

TAXREP 53/04

ATTRIBUTION OF PROFITS TO PERMANENT ESTABLISHMENTS – PART 1 (GENERAL CONSIDERATIONS)

*Memorandum submitted on 22 October 2004 to OECD by the Tax Faculty of the
Institute of Chartered Accountants in England and Wales to the Discussion Draft
issued by OECD on 2 August 2004*

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INTRODUCTION

1. The present paper comments on the discussion draft issued by OECD on 2 August 2004. A first discussion draft on the same subject was issued by OECD in February 2001.

WHO WE ARE

2. The Institute of Chartered Accountants in England and Wales ('ICAEW') is the largest accountancy body in Europe, with more than 126,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.
3. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry through the Accountancy Foundation. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy, including taxation.
4. The Tax Faculty is the focus for tax within the Institute. It is responsible for tax representations 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 ICAEW who pay an additional subscription.

COMMENTS

Key entrepreneurial risk taking (KERT) functions

5. We note the key role that KERTs will play in the future determination of profits attribution to Permanent Establishments (PE). It is quite conceivable that the KERTs will be represented by individuals within multi national corporations (MNC) and that these individuals will move between countries and so carry out their functions from a different country location.
6. It would be helpful for the Guidance to provide practical information as to how to seek to attribute profits to PEs in such circumstances.
7. It would also be helpful to have more detailed discussion in the Guidance as to the nature of KERTs as they are envisaged by OECD.

Problems with dependent agents constituting a PE

8. If the activities of agents are sufficient to constitute a PE then it will follow that the KERT functions attributed to the PE will also have income attributed to them. This

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will cause the profitability of such structures to be greater than if they were an economically equivalent buy/sell distributor without constituting a PE.

9. We believe this may cause MNCs to have to reorganise their existing commercial arrangements which have been set up for good commercial reasons in order to avoid the PE risk under the proposed new regime.
- Intra entity asset transfers*
10. We are concerned that under the new proposals transfers of assets between the PE and the 'parent' company could give rise to irrecoverable double taxation.
11. In addition we believe these proposals may breach the European Treaty as they would give rise to an exit charges and would fall within the recent decision in *De Lasteyrie du Saillant* (Case C 315/02). This is of some importance as 19 out to the 30 member countries of OECD are EU member states.
- Deemed royalties*
12. Under the new regime it may be possible for deemed royalties to arise for instance in respect of the use of intellectual property but the Guidance makes it clear that in such circumstances there will be no potential withholding tax.
13. We would welcome confirmation that if there are deemed interest or rental payments between the PE and its 'parent' there will also be no withholding tax in those circumstances.

IKY October 2004