

Comments on CRP12 (Technical Changes proposed for the 2021 Update of the UN Model)

-Rajat Bansal, Member, UN Committee

1. Part D (Clarification that registration for VAT/GST purposes is not relevant for determining a PE under a tax treaty): Justification given in para 9 of CRP21 is that large number of countries have VAT or GST. While it is true that mere registration for VAT or GST without a fixed place of business cannot be regarded as a permanent establishment, there may be relevance of VAT or GST registration for deciding on PE existence provided other conditions in Article 5 are fulfilled. Hence, there is no need to add paragraphs in OECD Commentary to UN Commentary in this regard. The Committee may discuss this matter.

2. Part K (Reference to a full credit in paragraph 63 of the Commentary on Article 23B):

At present paragraph 48 in the Commentary provides that if the withholding tax levied under para 2 of Articles 10,11 etc in source country is higher than the tax in residence country, if the Contracting States wish, they can agree for full credit by residence country. This can be achieved by deletion of second sentence of para 1 of Article 23B. It is an alternative only in the Commentary, which should not be done away with being in the interest of developing countries. In sum, I do not support changes in UN Commentary as per K. This issue was raised by me through written comments before the Subcommittee in its meeting on 4th May. However, through majority vote of those present, it was turned down. In this regard, attention is also drawn to para 2 of UN Model Commentary (which is not a quotation from OECD Commentary) on para 1 of Article 10 of UN Model as below:

*'2. This paragraph, which reproduces Article 10, paragraph 1, of the OECD Model Convention, provides that dividends may be taxed in the State of the beneficiary's residence. It does not, however, provide that dividends may be taxed exclusively in that State and therefore leaves open the possibility of taxation by the State of which the company paying the dividends is a resident, that is, the State in which the dividends originate (source country). When the United Nations Model Convention was first considered, **many members of the former Group of Experts from developing countries felt that as a matter of principle dividends should be taxed only by the source country. According to them, if both the country of residence and the source country were given the right to tax, the country of residence should grant a full tax credit regardless of the amount of foreign tax to be absorbed and, in appropriate cases, a tax-sparing credit. One of those members emphasized that there was no necessity for a developing country to waive or reduce its withholding tax on dividends, especially if it offered tax incentives and other concessions. However, the former Group of Experts reached a consensus that dividends may be taxed by the State of the beneficiary's residence. Current practice in developing/developed country treaties generally reflects this consensus. Double taxation is eliminated or reduced through a combination of exemption or tax credit in the residence country and reduced withholding rates in the source country.'***

The above reflects the view of developing country Members of erstwhile Committee and has not been taken into account while proposing changes as in K. I strongly request Committee not to make changes as per K as these are not in interest of developing countries.

(By the way, there is a typo in para 48. It should be paragraph 1 at the end and not paragraph 2)