



ICAEW TAX REPRESENTATION

**REVIEW OF DOUBLE TAXATION TREATIES 2012-13**

**Comments submitted on 3 February 2012] by ICAEW Tax Faculty in response to the request by HMRC Business International for views on priorities for the UK's network of double taxation agreements in the financial year 2012-13.**

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# REVIEW OF DOUBLE TAXATION TREATIES 2012-13

## INTRODUCTION

1. We are writing in response to the letter of 19 December 2011 from Steve Reszetniak, Senior Policy Adviser, in which he asked for comments on what should be the UK Government's priorities in the year to March 2013 for the updating of the UK's network of Double Taxation Agreements (DTAs).
2. In previous years HMRC has also asked for comments about Double Contribution Agreements. In relation to these we have noted in our previous submissions, most recently in 2011 (TAXREP 3/11), that the DCA network is currently small and as income tax and social security contributions are tending to converge in many countries it is increasingly important that the two networks are more evenly matched.
3. We also noted in last year's submission the fact that the UK has not concluded any new gift or inheritance tax treaties in the last 10 years despite the increase in cross-border migration. The lack of such treaties was mentioned in the European Commission paper of December 2011 (COM/2011/864) which also looked at other ways to reduce double taxation in the IHT area through coordination of their actions by the Member States.
4. The Commission paper indicates that the UK has five Double Tax Treaties dealing with IHT with other Member States of the European Union.
5. Within the EU alone, the European Commission has estimated that there are around 450,000 successions each year with a cross-border dimension ([Proposal for a regulation on international successions](#), 14 October 2009).
6. In the balance of this document we refer only to DTAs.
7. Our Ten Tenets for a Better Tax System which we use as a benchmark are summarised in Annex A.

## WHO WE ARE

8. The ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the ICAEW provides leadership and practical support to over 136,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The ICAEW is a founding member of the Global Accounting Alliance with over 775,000 members worldwide. The Tax Faculty is the focus for tax within ICAEW.
9. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
10. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax

services including the monthly newsletter TAXline to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire.

## GENERAL COMMENTS

11. We note the priorities that are followed when negotiating treaties, as set out in the Annex to the letter of Steve Reszetniak, and we think these reflect an appropriate and strategic approach.
12. Following the submission of our paper (TAXREP 7/11) on the programme of work for 2010-11 a small team from ICAEW Tax Faculty met with the HMRC treaty negotiating team on 11 February 2011. We welcome the approach of the team which is to ensure that we have in place a network of treaties with our major trading partners and that these treaties, for instance, aim to have minimal or zero withholding taxes and a PE threshold which mirrors the OECD approach.
13. We would welcome the addition of a compulsory arbitration clause to the Mutual Agreement Article of the Treaties with our major trading partners as this will encourage more productive negotiations under the Mutual Agreement procedures. This is now included in Article 25(5) of the 2010 model OECD Convention. Such an arbitration clause does not appear to have been included in the recent treaties with, for instance, China and Hungary and it would be useful to know the reasons for this.
14. We note that the SIs e.g. Jersey and Guernsey do not appear to be searchable on the HMRC website via the treaty search. If you use 'tax treaties' as your search on the HMRC Home Page you get to <http://search.hmrc.gov.uk/kb5/hmrc/hmrc/results.page?qt=tax+treaties> If you then use the A-Z search on the right hand side of the page you will get to the main alphabetical listing of the site but you can't search individual countries at this stage. You have to find 'Tax Treaties' under 'T' and that then takes you to <http://www.hmrc.gov.uk/taxtreaties/index.htm> You need to get to this latter page from the original search.
15. We have a number of general points in relation to the OECD Model Convention
16. **Article 4.3**  
Is the government's general policy to continue to include an effective management tie-breaker in the treaties it negotiates? As far as we can see, the only Mutual Agreement Procedure tie-breakers to date are in the treaties with Armenia, Canada, Hungary, Netherlands and the United States.
17. **Article 7.2**  
We cannot trace any new treaties that include the important revised article incorporating the functions, assets and risks tests. What is the government's policy in this regard?
18. **Article 12.2**  
There is a common problem in relation to the conflicting characterisation of software royalties. Paragraph 14 to the OECD Commentary on Article 12 expresses the view that the right to simply copy software onto the computer user's hard drive is an operational facility that does not amount to a copyright such as would exist if, as discussed in paragraph 13.1, the licensee had the right to distribute the programme, HMRC has reiterated this interpretation in its International Manual INTM342630. However, it seems that this principle is not always followed, particularly in non-OECD countries. In such a case, withholding tax is deducted at source from the licensing payments in the payer's country.

19. In this conflict situation it is unclear whether HMRC would allow the withholding tax to be offset against a UK company's corporation tax liability, even assuming that Article 12.2 of the relevant treaty included copyright within the royalty definition; although it is arguable that the source country definition should be respected. It is presumably possible that HMRC would instead suggest that the UK taxpayer seek a refund of the withholding tax from the foreign jurisdiction on the basis that the licensing fee does not relate to copyright.. That was the decision of the Finland Administrative Court in its recent judgement of 12 December- 2011-KHO 2011;101.
20. In order to minimise the risk of such conflicts, the government could give consideration to making specific reference in article 12.2 to software copyrights within the scope of paragraph 13.1 of the Commentary.

## DETAILED COMMENTS - COUNTRIES

### *Brazil*

21. We appreciate the particular problems posed by Brazil which has been the subject of discussion at earlier meetings. We would welcome an annual update.

### *Hungary*

22. The 'triangulation' provision in the Treaty denies withholding tax relief if interest received by a third country branch of e.g. a Hungarian company from a UK borrower where the overall Hungarian/third country tax rate on the interest received is < 60% of the Hungarian rate if all profits had been taxable in Hungary. Was this driven by the introduction of the UK foreign branch elective exemption as regards the reverse situation?

### *Israel*

23. Israel is right at the bottom of the countries listed in the Annex to Steve Resznetniak's December letter and so is anticipated to be the last of the 22 countries with which treaty negotiations will be concluded.
24. The current treaty dates back to 1962 and contains a 'subject to tax' condition in Article 8A(4) which results in SSE gains on Israeli subsidiaries becoming subject to Israeli tax.

### *Qatar*

25. Some of our members have encountered practical issues with the new UK/Qatar treaty where local practitioners and tax authorities are not familiar with the process for obtaining relief at source (or indeed relief by way of refund). Is it possible for HMRC to encourage new treaty partners to publicise and streamline such processes?

## Further contact

26. For any further enquiries please contact:

<p>Ian Young International Tax Manager, ICAEW Tax Faculty Email: <a href="mailto:ian.young@icaew.com">ian.young@icaew.com</a> Tel: +44 (0)20 7920 8652</p>	<p>Peter Cussons Partner, PwC LLP Email: <a href="mailto:peter.cussons@uk.pwc.com">peter.cussons@uk.pwc.com</a> Tel: +44 (0)20 7804 5260</p>
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## THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <http://www.icaew.com/~media/Files/Technical/Tax/Tax%20news/TaxGuides/taxguide-4-99-towards-a-better-tax-system.ashx> ).