

NEW INTERNATIONAL TAX TOOLKIT: HELPING DEVELOPING COUNTRIES UNLOCK BILLIONS FOR SDG FINANCING



Telecom antenna tower

On 3 June 2020, the Platform for Collaboration on Tax (PCT)—a joint initiative at secretariat level of the IMF, OECD, UN and World Bank Group—released the Toolkit on the Taxation of Offshore Indirect Transfers (OIT), which you can access [here](#).

The toolkit provides guidance on the tax treatment of sales of assets located in one country by an entity which is a tax resident in another country. Such sales of offshore holding entities deprive developing countries of billions of dollars in capital gains taxes, particularly in the case of mining and telecommunications assets.

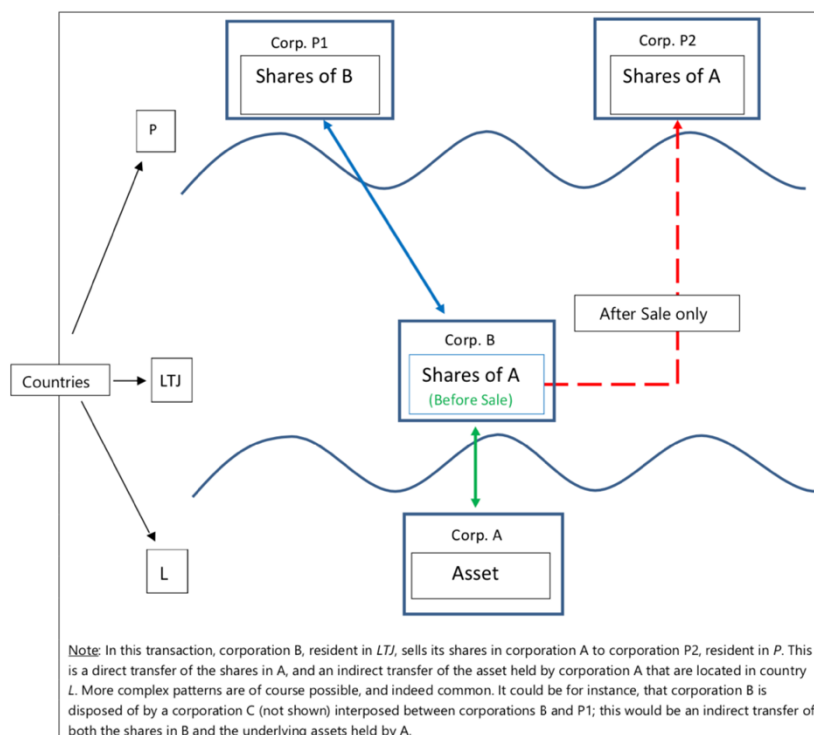
What is an "Offshore Indirect Transfer" (OIT) and why has it attracted so much public interest, particularly in developing countries?

Developing countries have long aired their grievances about OITs, but only recently did the problem gain traction as a high-priority tax issue.

An offshore indirect transfer refers to any arrangement where the interest in an asset, such as the share of a corporation, switches hands via an intervening entity *that does not reside in the country where the asset is located*. The change in ownership, either full or partial, is therefore indirect.

Given that OITs occur beyond the jurisdiction where the underlying asset is located, multinationals can accrue significant capital gains while escaping taxation. This also

Figure 1: Stylized Example of an OIT Structure



Source: [Toolkit on the Taxation of Offshore Indirect Transfers](#)

means that, when not taxing profits generated by OITs, host countries risk losing out on vast amounts of revenue. The significance of OITs particularly shows in its impact on resource-rich developing countries, whose economies rely heavily on extractive industries.



Social Distancing in the Market in Kenya; Photo: World Bank

Where does the tax treatment of OITs currently stand in international and domestic law?

Two international model tax conventions provide guidance on the treatment of OITs: the [UN Model Convention](#) and the [OECD Model Convention](#). Each model outlines a basic provision, Article 13(4), allocating the right to tax indirect transfers of immovable property. Both allocate the primary right to tax to the country where the immovable property is located, regardless of the residence of the company (or other vehicle) owning that property. The article is in effect, however, in only about 35% of all Double Tax Treaties. Where one treaty party is a low-income country, it is even less likely that such a provision is included.

The UN Model Convention, in its Article 13(5), extends the reach of offshore taxation beyond immovable property to also include shares (or comparable interests) of a company, partnership or trust resident in the source country, though this liability falls only on offshore *direct* owners of such entities. The OECD Model Convention has no such provision.

Ultimately, it is up to each country to design and enforce domestic legislation around such transfers: if it expects to derive benefits from taxation, as not all do. In other words, international treaties can motivate these efforts, but only domestic law can put them into force.



A bucket wheel excavator in an open pit mine.

While there is no approach recommended across the board, there is a need for broad practical guidance that will enhance tax certainty and bring coherence to international tax arrangements. Otherwise, developing countries leave a critical source of revenue from OITs largely untapped.

The United Nations and its expert tax committee took an early lead in identifying and addressing this complex problem, through the UN Model Tax Convention and [UN Handbook on Extractive Industries Taxation](#). The United Nations is now developing a new tax treaty provision in order to allow developing countries to have the right to tax capital gains derived from offshore indirect transfers in situations not addressed in the current UN Model (see note [E/C.18/2020/CRP.11](#)).

Enter: A new Toolkit on the Taxation of Offshore Indirect Transfers. What is the toolkit, and how can it help developing countries expand their revenue collection?

The Platform for Collaboration on Tax produced the first joint draft of the OIT toolkit in 2017. Two rounds of public consultation in 2017 and 2018 resulted in a rich and diverse set of inputs and viewpoints from country authorities, industry, academia and civil society.

The specifics of the toolkit are not meant to be binding, authoritative or standard-setting in any way. The toolkit offers advice—from a technical standpoint—to any country seeking to counter the evasive behavior of multinationals by way of confronting offshore indirect transfers.

The toolkit gives context to practical insight within a detailed discussion of the economic and legal considerations surrounding OIT taxation. It also examines past occasions when countries took unilateral action to tackle instances of OITs.

In three highly publicized cases involving India, Peru and Uganda as the source countries, each respective tax authority claimed US\$2 billion, \$482 million and \$85 million in capital gains tax revenue, respectively. Each country lost in court—or at least has not yet clearly won.

Nonetheless, the cases demonstrate growing efforts by source countries (e.g. Peru and Chile) to introduce new domestic legislation to tax offshore transfers.



The toolkit weighs the pros and cons of existing models that countries can select from and apply to the development of domestic legislation.

Each country will want to shape its own investment climate in line with national political, economic and social objectives. Harmonizing applications of international and domestic tax law is a tricky middle ground to navigate. With this toolkit, however, any interested tax authority will be equipped with constructive knowledge on how to amend its current legal system on the basis of internationally recognized, model conventions.

For more information:

The launch of the PCT toolkit will be complemented with a launch webinar later in June 2020. French and Spanish versions of the toolkit will follow, plus virtual learning opportunities based on the toolkit.

For the official press release and access to the toolkit, click [here](#).

For more about the Platform for Collaboration on Tax, click [here](#).

