European Business Initiative on Taxation - EBIT

Comments on the OECD's Discussion Draft on the "Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention"

Mrs Grace Perez-Navarro
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FRANCE

Brussels, 9 February 2012

Dear Mrs Perez-Navarro,

Re: EBIT Comments on the OECD's Discussion Draft on the "Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention"

This letter sets out the comments and concerns of the European Business Initiative on Taxation (EBIT)[1] on the OECD's Discussion Draft on the "Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention"

EBIT considers this to be a very important topic for the business community and therefore we welcome this opportunity to provide our comments on the Discussion Draft.

EBIT wishes to commend the OECD for its work so far. However, EBIT considers that there are a few major concerns which should be addressed and modified by the OECD. These concerns are explained in more detail below.

In developing this submission, EBIT has relied more on the practical and daily experience of its members, who are experienced VPs tax and tax directors of multinational companies, than on a theoretical analysis.

- **Issue 4: Home office as PE (proposed new paragraphs 4.8 and 4.9)**

  This would be the first OECD Model Commentary guidance on Home offices constituting PEs, and could potentially affect most multinational companies. Whilst the comments in proposed new paragraph 4.8 are arguably reasonable, including the question of whether the employer has required the employee to work from home, EBIT believes that there is no obvious logic apparent in the distinction drawn in paragraph 4.9 between the non-resident consultant present for an extended period (undefined) in another state and working from a presumably temporary "home" (as opposed to a hotel) as a PE, and the cross-frontier worker performing most of their work from their home rather than in the office made available to them in the other state not being a PE. The consultant may well simply choose to work from home, rather than being required to do so by their customer, as compared with the employer in the other example. If this is the decisive criterion envisaged by WP1, then the comments in paragraph 4.9 do not necessarily follow.

[1] At the time of writing this submission, members of EBIT included: AIRBUS, BP, CATERPILLAR, EADS, GE, DEUTSCHE LUFTHANSA, INFORMA GROUP, MTU AERO ENGINES, NUTRECO, REED ELSEVIER, ROLLS-ROYCE, ROMPETROL GROUP, SAMSUNG ELECTRONICS, SES GLOBAL and TUPPERWARE.

- **Issue 6: Time requirement for the existence of a PE (paragraph 6 of the Commentary)**

  Paragraphs 6.1 and 6.2 propose exceptions to the general practice of Contracting States that, unless a place of business is maintained for six months or more, it does not constitute a PE. The two examples of annually recurrent 5 week presence at an international commercial fair, and the single four month operation of a restaurant in a house in connection with filming a film on location may of themselves not be of general application, but the carving out of exceptions from the current norm that places of business operated for less than six months don't constitute a PE is clearly a seriously unwelcome development as far as EBIT is concerned. What would be then be the minimum time threshold for a PE? To EBIT this proposed change appears to be hostage to fortune to source tax based countries, particularly in a year when the UN is renewing their Model Tax Convention

- **Issue 7: Presence of foreign enterprise's personnel in the host country (paragraph 10 of the Commentary)**

  Whilst the proposed changes to paragraph 10 regarding secondees are helpful, the comments in paragraph 44 are of concern. These relate to the situation where a secondee remains on their home country payroll (often for HR / benefits / compensation / currency reasons) and the host company is charged on a cost plus basis. Paragraph 44 mentions the possibility that this cost plus indicates that what the secondee is doing in the host country is not part of the host company's activity but rather part of the home company's activity, hence there is PE exposure. Reference is then made to the criteria in paragraphs 8.13-8.15 of the Model Commentary regarding the host state company being the "economic employer " for Article 15 183 day protection purposes to avoid a home state company PE in the host country. Whilst the changes are designed to be helpful, given the multiplicity of criteria in paragraphs 8.13-8.15, and the subjectivity sometimes involved e.g. who instructs the individual (matrix management), the outcome may not always be certain. In the worst case, this might leave MNCs with the choice of accepting a local "economic employer" and so host country taxation of secondees even where present for no more than 183 days in the host country or accepting a PE of the non-resident company in the host state.

- **Issue 8: Main contractor subcontracting all aspects of a contract (paragraphs 10 and 19 of the Commentary)**

  EBIT believes that this should surely be dealt with under the dependent agency type PE rule rather than deeming the subcontractor(s) to be a PE of the non-resident main contractor. Also, this "principle" of deeming a third party subcontractor to be a new type of PE of the main contractor could be extended to other industries e.g. financial services regarding brokers acting for non-resident principals. EBIT believes this to be a very unhelpful proposal from the perspective of business.

- **Issue 14: Does a development property constitute a PE? (paragraph 22 of the Commentary)**

  EBIT is of the opinion that the OECD's analysis in paragraph 86 is surely incorrect in terms of interaction of treaty and domestic law. A domestic charge under the Business Profits Article 7 cannot be justified with respect to the host state being permitted to charge under the Capital Gains Article 13. EBIT would like to refer to the Malaysian High Court case of Euromedical Industries, in this respect, where in the absence of a PE, Malaysia's domestic withholding tax on technical assistance fees paid to a UK parent

was blocked (the fees being business profits for treaty purposes rather than royalties, but there being no Malaysian PE).

- **Issue 19: Meaning of "to conclude contracts in the name of the enterprise" (paragraph 32.1 of the Commentary)**

  The proposed addition to paragraph 32.1 will expressly provide that a principal enterprise bound by a contract concluded by another person with a third party would not be protected from having a PE in the country of that other person merely by virtue of that other person not disclosing that it was acting for the principal enterprise in its dealings with the third party. This would in particular appear to be targeted at principals in commissionaire arrangements, but as it is worded it goes much wider than this, so the proposed clarification is not helpful according to EBIT, and the analysis is incomplete. The existence or otherwise of a PE should be with respect to all the facts and in particular the conduct of the parties, and it would be preferable if the revised commentary reflected this.

EBIT would like to encourage the OECD in its consultation and hopes that the above concerns are helpful and are taken into account in your final report. EBIT looks forward to any further discussions in this respect. EBIT can be contacted through its Secretariat.

Yours sincerely,

The European Business Initiative on Taxation – February 2012

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