



TAXREP 3/13

(ICAEW REP 6/13)

ICAEW TAX REPRESENTATION

OECD Model Tax Convention Article 5 Permanent Establishment

Comments submitted on 31 January 2013 by ICAEW Tax Faculty in response to OECD discussion draft *OECD Model Tax Convention: Revised proposals concerning the interpretation and application of Article 5 (Permanent Establishment)* published on 19 October 2012

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the discussion draft OECD Model Tax Convention: Revised proposals concerning the interpretation and application of Article 5 (Permanent Establishment) published by OECD on 19 October 2012.
2. We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.
3. Information about the Tax Faculty and ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's Ten Tenets for a Better Tax System by which we benchmark proposals to change the tax system.

WHO WE ARE

4. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 138,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
5. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
6. The Tax Faculty is the voice of tax within ICAEW and is a leading authority on taxation. Internationally recognised as a source of expertise, the faculty is responsible for submissions to tax authorities on behalf of ICAEW as a whole. It also provides a range of tax services, including TAXline, a monthly journal sent to more than 8,000 members, a weekly newswire and a referral scheme.

COMMENTS

Issue 2: Meaning of "at the disposal of"

7. We suggest the addition of "and exercises that right via one or more employees or dependant agents physically present at the location" after "(e.g. where it has legal possession of that location)" in paragraph 4.2.
8. We do not believe it can be right that the mere right to legal possession, even if exclusive, constitutes a PE at that location if the right to possession is never exercised. A mere right of possession does not constitute economic activity. It simply excludes others from lawfully occupying the location.

Issue 6: Time requirement for the existence of a permanent establishment

9. We remain extremely concerned by the proposed exceptions to the general rule, which has been in place for more than 50 years, that a place of business can only constitute a permanent establishment (PE) if it has been in use for a period of more than six months.
10. Since the earlier discussion draft of October 2011 the examples have been changed and rather than an annually recurrent 5 week period there is now one of 3 months and while the single period of occupation remains at 4 months for the catering facilities example the background facts have been altered.

11. The likelihood is that countries will begin to argue that a PE has been established even though the fixed place of business has been in existence for less than 6 months and this will lead to considerable uncertainty.
12. One of the underlying rationales behind the OECD work in this area is to stimulate international trade and we are worried that the changes, currently proposed, will have exactly the opposite effect. Businesses will be concerned about beginning to operate in countries where they fear that those countries will begin to argue, almost from the outset, that what they are doing constitutes a PE. Business requires clear rules and certainty. The current proposals will create the opposite effect.
13. We accordingly recommend adding “The existence of a permanent establishment as illustrated above should be viewed as arising only in very exceptional circumstances and the general rule remains that a permanent establishment should not exist unless the local presence has subsisted for 6 months or more.” at the end of each of paragraphs 6.1 and 6.2.

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

14. Despite the fact that some changes are proposed in the revised discussion draft, the issue relating to the overall responsibility of the contractor on the on-site operation by the subcontractor has not been solved.
15. As previously stated, Issue 8 should surely be dealt with under the dependent agency type PE rule rather than deeming the subcontractor(s) to be a PE of the non-resident main contractor. Also, this "principle" of deeming a third party subcontractor to be a new type of PE of the main contractor could be extended to other industries e.g. financial services regarding brokers acting for non-resident principals. We believe this to be a very unhelpful proposal from the perspective of business.
16. We therefore strongly recommend that the wording change in paragraph 19 i.e. the addition of the words “all or” is not proceeded with and the necessary consequential changes are made.
17. Equivalently, the “acting alone or” wording in paragraph 10.1 should be deleted and the necessary consequential changes should be made.

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APPENDIX 1

ICAEW 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 [icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx](https://www.icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx))