Workshop on Double Tax Treaties and
Base-Eroding Payments for Developing Countries
Nairobi, Kenya, 21-24 March 2017

CASE STUDY ON SERVICES

1. Facts

Alpha Corporation is a resident of Country A for purposes of the tax laws of Country A and the tax treaty between Country A and Country B. Beta Corporation is a resident of Country B for purposes of the tax laws of Country B and the tax treaty between Country A and Country B. Alpha Corporation owns all of the shares of Beta Corporation. Alpha Corporation and Beta Corporation are both engaged in manufacturing automobiles. Beta Corporation manufactures and sells automobiles under license from Alpha Corporation. The license agreement provides that Beta Corporation will pay royalties of 2 million annually for the right to use Alpha Corporation's patents, trademarks and other proprietary information concerning the manufacturing of automobiles. In addition, the license agreement requires Beta Corporation to upgrade its manufacturing process and to pay Alpha Corporation 1 million for technical assistance in improving its manufacturing process.

Assume that there is a tax treaty between Country A and Country B that is identical to the United Nations Model Convention.

Alpha Corporation sends some of its employees to perform various functions in connection with Beta Corporation's manufacturing activities. Giulia is an engineer who specializes in quality-control processes. She is a resident of Country A, where she has lived her entire life. Giulia is sent by Alpha Corporation to Country B to monitor Beta Corporation's manufacturing activities and ensure that it adheres to technical standards set out in the license agreement. Giulia has the use of an office in Beta Corporation's manufacturing plant during her two years in Country B. Giulia is assisted in her work by a team of Alpha Corporation's employees who each spend 5 months in Country B. These employees work out of Giulia's office during their time in Country B.

Marco and Robert are also employed by Alpha Corporation as engineers. They are sent by Alpha Corporation to assist Beta Corporation in modernizing its manufacturing operations. Marco and Robert are both residents of Country A and both spend 14 months in Country B assisting Beta Corporation. Marco becomes an employee of Beta Corporation;

however, Robert remains an employee of Alpha Corporation in order to avoid complications concerning his pension. Beta Corporation reimburses Alpha Corporation on a monthly basis for Robert's salary and fringe benefits.

Beta Corporation engages two other individuals who are resident in Country A. Oscar is an engineering consultant who is hired to work on robotics in Beta Corporation's manufacturing facilities for 5 months. Oscar and Beta Corporation enter into a contract in which Oscar is described as an independent contractor and not an employee. Oscar works with other engineers who are full-time employees of Beta Corporation. He receives the same amount of basic compensation as the full-time employees and he is subject to the same supervision and control as the full-time employees. Lucinda also works on robotics alongside Oscar and the other engineers. She is an employee of Engineers International, a firm resident in Country A that supplies engineers to foreign companies for short-term overseas assignments. Lucinda also works for Beta Corporation for 5 months in Country B.

2. Questions

Assuming your country is Country B, is your country entitled to tax, under the provisions of its domestic law and the provisions of the treaty between Country A and Country B, the income derived by:

(a) Alpha Corporation from Beta Corporation;

(b) Giulia;

(c) Giulia's team of Alpha Corporation employees;

(d) Marco;

(e) Robert;

(f) Oscar; and

(g) Lucinda?