PLATFORM FOR TAX GOOD GOVERNANCE

Follow-up of the Communication on the External Strategy:

Tax Treaties between Member States and Developing Countries

Meeting of 14th June 2016

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INTRODUCTION

In its recent Communication on the External Strategy for Effective Taxation, the Commission suggested that Member States should apply a balanced approach to negotiating bilateral tax treaties with low-income countries, taking into account their particular situation. (1)

The Commission also announced that it would launch a debate with Member States, within the Platform on Tax Good Governance, on how to ensure fair treatment of developing countries in bilateral tax treaties.

This paper intends to open the discussion on this particular issue, by presenting some recent research in this area.

BACKGROUND

It is not the first time the Commission has considered the issue of bilateral tax treaties between EU Member States and developing countries.

In its 2009 Communication on Promoting Tax Good Governance, the Commission expressed the need to ensure more coherence between Member States' individual positions in the international tax scene and the agreed good governance principles, including in bilateral tax treaties with third countries:

The extent of coherence between the principles of good governance in the tax area and Member States' own tax policies, including bilateral tax treaties with third countries, should also be examined. It would be important to ensure that Member States do not, through their bilateral tax treaties, open up new opportunities for tax avoidance of other Member States' tax systems or for circumvention of EU directives. At the same time, the existence of good-governance obligations in EU level agreements with third countries would provide bargaining strength for Member States in their bilateral negotiations with those countries. (2)

Furthermore, in 2010 (3), the Commission committed to provide support for the adoption and implementation of the good governance principles, including by strengthening capacities to conclude and implement TIEAs and double tax treaties between Member States and developing countries.

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Moreover, the impact of Member States tax policies - including tax treaties - on developing countries has been recently investigated by reports made by an independent firm on behalf of two Member States' tax administrations (IRL, NL) (4), international organizations - OECD, UN, IMF – (5) and NGOs (6).

Ireland, the Netherlands and EuropAid will present their conclusions and recommendations at the June Platform meeting.

MAIN ISSUES

Whereas tax treaties between developing and between industrialized economies are symmetric, involving a similar amount of cross-border activity in each direction, a treaty between a developing and an industrialized economy is most likely asymmetric, having a larger flow of capital towards the developing and a larger opposing flow of capital revenues towards the industrialized economy.

Specific elements of tax treaties concluded with developing countries, such as the right to levy withholding taxes, are critical for domestic revenue mobilization. In fact, developing countries derive a greater proportion of their revenues from corporate income tax than developed countries do. In addition, due to the complexity of international taxation and their limited administrative capacity, developing countries are highly dependent on source-based taxation. Therefore withholding taxes on outbound payments are an essential component of their tax income. However, tax treaties override domestic rules and consequently reduce the capacity of developing countries to levy withholding taxes, which are must easier to administer and collect. In the External Strategy, the Commission invited Member States to reconsider aspects of their bilateral tax treaties with developing countries, such as provisions on withholding taxes.

Other tax treaty aspects of relevance for developing countries could also be considered in this context, such as permanent establishment, capital gains, transfer pricing or arbitration.

Platform members are asked to share their experience in this area and express their views on whether and how a fairer treatment of developing countries should be ensured in bilateral tax treaties.

4 IBFD, Possible Effects of the Irish Tax System on Developing Economies, 2015; IBFD, Onderzoek belastingverdragen met ontwikkelingslanden, 2013.

5 OECD, Implementing the BEPS package: establishment of an inclusive framework, 2015; United Nations, Protecting the Tax Base of Developing Countries, 2015.