THE TAX WORK OF THE UNITED NATIONS

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History of the UN Tax Committee

- Ad Hoc Group of Experts on Tax Treaties between Developed and Developing Countries established in 1968 pursuant to a resolution of the Economic and Social Council (Ecosoc)
- Renamed in 1980 as Ad Hoc Group of Experts on International Cooperation in Tax Matters
- Renamed in 2004 the Committee of Experts on International Cooperation in Tax Matters - Enhanced status

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Mandate of the Committee

- Review and update the UN Model Double Taxation Convention between Developed and Developing Countries as well as the Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries
- Provide a framework for dialogue with a view to enhancing and promoting international tax cooperation
- Consider how new issues could affect international tax cooperation and develop appropriate recommendations
- Make recommendations on capacity-building and the provision of technical assistance to developing countries and countries in transition
- Give special attention to developing countries and countries in transition in dealing with those issues

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Composition of the Committee

- 25 members nominated by Governments and acting in their personal capacity
- Selected to reflect an equitable geographical representation of developing countries, countries in transition and developed countries
- Appointed by the Secretary-General of the UN
- Mandate of 4 years (the mandate of the current Committee end in July 2013)

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Current membership of the Committee

- Developing countries experts (15)
  - Africa: Egypt, Ghana, Morocco, Nigeria, Senegal, South Africa
  - Asia: China, Korea*, India, Pakistan, Malaysia
  - Latin America and Caribbean: Barbados, Chile*, Brazil, Mexico*
- Developed countries experts (10)
  - Europe: Belgium, Bulgaria, Germany, Italy, Norway, Spain, Switzerland
  - Others: Japan, New Zealand, United States

* OECD Member States within developing regions

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Meetings of the Committee

- One annual session (5 days per year in Geneva)
- The current Chair of the Committee is the representative of Mexico
- Observers may attend and participate in the meetings (observers from Governments, GOs, NGOs and Civil society)
- Forthcoming session: 15-19 October 2012
- Website: http://www.un.org/esa/ffd/tax/index.htm

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The upgrading of the Committee?

- On 15 March 2012, the ECOSOC will examine again the strengthening of the Committee
- Three options have been identified :
  - Retaining the current format of the Committee while improving its functioning (with or without supplementary resources)
  - Converting the Committee into an intergovernmental commission (a subsidiary body of the ECOSOC) “which would offer developing countries a full seat at the table”
  - Creating an intergovernmental commission and retaining the existing Committee as a subsidiary body of that commission

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The upgrading of the Committee?

- On April 2011, the European Union recommended being prudent towards an initiative that could be seen as competing with existing institutions rather than aiming at improving international cooperation in the tax area:
  - efforts should focus on enhancing synergies with other international fora, in particular with the OECD, before considering upgrading the Committee
  - efforts should be made to ensure that the existing Committee functions in the most effective way
  - increased resource would be necessary if the Committee would be upgraded or its mandate expanded; this is problematic

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Work of the Committee

- A small Secretariat not just servicing the Committee
- Work is prepared by Subcommittees and Working Groups
  - Coordinated by a member of the Committee
  - Composed of members of the Committee and observers (including representatives of the civil society)
  - Work is achieved through exchange of emails and face-to-face meetings

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Current Subcommittees (and working group)

- UN Model Tax Convention Update (Robin Oliver)
- Tax Treatment of Services (Liselott Kana)
- Dispute Resolution (Claudine Devillet)
- Transfer Pricing Manual (Stig Sollund)
- Manual for Negotiation of Tax Treaties (Ben Arrindell)
- Capacity Building (Ifueko Omoigui Okauru)
- Capital Gains (Anita Kapur)
- Exchange of Information (Robin Oliver)
- Tax Treaty Issues Related to Climate Change Mechanisms (Claudine Devillet)

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The UN Model Tax Convention

- The 2011 update takes account of the developments over the last 10 years in international tax policies
- The UN Model favours the "source country" taxing rights as compared to those of the "residence country" of the investor
- It does not constitute recommendations of the United Nations: it is elaborated by 25 experts with a view to facilitate the negotiation and interpretation of bilateral tax treaties
- No reservations, observations or positions of countries in the Model
- Large quotation of the OECD Commentary

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The UN Model Tax Convention

- The UN Model helps non-OECD countries in negotiating tax treaties
- It added legitimacy to their positions
- It assists non-OECD countries in interpreting and applying tax treaties
- It gives more certainty to tax payers

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The 2011 Update of the UN Model

- Launch of the UN Model on 15 March 2012
- ECOSOC should seek country positions on the Model from UN Member States, to make it clear which countries adopted certain interpretations, especially when the Commentary notes differing interpretations
- The Updated version of the Model will be made available in printed form as soon as possible
- The Model will be freely available in downloadable form at the UN website
- Translation into the other official languages and publication in those languages should be achieved as soon as possible after publication of the English language version

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The UN Model Tax Convention

- Article 1 (Persons covered)
  - ➢ Improper use of tax treaties: Expanded Commentaries (§§ 8 to 103) to help countries that have limited experience in dealing with sophisticated tax-avoidance strategies
  - ➢ Partnerships: §§ 6.1 to 6.7 of the OECD Commentaries endorsing the conclusions of the Partnership Report are not retained
  - ➢ Collective Investment Vehicles: §§ 6.9 to 6.34 of the OECD Commentaries are not retained

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The UN Model Tax Convention

- **Article 4 (Resident)**
  - The UN Commentary quotes § 8.8 of the OECD Commentary, which states that if a State disregards a partnership for tax purposes and taxes the partners on their share of the partnership income, partners are eligible to the benefits of the treaty
  - A new paragraph follows the quoted § 8.8 and mentions that some members of the Committee do not agree with such view. They consider that a special rule is required in a Convention to provide such a result.

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The UN Model Tax Convention

- **Article 5 (Permanent establishment)**
  - The definition of PE under Par. 1 of Art 5 is identical in the UN and the OECD Models
  - The UN Commentary quotes the OECD Commentary on Par.1 of Art 5, except
    - § 5.5 (considering that a satellite in geostationary orbit cannot constitute a PE)
    - § 9 (concerning the leasing of containers which is covered under Art 12 of the UN Model)
    - § 9.1 (dealing with “roaming” agreements and considering that the place where the foreign network is situated does not constitute a PE for the home network operator)

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The UN Model Tax Convention

- **Article 5 (Permanent establishment)**
  - 6 months for a building or construction site rather than 12 months
  - the furnishing of services through employees or other personnel creates a PE if the activities continue (for the same or a connected project) for more than 183 days in any 12 months period
  - Art. 14 (Independent Personal Services) is retained; the Commentary provides guidance for countries wishing to delete Article 14 and to cover independent services under Art. 5
  - "delivery" is not mentioned in Par. 4 a) and b) and therefore might result in a PE
  - a "dependent agent" may constitute a PE, without having the authority to conclude contracts in the name of the enterprise, if he habitually maintains a stock of goods or merchandise and regularly makes deliveries from the stock
  - a PE may exist (except in regard to re-insurance) if a "dependent agent" collects premium or insures risks in a country without having the authority to conclude contracts in the name of the insurance enterprise

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The UN Model Tax Convention

- **Article 7 (Business Profits)**
  - The UN Model does not adopt the new Art. 7 of the 2010 OECD Update
  - This results from the decision of the Committee not to adopt the "Authorised OECD Approach" arising from the 2008 OECD Report on Attribution of Profits to PEs
  - The AOA is conflicting with Par. 3 of Art. 7 of the UN Model which disallows deductions for amounts "paid" (other than toward reimbursement of actual expenses) by a PE to its head office
  - The rule in Par. 3 is seen as continuing to be appropriate in the context of the UN Model
  - All references to Art. 7 of the OECD Model and its Commentary relate to the 2008 OECD Update (except for the specific UN provisions and where specific reference is made to the 2005 OECD Update)
  - The UN Commentary recognizes that a PE, treated as a separate and independent enterprise, should be expected to have adequate funding

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The UN Model Tax Convention

- **Article 7 (Business Profits)**
  - A limited force of attraction allows the country in which the PE is located to tax not only the profits attributable to the PE but also the profits from activities conducted directly by the home office within the country that are similar in nature to those conducted by the PE
  - Par. 3 is consistent with the approach adopted in interpreting Art. 7 in the 2008 OECD Update but it varies from the approach adopted by the 2008 OECD Report on Attribution of Income to PEs
  - The UN Model does not contain Par. 5 of Art. 7 of the 2008 OECD Model, which states, "No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise". Par. 5 was deleted from the OECD Model in 2010

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The UN Model Tax Convention

- ***Article 8 (Shipping, Inland waterways transport and Air transport)***
  - Several Members expressed concern with the comprehensive changes made in 2005 in the OECD Commentary on Art. 8
  - The paragraphs of the OECD Commentary referring to the income from directly connected and ancillary activities of shipping and air transport enterprises were therefore not retained
  - The changes need to be examined and discussed in detail in order to determine their implications

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The UN Model Tax Convention

- **Article 9 (Associated enterprises)**
  - The "appropriate adjustment" required by Par. 2 is not applicable in case of penalties for fraud, gross negligence, wilful default
  - § 3 of the 2001 UN Commentary endorses the arm's length principle and recommends that Contracting States follow the OECD Transfer Pricing Guidelines
  - For most Members of the Committee these views are still appropriate
  - For some Members these views are too broadly stated
  - § 3 has been amended to clarify that these views are expressed by the former Group of Experts and have not been fully considered by this Committee, although there was unanimity among the Committee Members that the arm's length principle underlies Art. 9 of the UN Model

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The UN Model Tax Convention

- **Article 11 (Interest)**

The Commentary addresses Islamic Financial Instruments

  - In a number of countries, Islamic Financial Instruments are assimilated to debt relations under domestic tax law although their legal form is not a loan. The definition of interest in Art. 11 applies to payments made under those instruments
  - Countries that do not deal in their domestic law with those instruments and generally follow an economic-substance-based approach for tax purposes may, nevertheless, apply the definition of interest to those instruments
  - Countries following a purely legal approach for tax purposes, may refer expressly to such instruments by inserting in the definition of "interest": "The term also includes income from arrangements such as Islamic financial instruments where the substance of the underlying contract can be assimilated to a loan".
  - This issue is currently discussed in the OECD

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The UN Model Tax Convention

- **Article 12 (Royalties)**
  - Source country taxation: the country of use of intellectual property has a right to tax profits accruing to the owner of the property
  - Payments for the use or the right to use industrial, commercial or scientific equipment
  - Art. 12 was not considered fully by the Committee and some changes included in the 2010 OECD Commentary were not incorporated in the UN Commentary
  - OECD commentaries on “know how” (§§ 11 to 11.6) were incorporated but disagreement was expressed on the last part of § 11, which limits the scope of Art. 12 to information arising from previous experience
  - A new sentence reflects the minority view that Art. 12 is not limited to information arising from previous experience
  - A view was also expressed that payments referred to in §§ 14, 14.1, 14.2, 14.4, 15, 16, 17.2 and 17.3 relating to computer programs may constitute royalties. A sentence in the UN Commentary acknowledges this view

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The UN Model Tax Convention

- **Article 13 (Capital gains)**
  - Par. 4 broadly corresponds with Par. 4 of the OECD Model (gains from the alienation of shares deriving more than 50% of their value from immovable property situated in a CS may be taxed in that CS)
  - Par. 5 allows the CS in which a company is a resident to tax gains on the alienation of any number of shares of that company as long as the shareholding is substantial at any time during the 12 month period preceding the alienation:
    - The substantial shareholding is determined according to the percentage decided during the bilateral negotiations
    - Even if a substantial shareholding is alienated through a number of transfers of smaller shareholdings, the taxing right will apply if the shares transferred were alienated at any time during a 12 month period

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The UN Model Tax Convention

- **Article 14 (Independent Personal Services)**
  - Art. 14 has been retained
  - The UN Commentary was fully discussed and remains unchanged
  - Some Members of the Committee consider that Art. 14 is applicable, in contradiction with § 9 of the UN Commentary, to income derived by a company from the furnishing of services through the activities of its employees (instead of Art. 7)
  - The UN Commentary does not endorse this view
  - § 11 of the UN Commentary states, however, that some countries interpret Art. 14 differently and that they may, therefore, clarify their positions bilaterally

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The UN Model Tax Convention

- **Article 15 (Dependent Personal Services)**
  - Similar to Article 15 of the OECD Model
  - The OECD Commentary is quoted (including §§ 8.1 to 8.28 relating to the determination of the person who is effectively the "employer" for the application of Par. 2 of Art. 15)
- **Article 16 (Director's Fees and Remuneration of Top-level Managerial Officials**
  - Under Par. 2, the remuneration paid to top-level managers (responsibilities for the general direction of the company) are subject to the same principle as directors' fees

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The UN Model Tax Convention

- Article 18 (Pensions and Social Security Payments)
  - Article 18 A
    - The State of residence has an exclusive right to tax pensions and other similar remuneration
    - The State of source has, however, an exclusive right to tax payments made within the framework of a public scheme which is part of the social security system of that State
  - Article 18 B
    - The State of residence may tax pensions and other similar remuneration
    - The State of source may, however, also tax pensions and other similar remuneration paid by a resident of that State (Art. 23A or 23B determines whether the State of residence shall exempt or shall allow a tax credit)
    - The State of source has, however, an exclusive right to tax payments made within the framework of a public scheme which is part of the social security system of that State
  - The new UN Commentary takes account of some OECD updates

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The UN Model Tax Convention

- Article 21 (Other income)
  - Par. 3 is an addition to Art. 21 of the OECD Model
  - It allows the Contracting State in which the income arises to tax also such income (in such case, Art. 23A or 23B determines whether the State of residence shall exempt or shall allow a tax credit)

- Article 23 (Methods for the elimination of double taxation)
  - Two alternatives as under the OECD Model
  - Art. 23A (Exemption method) does not include Par. 4 of the OECD Model which aims at preventing double non-taxation
  - Section E on conflicts of qualifications (§§ 32.1 to 32.7) is not included in the UN Commentary

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The UN Model Tax Convention

- **Article 25 (Mutual Agreement Procedure)**
  - The UN Model has 2 alternatives: Art. 25A without mandatory arbitration and Art. 25B with mandatory arbitration
  - Art. 25B includes mandatory arbitration as is provided for in par. 5 of the OECD Model but with 3 main differences:
    - arbitration may be initiated if the competent authorities are unable to reach an agreement on a case within 3 years from the presentation of that case (2 years under the OECD Model).
    - arbitration must be requested by the competent authority of one of the Contracting States (under the OECD Model, arbitration must be requested by the person who initiated the case): this means that a case shall not be submitted to arbitration if the competent authorities of both CS consider that the case is not suitable for arbitration and neither of them makes a request
    - the competent authorities may depart from the arbitration decision if they agree to do so within six months after the decision has been communicated to them

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The UN Model Tax Convention

- **Article 25 (Mutual Agreement Procedure)**
  - The UN Commentary quotes the OECD Commentary with some changes:
    - due to the differences in the rules of Par. 5 on mandatory arbitration
    - due to the differences in the rules for the implementation of arbitration
      - unless the competent authorities agree in a particular case that the arbitration board will issue an independent decision, the so-called "baseball arbitration" is followed
      - a case shall not be submitted to arbitration if it involves less than a certain amount of taxes (to be specified); such cases shall only be submitted to arbitration if both competent authorities agree that it is appropriate to do so
      - the mutual agreement contains rules determining the remuneration of the arbitrators
    - § 2 acknowledges the fact that some countries consider that in the absence of Par. 2 of Art. 9, economic double taxation arising from transfer pricing adjustments does not fall within the scope of mutual agreement procedure

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The UN Model Tax Convention

- **Article 26 (Exchange of information)**
  - Similar to Art. 26 of the OECD Model
  - Additional sentence in Par. 1: "In particular, information shall be exchanged that would be helpful to a Contracting State in preventing avoidance or evasion of such taxes." That addition was thought to be useful by Members from developing countries.
  - Additional Par. 6 that grants the authority to the competent authorities to agree on bilateral procedures for an effective exchange of information. The OECD Commentary considers that such authority is implicit under Art. 26 of the OECD Model
  - The UN Commentary includes an inventory of exchange of information mechanisms

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Tax treatment of services

- During the 5th meeting of the Committee, a Subcommittee was set up
- During the 6th meeting, Brian Arnold presented a paper on ways in which different articles of the UN Model deal with the taxation of services in general
  - He mentioned the lack of consistent policy treatments
  - He expressed the view that countries might take the position, based on their domestic law, that income from technical services was not income from carrying on business dealt with under Art. 7 but was "other income" taxable by a source country in accordance with Par. 3 of Art. 21 without any limitation
  - He expressed the view that allowing unlimited source country taxation of fees for technical services under article 21 was inappropriate in policy terms. Such fees from typically involve significant expenses. Any source country tax should be imposed on a net basis or at a low rate if taxed on a gross basis
  - Some Members of the Committee noted that source taxation of income from services could be a substantial source of revenue for developing countries and that the best collection strategy would be withholding taxes the gross payments

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Tax treatment of services

- During the 7th meeting, Wim Wijnen and Jan de Goede from the IBFD presented a study examining what kind of provisions countries use when dealing with services
  - Less than 5% of the treaties between two non-OECD countries or between a non-OECD country and an OECD country are dealing with services as part of the royalty definition
  - Only 13% of the treaties between two non-OECD countries and 6% of the treaties between a non-OECD country and an OECD country contain an autonomous services provision
  - Countries in principle prefer to follow the standard provisions of the Model without deviation
  - When there are no standard provisions available, as is the case with autonomous services provision, countries develop their own policy resulting in a diversity of provisions, which makes application of treaties challenging
  - Countries appeared to have strong preference for taxation of the net income rather than withholding tax on the gross income

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Tax treatment of services

- During the 7th meeting, the discussion focused on the ways of taking the work on services forward
  - Some called for a comprehensive approach: an article-by-article review of all the provisions of the Model dealing with services, paying especial attention to fees for technical services and permanent establishment issues
  - Others felt that under this approach it would not be possible to achieve concrete results within a reasonable period of time
  - It was agreed that the Committee will start with work on "fees for technical assistance" with a view of achieving concrete results for the 8th meeting but that it will also have a longer-term plan of work aiming at a comprehensive review of services issues generally

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Transfer Pricing Manual

- As clearly stated in the mandate of the Subcommittee, the manual should be based on the arm's length principle embodied in Art. 9 of the UN Model and should be consistent with the OECD Transfer Pricing Guidelines to which the UN Commentary refers
- It should try to make the arm's length approach as understandable and workable as possible for developing countries
- Special attention should, also, be paid to the experience of developing countries
- Participants in that work:
  - Stig Sollund (Norway - Coordinator); Mansor Hassan (Malaysia); Keiji Aoyama (Japan); Marcos Valadao (Brazil) and Amr El-Monayer (Egypt) of the Committee
  - Carmen van Niekerk (South Africa); Julius Bamidele (Nigeria); Harry Roodbeen (Netherlands); Toshio Miyatake (Adachi, Henderson, Miyatake & Fujita, Japan); Kyung Geun Lee (Yulchon Lawyers, Korea), Monique Van Herksen (Ernst and Young, Netherlands); Jolanda Schenk (Shell, Netherlands); TP Ostwal (Ostwal and Associates, India); Michael Kobetsky (Australian National University); Carol Dunahoo (Baker and McKenzie LLP); a representative from the OECD

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Transfer Pricing Manual

- Developing countries, especially those with weak or small administrations, are disadvantaged by:
  - the complexity of transfer pricing concepts and their practical application
  - the "fuzziness" of some of the concepts involved
  - the lack of data needed to evaluate the profit allocation and the cost of access to the relevant data
  - the huge human-resources and costs needed by transfer pricing cases
- The Manual will be integrated with an enhanced UN capacity building programme
  - addressing the policy and technical issues of the arm's length approach
  - providing tools to know where – in terms of risk management – developing countries can most effectively target their limited resources

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Transfer Pricing Manual

- The Subcommittee is reluctant to quote the OECD Transfer Pricing Guidelines in the Manual
  - Unintended or intended differences between the Manual and the OECD TPG
- The Subcommittee contemplates the inclusion in the Manual of a chapter dealing with “fixed rates methods”
  - Such method would only be feasible if the applicable rates were agreed by the other countries involved in a transfer pricing case. This seems unlikely as there may be significant variations within an industry sector depending on the location of the enterprises
  - The taxpayers should be able to rebut the fixed rates by reference to arm’s length methods. It is not clear if this possibility would be part of the method
  - If a developing country was requested to grant compensating adjustments because other countries are using fixed margins, this would add complexity to the system and could create problems of double taxation detrimental to the investment climate in that developing country
- It is unclear if the Manual will recommend arbitration in order to settle transfer pricing disputes

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