

OECD Officials Make Annual Visit to IFA World Congress

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Source taxation versus residence taxation was the theme of the International Fiscal Association's 2005 World Congress in Buenos Aires held September 12-16.

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Source taxation versus residence taxation was the theme of the International Fiscal Association's 2005 World Congress in Buenos Aires held September 12-16. Practitioners frequently found the discussion less than practical, but it was a breakthrough of sorts. The point was made more than once that developed, capital-exporting countries have stacked the accepted rules of the international tax system in their favor.

With its emphasis on residence-based taxation, the OECD model treaty, several speakers argued, grants superior taxing rights to capital exporting countries at the expense of countries that host their investors. The source country's superior right to tax the income is a platitude recited before it is taken away. There was nervous laughter when one speaker implied that the United States uses the OECD to do its dirty work in preventing source taxation and other impediments to what other speakers called "fiscal imperialism."

Mary Bennett, who recently replaced John Neighbour as head of the OECD tax treaty and transfer pricing division, told participants that the OECD is working on guidance on the interaction of thin capitalization rules with transfer pricing rules, and restructuring to avoid permanent establishment definitions (the subject of another IFA session).

She reported that the OECD's arbitration project is going well. Readers know that arbitration is to be used as a threat when competent authorities are deadlocked in transfer pricing cases. Bennett reported that the OECD has tentatively decided the new model treaty will include mandatory arbitration for cases that have been stuck in competent authority for two years. That model treaty clause, to be in article 25, would be optional, however. The OECD also plans to write an arbitration manual, which will have its own Web site. The next meeting of the joint working group about arbitration will take place in December. Bennett expects a consultation document to be issued in March 2006, with a final version in January 2007.

Mike Waters, departing chairman of OECD working party number 1, reported that the OECD expects to complete all four parts of its magnum opus on attribution of profits to PEs in January 2007. The OECD is now working on implementation of its ideas. Waters stated that the OECD believes the theoretical debate is over. So the OECD is working on correcting the commentary to model treaty article 7, which would consist of inserting the four reports themselves into the commentary as guidelines. Waters admitted the reports could be considered a departure from the existing commentary. Waters indicated the OECD may even rethink the legal wording of article 7 itself.

Another working group is looking at source taxation of employees under article 15, which depends on whether the payee is considered to have an employer in the source country. Waters reported that the OECD is concerned about abuses of the formal employer/employee relationship. The OECD is now backtracking on an unpopular discussion draft published in 2004. The OECD will change the objectionable examples in the draft while retaining its basic approach. There will be more consultation with business, and the guidance should be finished by February 2006.

Jacques Sasseville, who is in charge of tax treaties at the OECD, reported that the OECD has issued a new version of the model treaty that will be dated July 2005. (See *Tax Notes International*, Sept. 12, 2005, p. 998. See www.taxanalysts.com for a condensed version, including commentary.)

Among other things, this new version has a revised article 26 on information exchange. Under this revision, a country cannot refuse to hand over requested tax information on the ground that its bank secrecy rules would be violated, or its own tax administrator has no need for the information. The country receiving the request would have to tell the requesting country who owned a resident corporation, for example. Other changes in the new model relate to shipping, employee options, cross-border pensions, and multiple PEs.

There are changes to the commentary on source taxation of interest under article 11. The changes, according to Sasseville, "better present the alternative of no source taxation of interest." How's that again? Basically the changes amount to a simplified rewording of the previous capital-exporting country polemic against source taxation of interest, with the assertion that source taxation can be an obstacle to international trade. There is further argument that taxation of the gross amount of interest is somehow unfair to investors who may be using the borrowed funds to earn less than the interest being paid out. Income stripping goes unmentioned; double taxation is still seen as the chief problem.

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