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TAXATION CONVENTION AND PROTOCOL WITH THE GOVERNMENT OF SRI LANKA

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Mr. LUGAR, from the Committee on Foreign Relations, submitted the following

REPORT

[To accompany Treaty Docs. 99–10 and 108–9]

The Committee on Foreign Relations, to which was referred the Convention between the Government of the United States of America and the Government of the Democratic Socialist Republic of Sri Lanka for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed at Colombo on March 14, 1985, and the Protocol amending the Convention, together with an Exchange of Notes, signed at Washington on September 20, 2002, having considered the same, reports favorably thereon and recommends that the Senate give its advice and consent to ratification thereof, as set forth in this report and the accompanying resolution of ratification.

CONTENTS

		Page
I.	Purpose	1
II.	Background	2
III.	Summary	2
IV.	Entry Into Force and Termination	3
V.	Committee Action	4
VI.	Committee Comments	4
VII.	Budget Impact	13
VIII.	Explanation of Proposed Treaty	13
IX.	Resolution of Ratification	13

I. PURPOSE

The principal purposes of the proposed income tax treaty between the United States and Sri Lanka are to reduce or eliminate double taxation of income earned by residents of either country

from sources within the other country and to prevent avoidance or evasion of the taxes of the two countries. The proposed treaty also is intended to continue to promote close economic cooperation between the two countries and to eliminate possible barriers to trade and investment caused by overlapping taxing jurisdictions of the two countries.

II. BACKGROUND

The proposed treaty between the United States and Sri Lanka was signed at Colombo on March 14, 1985 but has not entered into force. The proposed treaty was not acted on by the Senate at the time because changes made to U.S. international tax rules by the Tax Reform Act of 1986 necessitated some modifications to the agreement. The proposed protocol to amend that treaty was signed at Washington on September 20, 2002. The United States and Sri Lanka exchanged notes on the same day to provide clarification with respect to the application of the proposed treaty. Unless otherwise specified, the proposed treaty, the proposed protocol, and the notes are hereinafter referred to collectively as the "proposed treaty."

The Convention was sent to the Senate for advice and consent to its ratification on October 2, 1985 (*see* Treaty Doc. 99–10). The proposed protocol was sent to the Senate for advice and consent to its ratification on October 28, 2003 (*see* Treaty Doc. 108–9). The Committee on Foreign Relations held a public hearing on the proposed treaty on February 25, 2004.

III. SUMMARY

The proposed treaty is similar to other recent U.S. income tax treaties, the 1996 U.S. model income tax treaty ("U.S. model"), the 1992 model income tax treaty of the Organization for Economic Cooperation and Development, as updated ("OECD model"), and the 1980 United Nations Model Double Taxation Convention Between Developed and Developing Countries, as amended in 2001 ("U.N. model"). However, the proposed treaty contains certain substantive deviations from these treaties and models.

As in other U.S. tax treaties, the purposes of the treaty principally are achieved through each country's agreement to limit, in certain specified situations, its right to tax income derived from its territory by residents of the other country. For example, the proposed treaty contains provisions under which each country generally agrees not to tax business income derived from sources within that country by residents of the other country unless the business activities in the taxing country are substantial enough to constitute a permanent establishment (Article 7). Similarly, the proposed treaty contains "commercial visitor" exemptions under which residents of one country performing personal services in the other country will not be required to pay tax in the other country unless their contact with the other country exceeds specified minimums (Articles 15, 16, and 18). The proposed treaty provides that dividends, interest, royalties, and certain capital gains derived by a resident of either country from sources within the other country generally may be taxed by both countries (Articles 10, 11, 12, and

13); however, the rate of tax that the source country may impose on a resident of the other country on dividends, interest, and royalties may be limited or eliminated by the proposed treaty (Articles 10, 11, and 12).

In situations in which the country of source retains the right under the proposed treaty to tax income derived by residents of the other country, the proposed treaty generally provides for relief from the potential double taxation through the allowance by the country of residence of a tax credit for certain foreign taxes paid to the other country (Article 24).

The proposed treaty contains the standard provision (the "saving clause") included in U.S. tax treaties pursuant to which each country retains the right to tax its residents and citizens as if the treaty had not come into effect (Article 1). In addition, the proposed treaty contains the standard provision providing that the treaty may not be applied to deny any taxpayer any benefits the taxpayer would be entitled to under the domestic law of a country or under any other agreement between the two countries (Article 1).

The proposed treaty also contains a detailed limitation-on-benefits provision to prevent the inappropriate use of the treaty by third-country residents (Article 23).

IV. Entry Into Force and Termination

A. ENTRY INTO FORCE

The proposed treaty will enter into force upon the exchange of instruments of ratification. With respect to each country, the proposed treaty will be effective with respect to taxes withheld at source for amounts paid or credited on or after the first day of the second month following the date on which the proposed treaty enters into force. With respect to other taxes, the proposed treaty will be effective for taxable periods beginning on or after the first day of January of the year in which the proposed treaty enters into force.

The Technical Explanation states that the provisions of Article 26 (Mutual Agreement Procedure) and Article 27 (Exchange of Information) of the proposed treaty will have effect from the date of entry into force of the proposed treaty, without regard to the taxable or chargeable period to which the matter relates.

B. TERMINATION

The proposed treaty will remain in force until terminated by either country. Either country may terminate the proposed treaty, after the expiration of a period of five years from the date of its entry into force, by giving six months prior written notice of termination to the other country through diplomatic channels. In such case, with respect to each country, a termination is effective with respect to taxes withheld at source for amounts paid or credited on or after the first day of January next following the expiration of the six-month notice period. With respect to other taxes, a termination is effective for taxable periods beginning on or after the first day of January next following the expiration of the six-month notice period.

V. Committee Action

The Committee on Foreign Relations held a public hearing on the proposed treaty with Sri Lanka on February 25, 2004. The hearing was chaired by Senator Lugar.[1] The committee considered the proposed treaty on March 4, 2004, and ordered the proposed treaty with Sri Lanka favorably reported by a vote of 19 in favor and 0 against. Ayes: Senators Lugar, Hagel, Chafee, Allen, Brownback, Enzi, Voinovich, Alexander, Coleman, Sununu, Biden, Sarbanes, Dodd, Kerry, Feingold, Boxer, Nelson, Rockefeller, and Corzine.

VI. Committee Comments

On balance, the Committee on Foreign Relations believes that the proposed treaty with Sri Lanka is in the interest of the United States and urges that the Senate act promptly to give advice and consent to ratification. The committee has taken note of certain issues raised by the proposed treaty and believes that the following comments may be useful to the Treasury Department officials in providing guidance on these matters should they arise in the course of future treaty negotiations.

A. STABILITY OF SRI LANKAN LAW

In the past, the Treasury Department has maintained that a country's political situation should be a factor in determining whether to build stronger economic ties with that country. As the Treasury Department explained in a letter to the Senate Foreign Relations Committee:

> A country's political situation is a factor that is considered in determining whether to build stronger economic ties with that country. When consideration of this and other factors leads to a policy of building stronger economic ties with a particular country, a tax treaty becomes a logical part of that policy. One of a treaty's main purposes is to foster the competitiveness of U.S. firms that enter the treaty partner's market place. As long as it is U.S. policy to encourage U.S. firms to compete in these market places, it is in the interest of the United States to enter tax treaties.
>
> Moreover, in countries where an unstable political climate may result in rapid and unforeseen changes in economic and fiscal policy, a tax treaty can be especially valuable to U.S. companies, as the tax treaty may restrain the government from taking actions that would adversely impact U.S. firms, and provide a forum to air grievances that otherwise would be unavailable.[2]

Background of Political Developments in Sri Lanka

The government of Sri Lanka is a constitutional democracy. For approximately the past 20 years, the country has experienced peri-

[1] The transcript of this hearing will be forthcoming as a separate committee print.

[2] Letter dated July 5, 1995 from the Department of the Treasury to the Senate Foreign Relations Committee, as quoted in the Report of the Senate Foreign Relations Committee on the Income Tax Convention with Ukraine, Exec. Rept. 104–5, August 10, 1995.

ods of significant conflict involving a separatist group that has been declared by the United States to be a terrorist organization. In recent years, the Norwegian government has facilitated a peace process designed to resolve this conflict. In November 2003, while the Sri Lankan prime minister was in Washington seeking support for the peace process, the Sri Lankan president removed three cabinet ministers, suspended parliament, and imposed martial law. In February 2004, the Sri Lankan president dissolved parliament and set April 2, 2004 for the next general election. The State Department has recently stated that Sri Lanka is currently experiencing a "domestic political crisis."[3]

Issues

Several issues arise in the consideration of a tax treaty with a government that is experiencing political instability. One issue is that it may be difficult to identify correctly the other country's competent authority in situations where there are competing claims as to who is authorized to exercise legislative, executive, or judicial authority. Another issue is the extent to which any political instability also causes uncertainty as to the precise nature of the substantive law of that country. These uncertainties may make it difficult to administer the treaty.

A more specific issue arises in the context of the exchange-of-information provisions of the proposed treaty (Article 27). The exchange-of-information provision requires that information that is exchanged shall be treated as secret by the receiving country in the same manner as information obtained under its local laws and may only be disclosed to persons involved in the assessment, collection, or administration of taxes covered by the provision. Several concerns may arise with respect to the utilization of this provision with a government that is experiencing political instability. First, it may be more difficult to assess whether confidentiality will be respected when the information is initially exchanged. Second, it may be more difficult to assess the possibility that inappropriate use will be made in the future of the exchanged information. Third, the country receiving the information could weaken (or potentially eliminate) the confidentiality protections under its local laws, which would concomitantly weaken or eliminate those protections for exchanged information. However, these issues involving exchange of information may be dealt with by the United States competent authority in administering the provisions of the proposed treaty.

Committee Conclusions

The committee has considered the political situation in Sri Lanka and its implications for the proposed treaty. The committee recognizes the benefits this treaty would provide to U.S. taxpayers and the positive effect the treaty could have on the Sri Lankan economic environment. On balance, the committee believes that it is appropriate to proceed with the consideration of this proposed treaty and recommends its ratification.

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[3] Press Statement by Adam Ereli, Deputy Spokesman, United States Department of State, Sri Lanka: Deputy Secretary Armitage's Meeting with Minister for Economic Reform, Science, And Technology Milinda Moragoda, December 29, 2003.

B. DEVELOPING COUNTRY CONCESSIONS

The proposed treaty contains a number of developing country concessions, some of which are found in other U.S. income tax treaties with developing countries. The most significant of these concessions are listed below.

Definition of Permanent Establishment

The proposed treaty departs from the U.S. model treaty by providing for relatively broad source-basis taxation. In particular, the proposed treaty's permanent establishment article permits the country in which business activities are performed to tax these activities in a broader range of circumstances than would be permitted under the U.S. model.

For example, under the proposed treaty, a building site, a construction or assembly project, or an installation or drilling rig or ship used for the exploration of natural resources constitutes a permanent establishment if such project, or activity relating to such installation, rig, or ship, as the case may be, continues for more than 183 days. The U.S. model uses a threshold of 12 months. The proposed treaty also provides that the furnishing of services (e.g., consulting services) by an enterprise through employees or other personnel engaged for such purpose constitutes a permanent establishment if the activity continues within the country for an aggregate of more than 183 days in any 12-month period. The U.S. model provides that these activities give rise to a permanent establishment only if conducted through a fixed place of business or by a dependent agent.

In addition, the proposed treaty provides that, except in the case of reinsurance, an insurance enterprise of one treaty country will be deemed to have a permanent establishment in the other treaty country if it collects premiums or insures risks situated in the other treaty country through a person other than an independent agent. The proposed treaty also provides that if the activities of an agent are devoted wholly or almost wholly on behalf of an enterprise, and the transactions between the enterprise and the agent do not conform to arm's-length conditions, then the agent may cause the enterprise to have a permanent establishment in the country in which the agent's activities are performed. In addition, the proposed treaty provides that if a dependent agent maintains in one treaty country a stock of goods or merchandise from which the agent regularly fills orders or makes deliveries on behalf of an enterprise of the other treaty country, and additional activities conducted in the source country on behalf of the enterprise have contributed to the conclusion of the sale of such goods or merchandise, then the enterprise is deemed to have a permanent establishment in the source country. These provisions all expand source-basis taxation beyond what is provided in the U.S. model.

Source Basis Taxation

Additional concessions to source basis taxation in the proposed treaty include a maximum rate of source country tax on dividends (15 percent) that is higher than that provided in the U.S. model treaty; and broader source country taxation of personal services in-

come (especially directors' fees) and income of artistes and athletes than that allowed by the U.S. model treaty.

Taxation of Business Profits

Unlike the U.S. model, the proposed treaty does not permit a permanent establishment to deduct payments that it makes to the head office, or any other office, of the enterprise that includes the permanent establishment if such payments constitute: (1) royalties, fees or other similar payments in return for the use of patents, know-how or other rights; (2) commissions or other charges for specific services performed or for management; or (3) interest on loans to the permanent establishment. Similarly, such payments made to the permanent establishment by the head office or other office of the enterprise that includes the permanent establishment are not taken into account in determining the taxable business profits of the permanent establishment.

Other Concessions to Source-Basis Taxation

In several instances, the proposed treaty allows higher rates of source-country tax than the U.S. model allows. The proposed treaty allows a maximum rate of source-country tax of 15 percent on dividends, which is consistent with the U.S. model, but it does not reduce this maximum rate to five percent in cases in which the shareholder owns at least 10 percent of the voting stock of the dividend-paying company, as the U.S. model does. The proposed treaty also allows source-country taxation of interest at a maximum rate of 10 percent, whereas the U.S. model generally does not permit source-country taxation of interest. Similarly, the proposed treaty allows source-country taxation of royalties at a maximum rate of 10 percent and certain equipment rentals at a maximum rate of five percent, whereas the U.S. model generally does not permit source-country taxation of such royalties and rental fees. The proposed treaty also allows the source country a non-exclusive right to tax "other income" (i.e., income not specifically dealt with in other provisions of the treaty), whereas the U.S. model provides for exclusive residence-based taxation of such income.

In addition, the proposed treaty permits source-country taxation of income derived by a resident of the other treaty country from the performance of independent personal services if the resident is present in the source country for a total of more than 183 days during any 12-month period, even if such income is not attributable to a fixed base or permanent establishment, as the U.S. model would require.

Grants

The proposed treaty includes a provision providing favorable treatment for grants received by a U.S. resident company from the government of Sri Lanka for purposes of investment promotion and economic development in Sri Lanka. The provision provides for the exclusion from income and from earnings and profits for U.S. tax purposes of a cash grant or similar payment by the government of Sri Lanka to a U.S. resident in respect of a wholly owned enterprise in Sri Lanka, or to a company resident in Sri Lanka that is wholly owned by a U.S. resident. No similar provision is found in

the U.S. model treaty, nor is any similar provision included in any U.S. bilateral tax treaty other than the U.S.-Israel treaty.

Issues

One purpose of the proposed treaty is to reduce tax barriers to direct investment by U.S. firms in Sri Lanka. The practical effect of the developing-country concessions could be greater Sri Lankan taxation (or less U.S. taxation) of activities of U.S. firms in Sri Lanka than would be the case under the rules of either the U.S. or OECD model treaties.

There is a risk that the inclusion of these developing country concessions in the proposed treaty could result in additional pressure on the United States to include them in future treaties negotiated with developing countries. However, these precedents already exist in the UN model treaty, and a number of existing U.S. income tax treaties with developing countries already include similar concessions. Such concessions arguably are necessary in order to obtain treaties with developing countries. Tax treaties with developing countries can be in the interest of the United States because they provide developing country tax relief for U.S. investors and a clearer framework within which the taxation of U.S. investors will take place.

Committee Conclusions

The committee is concerned that developing country concessions not be viewed as the starting point for future negotiations with developing countries. It must be clearly recognized that several of the rules of the proposed treaty represent substantial concessions by the United States, and that such concessions must be met with substantial concessions by the treaty partner. Thus, future negotiations with developing countries should not assume, for example, that the definition of permanent establishment provided in this treaty will necessarily be available in every case; rather, such a definition will be only adopted in the context of an agreement that satisfactorily addresses the concerns of the United States.

C. EDUCATION AND TRAINING

Under the proposed treaty, U.S. taxpayers who are visiting Sri Lanka and individuals who immediately prior to visiting the United States were resident in Sri Lanka will be exempt from income tax in the host country on certain payments received if the purpose of their visit is to engage in full-time education or to engage in full-time training. The exempt payments are limited to those payments the individual may receive for his or her maintenance, education or training as long as such payments are from sources outside the host country. In the case of an individual engaged primarily in training or education, but who is an employee of a person resident in his or her home country or who is participating in a program of the government of the host country or of an international organization, a different exemption applies. Such an individual is exempt from host country tax on up to $6,000 of personal service income. The exemption from income tax in the host country applies only for a period of one year or less.

Issues

Full-time students and persons engaged in full-time training

The proposed treaty generally has the effect of exempting payments received for the maintenance, education, and training of full-time students and persons engaged in full-time training as a visitor from the United States to Sri Lanka or as a visitor from Sri Lanka to the United States from the income tax of both the United States and Sri Lanka. This conforms to the U.S. model with respect to students and generally conforms to the OECD model provisions with respect to students and trainees.

This provision generally would have the effect of reducing the cost of such education and training received by visitors. This may encourage individuals in both countries to consider study abroad in the other country. Such cross-border visits by students and trainees may foster the advancement of knowledge and redound to the benefit of residents of both countries.

The proposed treaty applies a different standard when the visiting individual is an employee of a person in his or her home country or participates in a program sponsored by the government of the host country or of an international organization. For such an individual, exemption is not provided for payments from outside the host country for maintenance, education, and training; rather, such an individual may exempt, for the period of one year, up to $6,000 in personal services income from tax in the host country. In this regard the proposed treaty departs from the U.S. and OECD model treaties. The U.S. model limits exemptions for payments of maintenance, education, and training for one year in the case of business trainees but does not provide any exemption related to personal services income. The OECD model does not limit the duration of exemption for payments for maintenance, education, and training for business trainees and does not provide any exemption related to personal services income.

Depending upon the costs of maintenance, education, and training, the dollar value of the exemption to non-employee visitors may be greater than the dollar value of the exemption for employee (or program participant) visitors. By potentially subjecting such payments for maintenance, education, and training as well as all personal services income received to host country income tax in the case of visits by employees or program participants engaged in visits of greater than one year in duration, the cost for such cross-border visitors of engaging in education or training programs of longer duration would be increased. It could be argued that the training or education of an employee relates primarily to specific job skills of value to the individual or the individual's employer rather than enhancing general knowledge and cross-border understanding, as may be the case in the education or training of a non-employee visitor. This could provide a rationale for providing more open-ended treaty benefits in the case of non-employee students and trainees as opposed to employees. However, if employment provides the underlying rationale for disparate treaty benefits, it may be questioned as to why training requiring one year or less is preferred to training that requires a longer visit to the host country. As such, the proposed treaty would favor certain types of training arrange-

ments over others. Further, if employment provides the underlying rationale for disparate treaty benefits, why participants in a host country or international organization sponsored program of education or training would be treated like employees is less easily discerned.

Teachers and professors

The proposed treaty is consistent with the U.S. model in which no such exemption would be provided for the remuneration of visiting teachers, professors, or academic researchers. While this is the position of the U.S. model, an exemption for visiting teachers and professors has been included in many bilateral tax treaties. Of the more than 50 bilateral income tax treaties in force, 30 include provisions exempting from host country taxation the income of a visiting individual engaged in teaching or research at an educational institution, and an additional 10 treaties provide a more limited exemption from taxation in the host county for a visiting individual engaged in research. Four of the most recently ratified income tax treaties and the proposed treaty with Japan include such a provision.

The effect of such exemptions for the remuneration of visiting teachers, professors, and academic researchers generally is to make such cross-border visits more attractive financially. Increasing the financial reward may serve to encourage cross-border visits by academics. Such cross-border visits by academics for teaching and research may foster the advancement of knowledge and redound to the benefit of residents of both countries. On the other hand, such an exemption from income tax may be seen as unfair when compared to persons engaged in other occupations whose occupation or employment may cause them to relocate temporarily abroad. Such exemptions for remuneration of teachers, professors, and academic researchers could be said to violate the principle of horizontal equity by treating otherwise similarly economically situated taxpayers differently.

Committee Conclusions

The committee notes that the special rules for certain students and trainees differ from the U.S. and OECD model treaties. The committee also notes that while the treatment of visiting teachers and professors under the proposed treaty is consistent with the U.S. model, it is inconsistent with other U.S. tax treaties in force.[4] The committee encourages the Treasury Department to develop criteria for determining under what circumstances the inclusion of these special provisions is appropriate and to consult with the committee regarding these criteria.

[4] The treaties with Italy, Slovenia, and Venezuela, each considered in 1999, the treaty with the United Kingdom, considered in 2003, and the proposed treaty with Japan contain provisions exempting the remuneration of visiting teachers and professors from host country income taxation. The treaties with Denmark, Estonia, Latvia, and Lithuania, also considered in 1999, did not contain such an exemption, but did contain a more limited exemption for visiting researchers. The protocols with Australia and Mexico, ratified in 2003, did not include such exemptions.

D. DISCLOSURE OF INFORMATION IN CONNECTION WITH OVERSIGHT OF THE TAX SYSTEM

The proposed treaty provides that the two competent authorities will exchange such information as is necessary to carry out the provisions of the proposed treaty or of the domestic laws of the two countries concerning all national taxes insofar as the taxation thereunder is not contrary to the proposed treaty, as well as to prevent fiscal evasion. Any information exchanged under the proposed treaty is treated as secret in the same manner as information obtained under the domestic laws of the country receiving the information.

The exchanged information may be disclosed only to persons or authorities (including courts and administrative bodies) involved in the assessment, collection, or administration of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes to which the proposed treaty applies. Such persons or authorities must use the information for such purposes only. Exchanged information may be disclosed in public court proceedings or in judicial decisions.

Unlike the U.S. model and unlike virtually all recent U.S. tax treaties, the proposed treaty does not include a specific reference to disclosure of exchanged information to persons or authorities engaged in the oversight of the tax system (e.g., the tax-writing committees of Congress and the General Accounting Office). This lacuna could present a serious impediment to legislative branch oversight of the operation of the proposed treaty. The Treasury Department explained this omission as follows:

> The matter of access of information in connection with oversight by the GAO and certain Congressional committees was discussed during the course of the negotiations, and it was agreed with Sri Lanka that the language included in the provision allowed the necessary disclosures. Therefore, a specific reference to oversight was not considered necessary. Nevertheless, an outstanding clarifying this issue might be helpful in order to eliminate any doubt.[5]

Committee Conclusions

The committee proposes an understanding as part of the resolution of ratification to make clear that information exchanged under the treaty may be disclosed to appropriate congressional committees and the General Accounting Office. Although the negotiating history of the treaty indicates that this issue was discussed in the negotiations and that Sri Lanka agreed that Article 27 permitted such disclosure, the committee believes it useful to add this understanding in order to ensure that there is no doubt on this matter. The committee has not defined the term "appropriate congressional committees." The committee intends that it be given a broad reading and apply to any committees that, under applicable U.S. law or regulation, are authorized to have access to tax information in

[5] Testimony of Barbara M. Angus, International Tax Counsel, United States Department of the Treasury, before the Senate Committee on Foreign Relations on Pending Income Tax Agreements, February 25, 2004.

connection with their role in overseeing the administration of U.S. tax law.

E. U.S. MODEL TAX TREATY DIVERGENCE

It has been longstanding practice for the Treasury Department to maintain, and update as necessary, a model income tax treaty that reflects the current policies of the United States pertaining to income tax treaties. The current U.S. policies on income tax treaties are contained in the U.S. model. Some of the purposes of the U.S. model are explained by the Treasury Department in its Technical Explanation of the U.S. model:

> [T]he Model is not intended to represent an ideal United States income tax treaty. Rather, a principal function of the Model is to facilitate negotiations by helping the negotiators identify differences between income tax policies in the two countries. In this regard, the Model can be especially valuable with respect to the many countries that are conversant with the OECD Model. . . . Another purpose of the Model and the Technical Explanation is to provide a basic explanation of U.S. treaty policy for all interested parties, regardless of whether they are prospective treaty partners.

U.S. model tax treaties provide a framework for U.S. treaty policy. These models provide helpful information to taxpayers, the Congress, and foreign governments as to U.S. policies on often complicated treaty matters. For purposes of clarity and transparency in this area, the U.S. model tax treaties should reflect the most current positions on U.S. treaty policy. Periodically updating the U.S. model tax treaties to reflect changes, revisions, developments, and the viewpoints of Congress with regard to U.S. treaty policy would ensure that the model treaties remain meaningful and relevant.

With assistance from the staff of the Joint Committee on Taxation, the Senate Committee on Foreign Relations reviews tax treaties negotiated and signed by the Treasury Department before advice and consent to ratification by the full Senate is considered. The U.S. model is important as part of this review process because it helps the Senate determine the Administration's most recent treaty policy and understand the reasons for diverging from the U.S. model in a particular tax treaty. To the extent that a particular tax treaty adheres to the U.S. model, transparency of the policies encompassed in the tax treaty is increased and the risk of technical flaws and unintended consequences resulting from the tax treaty is reduced.

Committee Conclusions

The committee recognizes that tax treaties often diverge from the U.S. model due to, among other things, the unique characteristics of the legal and tax systems of treaty partners, the outcome of negotiations with treaty partners, and recent developments in U.S. treaty policy. However, even without taking into account the central features of tax treaties that predictably diverge from the U.S. model (e.g., withholding rates, limitation on benefits), the technical provisions of recent U.S. tax treaties have diverged substantively

from the U.S. model with increasing frequency. The proposed treaty continues this apparent pattern, which may be indicative of a growing obsolescence of the U.S. model. The important purposes served by the U.S. model tax treaty are undermined if that model does not accurately reflect current U.S. positions and the committee notes with approval the intention of the Treasury Department to update the U.S. model treaty and strongly encourages the Treasury Department to complete the update in the coming year.[6] In the process of revising the U.S. model, the committee expects the Treasury Department to consult with the committee generally, and specifically regarding the potential implications for U.S. trade and revenue of the policies and provisions reflected in the new model.

VII. Budget Impact

The committee has been informed by the staff of the Joint Committee on Taxation that the withholding tax changes and other provisions of the proposed treaty are estimated to cause a negligible change in Federal budget receipts during the fiscal year 2004-2013 budget period, based solely on the amount and type of historical income flows between Sri Lanka and the United States.

VIII. Explanation of Proposed Treaty

A detailed, article-by-article explanation of the proposed income tax treaty between the United States and Sri Lanka can be found in the pamphlet of the Joint Committee on Taxation entitled *Explanation of Proposed Income Tax Treaty Between the United States and Sri Lanka* (JCS-2–04), February 19, 2004.

IX. Resolution of Ratification

Resolved (two-thirds of the Senators present concurring therein), That the Senate advise and consent to the ratification of the Convention between the Government of the United States of America and the Government of the Democratic Socialist Republic of Sri Lanka for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed at Colombo on March 14, 1985 (Treaty Doc. 99–10), and the Protocol amending the Convention, together with an Exchange of Notes, signed at Washington on September 20, 2002 (Treaty Doc. 108–9), subject to the understanding that the authorities to which information may be disclosed under Article 27 include appropriate congressional committees and the General Accounting Office.

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[6] Testimony of Barbara M. Angus, International Tax Counsel, United States Department of the Treasury, before the Senate Committee on Foreign Relations on Pending Income Tax Agreements, February 25, 2004.