



April 15, 2024

United Nations Secretariat
Committee of Experts on International Cooperation in Tax Matters
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Re: NFTC Comments on the United Nations Committee of Experts on International Cooperation in Tax Matters Twenty-eighth Session - E/C.18/2024/CRP.8 - Workstream B - Article xx

The National Foreign Trade Council (the “NFTC”) is providing written comments on Proposed Article xx on Services (“Article xx”), a new Article combining Articles 5(3)(b), 12A and 14 for cross-border business services - relevant to Workstream B. The Subcommittee of the United Nations (“UN”) Committee of Experts on International Cooperation in Tax Matters (“Committee of Experts”) Twenty-eighth Session sought approval of the text of the proposed Article xx as provided in Annex B1.

The NFTC, organized in 1914, is an association of U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial, and service activities. Our members value work that focuses on establishing and maintaining international tax and transfer pricing norms that provide certainty to enterprises conducting cross-border operations.

General Comments

The role of a model convention is to provide norms of taxation as well as the starting point for negotiations between contracting states. We appreciate the Committee of Experts’ concerns about the evolution of the global economy and the historic reliance on physical presence tests. We recognize the issues surrounding the challenge of taxation with advances in technology and the ability to perform cross-border services without leaving one’s resident jurisdiction. Nonetheless, we are not supportive of Article xx as it would lead to double taxation and unreasonably increase compliance burdens for companies. Instead, we suggest that Article xx might be useful as part of the Commentary or a potential alternative to consider in treaty negotiations.

We further disagree with the suggestion that Article xx should replace Articles 5(3)(b), 12A and 14. Those Articles should remain in place, as the specificity and predictability of the tailored results produced by those provisions result in certainty for tax authorities and taxpayers. The specificity and predictability of the tailored results produced by Articles 5(3)(b), 12A and 14 are helpful to create tax certainty for tax authorities and taxpayers.¹ Should the Committee of Experts decide to proceed with Article xx in its current form, we urge taking additional measures to ensure that the prevention of double taxation is addressed.

We recognize that any effort to renegotiate international taxing rights will be complex. We urge the UN to work with the OECD to ensure that multiple systems are not created to address the same issues. The proposed rebalancing of taxing rights must provide a durable stabilization of the international tax system to succeed. As discussed during interventions at the 28th Meeting of the Committee of Experts, we recommend that an economic study is performed to understand the impact of Article xx, including the effect of gross-basis withholding taxes on each contracting state – with the recognition that any given country could act as either importer or exporter of services. It is particularly crucial to consider the impact of such a rule on low value-added services and whether developed or developing countries are more likely to provide low value-added services. Importing states need to consider the behavioral response of taxpayers as it relates to the additional tax revenue collected under Article xx. In some cases, the tax collected under Article xx will be passed on to the local person making the payment. In cases where the tax would be borne by the non-local service provider, the extra tax burden may make it unprofitable to do business in that state and some of those service providers may decide to no longer offer the service to local customers as a result.

We further urge that decisions on tax matters, especially new provisions for the UN Model Treaty, should be decided in a manner that is principled, avoids undue complexity, and avoids double taxation. Prior to the inclusion of any provision into the UN Model Treaty, the utility of the provision and whether sufficient willingness of both developed and developing countries exists should be considered. Failure to consider the utilization of a provision prior to its inclusion in the UN Model may lead to an unproductive use of resources in Treaty negotiations.

Specific Comments

Double Taxation

Article xx effectively permits double taxation with the interplay of Article xx(1) and Article xx(2). The purpose of Tax Treaties is to allocate taxing rights and eliminate double taxation. We recommend that the service income only be taxed under paragraph (1) or paragraph (2), but not both provisions. If the Committee of Experts chooses to permit taxation under both provisions, we strongly recommend that Article xx(2) include a net income option similar to Article 12B. In most

¹ If Article xx is included in the UN Model Treaty, we believe that it can co-exist with Article 5(3)(b), i.e., the 183-day threshold for permitting source country taxation on profits attributable to a permanent establishment while permitting a withholding tax on cross-border payments for Article xx services. This approach could also allow an election to replace the withholding tax with a net income equivalent. A similar approach could be taken to Article 14, allowing a withholding tax on services payments while permitting taxation on profits attributable to a fixed base or permanent establishment under the circumstances described in Article 14.

circumstances, it should be relatively easy to allocate costs to services and allow for net taxation. Failure to include a net income option will cause double taxation and potentially the payment of more tax than profit, resulting in a loss of income for the service company. Consideration should be given to the fact that services are not uniform in cost, some services come at high costs and others may not. The proposed revisions may also result in compliance costs that greatly exceed the profits earned and/or the amount tax due. In view of excessive compliance costs coupled with a potential inability to earn profits, companies may consider ceasing doing business in countries where this provision is effective.

Permanent Establishment

Article 5(3)(b) sets the minimum number of days required to create a permanent establishment in a Contracting State. We understand that the “elimination of threshold requirements based on physical presence for source country taxation of cross-border services is the fundamental goal of Article xx.” We also highlight that many small and medium businesses that may physically operate only in one country greatly benefit from the presence of clear, permanent establishment rules that eliminate regulatory burdens and unnecessary compliance costs across borders. If Article xx replaces Article 5(3)(b), there will be no bright-line test for a permanent establishment, resulting in a facts and circumstances test for every situation. Thus, taxpayers will need to prove that a permanent establishment did not exist after one day of presence in a contracting state, and the tax authorities of contracting states will need to prove the existence of a permanent establishment after 184 days, or even 365 days. The result will be an increase in disputes, expenditure of resources (financial and human), and uncertainty for tax authorities and taxpayers. NFTC strongly urges the Committee of Experts to retain Article 5(3)(b) in its current form, even if Article xx is adopted. We believe that these two provisions can co-exist, i.e., retain the 183-day threshold for permitting source country taxation on profits attributable to a permanent establishment but allow a withholding tax on cross-border payments for Article xx services (and also allow an election to replace the withholding tax with a net income equivalent).

Services

The contemplated scope of services which includes “any payment in consideration for any service” is extremely broad and should be revisited. The provision only provides a limited number of exclusions to this broad definition, which may impede the ability of developing countries to successfully negotiate this provision. The scope will create challenges for taxpayers both providing and receiving services, especially for single transactions as well as for contracts encompassing multiple consumers or jurisdictions. We request additional guidance to address the practical considerations to determine the party responsible for withholding, withholding mechanics, and how to allocate the income between jurisdictions. As discussed above, the potential elimination of threshold requirements, such as Article 5(3)(b), will create numerous compliance burdens and increase uncertainty. NFTC further recommends incorporating a revenue threshold to determine in-scope taxpayers as well as a de minimis rule exempting one-off and small dollar transactions into the provision. These rules will help ensure that compliance burdens do not outweigh the transaction costs.

Conclusion

We strongly urge the Committee of Experts to reconsider Article xx. At a minimum, we recommend that the Committee of Experts preclude the risk of double taxation and more thoroughly examine the economic impact of Article xx, including its impact on developing countries, prior to its inclusion in the UN Model Treaty. The current provisions in the Model UN Treaty have needed utility and should be retained.

We urge the UN to work collaboratively with the OECD and the Inclusive Framework to resolve concerns about international taxing rights in a manner that is principled, avoids undue complexity, and avoids double counting or double taxation of the same income. We believe that any outcome which fails to meet these objectives will cause instability in the international tax system.

We encourage engagement with the business community on Article xx and other tax issues being discussed at the UN, including at the Committee of Experts and Ad Hoc Committee. We are happy to answer any questions or provide clarification on any of the issues raised. Please contact Anne Gordon, Vice President, International Tax Policy at agordon@nftc.org.