

# OVERVIEW OF MODEL TAX CONVENTIONS



## LEARNING OUTCOMES

After studying this chapter, you would be able to:

- ❑ **appreciate** the need for Model Tax Convention;
- ❑ **appreciate** the key features of the OECD and UN Model Tax Conventions;
- ❑ **identify** the subject of the various articles of the OECD and UN Model Tax Conventions;
- ❑ **appreciate** the broad similarities and differences between the principles enshrined in certain articles of the OECD Model Tax Convention *vis-à-vis* the corresponding articles of the UN Model Tax Convention.



## 27.1 INTRODUCTION

In order to enable various countries to enter into treaties, which are standardized to some extent, Organization for Economic Cooperation and Development (OECD) and the United Nations (UN) have developed certain Model Tax Treaties. These treaties can be used by various countries as a starting point in their negotiations with other countries. While these Models are not legally binding, they have been extensively used by various countries as a reference point while entering into Tax Treaties. In some cases, they have been incorporated verbatim or with minor changes. However, in other cases, countries have made suitable changes in the draft model according to their economic environment and commercial and tax considerations.

The significant model conventions have been briefly discussed hereunder:

**OECD Model** - The emergence of present form of OECD Model Convention can be traced back to 1927, when the Fiscal Committee of the League of Nations prepared the first draft of Model Form applicable to all countries. In 1946 the model convention was published in Geneva by the Fiscal Committee of U.N. Social & Economic Council and later by the Organisation for European Economic Co-operation (OEEC) in 1963. However, in 1961, the Organisation for Economic Co-operation and Development (OECD) was established, with developed countries as its members, to succeed the OEEC, and OECD approved the draft presented to the OEEC. In 1977, the final draft was prepared in the present form which has been revised several times; the latest being in the year 2017.

OECD Model Convention (OECD MC) is essentially a model treaty **between two developed nations**. This model advocates residence based taxation, i.e., it lays emphasis on the right of state of residence to tax the income.

**UN Model** – In 1968, the United Nations set up an Adhoc Group of Experts from various developed and developing countries to prepare a **draft model convention between developed and developing countries**. In 1980, this Group finalised the UN Model Convention (UN MC) in its present form. Since its first publication in 1980, the Model has been updated previously in 2001, 2011 and 2017. The latest updation was in the year 2021.

The UN MC is a compromise between the source principle and the residence principle. However, it gives more weight to the source principle as against the residence principle of the OECD MC. UN MC is designed to encourage flow of investments from the developed countries to developing countries. It takes into account sharing of tax-revenue with the country providing capital.

The United Nations MC seeks to be balanced in its approach. As a corollary to the principle of taxation at source, the Articles of the Convention are based on a recognition by the source country that

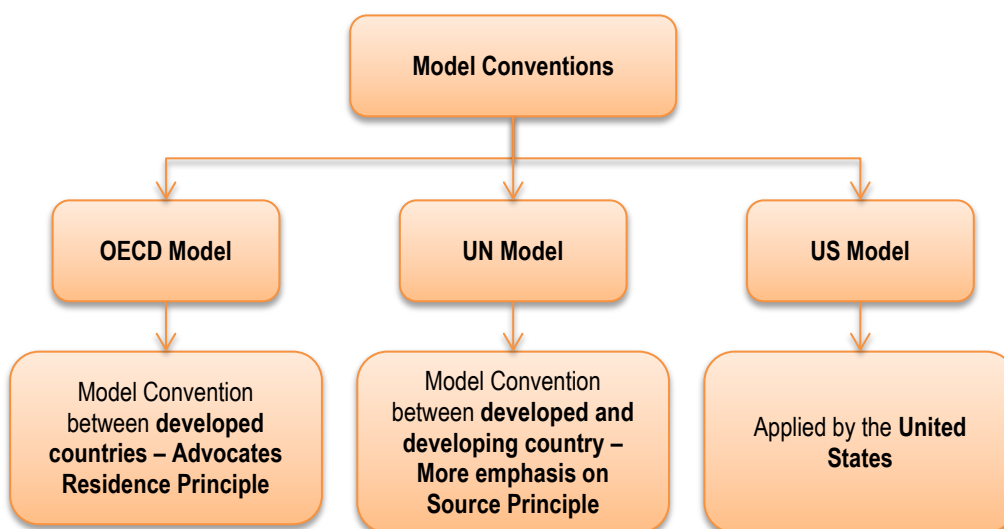
- (a) taxation of income from foreign capital should take into account expenses allocable to the earnings of the income so that such income is taxed on a net basis,
- (b) taxation should not be so high as to discourage investment and
- (c) it should take into account the appropriateness of the sharing of revenue with the country providing the capital.

In addition, the United Nations MC embodies the idea that it would be appropriate for the residence country to extend a measure of relief from double taxation through either a foreign tax credit or an exemption, as is also the case with the OECD Model Convention.

**US Model** – This Model Convention is used by the United States while entering into tax treaties with various countries. The US Model Convention was last revised in 2016.

These Models have a significant influence on international treaty practice, and have important common provisions. The similarities between these Models highlight the areas of consistency. The areas of divergence indicate some critical differences in approach or emphasis which need special focus. These differences are mainly in relation to the taxing rights which would be available to a country under domestic law and the extent to which any country should forego, under a bilateral tax treaty, in order to avoid double taxation and encourage investment.

The above model conventions have been illustrated in the following diagram:



OECD Model contains VII chapters comprising of 32 articles and UN Model also contains VII chapters but comprising of 31 articles. List of articles of OECD MC and UN MC is given below:

Article	OECD Model, 2017	UN Model, 2021
<b>Chapter I : Scope of the Convention</b>		
1	Persons covered	Persons covered
2	Taxes covered	Taxes covered
<b>Chapter II : Definitions</b>		
3	General definitions	General definitions
4	Resident	Resident
5	Permanent establishment	Permanent establishment
<b>Chapter III : Taxation of Income</b>		
6	Income from immovable property	Income from immovable property
7	Business profits	Business profits
8	International shipping and air transport	International shipping and air transport (Alternatives A & B)
9	Associated enterprises	Associated enterprises
10	Dividends	Dividends
11	Interest	Interest
12	Royalties	Royalties
12A		Fees for technical services
12B		Income from automated digital services
13	Capital gains	Capital gains
14		Independent personal services
15	Income from employment	Dependent personal services
16	Directors' fees	Directors' fees and remuneration of top-level managerial officials
17	Entertainers and sportspersons	Artistes and sportspersons
18	Pensions	Pensions and social security payments (Alternatives A & B)
19	Government service	Government service
20	Students	Students
21	Other income	Other income

Chapter IV : Taxation of Capital		
22	Capital	Capital
Chapter V : Methods for the Elimination of Double Taxation		
23A	Exemption method	Exemption method
23B	Credit method	Credit method
Chapter VI : Special Provisions		
24	Non-discrimination	Non-discrimination
25	Mutual agreement procedure	Mutual agreement procedure (Alternatives A & B)
26	Exchange of information	Exchange of information
27	Assistance in the collection of taxes	Assistance in the collection of taxes
28	Members of diplomatic missions and consular posts	Members of diplomatic missions and consular posts
29	Entitlement to benefits	Entitlement to benefits
30	Territorial extension	
Chapter VII : Final Provisions		
31/30	Entry into force	Entry into force
32/31	Termination	Termination

Now, let us discuss the comparative analysis of some of the significant Articles in the Model Tax conventions



## 27.2 COMPARATIVE ANALYSIS OF SOME OF THE SIGNIFICANT ARTICLES OF OECD AND UN MODEL CONVENTIONS

### **Title and Preamble to the Model Conventions**

The title of the UN Model Convention reads as follows:

***“Convention between (State A) and (State B) for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion”***

There is a specific reference to “the prevention of tax avoidance and evasion” in the title to emphasize its significance in the Model Convention.

The Preamble to the UN Model Convention reads as follows:

“(State A) and (State B),

Desiring to further develop their economic relationship and to enhance their cooperation in tax matters,

Intending to conclude a Convention for the elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax avoidance or evasion (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States)”

The Title and Preamble to the OECD Model Convention is almost identical to that of the UN Model Convention. The only minor difference is the reference to “tax evasion and avoidance” in the place of “tax avoidance and evasion” in the Title and Preamble.

The Preamble clearly indicates that the UN and OECD Model Conventions do not intend to create opportunities for non-taxation or reduced taxation through tax avoidance or evasion including through treaty shopping arrangements.

This language of the Preamble would help ensuring that the provisions of the Conventions are interpreted and applied to prevent abusive treaty shopping arrangements.

### **Significant Articles in the Model Conventions**

Over the years, both Model Conventions have seen a lot of convergence and the language is identical in quite a few Articles. However, there are key differences in approach and language in some Articles which will be the focus of our discussion, in the section below.

The jurisdiction or country of residence of the taxpayer is referred to as the Residence State and the jurisdiction or country where the source of income is located is referred to as the Source State.

### **Article 1: Persons Covered**

The OECD and UN Model Convention would apply to persons who are residents of one or both of the Contracting States.

For the purposes of these Conventions, income derived by or through an entity or arrangement that is treated as wholly or partly fiscally transparent under the tax law of either Contracting State shall be considered to be income of a resident of a Contracting State. However, the same would be treated as income only to the extent that the income is treated, for purposes of taxation by that State, as the income of a resident of that State.

### **Example**

*State A and State B have concluded a treaty identical to the Model Tax Convention. State A considers that an entity established in State B is a company, and taxes that entity on interest that it*

*receives from a debtor resident in State A. Under the domestic law of State B, however, the entity is treated as a partnership, and the two members in that entity, who share equally all its income, are each taxed on half of the interest. One of the members is a resident of State B and the other one is a resident of a country with which States A and B do not have a treaty. The paragraph provides that in such case, half of the interest shall be considered, for the purposes of Article 11, to be income of a resident of State B.*

**Note** – *The above example forms part of the Commentary to the UN Model Tax Convention.*

With the exception of benefits granted under certain Articles of these conventions, these Conventions would not affect the taxation, by a Contracting State, of its resident.

*Article 1 of UN Model Convention covers provision dealing with the application of the Convention to “Collective investment vehicles”. Funds that are widely-held, hold a diversified portfolio of securities and are subject to investor-protection regulation in the country in which they are established are referred to as “collective investment vehicles” (CIVs) like REITs.*

*These funds adopt different legal structures and may be set up, for instance, as companies, partnerships, trusts or contractual arrangements that create a joint ownership. It is to ensure that investing through a domestic CIV should result in a tax burden that is equal to the one that applies in the case of a direct investment, i.e. an investment where the CIV would not exist and where the investor in the CIV would have acquired directly its share of the assets held by the CIV.*

### **Article 2: Taxes Covered**

The OECD and UN Conventions would apply to taxes on income and on capital imposed on behalf of a Contracting State or of its political subdivisions or local authorities, irrespective of the manner in which they are levied.

Taxes on income and on capital cover all taxes imposed on total income, on total capital, or on elements of income or of capital, including taxes on gains from the alienation of movable or immovable property, taxes on the total amounts of wages or salaries paid by enterprises, as well as taxes on capital appreciation.

The existing taxes to which the Conventions would apply in case of each Contracting State are specifically to be mentioned.

The Convention shall apply also to any identical or substantially similar taxes which are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of significant changes made to their tax law.

**Article 4: Residence**

A taxpayer has to demonstrate that he is a resident of one or both Contracting States to be able to gain access to a tax treaty and avail the benefits thereunder.

The concept of 'resident of a Contracting State' has various functions and assumes significance in the following three scenarios:

- In determining a convention's scope of application;
- In solving cases where double taxation arises as a consequence of double residence;
- In solving cases where double taxation arises as a consequence of taxation in the state of residence and also in the state of source of income.

As per paragraph 1 of the UN Model Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of **that person's** domicile, residence, place of incorporation, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof **as well as a recognized pension fund of that State**. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.

Paragraph 1 of the OECD Model Convention is worded on similar lines. However, it does not contain reference to place of incorporation **and does not include recognized pension fund**.

Where by reason of the provisions of paragraph 1, an individual is a resident of both Contracting States, then, his status shall be determined as follows:

- (a) he shall be deemed to be a resident only of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests);
- (b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode;
- (c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national;
- (d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.



As per paragraph 3 of this Article, where by reason of the provisions of paragraph 1, a person other than an individual is a resident of both Contracting States, the competent authorities of the Contracting States shall endeavour to determine by mutual agreement, the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention. They shall do so having regard to its place of effective management, the place where it is incorporated or otherwise constituted and any other relevant factors. In the absence of such mutual agreement, such person shall not be entitled to any relief or exemption from tax provided by this Convention except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States.

The situation of dual residence may arise in case of companies in case where one Contracting State attaches importance to the place of incorporation and the other State to the place of effective management. The tie-breaker rule traditionally has been 'place of effective management'. Even India has used place of effective management in some of its treaties. In the latest update by OECD and UN, this has changed to a case by case approach considering the number of tax avoidance cases involving dual resident companies. Determination under the case by case approach will be requested by the concerned taxpayer through Article 25 (Mutual Agreement Procedure). Competent authorities will then rely on a range of factors to resolve the question of dual residency.

The last sentence of paragraph 3 of this Article provides that in the absence of determination by the competent authorities, the dual resident person would not be entitled to any relief or exemption from tax provided by this Convention except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States. This will not, however, prevent the taxpayer from being considered a resident of each Contracting State for purposes other than granting treaty reliefs or exemptions to that person.

#### **Article 5: Permanent Establishment**

The concept of "Permanent Establishment" (PE), defined in Article 5, has considerable importance as business profits (Article 7) of an enterprise cannot be taxed by a Source State unless it proves the existence of a PE.

The comparable term to PE under the Indian tax law is "business connection" [Section 9(1)(i)]. Generally speaking, the concept of "business connection" is wider than PE and hence, a business connection may exist even without a PE, but the absence of a "business connection" may indicate absence of a PE.

As the PE concept gives the Source State the right to tax, it is an important Article for developing countries. Hence, the UN Model Convention varies from the OECD Model Convention in the following respects:

- As per Article 5(3)(a) of the OECD Model Convention, a building site or construction or installation project constitutes a PE if it lasts more than twelve months. The UN Model Convention is wider as it covers “assembly or installation project” or “supervisory” activities in connection thereto and requires the activity in question to continue only for six months for constituting a PE.
- Article 5(3)(b) of the UN Model makes a specific reference to Service PE which is absent in the OECD Model. Article 5(3)(b) of the UN Model reads as follows –

*“The furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only if activities of that nature continue within a Contracting State for a period or periods aggregating more than 183 days in any 12 month period commencing or ending in the fiscal year concerned”.*

In the absence of a Service PE reference in OECD Model, the presence has to be ascertained through general principles under Article 5(1).

- Article 5(1) states the "basic rule" for a PE and expresses the primary meaning of PE. The definition of PE in Article 5 does not use the qualifying words "unless the context otherwise requires". As such, the definition needs to be followed in all cases unless specifically excluded.

Paraphrasing Article 5(1), a PE exists if the following conditions are satisfied cumulatively:

- There is an “enterprise”.
- Such enterprise is carrying on a "business";
- There is a "place of business";
- Such place of business is at the disposal of the enterprise (may be owned/rented but must be one which the enterprise has the effective power to use);
- The place of business is "fixed", that is, it must be established at a distinct place with a certain degree of permanence

The business of the enterprise is carried on wholly or partially through this fixed place of business.

A PE does not exist unless all the aforesaid conditions are satisfied.

- As per Article 5(2), the term "permanent establishment" includes especially:
  - a) a place of management;
  - b) a branch;
  - c) an office;
  - d) a factory;
  - e) a workshop, and
  - f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.
- Agency PE under OECD and UN Models targets activities done by a dependent agent of the enterprise in the Source State. The definition of dependent agent PE includes instances when an agent habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts routinely concluded without material modification by the enterprise.

In UN Model Convention, PE is constituted even if the person does not habitually conclude contracts nor plays the principal role leading to the conclusion of such contracts, but habitually maintains in that State, a stock of goods or merchandise from which that person regularly deliver goods or merchandise on behalf of that enterprise.

- The UN Model Convention has an additional Article 5(6) relating to insurance which is absent in OECD Model.

As per this Article, an insurance enterprise of a Contracting State shall, except in regard to re-insurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or insures risks situated therein through a person.

In the absence of similar Article in the OECD Model, a PE of an insurance enterprise has to be determined in accordance with provisions of Article 5(1) or 5(2) of the OECD model.

**Article 7: Business Profits**

Business profits of an enterprise can only be taxed by the Residence State. Right of Source State to tax business profits of an enterprise only exists if a PE exists in its jurisdiction.

As per the approach under the OECD Model Convention, once a PE is proven, the Source State can tax only such profits as are attributable to the PE. The UN Model Convention amplifies this attribution principle by a **limited** Force of Attraction rule (FOA).

The FOA rule implies that when a foreign enterprise sets up a PE in State of Source, it brings itself within the fiscal jurisdiction of that State (State of Source) to such a degree that profits that the enterprise derives from State of Source, whether through the PE or not, can be taxed by it (State of Source).

As per Article 7 of the UN Model Convention, if the enterprise carries on business in the other Contracting State through a PE, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to:

- (a) that PE;
- (b) sales in that other State of goods or merchandise of the same or similar kind as those sold through that PE; or
- (c) other business activities carried on in that other State of the same or similar kind as those effected through that PE.

**Article 11: Interest**

Paragraph 1 of this Article provides the right to Residence State to tax interest. Paragraph 2, however, also confers right to the Source State to tax interest. Generally, the interest is taxed in the Source State at a given rate on gross basis. However, if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged cannot exceed a specified percentage of the gross amount of the interest. The OECD Model specifies the percentage as 10%, but the UN Model leaves this percentage to be established through bilateral negotiations.

It may be noted that the definition of interest in both the models viz. OECD and UN Model is similar in that it essentially means income from debt claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment are not regarded as interest for the purpose of this Article.

**Article 12: Royalties**

This Article provides the right of Contracting States to tax income from royalty.

Key differences between the two Models are as follows:

- As per the OECD Model, royalties arising in the Source State and beneficially owned by a resident of the Residence State are taxable only in the Residence State. However, the UN Model provides that royalties may be taxed in the Residence State. Hence, the UN Model departs from the principle of exclusive right to tax provided to Residence State in the OECD Model. Thus, under the UN Model, the Source State may also tax royalties. However, if the beneficial owner is a resident of the Residence State, the tax charged by the Source State cannot exceed the specified percentage of the gross amount of royalties. This specified percentage is to be established through bilateral negotiations.
- The term “royalties” as per UN Model Convention means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment or for information concerning industrial, commercial or scientific experience.
- The definition of ‘royalties’ under the OECD Model does not include the following: (a) rentals for films or tapes used for radio or television broadcasting and (b) equipment rentals like rentals for industrial, commercial or scientific equipment.

**Article 12A: Fees for Technical Services**

India is the pioneer of the FTS concept which was added to the Income-tax Act, 1961 since 1976. Some of our tax treaties do contain a specific provision for FTS.

The UN Model has a specific article pertaining to Fees for Technical Services (FTS). There is no specific reference to FTS in the OECD Model.

Paragraph 1 of Article 12A provides that the FTS may be taxed in the Residence State but does not provide that the FTS is exclusively taxable in the Residence State.

Paragraph 2 establishes the right of the country in which FTS arises to tax in accordance with its domestic law, subject to the limitation on the maximum rate of tax on gross amount of the fees, if the beneficial owner is a resident of the other Contracting State. The maximum rate of tax is to be established through bilateral negotiations.

FTS is defined as payments for managerial, technical or consultancy services but excludes payment to an employee, payment for teaching in an educational institution or for teaching by an educational institution, payments by an individual for services for personal use. Management involves application of knowledge, skill or expertise in the control or administration of the conduct of a commercial enterprise or organization. Payments made to a consultant for advice related to the management of an enterprise (or of the business of an enterprise) would be FTS. Technical involves the application of specialized knowledge, skill or expertise with respect to a particular art, science, profession or occupation. Fees received for services provided by regulated professions such as law, accounting, architecture, medicine, engineering would constitute FTS. Services performed by other professionals, such as pharmacists, and scientists, etc. may constitute technical services if those services involve provision of specialized knowledge, skill and expertise. The ordinary meaning of “consultancy” involves the provision of advice or services of a specialized nature.

An example of FTS can be seen from the following facts: R Company is a financial institution resident in State R. R Company provides a wide variety of financial services to its customers, including acceptance of deposits, extension of credit, guarantees, foreign exchange, negotiable instruments. R Company’s business is conducted primarily in State R, but it also has clients in other countries, including State S. State R and State S have a tax treaty which contains an article akin to Article 12A. Payments received for services provided by a financial institution would constitute FTS if the services involve use of knowledge, skill and expertise to provide research, analysis or advice to a specific client related to particular circumstances. This has to be distinguished from provision of non-specialized services such as payment and transmission services, debit and credit card services, etc., which do not involve the application of any specialized knowledge, skill and expertise on behalf of a particular client.

#### **Article 12B: Income from Automated Digital Services**

With the advent of modern means of telecommunications and the spread of digitalization, enterprises have the ability to effectively engage in substantial business activities in the market country (source jurisdiction) without a fixed place of business there, or to conclude contracts remotely through technological means with no involvement of individual employees or dependent agents.

Article 12B was added to the United Nations Model Tax Convention in its 2021 update to preserve the domestic law taxing rights for States from which payments for automated digital services are made. There is no article in the OECD Model corresponding to Article 12B.

Paragraph 1 of Article 12B provides that the income from automated digital services arising in a Contracting State, underlying payments for which made to a resident of other Contracting State, may be taxed in the Residence State. It does not, however, provide that the income from automated digital services is exclusively taxable in the Residence State.

Paragraph 2 establishes the right of the country in which income from automated digital services arises to tax in accordance with its domestic law. However, if the beneficial owner of the income is a resident of the Residence State, the tax charged by the Source State cannot exceed the specified percentage of the gross amount of payments underlying the income from automated digital services. This specified percentage is to be established through bilateral negotiations.

“Automated digital services” is defined in paragraph 5 to mean any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider.

An important indicator of the concept of automated services is whether there is ability to scale up and provide the same type of services to new users with minimal human involvement. Once the service offering an automated digital service business is developed (such as a music catalogue or a social media platform), then, the business can provide that service to one user, or many more, on an automated basis with the same basic business processes. On the other hand, a non-automated digital service business would see a proportionate increase in the costs per unit in connection with providing the services to new customers.

Paragraph 6 lists examples of services that may constitute automated digital services. However, the provision is not self-standing; the requirements of paragraph 5 must also be met. Paragraph 6 simply provides an indication that an activity may constitute an automated digital service; it does not provide that an activity listed therein necessarily is an automated digital service. The following services are expressly mentioned in paragraph 6:

- (a) online advertising services;
- (b) supply of user data;
- (c) online search engines;
- (d) online intermediation platform services;
- (e) social media platforms;
- (f) digital content services;
- (g) online gaming;

- (h) cloud computing services; and
- (i) standardized online teaching services.

The categories are not mutually exclusive; for example, a digital content service could be funded in whole or in part by online advertising.

Paragraph 7 provides that the provisions of Article 12B shall not apply if the payments underlying the income from automated digital services qualify as “royalty” or “fees for technical services” under Article 12 or Article 12A.

### **Article 13: Capital Gains**

This is the most commonly used Article and it provides for the taxation of income arising from transfer of a capital asset, including transfer of shares. The right to tax income from capital gains may be exclusively with the Residence State, or shared between the Residence and Source States.

The Article does not specify what is a capital gain and how is to be computed, this being left to the applicable domestic law. The Article contains rules for taxation of gains made from alienation of different assets such as immovable property, immovable property forming part of a PE, ships and aircrafts, etc.

In respect of shares, both Models are identical. Rights are conferred to the Source State if more than 50 percent of the value of shares during the preceding 365 days is derived directly or indirectly from immovable property in such Source State. Otherwise, the Residence State would have the exclusive right to tax.

UN Model Convention allows a State to tax gains from the alienation of rights granted under the law of that State as long as these rights allow the use of resources that are naturally present in that State and that are under the jurisdiction of that State. This would cover, for example, the alienation of rights such as fishing quotas granted by the State; the right to fell timber in a forest; the right to extract water; the right to explore part of a territory of the State for oil, gas or minerals; the right to install wind or tidal stream turbines in part of the territory of the State as well as the right to use all or part of the radiofrequency spectrum in the State, including for cell phone purposes.

This provision does not cover rights granted contractually between private parties even if these rights are protected under the law of the State. Thus, the alienation of exclusive right to use know how in a given State would not be covered by the provision as that right granted by the owner of the know-how is not granted under the law of the State.



Both UN and OECD Model convention gives exclusive right to Residence State in case of gains from the alienation of any property other than covered in the other paragraphs of this Article.

#### **Article 14: Independent Personal Services**

Article 14 is only present in the UN Model. It was deleted from the OECD Model on 29-4-2000 on the basis of OECD Report (2000) on "Issues Related to Article 14 of the OECD Model Tax Convention". The Effect of deletion of Article 14 is that income derived from Professional Services etc., is now dealt with as 'Business Profits' (Article 7) under the OECD MC.

This Article deals with the taxation of income derived by a person for professional or specified services which are offered in the Source State through some presence. This article on Independent personal services in the UN Model reads as under:

- (1) Income derived by a resident of a Contracting State in respect of professional services or other activities of an independent character shall be taxable only in that State except in the following circumstances, when such income may also be taxed in the other Contracting State:
  - (a) If he has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in that other Contracting State; or
  - (b) If his stay in the other Contracting State is for a period or periods amounting to or exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned; in that case, only so much of the income as is derived from his activities performed in that other State may be taxed in that other State.
- (2) The term "professional services" includes especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.

Thus, the Article covers independent activities involving professional skills rendered by individuals on a principal to principal basis. The meaning of the term "professional services" is illustrated by some examples of typical liberal professions. The enumeration has an explanatory character only and is not exhaustive. It excludes industrial and commercial activities that are covered under the Article on Business Profits. Likewise, it also excludes professional services while in employment which are covered under the Article on Dependent Personal Services, e.g. a physician serving as a medical officer in a factory. Income of Artists, Athletes and Sportsmen, etc. is not covered by this Article. Also, income from Fees from Technical Services is also not covered.

**Article 21: Other Income**

This Article deals with taxation of items of income which are not specifically taxable under any other specific Article. Key differences are as under:

- OECD approach envisages that the exclusive right to tax is with the Residence State. UN Model contains an additional paragraph, Article 21(3), which provides that Source State may also tax other income.
- Article 21(2) of both OECD and UN Model provides that for income effectively connected with a PE maintained in a Contracting State by a resident of the other Contracting State, taxation is governed by the provisions of Article 7 (Business Profits). Additionally, UN Model provides that if the aforesaid income is effectively connected with a fixed base situated in a Contracting State by a resident of the other Contracting State, taxation would be governed by the provisions of Article 14 (Independent personal services).

**Articles 23A & 23B : Elimination of Double Taxation**

In many cases, the application of tax treaty may result into double taxation for tax payers. In such a case, in order to provide relief to such tax payers, Articles 23A and 23B which contains provisions relating to elimination of double taxation have to be applied. Articles 23A and 23B provide for the mechanism through which tax credit/exemption may be available in the Residence State for taxes deducted in the Source State.

The OECD and UN Model Conventions specify two approaches - Exemption method (Article 23A) and Credit method (Article 23B). Under the exemption method, tax exemption may be available in the Residence State. Under the credit method, tax credit may be available in the Residence State for taxes deducted in the Source State. These methods are not mutually exclusive and there may be cases where a treaty may adopt exemption method for certain types of income and credit method for other incomes.

The double taxation referred to here, is juridical double taxation, meaning the same income or capital is taxable in the hands of the same person by more than one State. It does not thus, encompass situations of economic double taxation, i.e. where two different persons are taxable in respect of the same income or capital. If two States wish to solve problems of economic double taxation, they must do so in bilateral negotiations.

**Article 25: Mutual Agreement Procedure**

There may be a situation wherein a tax payer may believe that the treatment accorded by either or both Contracting States is not in accordance with the provisions of the tax treaty. In such a case, there is a need for dispute resolution which is addressed by this Article. This Article requires

competent authorities of both countries to endeavor to resolve the conflict by engaging in bilateral negotiations.

The UN Model Convention provides two alternatives - Alternative A and Alternative B, for the article on Mutual Agreement Procedure which were introduced in 2011. Under OECD Model the taxpayer may make a request to either Contracting State while UN Model (Alternative A) contemplates taxpayer going to Residence State or the country of his nationality. Alternative B of UN Model Article 25 contemplates reference to an arbitration process as part of the Mutual Agreement Procedure. The decision arrived at, through the process is binding unless a person directly affected does not accept it.

Key differences between the OECD Model Convention (Article 25) and UN Model Convention (Article 25B - Alternative B) are as follows:

- Article 25B(5) of the UN Model provides that an arbitration may be initiated if the competent authorities are unable to reach an agreement on a case within three years from the presentation of that case. However, Article 25(5) of the OECD Model provides a time limit of two years from the date when all the information required by the competent authorities in order to address the case need to be provided to both competent authorities.
- Article 25B(5) of the UN Model provides that arbitration must be requested by the competent authority of one of the Contracting States. Once such a request is made, the taxpayer will be notified. However, as per Article 25(5) of the OECD Model, arbitration must be requested in writing by the person who initiated the case.
- Article 25B(5) of the UN Model allows the competent authorities to depart from the arbitration decision if they agree to do so within six months after the decision has been communicated to them.

#### **Article 26: Exchange of Information**

In order to complete tax cases, a country may require certain information which may be available with the treaty partner. Article 26 provides for the information which may be exchanged and the manner in which such a request has to be made. The purpose of Article 26 is to facilitate effective exchange of information between Contracting States. From the perspective of many developing countries, Article 26 is particularly important not only for curtailing cross-border tax evasion and avoidance, but also to curtail the capital flight that is often accomplished through such evasion and avoidance.

The OECD and UN Model Conventions are similar with respect to this Article. A Contracting State cannot be expected to provide confidential financial information to another Contracting State

unless it has confidence that the information will not be disclosed to unauthorized persons. A Contracting State can avoid the exchange of information obligations by showing that the information pertains to communication between an attorney and his client which is protected from disclosure under domestic law. However, lack of interest or use in such information cannot form the basis for a Contracting State to not co-operate with the exchange of information obligations.

**Resources:** The discussion on Model Tax Conventions in the above chapter is essentially based on the text and commentaries of the OECD Model Tax Convention, 2017 and UN Model Tax Convention, 2021 available at the websites <http://www.oecd.org/tax/treaties/> and <http://www.un.org>, respectively.

## SUMMARY

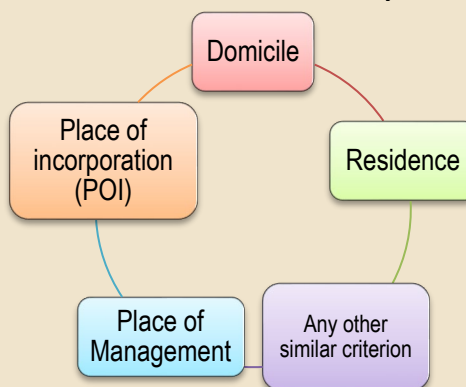
Article		OECD MC <i>vis-à-vis</i> UN MC Common paras & Significant differences					
<b>Chapter I : Scope of the Convention</b>							
1	<b>Persons covered</b>	<ul style="list-style-type: none"> <li>✚ <b>Resident of CS</b> - For application of treaty, a person has to be a resident of one or both of the Contracting States (CSs).</li> <li>✚ <b>Fiscally transparent entity</b> - Income derived by or through a fiscally transparent entity under the tax law of either CS to be considered to be income of a resident of a CS, to the extent such income is treated, for purposes of taxation by that State, as the income of a resident of that State.</li> <li>✚ <b>Collective investment vehicles</b> - Provision dealing with the application of the UN Model Convention to "Collective investment vehicles."</li> </ul>					
2	<b>Taxes covered</b>	<ul style="list-style-type: none"> <li>✚ <b>Taxes on income and capital</b> - The MCs apply to taxes on income and on capital imposed on behalf of a CS or of its political subdivisions or local authorities, irrespective of the manner in which they are levied.</li> <li>✚ <b>Coverage of taxes</b> - Taxes on income and on capital covers: <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: center;">Taxes imposed</th> <th style="text-align: center;">Taxes included</th> </tr> </thead> <tbody> <tr> <td style="vertical-align: top;"> <ul style="list-style-type: none"> <li>• On total income</li> <li>• on total capital</li> <li>• on elements of income or of capital</li> </ul> </td> <td style="vertical-align: top;"> <ul style="list-style-type: none"> <li>• taxes on <b>gains from alienation</b> of movable or immovable property</li> <li>• taxes on total amounts of <b>wages or salaries</b> paid by enterprises</li> <li>• taxes on <b>capital appreciation</b></li> </ul> </td> </tr> </tbody> </table> </li> </ul>		Taxes imposed	Taxes included	<ul style="list-style-type: none"> <li>• On total income</li> <li>• on total capital</li> <li>• on elements of income or of capital</li> </ul>	<ul style="list-style-type: none"> <li>• taxes on <b>gains from alienation</b> of movable or immovable property</li> <li>• taxes on total amounts of <b>wages or salaries</b> paid by enterprises</li> <li>• taxes on <b>capital appreciation</b></li> </ul>
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Chapter II : Definitions

4 Resident

✚ **Resident of either CS** - A taxpayer has to demonstrate that he is a resident of one or both CSs to be able to gain access to a tax treaty and avail benefits thereunder.

✚ **Meaning of “Resident of a Contracting State”**- Any person who, under the laws of that State, is liable to tax therein by reason of that person’s:



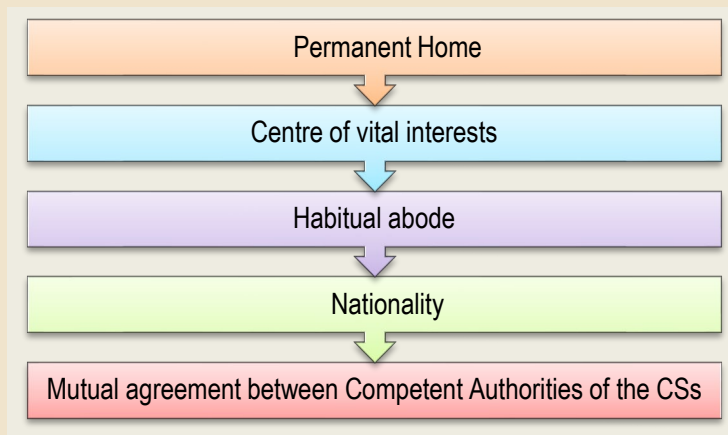
This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.

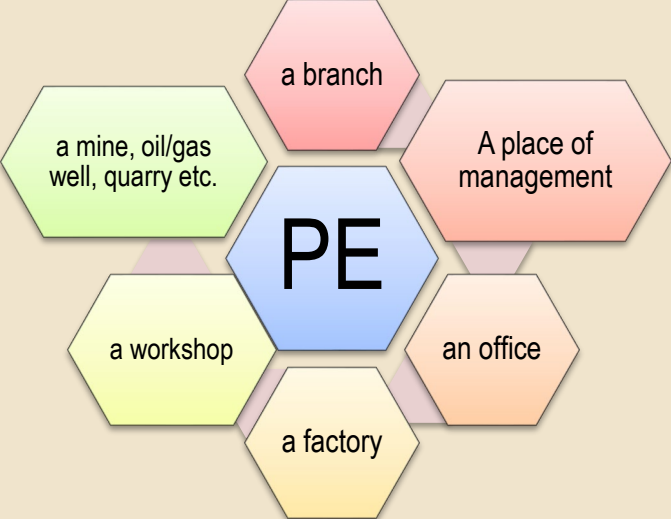
*Note - OECD MC does not contain reference to place of incorporation*

✚ **Tie-breaker Rule**

**In case of individuals**

Where an individual is a resident of both CSs as per domestic tax laws of that CS, then, his residential status shall be determined by applying the tie-breaker rule in the following sequence:





		<p><b><u>In case of companies</u></b></p> <ul style="list-style-type: none"> <li>• Dual residence arises where one CS attaches importance to POI and the other CS to the POEM.</li> <li>• The tie-breaker test involves a case by case approach considering the no. of tax avoidance cases involving dual resident Cos.</li> <li>• Request has to be made by the tax payer through Article 25 (MAP).</li> <li>• Competent Authorities will rely on range of factors to resolve the question of dual residency.</li> </ul>
5	<p><b>Permanent establishment (PE)</b></p>	<p><b>✚ Meaning of PE [Article 5(1)]</b></p> <ul style="list-style-type: none"> <li>• There should be an <b>"enterprise"</b> (Entr).</li> <li>• Such Entr should be carrying on a <b>"business"</b>;</li> <li>• There should be a <b>"place of business (POB)"</b>;</li> <li>• Such place of business (POB) should be at the <b>disposal of the Entr</b> (may be owned / rented but must be one which the Entr has the effective power to use);</li> <li>• The POB should be <b>"fixed"</b>, i.e., it must be established at a distinct place with a certain <b>degree of permanence</b></li> <li>• The business of the enterprise is carried on wholly or partially through this fixed POB.</li> </ul> <p>A PE does not exist unless all the aforesaid conditions are satisfied.</p> <p><b>✚ Specific inclusions in the meaning of PE [Article 5(2)]</b></p> 

		<p>✚ <b>Expansion of scope of Agency PE</b></p> <ul style="list-style-type: none"> <li>Agency PE targets activities done by a dependent agent (DA) of the Entr in the Source State (SS).</li> <li>DAPE now includes instances when an agent habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts routinely concluded without material modification by the enterprise.</li> <li>In UN Model Convention, PE is constituted even if the person does not habitually conclude contracts nor plays the principal role leading to the conclusion of such contracts, but habitually maintains in that State, a stock of goods or merchandise from which that person regularly deliver goods or merchandise on behalf of that enterprise.</li> </ul> <p>✚ <b>PE of an Insurance Enterprise</b></p> <table border="1" data-bbox="412 691 1258 1008"> <thead> <tr> <th data-bbox="412 691 822 753">UN MC</th> <th data-bbox="822 691 1258 753">OECD MC</th> </tr> </thead> <tbody> <tr> <td data-bbox="412 753 822 1008">UN MC has an additional Article 5(6) relating to insurance. An insurance Entr of a CS is deemed to have a PE in the other CS if it collects premiums in the territory of that other CS or insures risks situated therein through a person.</td> <td data-bbox="822 753 1258 1008">In the absence of similar Article in the OECD MC, a PE of an insurance Entr is to be determined in accord with Article 5(1) or 5(2).</td> </tr> </tbody> </table>	UN MC	OECD MC	UN MC has an additional Article 5(6) relating to insurance. An insurance Entr of a CS is deemed to have a PE in the other CS if it collects premiums in the territory of that other CS or insures risks situated therein through a person.	In the absence of similar Article in the OECD MC, a PE of an insurance Entr is to be determined in accord with Article 5(1) or 5(2).		
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7	<b>Business profits</b>	<p>✚ <b>Right of CS to tax business profits (BPs)</b></p> <table border="1" data-bbox="412 1124 1288 1734"> <thead> <tr> <th data-bbox="412 1124 593 1186">OECD MC</th> <th data-bbox="593 1124 1288 1186">UN MC</th> </tr> </thead> <tbody> <tr> <td colspan="2" data-bbox="412 1186 1288 1309">BPs of an Entr can only be taxed by the Residence State (<b>RS</b>). Right of Source State (<b>SS</b>) to tax BPs of an enterprise only exists if a PE exists in its jurisdiction.</td> </tr> <tr> <td data-bbox="412 1309 593 1734">Once a PE is proven, the <b>SS</b> can tax only such profits as are attributable to the PE</td> <td data-bbox="593 1309 1288 1734"> <ul style="list-style-type: none"> <li>✚ The attribution principle is amplified by a <b>limited</b> Force of Attraction rule (FOA).</li> <li>✚ The FOA rule implies that when a foreign enterprise sets up a PE in SS, it brings itself within the fiscal jurisdiction of that State to such a degree that profits that the Entr derives therefrom, whether through the PE or not, can be taxed by it (i.e., the SS).</li> <li>✚ Accordingly, if the Entr carries on business in the other CS through a PE, the profits of the Entr may be taxed in the other CS but only so much of them as is attributable to:</li> </ul> </td> </tr> </tbody> </table>	OECD MC	UN MC	BPs of an Entr can only be taxed by the Residence State ( <b>RS</b> ). Right of Source State ( <b>SS</b> ) to tax BPs of an enterprise only exists if a PE exists in its jurisdiction.		Once a PE is proven, the <b>SS</b> can tax only such profits as are attributable to the PE	<ul style="list-style-type: none"> <li>✚ The attribution principle is amplified by a <b>limited</b> Force of Attraction rule (FOA).</li> <li>✚ The FOA rule implies that when a foreign enterprise sets up a PE in SS, it brings itself within the fiscal jurisdiction of that State to such a degree that profits that the Entr derives therefrom, whether through the PE or not, can be taxed by it (i.e., the SS).</li> <li>✚ Accordingly, if the Entr carries on business in the other CS through a PE, the profits of the Entr may be taxed in the other CS but only so much of them as is attributable to:</li> </ul>
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			<p>(a) that PE;</p> <p>(b) sales in that other CS of goods or merchandise of the same or similar kind as those sold through that PE; or</p> <p>(c) other business activities carried on in that other State of the same or similar kind as those effected through that PE.</p>						
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12	Royalties (Roy)		<b>OECD MC</b>	<b>UN MC</b>												
		<b>Right of CS to tax Roy. income</b>	Roy. arising in SS and beneficially owned by resident of the RS is taxable only in RS. Thus, <b>RS has exclusive right to tax royalty income.</b>	<b>Roy may also be taxed in the SS.</b> However, if the beneficial owner is a resident of the RS, the tax charged by SS $\leq$ the specified %, (to be established through bilateral negotiations) of gross royalty.												
		<b>Definition of Roy</b>	Definition of Royalty does not include: (a) rentals for films/tapes used for radio/ TV broadcasting; and (b) rentals for industrial, commercial or scientific equipment.	Royalty includes: (a) rentals for films or tapes used for radio or TV broadcasting and (b) equipment rentals like rentals for industrial, commercial or scientific equipment.												
12A	FTS	<p>The UN MC has a specific article pertaining to Fees for Technical Services (FTS). There is no specific reference to FTS in OECD MC.</p> <p> <b>Right of CS to tax FTS [UN Model]</b></p> <table border="1" style="width: 100%;"> <thead> <tr> <th style="text-align: center;">Para of Article</th> <th style="text-align: center;">Right of CS to tax FTS</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;">1</td> <td>Confers right to the RS to tax FTS. However, does not state that FTS is exclusively taxable in the RS.</td> </tr> <tr> <td style="text-align: center;">2</td> <td>Establishes the right of the SS to tax FTS in accordance with its domestic law, subject to limitation on the max. rate of tax on gross amount of fees, to be established through bilateral negotiations, if the beneficial owner is a resident of the other CS.</td> </tr> </tbody> </table> <p> <b>Meaning of FTS [UN Model]</b></p> <p><b>FTS means payments for managerial, technical or consultancy services</b></p> <p><b><u>Exclusions from the meaning of FTS:</u></b></p> <table border="1" style="width: 100%;"> <tbody> <tr> <td style="text-align: center;">i</td> <td>payment to an employee</td> </tr> <tr> <td style="text-align: center;">ii</td> <td>payment for teaching in an or by an educational institution</td> </tr> <tr> <td style="text-align: center;">iii</td> <td>payment by an individual for services for personal use</td> </tr> </tbody> </table>			Para of Article	Right of CS to tax FTS	1	Confers right to the RS to tax FTS. However, does not state that FTS is exclusively taxable in the RS.	2	Establishes the right of the SS to tax FTS in accordance with its domestic law, subject to limitation on the max. rate of tax on gross amount of fees, to be established through bilateral negotiations, if the beneficial owner is a resident of the other CS.	i	payment to an employee	ii	payment for teaching in an or by an educational institution	iii	payment by an individual for services for personal use
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12B	<b>Income from Automated Digital Services</b>	<p>Article 12B was added to the United Nations Model Tax Convention in its 2021 update to preserve the domestic law taxing rights for States from which payments for automated digital services are made. There is no article in the OECD MC corresponding to Article 12B.</p> <p><b>✚ Right of CS to tax income from automated digital [UN Model]</b></p> <table border="1" data-bbox="417 397 1280 836"> <thead> <tr> <th data-bbox="417 397 575 488">Para of Article</th> <th data-bbox="575 397 1280 488">Right of CS to tax income from automated digital services</th> </tr> </thead> <tbody> <tr> <td data-bbox="417 488 575 614">1</td> <td data-bbox="575 488 1280 614">Confers right to the RS to tax income from automated digital services arising in a CS. However, does not state that FTS is exclusively taxable in the RS.</td> </tr> <tr> <td data-bbox="417 614 575 836">2</td> <td data-bbox="575 614 1280 836">Establishes the right of the SS to tax income from automated digital services in accordance with its domestic law, subject to the specified percentage of the gross amount of payments underlying the income from automated digital services, to be established through bilateral negotiations, if the beneficial owner is a resident of the other CS.</td> </tr> </tbody> </table> <p><b>✚ Meaning of Automated digital services [UN Model]</b></p> <p><b>Automated digital services any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider.</b></p> <p><b><u>Specific inclusions:</u></b></p> <table border="1" data-bbox="417 1054 1280 1464"> <tbody> <tr> <td data-bbox="417 1054 486 1097">i</td> <td data-bbox="486 1054 1280 1097">online advertising services</td> </tr> <tr> <td data-bbox="417 1097 486 1139">ii</td> <td data-bbox="486 1097 1280 1139">supply of user data</td> </tr> <tr> <td data-bbox="417 1139 486 1182">iii</td> <td data-bbox="486 1139 1280 1182">online search engines</td> </tr> <tr> <td data-bbox="417 1182 486 1224">iv</td> <td data-bbox="486 1182 1280 1224">online intermediation platform services</td> </tr> <tr> <td data-bbox="417 1224 486 1267">v</td> <td data-bbox="486 1224 1280 1267">social media platforms</td> </tr> <tr> <td data-bbox="417 1267 486 1309">vi</td> <td data-bbox="486 1267 1280 1309">digital content services</td> </tr> <tr> <td data-bbox="417 1309 486 1352">vii</td> <td data-bbox="486 1309 1280 1352">online gaming</td> </tr> <tr> <td data-bbox="417 1352 486 1394">viii</td> <td data-bbox="486 1352 1280 1394">cloud computing services</td> </tr> <tr> <td data-bbox="417 1394 486 1464">ix</td> <td data-bbox="486 1394 1280 1464">standardized online teaching services</td> </tr> </tbody> </table>	Para of Article	Right of CS to tax income from automated digital services	1	Confers right to the RS to tax income from automated digital services arising in a CS. However, does not state that FTS is exclusively taxable in the RS.	2	Establishes the right of the SS to tax income from automated digital services in accordance with its domestic law, subject to the specified percentage of the gross amount of payments underlying the income from automated digital services, to be established through bilateral negotiations, if the beneficial owner is a resident of the other CS.	i	online advertising services	ii	supply of user data	iii	online search engines	iv	online intermediation platform services	v	social media platforms	vi	digital content services	vii	online gaming	viii	cloud computing services	ix	standardized online teaching services
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13	<b>Capital gains</b>	<p>This Article provides for the taxation of income arising from transfer of a capital asset, including transfer of shares.</p> <p><b>✚ Right of CS to tax income from Capital Gains</b></p> <ul style="list-style-type: none"> <li>The right to tax capital gains may be exclusively with the RS, or shared between the RS and SS.</li> </ul>																								

		<ul style="list-style-type: none"> <li>• The Article does not specify what is a capital gain and how is to be computed, this being left to the applicable domestic law.</li> <li>• The Article contains rules for taxation of gains from alienation of different assets such as immovable property, immovable property forming part of a PE, ships &amp; aircrafts, etc.</li> <li>• In respect of shares, OECD and UN MCs are identical. Rights are conferred to the SS if more than 50% of the value of shares during the preceding 365 days is derived directly or indirectly from immovable property in such SS. Otherwise, the Residence State would have the exclusive right to tax.</li> <li>• UN MC allows a State to tax gains from the alienation of rights granted under the law of that State as long as these rights allow the use of resources that are naturally present in that State and that are under the jurisdiction of that State.</li> <li>• Both UN and OECD Model convention gives exclusive right to Residence State in case of gains from the alienation of any property other than covered in the other paragraphs of this Article.</li> </ul>															
14	<p><b>Independent personal services</b></p>	<p>This Article present only in the UN MC deals with the taxation of income derived by a person for professional or specified services which are offered in the SS through some presence.</p> <p><b>✚ Right of CS to tax income from professional services (IPS) [UN MC]</b></p> <table border="1" data-bbox="412 987 1277 1713"> <tr> <td data-bbox="412 987 624 1108"><b>Right of RS</b></td> <td colspan="2" data-bbox="624 987 1277 1108"><b>Income derived by a resident of a CS in respect of professional services or other activities of an independent character is taxable only in the RS.</b></td> </tr> <tr> <td data-bbox="412 1108 624 1713"><b>Right of SS</b></td> <td colspan="2" data-bbox="624 1108 1277 1199">In the following circumstances, however, IPS may also be taxed in the other CS (i.e., the SS):</td> </tr> <tr> <td data-bbox="624 1199 917 1280"></td> <td data-bbox="624 1199 917 1280"><b>Circumstance</b></td> <td data-bbox="917 1199 1277 1280"><b>Extent of income taxable in SS</b></td> </tr> <tr> <td data-bbox="624 1280 917 1464"></td> <td data-bbox="624 1280 917 1464">If he has a fixed base regularly available to him in the SS for the purpose of performing his activities</td> <td data-bbox="917 1280 1277 1464">Only so much of the income as is attributable to that fixed base may be taxed in the SS.</td> </tr> <tr> <td data-bbox="624 1464 917 1713"></td> <td data-bbox="624 1464 917 1713">If his stay in the SS is for a period &gt; 183 days in any 12 month period commencing or ending in the fiscal year concerned</td> <td data-bbox="917 1464 1277 1713">Only so much of the income as is derived from his activities performed in the SS may be taxed in that State</td> </tr> </table>	<b>Right of RS</b>	<b>Income derived by a resident of a CS in respect of professional services or other activities of an independent character is taxable only in the RS.</b>		<b>Right of SS</b>	In the following circumstances, however, IPS may also be taxed in the other CS (i.e., the SS):			<b>Circumstance</b>	<b>Extent of income taxable in SS</b>		If he has a fixed base regularly available to him in the SS for the purpose of performing his activities	Only so much of the income as is attributable to that fixed base may be taxed in the SS.		If his stay in the SS is for a period > 183 days in any 12 month period commencing or ending in the fiscal year concerned	Only so much of the income as is derived from his activities performed in the SS may be taxed in that State
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		<p> <b>Definition of “Professional Services” [UN MC]</b></p> <p>The term "professional services" includes especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.</p> <p><b>Note</b> – OECD MC does not contain a separate article on IPS. The same is dealt with as “Business Profits (Article 7)” under the OECD MC.</p>											
21	<b>Other income (OI)</b>	<p>This Article deals with taxation of items of income which are not specifically taxable under any other specific Article [i.e., upto Article 20].</p> <table border="1"> <thead> <tr> <th></th> <th>OECD MC</th> <th>UN MC</th> </tr> </thead> <tbody> <tr> <td><b>Right to tax OI</b></td> <td>Exclusive right to tax is with the RS.</td> <td>Contains an additional para, Article 21(3), which provides that SS may also tax other income.</td> </tr> <tr> <td rowspan="2"><b>Right to tax income [other than income from immovable property] effectively connected with PE</b></td> <td colspan="2">Article 21(2) of both OECD and UN MC provides that for income effectively connected with a PE maintained in a CS by a resident of the other CS, taxation is governed by the provisions of Article 7 (Business Profits).</td> </tr> <tr> <td></td> <td>Additionally, UN Model provides that if the aforesaid income is effectively connected with a fixed base situated in a CS by a resident of the other CS, taxation would be governed by the provisions of Article 14 (IPS).</td> </tr> </tbody> </table>		OECD MC	UN MC	<b>Right to tax OI</b>	Exclusive right to tax is with the RS.	Contains an additional para, Article 21(3), which provides that SS may also tax other income.	<b>Right to tax income [other than income from immovable property] effectively connected with PE</b>	Article 21(2) of both OECD and UN MC provides that for income effectively connected with a PE maintained in a CS by a resident of the other CS, taxation is governed by the provisions of Article 7 (Business Profits).			Additionally, UN Model provides that if the aforesaid income is effectively connected with a fixed base situated in a CS by a resident of the other CS, taxation would be governed by the provisions of Article 14 (IPS).
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<b>Chapter V : Methods for the Elimination of Double Taxation</b>													
23A/ 23B	<b>Exemption method/ Credit Method</b>	<p>In many cases, the application of tax treaty may result into double taxation (DT) for tax payers. In such a case, Articles 23A and 23B provide for the mechanism through which tax credit/exemption may be available in the RS for taxes deducted in the SS.</p> <p> <b>Two approaches for elimination of DT under MCs:</b></p> <table border="1"> <thead> <tr> <th>Exemption method (Article 23A)</th> <th>Credit method (Article 23B)</th> </tr> </thead> <tbody> <tr> <td>Tax exemption may be available in the RS for taxes deducted in the SS.</td> <td>Tax credit may be available in the RS for taxes deducted in the SS.</td> </tr> </tbody> </table> <p>These methods are not mutually exclusive and there may be cases where a treaty may adopt exemption method for certain types of income and credit method for other incomes.</p> <p> <b>Juridical DT and Economic DT:</b></p> <table border="1"> <thead> <tr> <th></th> <th>Juridical DT</th> <th>Economic DT</th> </tr> </thead> <tbody> <tr> <td><b>Meaning</b></td> <td>The same income or</td> <td>Two different persons are taxable in</td> </tr> </tbody> </table>	Exemption method (Article 23A)	Credit method (Article 23B)	Tax exemption may be available in the RS for taxes deducted in the SS.	Tax credit may be available in the RS for taxes deducted in the SS.		Juridical DT	Economic DT	<b>Meaning</b>	The same income or	Two different persons are taxable in	
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<b>Meaning</b>	The same income or	Two different persons are taxable in											

			capital is taxable in the hands of the same person by more than one State	respect of the same income or capital
		<b>Example</b>	FTS may be taxable in the hands of the recipient both in the RS as well as in SS, based on the domestic laws of the CSs.	In respect of dividend distributed by a Co., DDT may be payable by the Co. in SS, whereas the dividend may be taxable in the hands of the shareholder of the other CS, on the basis of his residence.
		<b>Type of DT addressed by Article 23A &amp; 23B</b>	Articles 23A & 23B address Juridical DT.	The Articles do not address Economic DT. If two States wish to solve problems of economic DT, they must do so in bilateral negotiations.
<b>Chapter VI : Special Provisions</b>				
25	<b>Mutual agreement procedure (MAP)</b>	Where a tax payer believes that the treatment accorded by either or both CSs is not in accordance with the provisions of the tax treaty, this Article provides for dispute resolution through bilateral negotiations between competent authorities (CAS) of both CSs.		
			<b>OECD MC</b>	<b>UN MC</b>
		<b>Request for MAP</b>	The taxpayer may make a request to either CS	<b>Alternative A</b> - Taxpayer has to approach RS or the country of his nationality <b>Alternative B</b> - Reference to an arbitration process as part of MAP. The decision arrived at through the process is binding unless a person directly affected does not accept it.
		<b>Time limit</b>	Stipulates a time limit of 2 years from the date when all the information required by the CAS in order to address the case need to be provided to both CAS.	An arbitration may be initiated if the competent authorities (CAS) are unable to reach an agreement on a case within 3 years from presentation of that case [Alternative B]
		<b>Who can request for Arbitration?</b>	Arbitration must be requested in writing by the person who initiated the case	Arbitration must be requested by the CAS of one of the CS. Once such a request is made, the taxpayer will be notified [Alternative B]

		<b>Departure from arbitration by CAS</b>	No specific provision for departure from arbitration.	The CAS may depart from the arbitration decision if they agree to do so within 6 months after the decision has been communicated to them [Alternative B]
26	<b>Exchange of information (EOI)</b>	<p>✚ <b>Purpose of Article 26</b> In order to complete tax cases, a country may require certain info which may be available with the treaty partner. Article 26 provides for:</p> <ul style="list-style-type: none"> <li>• the info which may be exchanged</li> <li>• the manner in which such a request has to be made.</li> </ul> <p>✚ <b>Importance of Article 26:</b></p> <ul style="list-style-type: none"> <li>• facilitates effective exchange of information between CSs.</li> <li>• curtails cross-border tax evasion and avoidance,</li> <li>• curtails the capital flight that is often accomplished through tax evasion &amp; avoidance. This is particularly relevant in the perspective of developing countries.</li> </ul> <p>✚ <b>Similar provisions contained in OECD and UN MCs</b></p> <ul style="list-style-type: none"> <li>• A CS cannot be expected to provide confidential financial info to another CS unless it has confidence that the info will not be disclosed to unauthorized persons.</li> <li>• A CS can avoid the EOI obligations by showing that the info pertains to communication between an attorney and his client which is protected from disclosure under domestic law.</li> <li>• Lack of interest or use in such info cannot, however, form the basis for a CS to not co-operate with the EOI obligations.</li> </ul>		

## TEST YOUR KNOWLEDGE

### Questions

1. Explain briefly the significant difference between the UN and OECD Model Tax Convention.
2. When does it become necessary to apply the tie-breaker rule? Discuss the manner of application of the tie-breaker rule.
3. Explain the meaning of “interest” and “fees for technical services” under the UN Model Convention.
4. What is the meaning of Automated Digital Services? Elucidate.
5. What are the payments covered within the scope of “Royalties” under the UN Model Convention and OECD Model Convention. Elucidate.

### Answers

1. OECD Model is essentially a model treaty between two developed nations whereas UN Model is a model convention between a developed country and a developing country.

Further, OECD Model advocates the residence principle, i.e., it lays emphasis on the right of state of residence to tax the income, whereas the UN Model is a compromise between the source principle and residence principle, giving more weight to the source principle as against the residence principle.

2. Every jurisdiction, in its domestic tax law, prescribes the mechanism to determine residential status of a person. If a person is considered to be resident of both the Contracting States, relief should be sought from Article 4 of the Tax Treaty. A series of tie-breaker rules are provided in Paragraph 2 Article 4 of Model Convention to determine single state of residence for an individual.

The tie-breaker rule would be applied in the following manner:

- (i) The first test is based on where the individual has a **permanent home**. Permanent home would mean a dwelling place available to him at all times continuously and not occasionally and includes place taken on rent for a prolonged period of time.
- (ii) If that test is inconclusive for the reason that the individual has permanent home available to him in both Contracting States, he will be considered a resident of the Contracting State where his personal and economic relations are closer, in other

words, the place where lies **his centre of vital interests**. Thus, preference is given to family and social relations, occupation, place of business, place of administration of his properties, political, cultural and other activities of the individual.

(iii) Paragraph (ii) establishes a secondary criterion for two quite distinct and different situations:

- The case where the individual has a permanent home available to him in both Contracting States and it is not possible to determine in which one he has his centre of vital interests;
- The case where the individual has a permanent home available to him in neither Contracting State.

In the aforesaid scenarios, preference is given to the Contracting State where the individual has an **habitual abode**.

(iv) If the individual has habitual abode in both Contracting States or in neither of them, he shall be treated as a resident of the Contracting State of which he is a **national**.

(v) If the individual is a national of both or neither of the Contracting States, the matter is left to be **considered by the competent authorities** of the respective Contracting States.

3. As per Article 11 of the UN Model Convention, "Interest" essentially means income from debt claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment are not regarded as interest for the purpose of this Article.

As per Article 12A of the UN Model Convention, "Fees for technical services" is defined as payments for managerial, technical or consultancy services but excludes payment to an employee, payment for teaching in an educational institution or for teaching by an educational institution, payments by an individual for services for personal use.

4. As per Article 12B of UN Model Convention, "Automated digital services" means any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider.



The term “Automated digital services” includes specially:

- (a) online advertising services;
  - (b) supply of user data;
  - (c) online search engines;
  - (d) online intermediation platform services;
  - (e) social media platforms;
  - (f) digital content services;
  - (g) online gaming;
  - (h) cloud computing services; and
  - (i) standardized online teaching services.
5. The term “royalties” as per UN Model Convention means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment or for information concerning industrial, commercial or scientific experience.

The definition of ‘royalties’ under the OECD Model Convention does not include the following: (a) rentals for films or tapes used for radio or television broadcasting and (b) equipment rentals like rentals for industrial, commercial or scientific equipment.

