Eric Mensah - Replies to questionnaire

What are the basic differences between UN and OECD Tax treaties? What is the impact of UN and OECD type tax treaties in developing countries?

The UN Model generally follows the pattern of the OECD Model Treaty, many of its provisions are identical. The most prominent difference between the two models is that the UN Model imposes fewer restrictions on the taxes that may be imposed by developing countries. For instance with respect to the withholding rates on passive income to be imposed by source countries the UN Model Treaty does not impose specific limitations instead it has left it to bilateral negotiations between the contracting parties.

The UN Model Treaty also allows the source country to tax more cross border business profits than the OECD Model Treaty by lowering the threshold for a PE. For instance the OECD Model in Article 5 has the following as the threshold for what constitutes a PE *"A building site or construction or installation project constitutes a permanent establishment only if it lasts more than twelve months."* Whilst the UN Model also under Article 5 has the following in terms of the threshold for a PE as *"a building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only if such site, project or activities last more than six month"*

The OECD Model further favours residence (capital exporting) countries over source (capital importing) countries as found in the UN Model Treaty. The OECD Model therefore requires that the source country gives up some or most its taxing rights on certain categories of income earned by the residents of the other Treaty State.

The Commentaries on the Articles in the OECD Model treaty are easier to change as compared to the Articles of the OECD Model Treaty.

Most developing countries base their Models on the UN Model as a result of the differences stated above.Since most developing countries are capital net importers the UN Model favours therefore developing countries. Since the Treaties are based on negotiation when the Treaties are negotiated it usually becomes a combination of both. For other developing countries their model is a combination of both and they therefore choose and pick what favours the depending on their tax policy considerations.

How do treaties signed by the EU allow for double-non-taxation? What is the effect of tax treaties on tax evasion and tax avoidance?

In general Treaties signed by contracting parties is to eliminate tax avoidance and evasion and to prevent double taxation as stated in the title and in the preamble of Treaty Models. The preamble is currently mandatory for all countries since its states the clear intention of the contracting parties. The occurrence of globalisation in the world's economy has resulted in differences with respect to the application of tax regimes to taxpayers. This is with respect to the paucity of information especially where income is located outside the jurisdiction. Governments have recently focused on addressing these gaps in the interaction of the domestic tax systems which result in double non taxation. Where residents are not taxed in both jurisdictions there is the occurrence of double non taxation. This defeats the object and purpose of the Treaty since it is against double taxation and not in favour of double non taxation.

In some cases tax sparring provisions are found in some Treaties and this leads to double non taxation. In instances where developing countries want to encourage foreign direct investments, it provides for tax sparring provisions in its Treaties to attract these investors. When the other treaty partner does not tax that particular income it means that the resident taxpayer avoids the payment of taxes altogether in both jurisdictions.

As stated earlier the objective of the treaty is to prevent tax avoidance and tax evasion, however there are many instances where this objective has not been reached. Resident taxpayers exploit the provisions of the Treaty to their advantage in order to avoid or evade the payment of taxes to both contracting States. Developing countries lose out on revenue that should come to her since these taxpayers are sophisticated and are far advanced as compared to the capacity of Revenue Authorities in developing countries. They employ sophisticated means to be able to avoid and evade taxes under the Treaties by setting up conduit companies just to benefit from the provisions even though under normal circumstances it will not benefit.

Before the G20/OECD's work on BEPS, taxpayers could abuse the provisions of the Treaties signed, especially where there were no general anti avoidance provisions under domestic law so that the Tax Authorities could disallow the benefits as claimed by the Tax payer. With the work of the OECD on Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6, it makes a change to the Model Treaty. This change is to clarify that the intention of tax treaties are not to create opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping). The report

also addresses treaty shopping through alternative provisions and by establishing a minimum standard for which all participating countries have agreed to. The report also includes specific treaty rules to address other forms of treaty abuse and ensures that tax treaties do not inadvertently prevent the application of domestic anti-abuse rules. Countries therefore will have to meet this standard by adopting in their tax treaties one of three alternatives as follows:

(1) adopt the principal purpose test (PPT) rule;

(2) adopt the PPT rule and the simplified limitation on benefits (SLOB) rule; or

(3) adopt a detailed limitation on benefits (LOB) rule supplemented by a specific rule to deal with so-called conduit financial arrangements.

Some countries have done that bilaterally (Ghana renegotiated its Treaty with Netherlands to include an anti-abuse provision) whilst others with a wide Treaty network will need to sign unto the Multilateral Instrument (MLI).

What is in your view the impact of the tax treaties signed by the EU on developing countries?

Most developing countries will not initiate the process of negotiating a Treaty with another jurisdiction. Ghana has currently nine (9) Double Taxation Agreements in force. For almost all the ratified treaties, Ghana was approached by the other Contracting State. There may or may not be an increase in FDI flows into the country if a DTA exists between both countries. There are numerous considerations that are made by investors before they invest in a particular jurisdiction. Some studies have shown that tax is the least of them. Other studies have also shown that tax considerations are important for investors. The residents of Contracting Parties who therefore invest in Ghana, take advantage of the benefits in the agreement to minimise their tax obligations once they are entitled it. Others also shop around to look for the best jurisdictions where they can take advantage of the tax provisions and set up entities or companies there. An example can be given of ActionAid report on the abuse of treaties titled ‘Calling Time Report’. Data from Ghana’s investment Agency showed that the highest investments in the country was not from a treaty partner. In effect it is good to sign tax treaties with other countries not only to benefit from FDIs but also the assistance in

collection of taxes, exchange of information and benefits from the mutual assistance procedure.

What would your recommendation be to this committee regarding action that the EU should take in tax matters?

- The EU should be more consistent in tax matters
- It should ensure that it walks the talk and try as much as possible not to have too many reservations on the OECD Model Treaty as they are not bound by the Articles in the Treaty when there is a reservation.
- Encourage developing countries to build their capacity in order to negotiate on an equal footing with developed countries

What a fair tax treaty should look like?

Treaties should not be imposed on developing countries, it should be a matter of choice. Since it is a matter of negotiations, the best negotiating team will have an upper hand, we can only have a fair tax treaty where both contracting parties can negotiate on an equal footing