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**Committee of Experts on International Cooperation in Tax Matters**

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Item 3 (c) of the provisional agenda

Tax treatment of services

**ADDITIONAL COMMENTS ON FOLLOW UP NOTE ON TAXATION OF FEES  
FOR TECHNICAL SERVICES**

*Summary*

The attached note represents comments by El Hadji Ibrahima Diop, a Member of the Committee of Experts on International Cooperation in Tax Matters, on the follow up note prepared by Professor Brian J. Arnold on Taxation of Fees for Technical Services, which is for consideration at the Annual Session as document E/C/2012/CRP.4. The note is prepared to assist the Committee in its consideration of Professor Arnold's note.

## REMARKS ON THE NOTE ON THE TAXATION OF FEES FOR TECHNICAL AND OTHER SERVICES UNDER THE UNITED NATIONS MODEL CONVENTION

El Hadji Ibrahima DIOP<sup>1</sup>

First of all, we congratulate the author of the note (Professor Brian J. Arnold) for the quality of the work in his follow up note.<sup>2</sup> He has given very good summary of the state of taxation law of fees for technical and other services under United Nations Model Convention and has presented relevant propositions for consideration by the Committee of Experts.

However, we have some comments about the form and the content upon which depends my position:

### **1- About the form**

The paragraph 2.2 is not related to identification or definition of technical and other services, when it is inserted in the section 2 dealing with “What are technical and other services?” This point address the issue of the tax rules applied to technical and other services. It should be linked to the section 3 (The treatment of fees for technical and other services...). So the section 2 could be more developed. And in our opinion, it was the occasion of proposing a definition and/or a classification of technical services, even though, at this point in time, any definition is available in the tax treaties. The subcommittee would have been able to discuss, improve or dismiss such a proposition. As far as we are concerned, we propose further a definition of fees for technical services and other services (cf. 3- Our position).

### **2- About the propositions**

All the options proposed by the author have advantages and help in different levels to deal with the issue of taxation of fees for technical services. In order to make a justified choice among all the approaches proposed, we address some comments on each option as follows.

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<sup>2</sup> Document [E/C.18/2012/CRP.4](#)

§	Options	Comments
	<i>Revise the commentaries</i>	<i>Generally, the revision of the commentary would have a narrowed impact for such an important issue like technical fees. It would be more significant to emphasize through an article and commentaries rather than commentaries only.</i>
4.1	Revise the Commentary to Provide a Discussion of the Treatment of Income from Technical and Other Services	The inclusion of a discussion of the issue in the Commentary would be useful to identify and explain the issue for tax administrations of developing countries. But would not actually help the administrations to deal with that issue. So, this proposal is not useful in a large extend as far as it does not allow countries to overcome the issue.
	Revise the Commentary to Provide a Discussion of the Issue and Identify Alternative Provisions that Countries Might Adopt Based on Existing Country Practices	This option is useful in the sense that it gives a description of the provisions dealing with technical services which have been already adopted in some treaties. Nevertheless, it will be of no use for countries which adopt specific article dealing with technical services.
4.4	Revise the Commentary to Provide a Discussion of the Issue and Alternative Provisions that Countries Might Adopt	This option has the advantage to be consistent because the Commentary would include not only a discussion of the issue but also alternative provisions that countries would be encouraged to use if they agree to go in such way.
	<i>Revise articles</i>	<i>Generally, revising articles has a broader impact, as articles may have greater legal value than commentaries.</i>
4.2	Reduce the Threshold Period for the Application of Article 5(3)(b) and Article 14(1)(b)	This approach can be relevant for developing countries as it expands taxing rights over income from business and technical services as for other types of services. However, it will be necessary to define the scope of the income that will be concerned by the

		<p>reduced time threshold although we prefer this reduction being applied on all types of services.</p> <p>In the other hand, it will be better to specify clearly the reduced time threshold in the articles to be negotiated by the parties. Otherwise, developed countries may attempt to make their option prevailed over those of developing countries.</p>
4.5	Revise Article 12 to Include Technical and other Services	<p>This option would not deal with the issue of technical services specifically; consequently, the provision of Article 12 would be more complex and difficult to understand and implement, as its scope would become wider.</p>
4.6	Revise Article 14	<p>This proposition goes with option 4.2. In addition of reducing the time threshold, it allows source country to tax any payments for technical services. In that way, its advantage consists in restoring more fiscal justice and equity.</p>
4.7	Revise Article 21	<p>In general, Article 21 can only be applicable to fees for technical services in a very limited number of cases. As, the UN Model Convention does not contain specific provisions dealing with fees for technical, management, and consulting services provided by a resident of one contracting state to a resident of the other contracting state, income from business services performed in a country is governed by Article 7 (Business Profits) or Article 14 (Independent Personal Services). However, as there is no clear and complete definition of services, article 21 can apply in some cases. Article 21 has broad scope, it concerns all services not dealt with in the previous articles. It can be also considered as an alternative option in dealing with technical services and other similar services. But a new and specific article remains the most appropriate option.</p>

	<p><i>Add a new article</i></p> <p><i>This option has the advantage of being more relevant and appropriate. It points out clearly the position of UN Model Convention. The commentary which goes with the new article can make all the necessary precisions.</i></p>
4.8	<p>Add a New Article and Commentary Dealing Expressly with the Taxation of Income from Technical and Other Services</p> <p>This proposal has the advantage to indicate clearly the way the UN Model Convention is ready to threat technical fees and other services for tax matters. It offers the opportunity to specify the scope of the services to which these provisions apply.</p> <p>The fact such an article exists in the UN model will be an opportunity for developing countries to negotiate their treaties with secure conditions in the way to preserve their taxing rights.</p> <p>According to me, even if it is difficult, it would be better to have a definition of the services dealt in that article or to determine some criteria or examples for those services (like article dealing with PE).</p> <p>If that is not possible, we could follow and clarify further the wording of the existing provisions in some actual treaties.</p>
<p><i>Treat a subsidiary like a PE</i></p>	
4.9	<p>Deem a Subsidiary to be a Permanent Establishment</p> <p>With this approach, any income derived by the parent corporation from services provided to its subsidiary would be subject to source country taxation in accordance with the rules of Article 7. It can be a good alternative to tax technical services delivered by a parent company to its subsidiary as regards to the payments. Technical services fees are a good way for parent companies to transfer profits made by its subsidiaries.</p> <p>Treating a domestic subsidiary as a PE of its nonresident parent corporation can raise some difficulties related to the definition of a subsidiary and the treatment of payments made between related entities.</p>

### **3- Our position: special treatment of (technical) “services”**

Altogether, we are favorable for the proposal consisting in adding a new article and commentary dealing expressly with the taxation of income from technical and other services (Option # 4.8) for the reasons stated above.

Therefore, we propose these definitions of technical services:

- *Wide definition*
  - ✓ any specialized help provided by third parties in connection with the business activity of the enterprise or
  - ✓ payments in consideration of services of managerial, technical or consultancy nature, including the provision of services of technical or other personnel or
  - ✓ (in other words) payments of any kind to any person, other than payments to an employee of the person making the payments and to any individual for independent personal services, in consideration for services of a managerial, technical or consultancy nature
  
- *Narrow definition (“included services”):*
  - ✓ technical services are those “requiring expertise in technology”
  - ✓ excludes consultancy in non-technical sectors

The main difference between the two definitions is the presence of a “make available” clause, which means that the services provided should make available the technical knowledge, experience, skill, know-how or processes, etc. to the user. Even if the services are in the nature of managerial, technical or consultancy services, but if they do not make available any technical knowledge, experience, etc., as discussed above, then the consideration would not qualify as fees for technical services under the narrow definition.

However, we believe that the scope of the definition of fees for technical services should be narrowed down to include only those services, which make available any technical know-how, skill, knowledge etc.

## ANNEX

(Why do we propose a definition of technical services? – Benchmark)

We know that “Technical services” includes a range of services involving technical knowledge, assistance in technical operations, maintenance and other support in respect of technical matters. Moreover, the term “fees for technical services” has not been defined in either OECD or UN Model Conventions. However, the same is defined in US Model Convention.

US Model Convention defines “fees for technical services” as under:

“**Fees for included services**” means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including the provision of services of technical or other personnel) which:

- are ancillary and subsidiary to the enjoyment of the property for which a payment described as “Royalty” is received; or
- make available technical knowledge, experience, skill, know-how or processes, or consist of the development and transfer of a technical plan or technical design.

It **specifically excludes** the following amounts paid:

- for services that are ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of property, other than property described as “Royalty”;
- for services that are ancillary and subsidiary to the rental of ships, aircraft, containers or other equipment used in connection with the operation of ships, or aircraft in international traffic;
- for teaching in or by educational institutions;
- for services for the private use of the individual or individual making the payment; or
- to an employee of the person making the payments or to any individuals or partnership for professional services i.e. Independent personal services.

Moreover, the Protocol to the US Double Tax Avoidance Agreement with some countries (e.g.: India) further clarifies the provisions pertaining to the definition of the treaty by laying down the following principles regarding characterization of fees for technical services under the treaty:

- that consultancy services which are **not of a technical nature** cannot be included services;
- fees for included services exclude any service that does not make technology available to the person acquiring the service. The technology will be

- considered “made available” when the person acquiring the service is **enabled to apply the technology independently**;
- the fact that the provision of services may require technical input by the person providing, it does not *per se* mean that the technical knowledge or skill, etc. are made available to the person purchasing the service.