INTERNATIONAL TAXATION

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1 INTRODUCTION

1.1 International tax law

International tax law is about

- international public law
- sovereignty of States
- economic policy

1.2 States are sovereign

States decide freely on

- the tax system
- the taxable matter
- the taxable basis
- the tax rates
- the exemptions

Criteria most often used to “justify” taxation:

- citizenship (political nexus)
- residence (territorial nexus)
- source of income (territorial nexus)
- functions (sailors on a ship with national flag, international organizations, etc.)

1.3 Power to command: *imperium*

The sovereignty of a State is limited by the sovereignty of the others: a State can use its power to enforce its legislation within its territory only

- The choice of a tax system may depend on the efficiency of enforcement

1.4 Influence of international soft and hard laws

- at OECD level (soft law)
  - OECD model conventions; anti-BEPS recommendations
  - UN model convention
- At OECD level Multilateral Instrument is hard law for contracting states

2 INTERNATIONAL MULTIPLE TAXATION

2.1 Juridical double taxation

- same taxpayer must pay twice (in two different countries)
- taxes of the same nature
- on the same item of income

- Combination of criteria most often used to “justify” taxation:
  - citizenship, nationality, incorporation (political nexus)
  - residence, establishment (territorial nexus)
  - source of income (territorial nexus)
  - functions

Or :

- overlapping definitions of citizenship, nationality, incorporation
- overlapping definitions of residence, establishment
- overlapping definitions of source
- migration issues
- timing issues

2.2 Juridical double taxation # economic double taxation

UN and OECD Model are about juridical double taxation only (but for article 9 about transfer pricing

2.3 No *ne bis in idem* in international tax law

(sovereignty)

2.4 Remedy to double taxation depends on political choices

3 BASIC PRINCIPLES OF INTERNATIONAL TAXATION

3.1 INTERNATIONAL LAW IS NATIONAL

- Sovereignty determines whether a treaty is signed or terminated
- A treaty must be approved according to domestic legislation
- A treaty is applied by the authorities of each contracting States

3.2 GOALS OF DOUBLE TAX TREATIES

3.2.1 Remedy to double juridical taxation

to improve economic relationships and to enhance administrative cooperation in tax matters

See preamble to the 2017 OECD Model treaty after BEPS actions

3.2.1.1 Juridical double taxation defined

- Same taxpayer
- Same income
- Same type of tax

3.2.1.2 Mechanism – limitation on the sovereignty

Contracting States commit not to apply their legislation beyond the provisions of the treaty

- "Distributive rules" (art. 6 to 22)
  - A country may in principle tax its residents on any kind of income (read art. 21)
  - However, the source country may also tax income if the nexus with its territory is enough
    - Definition of "source"
      - Where the land or building is situated (art. 6)
      - Where an enterprise maintains a permanent establishment (art. 7)
      - Where the interest "arises" (art. 11)
      - Where the employment is exercised + additional criteria (art. 15)
      - …

- Source taxation :
  - Unlimited power to tax (art. 6, 7, 9,13.5,, etc)
  - limited power to tax (art. 10 and 11)

- "Remedy to double taxation" (art. 23)

  If both the residence country and the source country may tax the same income under the distributive rule, the residence country must remedy double taxation

  Art. 23 applies to the residence country only

  - Exemption method
  - Credit method

  See appendix

- The mechanism works only if a taxpayer has one residence (for treaty purposes)
  - See below art. 4 : tie-breaker rules

- BEPS: emphasizes on art. 23A(4):
  The provisions of paragraph 1 shall not apply to income derived or capital owned by a resident of a Contracting State where the other Contracting State applies the provisions of this Convention to exempt such income or capital from tax or applies the provisions of paragraph 2 of Article 10 or 11 to such income.

3.2.2 Remedy to economic double taxation

- Art. 9(2)

- Comp. art.7(3) about juridical double taxation

- Transfer Pricing issues (pricing dealings between affiliated enterprises)

- Mutual agreement procedure ("MAP") - Arbitration (art. 25)
  - Reasoned arbitration
  - Base-ball procedure

3.2.3 Remedy to the territorial limitation on enforcement

- Exchange of information (art. 26)
- Assistance in the collection of taxes (art. 27)
- Prevention of tax evasion and avoidance
  - See the title of the OCDE Model and the preamble of the OECD (2017) Model

3.2.4 Non-discrimination

- art. 24: no discrimination based on citizenship (v. residence)

Appendix

A taxpayer earns 200 in country A where the tax rate is 50 %

Total income	200
Taxable basis	200
Tax	100

The same taxpayer earns 100 in country A and country B where the tax rate is 30% (in the absence of tax treaty)

		Country A	Country B
Total income	200	100	100
Taxable basis		200	100
Tax	130	100	30

CREDIT METHOD

Country A remedies double taxation using the credit method

		Country A	Country B
Total income	200	100	100
Taxable basis		200	100
Tax		100	
		-30	30
	100	70	

The taxpayer pays the same aggregate amount of taxes as if it earned 200 in A

If country B taxes at the rate of 60%

		Country A	Country B
Total income	200	100	100
Taxable basis		200	100
Tax		100	
		-50	60
	110	50	

Country A limits the credit to the amount of tax that it levies on the foreign income (no subsidy available to foreign operations or investments)

If country B is a tax heaven

		Country A	Country B
Total income	200	100	100
Taxable basis		200	100
Tax		100	
		-0	0
	100	100	

Country A discourages the use of low-tax jurisdictions

EXEMPTION METHOD

Country A remedies double taxation by using the exemption method. The taxpayer bears the same tax burden on its income from B as the competitors in B

		Country A	Country B
Total income	200	100	100
Taxable basis		200	100
		-100	
		100	
Tax	80	50	30

Country B is a tax heaven

		Country A	Country B
Total income	200	100	100
Taxable basis		200	100
		-100	
		100	
Tax	50	50	0

The taxpayer is left in the same situation as its competitors in the source country

3.3 GOVERNING PRINCIPLES

3.3.1 Priority rules

- *Pacta sunt servanda*
  Art. 26 of the Convention of Vienna (23 May 1969) on the laws of Treaties
  USA signed in 1970 but never ratified the Convention of Vienna and use the *later in time rule* (possible treaty override)
  France never signed the Vienna Convention but included the rule in its Constitutional law

- Taxpayer may use the treaty protection if its rules have *direct effect*
  Sufficiently precise rules grant taxpayers a right to dispute the application of domestic tax laws. The T/P exactly knows what he is entitled to.

3.3.2 Tax treaties limit the application of domestic tax legislation and do not create taxes

No need to apply a tax treaty if domestic legislation does not provide for taxation

3.3.3 Treaty application is not optional

Risk: double taxation that cannot be cured (procedural time limits to obtain a refund of the undue tax

3.3.4 The taxpayer may choose the treaty that is more favorable to him

3.3.5 The treaty may influence the treatment under domestic law, even when it acknowledges the contracting state's jurisdiction to tax

conflict of laws arbitration

3.3.6 Treaty definitions cannot be used to modify domestic law definitions

Example: resident for domestic law purposes / not a resident for treaty purposes

However, domestic definitions may be used to interpret treaty terms (art. 3(2))

3.3.7 The treaty does not determine the taxable basis

Power to tax an item of income # Calculation of the amount of taxable income

Art. 7 does not determine the net taxable basis although its rules the allocation of revenues and expenses

But: art. 24 may modify the domestic rules on the determination of the taxable basis

3.3.8 The treaty does not overrule the domestic procedure

Exchange of information: always the rules of the requested country (art. 26)

Comp. US FATCA

4 SCOPE OF DOUBLE TAX TREATIES

4.1 TAXES COVERED

General definition (art. 2(2))

Supplemented by a list (art. 2(3))

Future changes in domestic tax system (art. 2(4))

art. 24, 26, 27 : all types of taxes

"On behalf of the State, its political subdivisions"

Switzerland
USA, Brazil, Canada (only federal taxes)

4.2 TERRITORIAL SCOPE

4.2.1 Double taxation => generally no DTC with tax havens

4.2.2 Between States

No treaty with countries that are not recognized as States

4.2.3 Bilateral treaties

Multilateral treaties are seldom signed in tax matters

Even the multilateral convention of 1988 on the administrative assistance and the MLI (BEPS action) are designed to apply on a bilateral basis (match)

4.2.4 Territory of a contracting State

Territory in which the tax administration of the country applies the country's taxes

Including territorial sea

The sky ?

Usually regions with a special tax regime (tax holiday) are excluded

Svalbard in Norway

4.3 ENTRY INTO FORCE AND TERMINATION

- Negotiation

- Signature
- National procedure necessary to introduce the treaty into the effective legislation
  - Monist countries v. dualist countries
- Ratification (art. 30)
- Official publication by each country
- Entry into force
  - # effective date: date from which the income are covered
    - may be after the entry into force : as from January 1 of the year following …
    - may be retroactive : as from January 1 of the year following the signature
    - may apply to situations existing before the negotiations
- The treaty applies according to the situation of the taxpayer at the time he earns the income, not at the time he cashes the income
- Termination
  - Notice (art. 31)
  - Usually not terminated before a new treaty is signed
- Suspension
  - For the time another treaty applies

4.4 ENTITLEMENT TO TREATY BENEFIT

4.4.1 The rule: Taxpayer resident in one or both countries

Art. 1:

Person: art. 3 (broad: even a group of persons qualifies)

Resident: art. 4 (narrow)

Art.4:

- Refers to the rules of the contracting states

  Example: partnerships seen as transparent for domestic tax purposes are not "residents"

- Provided that residence is based on a territorial criterion

  US citizens are not residents in the meaning of the OECD Model

- Provided that the resident is taxed on its worldwide income

  Otherwise: no double taxation

  Offshore tax regimes (Hong Kong, France)

  Pension funds and charities: only if explicitly included

  Subject to tax although taxed on a lump sum taxable basis?

  Treaty exemptions do not result in an exclusion from the scope of another treaty

- The resident is also the beneficiary of the income

  The treaty generally refers to the situation where the beneficiary of the income is a resident of a contracting State

Art. 24, 26 and 27 apply to taxpayers that are not residents of contracting States

Art. 25: students who were residents before studying abroad.

Resident in one sole country: <u>Tie-breaker rules</u> art. 4(2) and 4(3)

BEPS: Dual resident companies : new tie-breaker rule in art. 4(3) OECD Model 2017.

4.4.2 BEPS: Limitation on benefits

=> art. 29 of the 2017 OECD Model:
- Ownership test
- Base erosion test
- Derivative benefit test
- Active conduct of business test
- Discretionary relief
- Principal purpose test

5 TREATY INTERPRETATION

5.1 Art. 3(2)

As regards the application of the Convention at any time **(5)** *by a Contracting State, any term* **(1)** *not defined therein* **(2)** *shall, unless the context otherwise requires* **(6)***, or the competent authorities agree to a different meaning pursuant to the provisions of Article 25, have the meaning that it has at that time* **(5)** *under the law of that State* **(3)** *for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State* **(4)***.*

"Any term" (1)

v "any mechanism"

Not defined in the treaty (2)

Defined by domestic law (3)

Tax laws prevail (4)

Ambulatory v. historical interpretation

At any time… at that time (5)

Treaty override

Unless the context otherwise requires (6)

5.2 Vienna convention

- Bilateral (ex. Canada, *Prevost Cars*)
- Not written = not agreed
- Systematic interpretation (context)
- Interpretation according to the goal
- Good faith

5.3 Source country's definition

As regards the application … by a contracting state … under the laws of that state

– John Avery Jones
– OECD 1999
– Included in commentary

Distributive rules v. remedy to double taxation (art. 23)

5.4 BEPS: preamble of the OECD Model 2017

Desiring to further develop their economic relationship and to enhance their cooperation in tax matters,
Intending to conclude a Convention for the elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States),
Have agreed as follows: …

Can the preamble modify a clear text?

BUSINESS PROFITS AND INCOME FROM PERSONAL SERVICES

6 ARTICLE 7: BUSINESS PROFITS

6.1 BUSINESS PROFITS DEFINED

The models do not define the term “profit” => art. 3(2).

- Civil law countries have a broad definition.
- Anglo-Saxon countries would limit the concept to profits from trade or business and set aside income from passive investments (such as dividends, interest, royalties, rental payments).

Article 7(4) results in a common application:

Where profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.

Civil law countries would include passive income in business profits but would have to look at more specific provisions while the common law countries would only look at the specific provisions when dealing with passive income.

Business profits include income from independent personal services (art.3(1)(c) and (h))

6.2 THE RULE

Profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits that are attributable to the permanent establishment in accordance with the provisions of paragraph 2 may be taxed in that other State (art. 7(1).

6.3 PERMANENT ESTABLISHMENT DEFINED

6.3.1 Fixed place of business (art. 5(1))

For the purposes of this Convention, the term “permanent establishment” means a fixed place **(1)** *of business through which* **(2)** *the business of an enterprise is wholly or partly carried on* **(3)**.

(1) Fixed place: permanence
- in time
- in the geographic area (narrowly defined)

(2) Through which (not incidental)

(3) The business is carried out

6.3.2 Dependent agent (art. 5(5))

Even in the absence of a fixed place of business, an enterprise may have a permanent establishment in the other contracting country.

6.3.2.1 2014 OECD Model

*a person - **other** than an agent of an **independent status** […] is acting **on behalf of an enterprise** and has, and habitually exercises, in a Contracting State **an authority to conclude contracts in the name** of the enterprise.*

Does art. 5(6) add anything new?

Please note: *The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other* (art. 5(7)).

A subsidiary acting as a broker or a commission agent for the benefit of its parent company is not a PE of the latter.

Philip Morris case (Italy) comp. Zimmer case (France)

6.3.2.2 2017 OECD Model

6.3.3 Permanent establishment exemptions in art 5(4)

Fixed place of business or agent used <u>only</u> for the purposes of <u>preparatory or auxiliary</u> activities

How much does an enterprise earn in the situations covered by art 5(4)?

Which purpose would the hosting country achieve in treating the foreigner as a taxpayer?

BEPS: new language in 2017 OCDE Model (art. 5(4.1)): anti-fragmentation rule

6.3.4 Building site or installation project of more than 12 months (art. 5(3))

*A **building site** or **construction** or **installation project*** (1) *constitutes a permanent establishment only if it lasts more than twelve months* (2).

(1) Maintenance is not an installation project.
(2) Many treaties provide for a shorter period.

6.3.5 Provision of services for a certain duration or a certain compensation (UNO)

3. The term "permanent establishment" also encompasses:…
(b) The furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only if activities of that nature continue (for the same or a connected project) within a Contracting State for a period or periods aggregating more than 183 days in any 12-month period commencing or ending in the fiscal year concerned.

6.3.6 BEPS

The goal is to tax income where people functions are the source (v. residence)

6.4 PROFIT ALLOCATION RULE

1. Profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein **(1)***. If the enterprise carries on business as aforesaid, the profits that are attributable* **(2)** *to the permanent establishment in accordance with the provisions of paragraph 2 may be taxed in that other State.*

2. For the purposes of this Article and Article [23 A] [23 B], the profits that are attributable in each Contracting State to the permanent establishment referred to in paragraph 1 are the profits it might be expected to make, in particular in its dealings with other parts of the enterprise, if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the ***functions*** *performed,* ***assets*** *used and* ***risks*** *assumed by the enterprise through the permanent establishment and through the other parts of the enterprise* **(3)***.* (art. 7)

3. Where, in accordance with paragraph 2, a Contracting State adjusts the profits that are attributable to a permanent establishment of an enterprise of one of the Contracting States and taxes accordingly profits of the enterprise that have been charged to tax in the other State, the other State shall, to the extent necessary to eliminate double taxation on these profits, make an appropriate adjustment to the amount of the tax charged on those profits. In determining such adjustment, the competent authorities of the Contracting States shall if necessary consult each other.

(1) See article 5 above.

(2) No "attraction" in OECD Model: profits not derived through the PE are not taxable in the PE's country – see however UN Model, art. 7.

(3) A.O.A.: profits are determined as if the PE were an independent enterprise (transfer pricing rules apply), taking into account its function, the risks it would bear as an independent entity and the assets needed to conduct the business as an independent entity. The capital equity that an independent enterprise would need is also taken into account.

6.5 REMEDY TO DOUBLE TAXATION

6.5.1 The rule

For the purposes of this Article ***and Article [23 A] [23 B],*** *the profits that are attributable in each Contracting State to the permanent establishment referred to in paragraph 1 are the profits it might be expected to make, in particular in its dealings with other parts of the enterprise, if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the* ***functions*** *performed,* ***assets*** *used and* ***risks*** *assumed by the enterprise through the permanent establishment and through the other parts of the enterprise* (art. 7(3)).

The residence country of the enterprise must acknowledge the portion of income attributable to the PE and apply article 23 to the same amount of income.

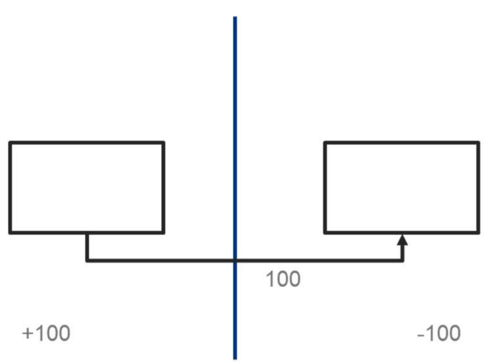
6.5.2 BEPS : OECD Model 2017 (art. 29(8))

6.6 RELATED ENTERPRISES (ARTICLE 9)

Para (1) allows the country whose enterprise transferred profits to a related enterprise to amend the first one's situation.

Because the second one is expected to have reported profits that it did not deserve, its country of residence is expected to review its tax situation and avoid economic double taxation.

Comp art. 7(3) above.



7 ARTICLE 15: EMPLOYMENT INCOME

7.1 EMPLOYMENT DEFINED

Authority and supervision

7.2 THE RULES

1. … salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.
2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:
a) the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve month period commencing or ending in the fiscal year concerned, and
b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State, and
c) the remuneration is not borne by a permanent establishment which the employer has in the other State.

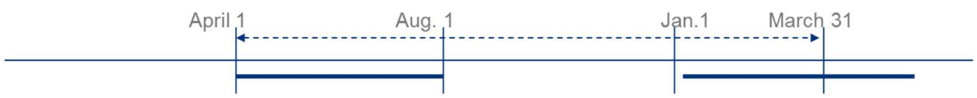
Default rule: country of residence Exception: where the employment is exercised Sub-exception: Residence IF in the country where the employment is exercised a. **Not** more than 183 days of presence b. employer **not** a resident **AND** c. **No** PE that bears the salary	Suggested reading : Default rule: country of residence Exception: where the employment is exercised IF in the country where the employment is exercised a. ~~Not~~ **more** than183 days of presence b. employer **is** ~~not~~ a resident ~~AND~~ **OR** c. ~~No~~ PE that bears the salary

7.3 EMPLOYMENT EXERCISED

Physical presence test (# where the employee reports)

7.4 SUBSTANTIAL PRESENCE TEST

184 days at a minimum in any twelve month period



7.5 THE EMPLOYER'S RESIDENCE

The employer is a resident of the country where the employment is exercised

Authority and supervision

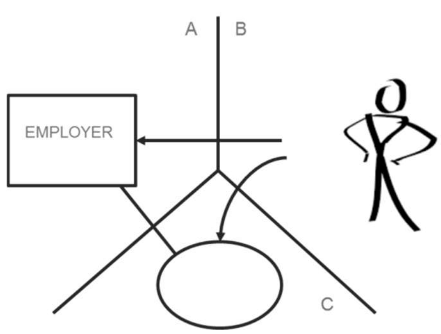
Economic benefit of the employee's work

Secondment/posting of worker

Temporary/agency workers

7.6 THE EMPLOYER'S PERMANENT ESTABLISHMENT BEARS THE SALARY

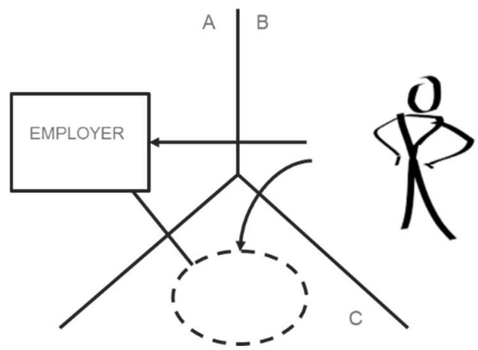
7.6.1 Figure 1



Treaty A-B:
art. 15(2)(b) not satisfied; art. 15(1): taxable in A; B applies art. 23

Treaty B-C:
art. 15(2)(c) not satisfied; art. 15(1): taxable in C; B applies art. 23

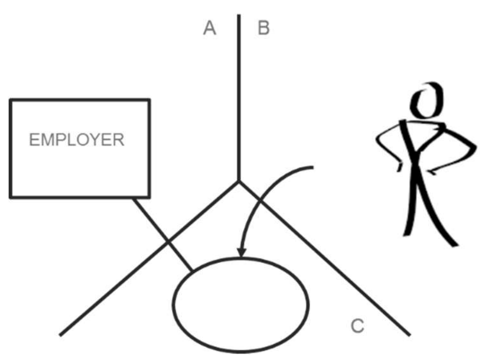
7.6.2 Figure 2



Always verify whether the premises where the employee works constitute a PE (art. 5(1), 5(3) and 5(4))

If not, the salary earned in C is taxable in B unless the employee stays more than 183 days in C

7.6.3 Figure 3



The employee constitutes a PE of the employer if he is a dependent agent of the employer (art. 5(5)). Such a PE bears the salary.

Treaty A-B:
art. 15(1): salary taxable in B only (no work performed in A)

Treaty B-C:
art. 15(2)(c) not satisfied; art. 15(1) : taxable in C; B applies art. 23

8 ARTICLE 16: DIRECTORS' FEES

8.1 DIRECTORS' FEES DEFINED

Directors' fees and other similar payments derived by a resident of a Contracting State ***in his capacity as a member of the board of directors of a company*** *which is a resident of the other Contracting State may be taxed in that other State.*

8.2 BILATERAL PROVISION

Directors' fees and other similar payments derived by ***a resident of a Contracting State*** *in his capacity as a member of the board of directors of a* ***company which is a resident of the other Contracting State*** *may be taxed in that other State.*

Art. 23 applies in the director's residence country.

PASSIVE INCOME

9 ARTICLE 6: INCOME FROM IMMOVABLE PROPERTY

9.1 IMMOVABLE PROPERTY INCOME DEFINED

The term "immovable property" shall have the meaning which it has under the law of the Contracting State in which the property in question is situated. The term shall in any case include property accessory to immovable property, livestock and equipment used in agriculture and forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources (1)*; ships, boats and aircraft shall not be regarded as immovable property.*

(1) Comp. art. 5(2).

The provisions of paragraph 1 shall apply to income derived from the ***direct use*** (2)*, letting, or use in any other form of immovable property.*

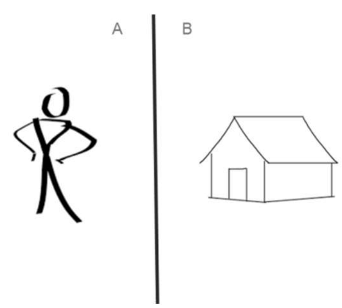
(2) "imputed income" for the use of property.

9.2 BILATERAL PROVISION

Income derived ***by a resident of a Contracting State*** *from immovable property (including income from agriculture or forestry)* ***situated in the other Contracting State*** *may be taxed in that other State.*

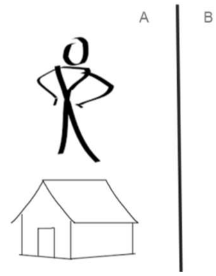
9.2.1 Figure 4

The owner is a resident of A and rents his house situated in B.



Income is derived by a resident **of country A** from immovable property **situated in country B** and may be taxed in **country B** (art. 6(1)). Art. 23 applies in country A.

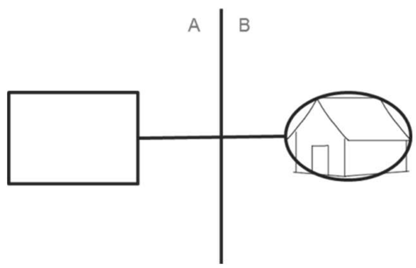
9.2.2 Figure 5



Imagine that the lessee is a resident of country B and the laws of country B provide that the rental paid by a resident of country B is taxable in country B. The lessee is a resident of country A and the building is situated in country A.

Art. 6 of the treaty b/w countries A and B does not apply because art. 6 is a bilateral provision. Art. 21 may apply (taxation in country A only). There is no room for art. 23.

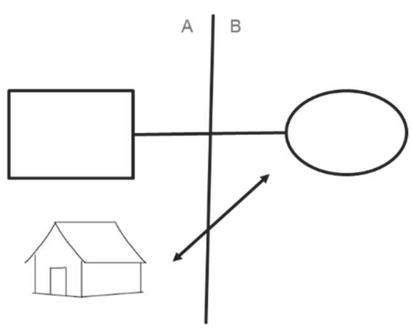
9.2.3 Figure 6



The owner is a company residing in A and it maintains a fixed place of business in a building that it owns in B. Art. 6 supersedes art. 7 and art. 6 applies to the walls of the permanent establishment (art. 6(4) and 7(3)).

Even if the fixed place of business in B was an art. 5(4) case, the (imputed) income from the occupancy of the building by company A would be taxable in B.

9.2.4 Figure 7

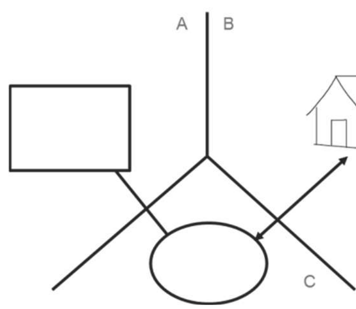


Assume that the building situated in A is invested by the company (resident in A) in its permanent establishment situated in B and is rented.

Art. 6 should not apply (while art. 7 could apply (in civil law countries) and country B could tax) but the OECD commentary interprets art. 6(4) as saying that country A should be the only country allowed to tax.

The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise (art.6(4))

9.2.5 Figure 8



Cy A maintains a PE in C and its building in B is part of its investments related to its PE situated in C. The rentals of the buildings are recorded in the PE's accounts.

Treaty A-B:
art. 6 => B may tax / art. 23 => A must apply art. 23

Treaty A-C:
art. 7 => C may tax / art. 23 => A must apply art. 23

How to avoid double taxation in B and C? OECD commentary: art. 21 of the treaty A-C allows taxation in country A only, while under the treaty A-B, B may tax and A must apply art. 23)

9.3 CAPITAL GAINS

*Gains derived by **a resident of a Contracting State** from the alienation of immovable property referred to in Article 6 and situated in the other Contracting State may be taxed in that other State* (art. 13(1))

Article 13(1) is a bilateral provision. See figure 4 (see para. 9.2.1 above)

Gains from the alienation of any property, other than that referred to in paragraphs 1, 2, 3 and 4, shall be taxable only in the Contracting State of which the alienator is a resident (art. 13(5))

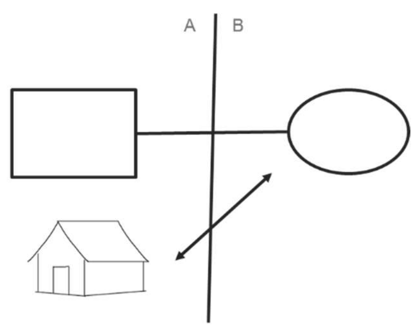
Comp. figure 8 (see para. 9.2.5 above)

Gains derived by a resident of a Contracting State from the alienation of shares deriving more than 50 per cent of their value directly or indirectly from immovable property situated in the other Contracting State may be taxed in that other State (art. 13(4) of the 2014 OECD Model).

Gains derived by a resident of a Contracting State from the alienation of shares <u>or comparable interests, such as interests in a partnership or trust</u>, may be taxed in the other Contracting State <u>if, at any time during the 365 days preceding the alienation, these shares or comparable interests derived</u> more than 50 per cent of their value directly or indirectly from immovable property<u>, as defined in Article 6,</u> situated in that other Contracting State (art. 13(4) of the 2017 OECD Model).

Shares are "movable" property. However, art. 13(4) provides for a specific regime if the issuing company (or a similar body) invests in land and building.

9.3.1 Figure 9



Assume that the building situated in A is invested by the company (resident in A) a permanent establishment situated in B and is rented.

Art. 13(1) does not apply; art. 13(5) applies.

Comp. figure 7 (para. 9.2.4 above).

10 ARTICLE 10: DIVIDEND INCOME

10.1 DIVIDEND DEFINED

Art. 10(3)

10.2 BILATERAL PROVISION

*Dividends paid by a company which is a **resident of a Contracting State** to a **resident of the other Contracting State** may be taxed in that other State* (art. 10(1))*.*

10.3 TAXATION IN THE SHAREHOLDER'S RESIDENCE COUNTRY

*Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be **taxed in that other State**.*

10.4 LIMITED TAXATION AT SOURCE

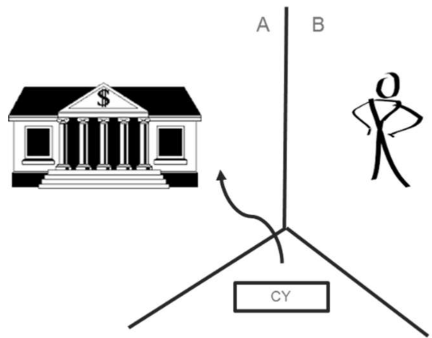
However, dividends paid by a company which is a resident of a Contracting State may also be taxed in that State according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed:
*a) 5 per cent of the gross amount of the dividends if the beneficial owner is **a company** (other than a partnership) which holds directly at least 25 per cent of the capital of the company paying the dividends [365 holding period];*
b) 15 per cent of the gross amount of the dividends in all other cases (art. 10(2))*.*

10.5 REMEDY TO DOUBLE TAXATION

Tax credit: art. 23A(2) and art. 23B.

nb: Art. 23A(2) only applies where art. 10 applies (# art. 7 or 21) but treaties actually signed may vary (Belgium).

10.5.1 Figure 10



The shareholder resident of B cashes in A his dividend paid by a company resident of country C

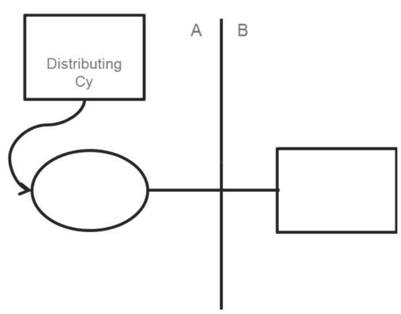
Treaty A-C:
Art. 10(1) and (2): taxation in B; taxation limited to 15% also possible in C; tax credit in B if applicable (art. 23)

Treaty A-B:
The distributing company is not a resident of a contracting country; art. 21: taxation in B only.

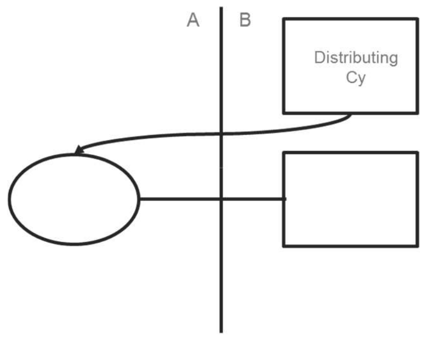
End result: 15% max in country C, taxation in B with a credit for the tax paid in C.

10.6 Shares invested in a permanent establishment (art. 10(4))

10.6.1 Figure 11

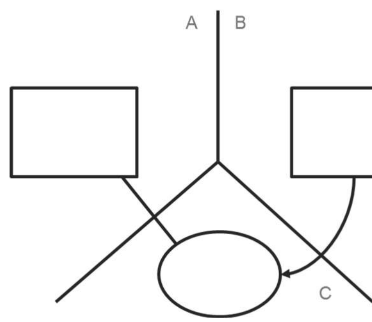


10.6.2 Figure 12



Art. 10 does not apply (no bilateral situation)
Art. 7 or 21(2) applies: taxation in A (same result as art. 10(4))
B applies art.23A(1) or 23B as a remedy related to art.7 or 21(2)

10.6.3 Figure 13



Treaty A-B:
Art. 10(1) and (2) : taxation in A, taxation in B limited to 5 or 15%
Art. 23: credit in A

Treaty A-C:
Art. 10 does not apply
Art. 7 or 21(2): taxation in C; A applies art. 23

The taxpayer may lose its credit in A for the tax paid in B pursuant to treaty A-B because the tax left to A after the application of the treaty A-C might be lower than the credit due under the treaty A-B (this always the case where country A is an exemption method country).

11 ARTICLE 11: INTEREST INCOME

11.1 INTEREST DEFINED

Art. 11(3)

11.2 Bilateral Provision

Interest ***arising in a Contracting State*** *and paid* ***to a resident of the other Contracting State*** *may be taxed in that other State.*

11.3 SOURCE OF THE INTEREST

Interest shall be deemed to ***arise*** *in a Contracting State when* ***the payer is a resident of that State****. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has* ***in a Contracting State a permanent establishment*** *in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment, then such interest shall be deemed to arise in the State in which the permanent establishment is situated* (art. 11(5))*.*

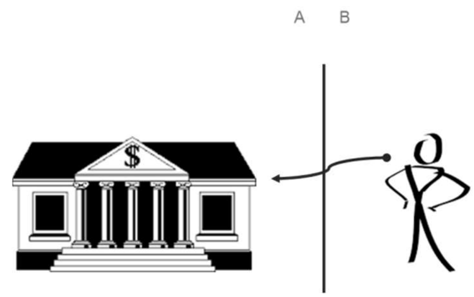
11.4 TAXATION IN THE RESIDENCE COUNTRY OF THE CREDITOR

Interest arising in a Contracting State and paid to a resident of the other Contracting State may be ***taxed in that other State*** (art.11(1))*.*

11.5 LIMITED TAXATION IN THE SOURCE COUNTRY

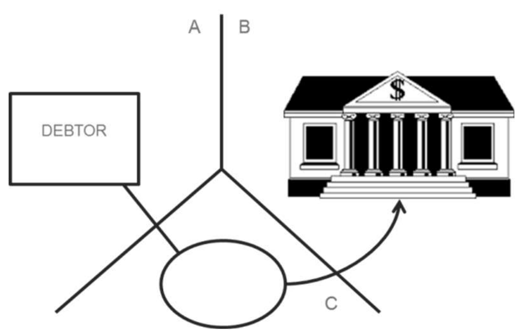
2. However, interest arising in a Contracting State may also be taxed in that State according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the interest. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation (art.12(2))*.*

11.5.1 Figure 14



Art. 11(5) : interest arises in B
Interest is paid to a resident of A
Interest is taxable in A and B may tax (10% max.) (art. 11(1) and (2))
A grants a credit for the tax paid in B (art. 23)

11.5.2 Figure 15



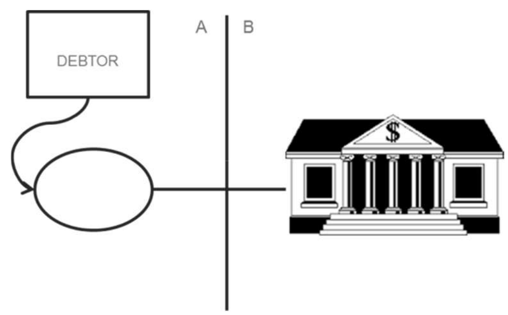
Treaty A-B:
Art. 11(5) : interest arises in A
Interest is paid to a resident of B
Interest is taxable in B and A may tax (10% max.) (art. 11(1) and (2)
B grant a credit for the tax paid in A (art. 23)

Treaty B-C:
Art. 11(5): interest arises in C
Interest is paid to a resident of B
Interest is taxable in B and C may tax (10% max.) (art. 11(1) and (2)
B grant a credit for the tax paid in C (art. 23)

⇨ A and C may tax (unlimited)
B should grant two credits (taxes paid in A and C) if the remaining tax in B is big enough to do so.

11.6 PAYMENT TO THE CREDITOR'S PE

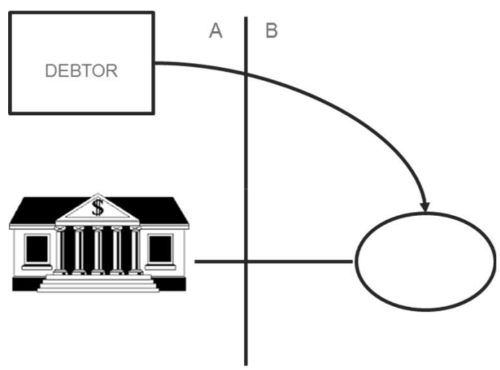
11.6.1 Figure 16



The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other ***Contracting State in which the interest arises*** *through* ***a permanent establishment*** *situated therein and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.* (art. 11(4))

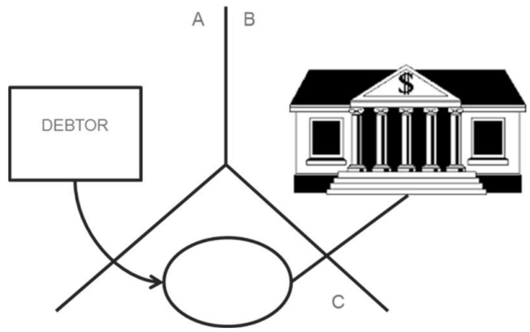
Because art.7 or 21(2) applies, country B applies art.23A(1) or art. 23B.

11.6.2 Figure 17



Art. 11(5): interest arises in A. Interest is paid to a resident of A. Art. 11 does not apply. Art. 7 or 21(2) applies. Unlimited taxation in B and A applies art. 23 (art.23A(1) or art. 23B).

11.6.3 Figure 18

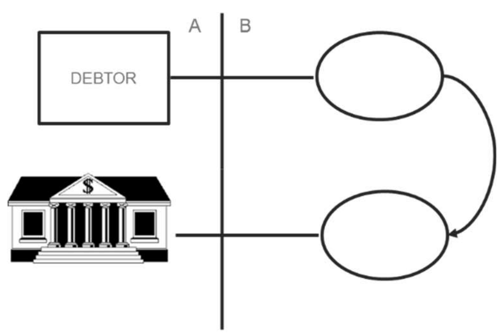


Treaty A-B:
Interest arises in A
Interest is paid to a resident of B
Interest is taxable in B and A may tax (10% max) (art. 11(1) and (2)
B grants a credit for the tax paid in A

Treaty B-C:
Interest does not arise in a contracting country => article 11 does not apply
Art. 7 or 21(2) : interest is taxable in C and country B applies art. 23

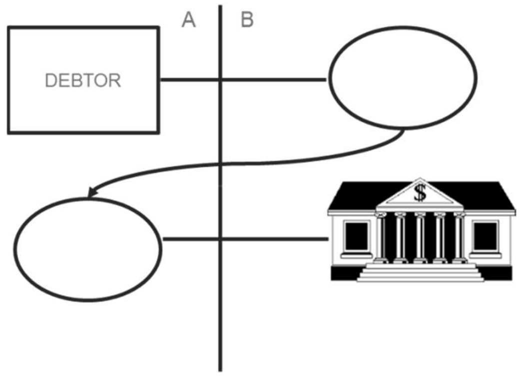
B may not be able to also grant a credit for the tax paid in A under treaty A-B

11.6.4 Figure 19



Art. 11(5): B is the source; art. 11(4): taxation in B; A applies art. 23

11.6.5 Figure 20



Art. 11(5): interest arises in B; interest is paid to a resident of B; art. 11 does not apply
Art. 7 applies: taxation in A and B applies art. 23

12 ARTICLE 12: ROYALTIES

12.1 ROYALTY DEFINED

The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.

You really need a specialist in intellectual property law to characterize the income. So-called royalties may be genuine business profits (customization of a software), capital gains (temporary relinquishment may be a sale or a concession).

In previous versions of the OECD model, compensation for the use of machinery and equipment was covered by art.12

12.1 BILATERAL PROVISION

*Royalties **arising in a Contracting State** and beneficially **owned by a resident of the other Contracting State** shall be taxable only in that other State.*

However, article 12 does not define the source of royalties. Comp. treaties between countries that include a definition of the source.

12.2 TAXATION IN THE RESIDENCE COUNTRY OF THE BENEFICIARY

Royalties arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other State.

No taxation in the source country in the OECD model. However, many treaties provide for a source country taxation.

13 COMMON RULES REGARDING INCOME FROM SHARES, RECEIVABLES, AND INTELLECTUAL PROPERTY

13.1 ARM'S LENGTH PRINCIPLE

Articles 11 and 12 only apply to *normal* interest and royalties.

Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the interest, having regard to the debt-claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.(art. 11(6))

Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention (art. 12(4)).

Because a dividend never is excessive, art. 10 does not include a similar provision.

13.2 CAPITAL GAINS (ARTICLE 13)

5. Gains from the alienation of any property, other than that referred to in paragraphs 1, 2, 3 and 4, shall be taxable only in the Contracting State of which the alienator is a resident.

2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State, including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise), may be taxed in that other State.

4. Gains derived by a resident of a Contracting State from the alienation of shares deriving more than 50 per cent of their value directly or indirectly from immovable property situated in the other Contracting State may be taxed in that other State. [see above the wording of art. 13(4) in the 2017 OECD Model)

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