

# WATAF COMMENTS FOR INC/WORKSTREAM

## WORKSTREAM II

**1. Current taxation rules and why change is needed.** The two tax systems presented by the developing and developed countries are:

Developing countries use withholding taxes on gross income, regardless of where services are performed. It is easier to enforce and avoids complex calculations while the developed countries prefer net income taxation based on where services are physically performed.

With respect to the above views by the developing and developed countries, the following issues are identified: Older tax treaties limit the ability of developing countries to impose their preferred tax methods (gross-basis withholding taxes on payments to non-residents).

Transfer pricing rules are hard for developing countries to apply due to insufficient databases, capacity, and resources.

The rules that limit source-state taxation do not reflect the current ways of doing business (digital age), where services can be provided remotely without physical presence.

**2.** Future drafts can strongly emphasise the right of developing countries to **tax services that are consumed in their jurisdiction**, especially when the service provider has no physical presence but earns income from their markets. In essence, the gross-based withholding taxation system which is easier and preferred by developing countries should be encouraged in instances where it is practicable, e.g with respect to traditional business to business services where deduction is possible. It seems less cost burdensome to manage in small open economies such as in some WATAF member states. With regards to a more complex digital services and Business to consumers services, a more innovative approach may be adopted to ensure effective collection of taxes. A net-based approach may also be made optional where the services can be attributed to a PE or where the taxpayer has sufficient and accurate documentation.

**3.** WATAF emphasises the need for clear definitions of fairness and independence in dispute resolution mechanisms, given the potential for subjective interpretations.

**4.** The old tax treaties that limit the ability of developing countries to impose their preferred **tax methods can be updated**. The reason is that these tax treaties are usually in favour of the source countries. The protocol could provide clear guidance to update outdated treaty provisions, to allow developing countries to reclaim their taxing rights in the current globalized, digitalised economy.

**5.** It has been stated clearly that transfer pricing methods are difficult for developing countries to put in practice due to lack of data, capacity and resources. To this effect, WATAF agrees that it is pertinent that the protocol could allow for **simple administrable**

**rules** rather than relying on complex transfer pricing. Moreover, State parties could include **database development and exchange of information as parts of the infrastructure to build**<sup>1</sup>.

6. Finally, the population in the developing countries provide the market for the services rendered by the source countries, and knowing fully well that there cannot be profitable supply without adequate demand for the services supplied, the developing countries could be given the right to a fair<sup>2</sup> share of the tax base.