TAX LAW

Academic Year 2016 / 2017

AGENDA - Session 5-

- Introduction to Tax Treaty Provisions

  a) The OECD Model Convention
  b) The OECD Commentary
  c) UN MODEL

Required readings:

- ***Introduction to the OECD MC; Art.1 and Art 2 of the OECD MC; and***
- ***OECD Commentary to Art. 1 (paragraphs: 1, from 7 to 12, 21, 26.2)***
- ***OECD Commentary to Art. 2 (paragraphs 1 through 8)***

Introduction to Tax Treaty Provisions

International double taxation.

- **Juridical double taxation**. the imposition, in the hands of the same taxable person, of comparable income taxes by two or more sovereign countries on the same item of income.
- **Economic international double taxation**. Double taxation occurs whenever there is multiple taxation of the same items of economic income in the hands of two or more different taxable persons.

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EXEMPTION METHOD

- Under the exemption method, the country of residence taxes its residents on their domestic-source income and exempts them from domestic tax on their foreign-source income. As a result, jurisdiction to tax rests exclusively with the country of source.

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CREDIT METHOD

- Under the credit method, foreign taxes paid by a resident taxpayer on foreign-source income generally reduce domestic taxes payable by the amount of the foreign tax.
- NO refund of excess tax credit (Ordinary tax credit)

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TAX TREATIES

- Treaties are agreements between sovereign nations. They confer rights and impose obligations on the Contracting States.
- *Domestic/Treaty Law*. The basic principle is that a treaty should prevail in case of conflict between domestic law and treaty provisions.

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TAX TREATIES

- *Taxes covered*. In general, tax treaties apply to all income taxes imposed by the Contracting States, including taxes imposed by local or subnational governments.
- *Limitation of taxation*. Most tax treaties do not impose tax. Rather, they limit the taxes otherwise imposed by a state.

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TAX TREATIES

- *Modification*. Once a treaty has been adopted, it may be modified in minor or major ways by the mutual conset of the Contracting States.
  - a) Protocols.
  - b) Interpretative process.
  - c) Domestic rules.
- *Treaty Override*.

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OECD MC

- Development. The early diplomatic treaties of the 19th century are the historical basis for the OECD Model treaty.
- Early stage. The very first model conventions appeared in 1943 and 1946, but they were not unanimously accepted. The work of creating an acceptable model treaty was taken over by the OECD.

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OECD MC

- ❑ Recent drafts. The first OECD Model Tax Treaty was published in 1963; it was revised in:
  - ✓ 1977
  - ✓ 1992
  - ✓ 2000
  - ✓ 2003
  - ✓ 2010….2014

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OECD MC

- ❑ Basic features. The OECD MC basically tends to favor capital exporting countries over capital importing countries. Often it eliminates or mitigates double taxation, by requirig the source country to give up some or all of its tax on certain categories of income earned by residents of the other treaty country.

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OECD MC

- Ch I Scope (personal, taxes): artt. 1 - 2   (see also 28, 29)
- Ch II Definitions: artt. 3-5
- Ch III Assignment of income elements: artt. 6 - 21
- Ch IV Assignment of capital elements: art. 22
- Ch V Relief of double taxation: art. 23
- Ch VI Special provisions: artt. 24 - 27 (nondiscrimination, mutual agreement, exchange of information)

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OECD MC. Mechanism of application

Resident of State R receives income from State S

- ❑ Treaty gives State R an exclusive right to tax. State S does not tax. *Example: Art. 18 (pensions).*
- ❑ Treaty gives State S an exclusive taxing right and State R first includes taxable element in worldwide income of R and next provides double taxation relief. *Examples: Art. 6 (immovable property: regular taxation by State S) Art. 10 (dividends: limited taxation by State S)*

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OECD COMMENTARY

- For each Article in the MC there is detailed Commentary that is intended to illustrate or interpret the MC provisions.
- Observations on the Commentaries may have been made by member countries that are unable to concur in the interpretation given in the Commentary.
- Reservations may be recorded as well by member countries.

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UN Model treaty

- Development. The UN Model Treaty was published in 1980 by the United Nations. It was drafted by the U. N. Group of Experts on Tax Treaties between Developed and Developing Countries, established in 1967 by the Economic and Social Council of the United Nations.

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UN Model treaty

- Difference with OECD Model. The main difference between the two models is that the UN Model imposes fewer restrictions on the tax jurisdiction of the source country (for example it does not contain specific limitations on the withholding tax rates on dividends, interest and royalties imposed by the source country).