

Peer Exchange Discussion during XIX Session of the United Nations Committee of Experts on International Cooperation in Tax Matters

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Report

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1. Introduction

During the XIX Session of the United Nations Committee of Experts on International Cooperation in Tax Matters (UNTC), the South Centre, in partnership with the International Centre for Tax and Development (ICTD) and the BEPS Monitoring Group, organized an expert-level peer exchange.

The event was conceptualized as a one day expert-level peer exchange open for participation by developing country Members of the UNTC, Member States of the Group of 77 and China (G77) in Geneva and experts or developing country officials working with or nominated by the South Centre or the ICTD. The discussions among participants were held off-the-record.

The aim of the discussion was to better inform participants about the meetings of the UNTC and its subcommittees and generate a thorough dialogue among UN Tax Committee members, G77 members and developing country experts and tax officials on addressing the different matters discussed under the agenda of the UNTC, in particular the challenges on taxing the digital economy and the modifications of the UN Model Convention.

2. Context

The XIX Session of the UN Committee of Experts on International Cooperation in Tax Matters took place in a moment in which long standing traditions and assumptions on tax practices are being reformed. Events are moving at a rapid pace but there is the ever-present danger that the burden of the past may yet impose itself on the future.

Current tax discussions at the international level have focused on the taxation of the digital economy. Different forums have brought possible 'solutions' to the challenges brought by the digital economy. Nonetheless, the OECD has come out with its latest update on Pillar 1, the so-called 'Unified Approach', which states that it is combining elements of the three proposals on taxing the digital economy which are by the US, UK and G24 respectively. Discussions on this matter focus on considering if this proposal has indeed given enhanced taxing rights to source jurisdictions through redefining nexus and profit allocation rules and whether it has addressed the fundamental problems of the arm's length method. Likewise, it is essential to ponder if developing countries concerns and interests are effectively reflected in the proposal, or if it will be ineffective, and if so what can be an appropriate response that safeguards their interests in a balanced way. Looking at the role of the UN Committee in such discussions will also allow developing countries to consider other solutions, for example by re-examining relevant provisions in its own model treaty, notably article 5.3.b for a services PE, or article 7 on attribution of profits.

At the same time, the UN Model Convention is undergoing some significant modifications that would codify rules on some of the most important sources of revenue for the South. There are the proposed changes to Article 13 (Capital gains) which would impact the taxation of offshore indirect transfers of assets other than

immovable property situated in the source country. This strikes at the heart of the perennial charade of mergers and acquisitions taking place through tax havens and countries which try to counter this avoidance being taken to investor-state dispute arbitral tribunals. What are the changes discussed, and how should developing countries respond?

Finally, concerns over collective investment vehicles have also gained attention of the UN Tax Committee. Insurance and pension funds in particular form an enormous aspect of international finance and dwarf the GDP of many countries. Effectively taxing them is a vexed issue that has hurt many developing countries. The discussion focuses around how tax treaties affect the tax treatment of collective investment vehicles. How can treaties be modeled in a way that ensures that these massive funds do indeed enrich the future of the 99% rather than the 1%?

3. Summary of discussions

Introducing the issues to be discussed during the peer exchange, Abdul Chowdhary, Senior Programme Officer of the South Centre for Tax Matters, considered two challenges that the world is currently facing and the different means that the tax justice movement can use to cope with such challenges.

The first challenge is an upcoming global recession as the global economy is entering a slowdown. For Mr. Chowdhary, monetary policy tools have limited efficacy in reviving growth without exacerbating macroeconomic risks, and therefore fiscal policy has important tools which can be used to face the global recession. For him, taxation in particular has a primary role as redistribution through taxation is an effective method to revive growth – revenue can be raised without increasing debt levels which can in turn stimulate aggregate demand, encouraging private investment to expand, kick-starting the overall economy. It can also reduce inequality, essential in a world where it has reached unacceptable levels and poses a threat to social cohesion. The other great challenge which impinges upon the tax justice movement is climate change. For Mr. Chowdhary, taxation is the foundation on which resources are mobilized to finance the climate transition and the reason why the South Centre Tax Initiative (SCTI) is a subset of our Sustainable Development and Climate Change Program.

He continued by explaining that the South Centre, as an intergovernmental organization of developing countries, stands ready to provide all the resources needed to achieve this goal for developing countries, so that they can proactively advance and set the agenda of international tax matters.

For achieving these goals, the SCTI core objective is the establishment of a peer exchange network, where experts and government officials could exchange their knowledge and expertise to strengthen a 'community of practice'. Such endeavor will be accompanied by workshops that provide technical skills, for example through learning software to analyze data obtained through exchange of information agreements. Likewise, he explained that the SCTI seeks to amplify the voice of

developing countries in the forums responsible for making the rules of international tax. The efforts of the South Centre will focus on providing what he called a 'megaphone' to the voice of the South in as many of these forums as possible. He continued by mentioning that the series of events organized by the South Centre will give special focus to what the OECD does not generally address, such as extractives or fugitive economic offenders. Finally, Mr. Chowdhary emphasized that the Tax Initiative will also support Member States submit responses to international tax policy proposals, such as those routinely put out by the OECD. By having more and more countries 'speak up', developing countries will strengthen their position in shaping the agenda in the favor of the South.

3.1. Digital Economy- Nexus Rules and Allocation of Taxing Rights and Income

After the short introduction to the South Centre Tax Initiative and presentation of participants, discussions flowed to challenges faced by developing countries in the taxation of the digital economy. One participant stressed that digital tax is a low hanging fruit because the economy is becoming service oriented. He continued by mentioning that developing countries could benefit from adopting Article 5.3(b) of the UN Model Tax Convention which states that the provision of services, including consultancy services, qualifies for a Permanent Establishment (PE) and hence nexus. The interpretation of a group of countries favors the idea that no physical presence is required to allocate taxing rights to the 'host state'. He mentioned that this option could be an alternative to the position of the OECD, and that the time framework established by the provision should not be a limit for starting the conversation on its reform.

Following this statement, one of the participants inquired if this discussion will be part of the agenda of the UN Tax Committee or if it will be a new agenda. Another participant explained that provision 5.3(b) was interpreted differently by different countries. In some cases, countries considered that allocation of taxing rights will not require the physical presence of agents of foreign company for 6 months, as long as services were rendered for that period of time. Others on the contrary, consider the need for physical presence was required. Nonetheless, the same participant was of the view that the world has changed since this provision was conceived, and that the OECD is bringing a new nexus provision, an additional parallel provision. For him, the UN Model already includes a virtual nexus provision, but this understanding should be refined.

Another participant explained that the previous UNTC considered the interpretation of provision 5.3(b) and that there was a lot of debate on whether it was meant to be a physical presence. Discussions went to recognize that such establishment was to be done to employees, making them resident in 'source state'. He considered that there might be room for looking back at this issue, but it will require a 'big fight' to touch it again, especially if the UN is attempting to get ahead on the digital economy. The UN has always been ahead, it had identified the BEPS issues, but the OECD pushed it aside. It was stressed that the work of the UNTC is hampered by its lack of resources, and the committee composition made it difficult to move, since there are vested

interests that block it. The UN has had it for years and has been unable to develop it. The interpretation of provision 5.3(b) is a great proposal, those who have it in their treaty can interpret it as they want and should not be bound by the commentary.

For another participant, although consistently interpreting the provision in question as not requiring physical presence could be an alternative, achieving such a solution is not simple, as provision 5.3(b) is subject to a number of interpretations. Similarly, another participant considered the need to pay attention to power dynamics in the committee. This concern was shared by another discussant who considered that given the Committee's dynamics, changing the commentary and interpretation to Article 5.3(b) might not be very advisable since there are interpretation issues. The participant was of the view that adding new content to the commentary would be like having a new provision altogether, and therefore a possible solution could be to confine the debate to whether it already caters to digital economy or not.

The time period of 183 days as threshold was also an issue of concern. Some participants considered that this time framework could leave several services out of tax liability. Given the time and budgetary limitations of the UNTC, some discussants considered that it might be more important to review the OECD secretariat proposal and analyze its pros and cons, and then propose alternatives. One stated that though it called itself a 'Unified Approach' and claimed to include common elements from all three proposals, in reality it was entirely the US' approach of marketing intangibles. This was also a concern brought by another discussant who considered the need to clarify the role of the Committee, particularly how it will deal with OECD outcomes and how to propose new alternatives. A participant responded to this concern explaining that the Committee is preparing a chapter on alternative approaches to digital taxation, and that efforts should be kept on that basis for now and that expert views are necessary on this matter.

3.2. Updates to UN Model Convention

After discussion on the challenges allocating taxes in the digital economy, the discussions centered on the new updates to the UN Model Convention (UNMC) and its possible reform. One participant started the discussion by examining some of the changes proposed to the definition of beneficial ownership. The Subcommittee on updating the UN Model Convention proposed that the latest OECD Model commentaries on the concept of beneficial ownership be incorporated into the UN Model. The changes also sought to give beneficial ownership a "contextual" meaning that cannot be interpreted with reference to domestic law. The participants discussed the pros and cons of these changes.

Another topic was the taxation of offshore indirect transfers (OIT). A paper prepared by the UN Committee member from India gave developing countries two suggestions on effectively taxing OITs: 1) ensuring that domestic laws allow taxing the gains of an OIT and 2) ensuring that bilateral treaties are drafted in a way that preserve domestic laws ability to impose the tax. Participants discussed these aspects along with the practical challenges of administering withholding taxes on OITs.

The last aspect discussed dealt with tax treaties and collective investment vehicles (CIVs). A note prepared by the UN Tax Committee's Secretariat raised the following questions: 1) should a developing country include provisions on collective investment vehicles in its tax treaties? 2) The impact of different CIV structures on their taxation, particularly the role of trusts? 3) Should foreign pension funds be entitled to treaty benefits? 4) Whether and to what extent the income of pensions funds should be exempt from source taxation? The subsequent discussion threw up more questions on answers, revealing how much ground needs to be covered on taxing CIVs.

Another discussant explained that their research has been focused in collecting data from African countries with regard to CIVs. Finally, the discussants also commented on the difficulties brought by the traditional view of permanent establishment in these areas, and problems of avoiding payment of VAT on management fees.

4. Conclusion

The discussion was regarded as useful by the participants, particularly the members of the UNTC. They requested the South Centre, ICTD and civil society members to continue providing inputs which would assist their work. Of particular interest were alternative proposals on taxing the digital economy. The South Centre assured the Committee Members of its continued support and enhanced engagement in subsequent tax discussions.

Annex - Pictures

