the recipient is an enterprise with a permanent establishment in the source country and the property or rights giving rise to the royalty is effectively connected with the permanent establishment. In that event the royalty will be taxed as business profits (Article 7).

The proposed treaty provides that in the case of royalty payments between related parties or persons otherwise having a special relationship, only that portion of the payment that represents an arm's-length royalty will be treated as a royalty under the treaty. Payments in excess of the arm's-length amount will be taxable according to the law of each country with due regard being given for the other provisions of this treaty.

Article 13. Capital Gains

The proposed treaty generally provides that capital gains derived by a resident of one country will be exempt from tax by the other country. Under the Code, capital gains derived from U.S. sources by foreign investors are generally exempt from U.S. tax unless the gain is effectively connected with the conduct of a trade or business in the United States or, in the case of a nonresident alien, he is present in the United States for more than 183 days during the taxable year.

The exemption does not apply where a resident of one country sells or exchanges real property or stock of a company (including interests in a real property cooperative) whose assets consist principally of real property located in the other country. Accordingly, the treaty would permit the United States to continue to tax the disposition of a U.S. real property interest in a corporation as if the treaty did not come into effect.

The exemption also does not apply where a resident of one country sells or exchanges property which is effectively connected with a permanent establishment or a fixed base (in the case of an individual) located in the other country. Finally, the exemption does not apply if an individual is a resident of one country and is present in the other country for at least 183 days during the taxable year.

Gain from the sale of property which is effectively connected with a permanent establishment in the other country is to be taxed in accordance with the provisions of Article 7 (Business Profits).

Article 14. 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 (the source country) by a resident of the other country is exempt from tax in the source country, unless (1) the person performing the personal service is present in the source country for 183 or more days during the taxable year, or (2) the individual has a fixed base in that country for a period of 90 days or more during the taxable year, or (3) the gross amount of the compensation exceeds $5,000 for the taxable year. In the second situation, the source country can only tax that portion of the individual's income which is attributable to the fixed base. Independent services means all activities (other than commercial, industrial, or agricultural activities) independently carried on by a person for his own account, where he receives the proceeds or bears the loss arising from these activities.

Article 15. Dependent Personal Services

Under the proposed treaty, a person who performs services as an employee in one country (the source country) and who is a resident of the other country may be taxed by both countries. However, income from such services (other than as a member of a board of directors) will not be taxable in the source country if three requirements are met: (1) the individual is present in the source country for less than 183 days during the taxable year; (2) his employer is a resident of the other country or is a permanent establishment maintained in that country by a nonresident of that country; and (3) the compensation is not borne by a permanent establishment of the employer in the source country.

Compensation 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 compensation is in respect of employment as a member of the regular complement of the ship or aircraft.

Article 16. Entertainers and Athletes

The proposed treaty contains a separate set of rules which govern the taxation of income earned by professional entertainers (such as theater, film, radio or television performers and musicians) and athletes. The proposed treaty provides that, notwithstanding the other provisions dealing with the taxation of personal services (Articles 14 and 15), entertainers or athletes may be taxed on the income from their personal services by the country in which the services are performed. However, this provision does not apply to income from services performed in one country by a non-profit organization (or its employees, unless acting for their own account) which is a resident of the other country. As in the case of the other provisions dealing with personal services income, this provision does not bar the country of residence or citizenship from also taxing that income (subject to a foreign credit).

In addition, the proposed treaty provides that where income in respect of personal services performed by an entertainer or athlete is paid not to the entertainer or athlete but rather to another person or entity, that income may be taxable by the country in which the services are performed. (This provision applies notwithstanding Articles 7, 14, and 15.) This provision prevents highly paid performers and athletes from avoiding tax in the country in which they perform by routing the compensation for their services through a third person such as a personal holding company.

Article 17. Government Functions

Under the proposed treaty, compensation paid out of public funds by one country, its political subdivisions or local authorities, to a citizen of that country for labor or personal services performed for the paying governmental entity in the discharge of governmental functions is exempt from tax by the other country. Governmental pensions and other similar benefits are included in the types of compensation covered by this provision.

Article 18. Students and Trainees

Under the proposed treaty, an individual who is a resident of one treaty country and who becomes temporarily present in the other country, for the primary purpose of (i) studying at a university or other recognized educational institution in that country, (ii) securing training required to qualify him to practice a profession or professional speciality, or (iii) studying or doing research as a recipient of a grant, allowance, or award from a governmental, religious, charitable, scientific, literary, or educational organization, is eligible for the student exemption. Persons eligible for the student exemption will be exempt from tax in the host country on gifts from abroad used for maintenance, education, study, research or training and on any grant, allowance or award described in (iii). In addition, a $2,000 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. However, the exemptions apply only for a period of 5 years.

Article 19. Private Pensions and Annuities

Under the proposed treaty, pensions (and other similar remuneration) paid to residents of either country are subject to tax only in the recipient's country of residence. This rule does not apply in the case of pensions which are subject to the provisions covering government service (Article 17). As used on this article, the term "pensions and other similar remuneration" means periodic payments which are made after retirement or death and which are made in consideration of services rendered or as compensation for injuries received in connection with past employment.

The proposed treaty also provides that annuities and alimony will only be taxed in the recipient's country of residence. Annuities are defined as a stated sum paid periodically at stated times during life or during a specified number of years, under an obligation to make the payments in return for adequate and full consideration (other than services rendered). Alimony is defined as periodic payments which are made pursuant to a decree of divorce, separate maintenance agreement, or support or separation agreement, and which are subject to tax in the recipient's country of residence.

Article 20. General Rules and Taxation

The proposed treaty contains the basic general rules of taxation which are found in many U.S. income tax treaties. A resident of one country may be taxed by the other country only on income from sources within that other country (subject to any limitations contained in the treaty). For this purpose, the source rules of Article 5 are to be applied. The proposed treaty also contains the customary rule that it may not be applied to increase the tax burden imposed on residents 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.

The proposed treaty contains the "saving clause" contained in all U.S. income tax treaties which provides, with specified exceptions, that the treaty is not to affect a country's taxation of its citizens and residents. Exceptions to the saving clause are provided for the benefits conferred by the articles dealing with relief from double taxation (Article

21), nondiscrimination (Article 22), and the mutual agreement procedure (Article 25). Thus, the benefits of those articles will be conferred by each country on its own citizens and residents as well as the residents of the other country. In addition, the benefits conferred by the articles dealing with the taxation of income from governmental functions (Article 17), and the income of students and trainees (Article 18) are to be provided by each country to its residents provided those residents are neither citizens of, nor have immigrant status in, that country.

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 corporations. Under the proposed treaty, a Moroccan corporation will be exempt from the personal holding company tax if at all times during the taxable year all of its stock is owned by individuals who are residents of Morocco. In addition, a Moroccan 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 a Moroccan 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)).

The proposed treaty also has a rule regarding income arising in one country which, under the treaty, is exempt from tax (or subject to a reduced treaty rate) in that country and which is not subject to tax in the other country until it is remitted. The proposed treaty provides that in such situations the income is only relieved from tax under the treaty to the extent that the income is remitted to the other country.

Article 21. Relief From Double Taxation

Under the proposed treaty, each country agrees to allow a foreign tax credit for the appropriate amount of income taxes paid to the other country. The amount of the foreign tax credit allowed under the treaty for U.S. tax purposes will be based upon the amount of tax paid to Morocco but cannot exceed that portion of the taxpayer's U.S. tax which the taxpayer's net income from sources within Morocco bares to his entire net income for that year.

The credit allowed for U.S. tax purposes is in accordance with the provisions and subject to the limitations of U.S. law applicable to the year in question. Under present law, the United States only allows a credit for foreign income taxes (sec. 901 of the Internal Revenue Code), or foreign taxes imposed in lieu of income taxes (Code sec. 903), and the credit is limited to the amount of the pre-credit U.S. tax which is attributable to foreign source income (Code secs. 904 and 907).

The proposed treaty provides that a U.S. citizen or resident who receives income or dividends from Morocco may elect to treat any amount required to be invested in Moroccan equipment bonds (under Article 37 of the Royal Decree No. 1.010–65 of the 8th of Ramadan 1385 (December 31, 1965) containing the Finance Law for the year 1966) as a creditable foreign tax. However, the taxpayer must also agree that any repayment of the bonds by the Moroccan Government will be treated as a refund of Moroccan tax for the year of repayment.

It is understood that the repayment will be considered a refund of tax even if any limitations period provided under U.S. law has expired. In effect this provision can be reviewed as a loan from the U.S. government to Morocco with the taxpayer acting as the intermediary. Because of the per country limitation in this treaty, the taxpayer would have to have Moroccan income for this provision to have effect.

As stated above, the United States allows a credit for foreign income taxes or for foreign taxes imposed in lieu of income taxes. Under present law, principal amounts lent to the Moroccan government under a compulsory loan program would not qualify either as a foreign income tax or as a foreign tax imposed in lieu of an income tax.

Article 22. Nondiscrimination

Under the proposed treaty, neither country can discriminate against citizens of the other country by imposing more burdensome taxes on citizens of the other country than it imposes on its own citizens who are in the same circumstances. 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 civil status or family responsibilities which it grants to its own residents.

Similarly, neither country may tax a permanent establishment of an enterprise of the other country less favorably than it taxes its own enterprises carrying on the same activities. The nondiscrimination provision also applies to corporations of one country which are owned by residents of the other country. Thus, a U.S. corporation, part or all of whose capital is owned or controlled (either directly or indirectly) by residents of Morocco, will not be subject to any more burdensome taxation (or other requirement connected with taxes) than is a U.S. corporation which carries any similar activities and which is wholly owned or controlled by one or more U.S. residents.

The provision is not intended to override the right of the United States to tax foreign persons on their dispositions of a U.S. real property interest because the effect of the provisions imposing the tax is not discriminatory, nor is it intended to permit foreign corporations to claim the benefit of U.S. provisions intended to eliminate U.S. double tax, such as the dividends-received exclusion provided by section 243.

Article 23. Diplomatic and Consular Officers

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

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 which the proposed treaty provides for dividends, interest, royalties, and capital gains derived from the other country. At the present time, neither Morocco nor the United States grants to investment or holding companies the type of tax benefits with respect to dividends, interest, and royalties which would make this provision of the proposed treaty applicable. Thus, the provision will have effect only if Morocco or the United States should subsequently enact special tax measures granting preferential tax treatment to dividends, interest, and royalties received by an investment or holding company.

Article 25. Mutual Agreement Procedure

The proposed treaty contains the standard mutual agreement provision which authorizes the competent authority of Morocco and the United States to consult together to attempt to alleviate individual cases of double taxation or cases of taxation not in accordance with the proposed treaty.

Under the proposed article a resident or citizen of one country who considers that the action of the countries or any one of them will cause him to pay a tax not in accordance with the convention may present his case to the competent authority of the country of which he is a resident or citizen. The competent authority then makes a determination as to whether or not the claim has merit. If the claim does have merit, that competent authority endeavors to come to an agreement with the competent authority of the other country to limit the taxation which is not in accordance with the provisions of the treaty.

A second provision directs the competent authorities to resolve any difficulties or doubts arising as to the application of the convention. Specifically, they are authorized to agree as to the attribution of profits to a resident of one country and its permanent establishment in another country, the allocation of income, deductions or credits, the determination as to source of income, and a common meaning of terms.

The treaty authorizes the competent authorities to communicate with each other directly for purposes of reaching an agreement in the sense of the mutual agreement provision. It also authorizes them to meet together for an oral exchange of opinions. These provisions make clear that it is not necessary to go through normal diplomatic channels in order to discuss problems arising by the application of the convention and also removes any doubt as to problems which might arise by reason of the confidentiality rules of the United States or Morocco.

Article 26. Exchange of Information

This article forms the basis for cooperation between the two states to attempt to deal with avoidance or evasion of their respective taxes and to enable them to obtain information so that they can properly administer the convention. The proposed treaty provides for the exchange of information which is necessary to carry out the provisions of the proposed treaty or for the prevention of fraud or for the administration of statutory provisions concerning taxes to which the convention applies. The exchange is limited, however, to information that could be obtained under the laws and administrative practices of each of the countries with respect to its own taxes. The information exchanged may relate to tax compliance generally and not merely to avoidance or evasion of tax.

Information exchanged is to be treated as secret except that it may be disclosed to any person concerned with or made a part of a public record with respect to the assessment or collection, or litigation concerning, the taxes to which the treaty applies. It is not clear from the language of the proposed treaty that Congress, in the exercise of its oversight responsibilities could have access to the information. However, a country is not required to carry out administrative measures contrary to its law or administrative practice, to supply particulars not obtainable under its laws or in the normal course of administration, or to supply information that would disclose a trade secret or the disclosure of which would be contrary to public policy.

Article 27. Extension to Territories

The proposed treaty contains a provision similar to that found in some of our other income tax treaties by which the treaty may be extended to possessions or territories of either country which are not otherwise covered by the proposed treaty. This provision applies only to a possession or territory of a country if the country is responsible for the area's international relations and the area's imposed taxes are substantially similar to those covered by the treaty. The treaty may be extended pursuant to this provision either in its entirety, or with any necessary modifications. The extension is to be effected by a written notification given the other country and assented to in written communication, which notification and communication are then to be ratified by each of the two countries.

At any time after the entry into force of an extension under this provision is made, either country may terminate the extension on 6 months' prior notice through diplomatic channels.

Article 28. Entry into Force

The proposed treaty is subject to ratification in accordance with the applicable procedures of each country and the instruments of ratification will be exchanged as soon as possible at Washington, D.C. The treaty will enter into force when the instruments of ratification are exchanged. The treaty will apply to taxes due at the source for income payable or paid on and after the first day of the month following the exchange of instruments of ratification. With respect to all other taxes, the treaty will become effective for taxable years beginning on or after January 1 of the year in which the proposed treaty comes into force.

Article 29. 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 notice prior to June 30th of any calendar year through diplomatic channels. In the event of a termination of the treaty, the treaty will continue to apply to taxes due at the source on income payable or paid no later than December 31 of the year in which the termination occurred. The treaty will also continue to apply to other taxes imposed on income for taxable periods ending not later than December 31 of the year of termination.

Exchange of Notes

In notes exchanged at the time of the signing of the treaty, the United States offered assurances to Morocco that, when circumstances permitted, the United States would be prepared to resume discussions with a view to incorporating provisions into the treaty, whereby the United States would grant a "tax sparing" credit against the U.S. tax to citizens and residents of the United States deriving certain profits and interest payments that are exempt from Moroccan taxation.

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