



OECD Tax Developments

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Themes of the OECD's Recent Work

- Measuring and allocating international income with uncertain jurisdictional connections
 - “Source”
 - Treaty benefits
 - Measurement standards for transfer pricing
 - Adjusting for changes in jurisdictional “business intensity” within multinational groups
- International tax avoidance
 - “Transparency” and co-operation by tax administrators
 - Financial transactions by / facilitated by banks

OECD Projects I – Transfer Pricing

■ Transfer Pricing

- Continuing study of “business restructuring” and collection / evaluation of comments on September 19, 2008 Discussion Draft “Transfer Pricing Aspects of Business Restructurings” including June 2009 conference
- Proposed revisions of Transfer Pricing Guidelines on September 9, 2009 in “Proposed Revision of Chapters I – III of the Transfer Pricing Guidelines” and collection / evaluation of comments

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OECD Projects II – The OECD Model Tax Convention And Commentary

■ Revisions of the Model Tax Convention

- “Revised Discussion Draft of A New Article 7 of the OECD Model Tax Convention (November 24, 2009)
- “Discussion Draft on Tax Treaty Issues Related to Common Telecommunications Transactions (November 25, 2009)
- “Discussion Draft on the Application of Tax Treaties to State-Owned entities, Including Sovereign Wealth Funds” (November 25, 2009)

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OECD Projects III – The OECD Model Tax Convention And Commentary

- Discussion Draft -- "The Granting of Treaty Benefits with Respect to Income of Collective Investment Vehicles" (December 9, 2009)
 - Related to Discussion Draft -- "Report by the Pilot Group on Improving Procedures for Tax Relief for Cross-Border Investors Possible Improvements to Procedures for Tax Relief for Cross-Border Investors: Implementation Package" (February 8, 2010)
- "Discussion Draft On the Application of Article 17 (Artistes and Sportsmen) of the OECD Model Tax Convention" (April 23, 2010)

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OECD Projects IV – Tax Avoidance and Tax Compliance

- "Building Transparent Tax Compliance by Banks" (May 28 / 29, 2009)
- "A Framework for Successful Offshore Voluntary Compliance Programmes" (January 15, 2010)
- "Promoting Transparency and Exchange of Information for Tax Purposes" (March 24, 2010)
- Protocol to amend the Convention on Mutual Administrative Assistance in Tax Matters (Agreement by the OECD and Council of Europe April 4, 2010 – Canada as signed but not ratified)

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Measuring International Income – Changes In Business

- “Business restructuring”
 - Changes in the intensity with which business is conducted in a particular jurisdiction
 - Key considerations:
 - “Profit potential”
 - “Intangibles”
 - Conduct of rational self-interested economic actors
 - The nature of a multinational group and “substance”
 - In short, two issues
 - Mobile income
 - Infirm or doubtful jurisdictional connections

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Measuring International Income – What is the Standard?

- Transfer pricing methodologies and analysis
 - Denial of “formulary”, reinforcement of the analytical integrity and administrative hegemony of the “arm’s length principle”
 - Affirmation of profit based methods
 - Focus on (economic) substance

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Measuring International Income – Significance for Canada

- Economic analysis may illuminate taxpayers' business choices and assist to quantify value, but is it a substitute for the tax system legislating when transfers of value ("soft intangibles") referable to commercial events?
 - "Taxable object"
 - "Taxable event"
- Focus is on international profit allocation
 - Canada-United States Income Tax Convention adopts PE income attribution standards akin to OECD's which rely on transfer pricing

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Measuring International Income – Article 7

- Recognizing "dealings" as commercial events and "economic ownership" of holdings of property producing income
- Adjustments of income and relief of double taxation applying entity-entity standards / approaches
- Connection to OECD Report "Attribution of Profits to Permanent Establishments" – Transfer pricing influence
 - Expects profits to be determined in the same way for all relevant countries

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Sovereign Wealth Funds – Conceding Tax Base

- “Residence”
- OECD’s focus
 - Relief from tax separate from “customary international law” principle of “sovereign immunity though results could be compatible
 - No presumptive relief; depends on whether fund acting qua government or in another capacity, i.e., as a business
 - Consider Canada-US Income Tax Convention, Article XXI
- Justification for ceding tax base

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Telecommunications Income – Where is it?

- “Source”, payments for “use”, “at disposal”
- Where is the income earned?
 - Permanent establishment?
 - Carrying on business?
 - When is property “used”?
 - Commercial law analysis
 - Services versus lease payments
- In microcosm, thinking about mobile income where the commercial nature of the activity is not clear and the income’s connection to any “place” may not be readily sustainable using typical measures

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Collective Investment Vehicles

- When should treaty – based tax concessions, i.e., relinquishing tax base, take place?
- Following portfolio income to its “owners
- Applying treaty principles: “person”, “resident”, “beneficial owner”
- Relief in spite of application of treaty principles allocating tax jurisdiction – Common standards but no common solution; compliance issues paramount
- Treaty policy, i.e., “treaty shopping”

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Artistes and Sportsmen – Article 17

- Income earning activities are mobile because the earners are mobile
- Questions arise about connections of direct and related income (i.e., sponsorship) to particular jurisdictions and how allocated income is to be computed
- Where is income derived? Where is the income earning activity “exercised”
- Fundamental “source” and “allocation” issues – analogue for more typical business income issues

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Themes?

- Income associated with “high value” inputs of business is mobile, and not readily associated with particular jurisdictions
- Treaty partners may not apply common income measurement standards; taxation “in accordance with” a Convention as the portal for treaty relief increasingly more important
- Qualitative, legal, economic and practical judgements underlying sharing tax base more difficult as traditional “signposts” become more

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Back to the Future?

- Recall early work on international income allocation, notably “transfer pricing” and treaties
 - League of Nations (1920s)
 - Mitchell B. Carroll
 - OEEC
 - OECD
- Accommodate international trade; tax accommodations amount to “commercial” bargains between countries – “quid pro quo’s” according to common approaches / principles

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Where is the Future?

- Adopt “fictions” that as closely as possible reflect how income is earned, which should assist in detecting where and by whom it is earned
 - Where is business capital deployed?
 - What is business capital?
 - Where are the people who conduct the business?
 - Where does business revenue originate and where are expenses incurred in relation to it?
- These underlie Articles 5 and 7 of the Model Tax Convention and their actual treaty analogues

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International Tax Avoidance

- A “new world tax order”?
 - Heightened formal co-operation among tax administrations
 - Heightened sensitivity to perceptions of “tax avoidance”
 - Consistent, if not co-ordinated national reactions to particular formulations of perceived tax avoidance, i.e., “foreign tax credit” transactions
 - Formation of international “compliance vehicles”, i.e., JITSIC
 - Enhanced self-assessment of “tax avoidance” transactions, “Codes of Conduct”

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Some Fundamental Questions

- What is the standard or point of reference for “tax avoidance”?
 - Are experiences by countries common?
 - Comparability of relevant domestic laws
 - How are judgments made?
- Distinguishing between substantive tax avoidance and disclosure / reporting obligations

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Recent Canadian Developments In This Context

- Quebec tax avoidance reporting rules
- Proposed federal tax avoidance reporting rules
- Attention to hybrid entities in Articles IV(6) and (7) of the Canada-United States Income Tax Convention
- TCC inquires about how to establish treaty benefits when treaty partners perceive taxpayers and their circumstances differently
- Attention to hybrid entities and instruments, i.e., proposed “foreign tax credit generator” rules

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Summing Up I

- Each recent development in itself may not seem to be very significant
- However, they reflect common themes, and common insecurities about how robust are the established regimes for rationalizing and allocating international income and countries' tax bases

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Summing Up II

- Looked at together, these developments help to illuminate the significance the OECD's evolving attempts to adapt entrenched international tax notions / "norms", with due regard to their historical antecedents to modern notions of business and prevailing opportunities for commercial and personal mobility
- A common "world tax order" / administration?

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