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**Committee of Experts on International
Cooperation in Tax Matters
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Item 3(c) of the provisional agenda

**Issues related to the United Nations Model Double Taxation Convention between
Developed and Developing Countries**

The treatment of income arising from extractives and other natural resources

Summary

At its Twenty-eight Session, the Committee discussed E/C.28/2024/CRP.14, which included a proposed new Article 5A and draft Commentary that would establish lower thresholds for source State taxation with respect to certain natural resource activities.

The Subcommittee considered comments made at the Twenty-eighth Session and several written comments received afterwards. It now presents a revised text of Article 5A and its Commentary for the Committee's consideration.

The Committee is invited to ***discuss and approve*** the draft provision set out in paragraph 8 and the proposed Commentary in paragraph 9.

I. Introduction

1. At its Twenty-third Session, the Committee of Experts identified “[t]ax treaty provisions related to exploration and extraction of natural resources” as a priority issue to be considered in conjunction with the next update of the UN Model. At the same session, the Committee approved a mandate for a Subcommittee on Extractives Industry Taxation, which includes as an item “Work on tax issues related to tax incentives and permanent establishment, with the view to minimizing tax losses and contraction of the tax base.” At the Twenty-fourth Session of the Committee, the workplans for both Subcommittees were approved.

2. The importance of this issue to many developing countries is discussed in the United Nations Handbook on Selected Issues for Taxation of the Extractive Industries by Developing Countries:

2.1.3.1 Developing a country’s natural resources can provide a significant boost to economic development for a country. Planned well, and implemented accurately, natural resource development can provide revenues and other economic benefits to a country and its citizens. Special considerations are required when a country decides to develop its natural resources since such resources are finite; the country would thus generally focus on obtaining the maximum benefit from the “one-time” extraction of such natural resources. From an investor stand-point, extractive industries investment has unique considerations as compared to regular investments. While the resources are finite, their extraction and development are risky and capital intensive, with large investment required at the early stages of the project life and a long lead time until profitability is achieved. The sector also requires highly specific expertise for extraction and development.

2.1.3.2 Countries embarking on natural resource development will seek to find a balance between achieving a maximum benefit for the country in a sustainable way, while providing investors with a return on their investments commensurate with the risks taken...

3. In discussing this issue, the Subcommittee was of the view that many of the considerations set out in paragraph 2 are not limited to finite resources but apply also to renewable resources. Accordingly, at the Twenty-eighth Session of the Committee, the Subcommittee presented [E/C.18/2024/CRP.14](#), which included a new Article 5A and draft Commentary that would establish lower thresholds for source State taxation with respect to certain natural resource activities involving both non-renewable and renewable resources. The drafting of that note benefited from close coordination with the Extractives Subcommittee.

4. The report of the Twenty-eighth Session includes this description of the discussion of [E/C.18/2024/CRP.14](#):

13. [Mr. Protto] then presented a note on the treatment of income arising from extractives and other natural resources ([E/C.18/2024/CRP.14](#)), which included a proposed new article 5A and draft commentary establishing lower thresholds for source State taxation relating to certain natural resource activities. He acknowledged the benefit of close coordination with the Extractives Subcommittee as that provision was being developed.

14. There was general support for the proposed provision, although one observer State suggested that the provision should be included as an alternative in the commentary rather than in the text of the Model Convention, as it might not be applicable to all developing

countries. The same observer indicated a preference for limiting the provision to specialized services, rather than applying it to all services that supported natural resource activities. It was noted that that view had already been addressed in the commentary.

15. Another observer suggested that several provisions that were included in the commentary as alternative provisions, because they had not received sufficient support from participants in the Subcommittee, should form part of the text of the Model Convention. Members and observers also made a number of technical comments with regard to the proposed provision, many of which had already been discussed by the Subcommittee. It was agreed that the Subcommittee would consider the comments and make any appropriate modifications before the twenty-ninth session of the Committee.

5. After the Twenty-eighth Session, the Subcommittee discussed the suggestion that the provision be included in the Commentary as an alternative provision. The Subcommittee does not propose adopting this suggestion as the allocation of income from natural resources to the Contracting State in which the natural resources originate is viewed as a matter of principle that is widely accepted by both developed and developing countries. It is also the case that a country may become aware of the existence of valuable natural resources in its territory only after the date on which a tax convention has entered into force, when it might be more difficult to negotiate a revision that allows it to tax. For these reasons, the Subcommittee was of the view that tax treaties should, as a matter of course, include an article dealing with the issue of natural resources.

6. The Subcommittee has made several other changes to the provision in response to technical comments. They are marked in the draft provision and commentary found in paragraphs 5 and 6.

7. The Subcommittee also notes, for the benefit of the Committee, that work on this provision began before discussion of Article xx. The intention of this work was to allow the country in which natural resources are located to retain taxing rights over the profits generated in connection with the exploitation of those resources. In this regard, Article 12A already generally allows a State to retain taxing rights with respect to technical services related to those activities when fees for such services are paid by a resident of the country or a permanent establishment located in that country. Article 5A, on the other hand, allows for taxation based on where the services are performed no matter who is making the payment. If Article xx is adopted, a State generally will be allowed to tax, under Article xx, all payments arising in that State to persons providing those services. The primary effect of Article 5A in that case, when services relating to relevant activities are performed for more than 30 days, would be to shift taxation from Article xx to Article 7 with respect to income derived by the resulting permanent establishment.

II. Possible Stand-Alone Provision

8. The Committee therefore is invited to discuss the following draft provision:

Article 5A

Income from the Exploration for, or Exploitation of, Natural Resources

1. The provisions of this Article shall apply notwithstanding the provisions of Articles 5, 8 and 14 of this Convention.

2. (a) For purposes of this Convention, a resident of a Contracting State which carries on activities in the other Contracting State which consist of, or are connected with, the exploration for, or exploitation of, natural resources that are present that other State due to natural conditions (the “relevant activities”) shall be deemed in relation to those activities to be carrying on business or performing independent personal services in that other State through a permanent establishment or a fixed base situated therein, unless such activities are carried on in that other State for a period or periods not exceeding in the aggregate 30 days in any twelve month period commencing or ending in the fiscal year concerned.

(b) Article 8 shall apply to income from the operation of ships or aircraft in international traffic constituting relevant activities as defined in subparagraph (a) only if any part of the transport by ships or aircraft constituting such operation is carried out in the other Contracting State for a period or periods not exceeding in the aggregate 30 days in any twelve-month period commencing or ending in the fiscal year concerned.

3. For the sole purpose of determining whether the 30 day threshold in paragraph 2 has been exceeded, where an enterprise of a Contracting State carries on relevant activities in the other Contracting State and substantially the same such activities are carried on in that other Contracting State during different periods of time by one or more enterprises closely related to the first-mentioned enterprise within the meaning of paragraph 9 of Article 5, these different periods of time shall be added to the period of time during which each of the enterprises has carried on such activities.

4. For the purposes of this Article,

(a) the term “natural resources” means natural assets that can be used for economic production or consumption, whether non-renewable or renewable, including fish, hydrocarbons, minerals and pearls, as well as solar power, wind power, hydropower, geothermal power and similar sources of renewable energy; and

(b) the term “exploration for, or exploitation of, natural resources” means any activities carried on in connection with:

(i) the exploration for, or exploitation of, the natural resources described in subparagraph (a), including the extraction, development, production, processing, transport or storage of such natural resources;

(ii) the decommissioning and abandonment of facilities used in connection with the activities described in subdivision (i); and

- (iii) the restoration and rehabilitation of the land or other site used in connection with the activities described in subdivision (i).

III. Draft Commentary

9. The Committee is also invited to consider the following draft Commentary to the provision set out in paragraph 5:

Article 5A

Income from the Exploration for, or Exploitation of, Natural Resources

A. General Considerations

1. This article was added to the Model in [2025] to ensure that the State in which natural resources are located will capture an appropriate share of the location-specific economic rents attributable to these valuable assets. The Committee viewed the addition of such a provision as a high priority because of the importance of natural resources in the economies of many developing countries.

2. Many bilateral tax treaties, entered into by both developed and developing countries, include provisions that deal with natural resources. Such provisions vary significantly; some deal only with hydrocarbons while others address only activities taking place offshore. The inclusion in the Model of Article 5A should support greater consistency of such provisions across treaties, which will aid countries in negotiating such provisions in the future. The Committee decided that the provision should have a broad scope to ensure that it will continue to provide an appropriate allocation of taxing rights as technologies and business models evolve over time.

B. Commentary on the Paragraphs of Article 5A

Paragraph 1

3. Paragraph 1 establishes the relationship between Article 5A and Articles 5, 8 and 14 of the Model. Article 5A provides specific nexus tests that apply notwithstanding the provisions of those other Articles. Accordingly, a resident of a Contracting State that meets the requirements of Article 5A with respect to a Contracting State will have a permanent establishment or fixed base in that State even if it would not have had a permanent establishment in that State under Article 5 or a fixed base in that State under Article 14. Article 5A does not affect the application of Article 6 to income from “rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources” as the taxing rights under Article 6 do not depend on the existence of a permanent establishment.

4. The permanent establishment or fixed base exists for all purposes of the convention. For example, for purposes of Article 13(2), equipment used in the relevant activities in a Contracting State will constitute movable property forming part of the business property of a permanent establishment or pertaining to a fixed base in that State. As a result, such

movable property will be taken into account when determining whether the 50 per cent threshold of Article 13(7)(b) has been met.

5. Furthermore, if an enterprise of a Contracting State has a permanent establishment in the other Contracting State as a result of the application of Article 5A, that enterprise's employees who are working in that other Contracting State and whose remuneration is borne by that permanent establishment will not qualify for the exemption of Article 15(2) with respect to their income from such employment. Article 5A will not have any effect on the treatment under Article 15 of any employees of the enterprise whose remuneration is not borne by the permanent establishment or fixed base, such as auditors or other head office employees who visit a working site for a few days. There is no need for Article 5A to make a specific reference to Article 15 to achieve these results because it is a natural consequence of the existence of a permanent establishment or fixed base of the enterprise.

6. Some countries also wish to tax employment income derived in connection with relevant activities, even if the employer does not have a permanent establishment or fixed base in that State. Those countries may include the following additional paragraph in Article 5A:

Salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment connected with relevant activities in the other Contracting State may be taxed in that other State if the employment is performed in that other State for a period or periods exceeding in the aggregate 30 days in any twelve-month period commencing or ending in the fiscal year concerned.

In that case, paragraph 1 should read as follows:

The provisions of this Article shall apply notwithstanding the provisions of Articles 5, 8, 14 and 15 of this Convention.

7. As discussed in paragraphs 19 and 20 below, paragraph 2(b) of Article 5A limits the application of Article 8 in the case of relevant activities.

8. Some bilateral provisions address additional matters relating to natural resources that are not included in Article 5A. In most cases, this is because such matters are already addressed in a more comprehensive manner (that is, not limited to the context of natural resources) elsewhere in the Model. This is the case, for example, with respect to gains relating to natural resources as Article 13 includes a comprehensive set of provisions allowing for taxation in the situs State of gains from the alienation of a wide range of assets, including gains from the transfer of rights to resources naturally occurring in that State. Another case is fees for technical services related to natural resources. Article 12A of the Model provides that the State in which such fees arise may tax such fees, without the requirement that the beneficial owner have a permanent establishment or fixed base in that State. As noted in paragraph 13 below, many of the services performed by subcontractors fall within the scope of Article 12A.

Paragraph 2

9. Paragraph 2(a) deems a resident of a Contracting State to have a permanent establishment or a fixed base in the other Contracting State if it conducts certain activities in the other Contracting State for at least 30 days in any twelve-month period commencing or ending in the fiscal year concerned. The “relevant activities” consist of, or are connected with, the exploration for, or exploitation of, natural resources in that other State, as defined in paragraph 4.

10. Paragraph 2(a) refers to activities conducted “in” a Contracting State, and natural resources that are present “in” a Contracting State due to natural conditions. These are two different requirements, each of which must be met in order for Article 5A to apply. For example, ore may be extracted from Country A and transported to Country B for smelting. The extraction activities in Country A would be covered by Article 5A, as would the transport from Country A to Country B. However, the smelting process in Country B would not be covered as the ore is not present in Country B as a result of natural conditions.

11. There is no question that activities taking place on land, such as mining activities, fall within the scope of paragraph 2(a). Although Article 3 (Definitions) of the Model does not include a definition of each of the Contracting States, many, if not most, bilateral treaties include such definitions. These definitions generally are intended to ensure that activities taking place offshore in areas over which a Contracting State exercises certain economic rights will give rise to the same taxing rights as such activities that take place onshore. Care should be taken to ensure that any definition of the Contracting States included in Article 3 supports the intended allocation of taxing rights under Article 5A.

12. In many cases, an enterprise engaged in relevant activities will have one or more permanent establishments in a Contracting State under Article 5 because its facilities will constitute a fixed place of business through which the business of the enterprise is carried on, within the meaning of Article 5(1). For example, production facilities represent significant capital investments and therefore are relatively permanent, so that they will meet the six-month rule of thumb applicable under Article 5(1); in those cases, the lower, 30-day threshold provided by paragraph 5A(2) therefore generally will not expand the source State’s taxing rights. The detailed guidance under Article 5 should be applied to determine when the permanent establishment is created and when it ceases to exist with respect to those enterprises.

13. Paragraph 2(a) will be most relevant to the taxation of contractors and subcontractors. For example, in the absence of Article 5A, independent drilling contractors engaged in the exploration for oil could spend significant amounts of time on a country’s continental shelf without establishing a fixed place of business within the meaning of Article 5. Similar considerations could apply to operators of windmill farm vessels, which engage in the construction, maintenance, repair and disassembly of windmills at sea. Under Article 5A(2), they will be treated as having a permanent establishment as soon as they are engaged in such activities in a Contracting State for more than 30 days.

14. A [XX minority] of the Committee were of the view that the State in which natural resources are located should have the right to tax relevant activities without a threshold.

Countries sharing that view with respect to either 2(a) or 2(b) or both are free to use the following versions of those paragraphs:

2. (a) For purposes of this Convention, a resident of a Contracting State which carries on activities in the other Contracting State which consist of, or are connected with, the exploration for, or exploitation of, natural resources in that other State (the “relevant activities”) shall be deemed in relation to those activities to be carrying on business or performing independent personal services in that other State through a permanent establishment or a fixed base situated therein.

(b) Article 8 shall not apply to income from the operation of ships or aircraft in international traffic constituting relevant activities in a Contracting State as defined in subparagraph (a).

Inclusion of these paragraphs would result in an enterprise engaged in relevant activities in a Contracting State being deemed to have a permanent establishment in that State and being subject to taxation of the relevant income under Article 7.

15. Many of the services performed by contractors will also constitute “technical services”, fees for which would be taxable under Article 12A. However, once the 30-day threshold has been met, so that the contractor is deemed to have a permanent establishment or fixed base, paragraph 4 of Article 12A provides that such fees will be taxable under Article 7. The same would be true of any income from automated digital services that were connected to relevant activities in the Contracting State.

16. Paragraph 2(a) applies to all persons conducting activities that take place in connection with the exploration or exploitation of natural resources, not only those persons who are performing specialized services. Accordingly, the provision would apply to contractors who provide, for example, catering services on an oil rig or at a mining facility. It will not matter if this catering company also provides services to other non-extractive businesses around the world. The provision will not apply, however, to persons conducting activities that utilize the natural resources in businesses that are not connected to exploration or extraction, such as enterprises using steel or aluminum to manufacture automobiles. Some Members of the Committee expressed concern that the services were not limited to specialized services, noting that two companies providing the same service may be treated differently depending on whether they provide the service at a mining facility or a non-extractive business location.

17. The determination of whether the 30-day threshold has been met is made independently with respect to each taxpayer. If a taxpayer’s relevant activities continue in a Contracting State for 30 days or more, the taxpayer will have a permanent establishment from the day that its activities begin, without regard to whether or when any other entity (such as a license holder) has a permanent establishment. In the example in paragraph 12, the drilling contractors would have a permanent establishment if their activities continue for at least 30 days, even if the company for which they are providing the services never has a permanent establishment. Conversely, a mining company may have had a permanent establishment for years, but an independent contractor brought in to conduct a rescue after a mine cave-in will only have a permanent establishment or fixed base under Article 5A if the 30-day threshold is met with respect to the activities of that contractor.

18. Article 5A merely changes the relevant threshold for source State taxation under Articles 7 and 14. The manner of taxation under those articles is not changed by Article 5A.

19. Paragraph 2(b) provides that Article 8 will apply to income from the operation of ships or aircraft in international traffic that constitute relevant activities only if any of the transport constituting such operation continues in that State for 30 days or less. In the case of international traffic that involves transport that takes place between the state in which natural resources are present and another state, days in which any part of the transport that constitutes relevant activities takes place in the Contracting State are counted in order to determine whether the 30-day threshold is met.

20. This provision will be most relevant when the relevant bilateral treaty includes Article 8 (Alternative A), which provides for exclusive residence State taxation. In that case, an enterprise of a Contracting State that was engaged in transporting ore from a mine in the other Contracting State to a processing facility outside that other State would not be taxable in that other Contracting State on the income from such transport. The Committee viewed this result as inequitable and provided, in subparagraph 2(b), for taxation in the State in which the ore is mined as long as the shipping enterprise conducts its activities in that State for at least 30 days in the relevant twelve-month period.

21. Paragraph 2(b) applies only if the international transport is “connected” to the exploration or exploitation of natural resources. Accordingly, it would apply to flights that are contracted or chartered to transport personnel to a remote mine or oil rig but not to regularly-scheduled commercial flights that happen to carry such personnel to an airport close to a mine.

Paragraph 3

22. Paragraph 3 provides rules for aggregating the activities of related parties for purposes of determining whether the 30-day threshold in paragraph 2 has been exceeded. The aggregation rule is intended to prevent taxpayers from avoiding the time threshold by artificially splitting activities between different related entities. If they do, the period of time that each of the enterprises conducts such activities shall be added to the period of time during which the closely-related enterprise has carried on such activities in order to determine whether each of them has exceeded the 30-day limit.

23. Thus, the rule will not apply to the extent that the activities of the two persons are being carried on at the same time. For example, if an enterprise of State R that carries on exploration activities for twenty days in State S is closely related to another enterprise of State R, and that closely-related enterprise carries on substantially similar exploration activities in State S for twenty days after the first-mentioned enterprise has ceased such activities in State S, each of the enterprises will be deemed to have satisfied the threshold so that the income derived from the relevant activities will be attributable to a permanent establishment of that enterprise. For purposes of paragraph 3, paragraph 9 of Article 5 will be used to determine whether two persons are closely related to each other.

Paragraph 4

24. Paragraph 4 defines the terms that are used in the substantive rules of Article 5A.

25. Subparagraph 4(a) defines the term “natural resources” as any natural assets that can be used for economic production or consumption, whether non-renewable or renewable, including fish, hydrocarbons, minerals, pearls and solar power, wind power, hydropower, geothermal power and similar sources of renewable energy. Renewable natural resources are those that are not reduced by their exploitation or that, after exploitation, can return to their previous stock levels by natural processes of growth or replenishment while non-renewable natural resources are exhaustible natural resources such as mineral resources that cannot be regenerated after exploitation. The list of specific natural resources is not exclusive; the term is intended to be expansive and flexible. In determining whether it applies in other circumstances, the key issue is whether the exploitation of the product results in location-specific economic rents.

26. Under subparagraph 4(b), the term “exploration for, or exploitation of natural resources” is intended to cover every stage in the value chain, from exploration to decommissioning. This is necessary because, even though a company may not have started, or may no longer be, generating income from production activities in the situs State of the natural resources, contractors may be doing so.

27. Accordingly, subparagraph 4(b) specifically refers to the exploration or exploitation of the natural resources described in subparagraph (a), including the development, production, processing, transport or storage of such natural resources and the decommissioning and abandonment of facilities used in connection with such activities and the restoration and rehabilitation of the land or other site. “Processing” can relate to either non-renewable resources (refining or smelting of ore, for example) or renewable resources (e.g., fish processing on a ship). As in the case of subparagraph (a), the listed activities are intended to be illustrative, not exhaustive.

IV. Issues for the Committee

10. The Committee is invited to *discuss and approve* the draft provision set out in paragraph 8 and the proposed Commentary in paragraph 9.