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18 October 2019



HAPPY FRIDAY!

The **Unified Approach** lacks unified support amongst **developing countries**; **aviation tax** takes off in **Germany**; the **US** tech industry cries to **Washington** (and not **Mexico City**); and **Luxembourg** rules out grandfathers!

Sharpcan loses its gamble; the **Indian** tax authorities can't leave **Mauritius** alone; **Argenta Spaarbank** loses its notional deduction; but the **Irish Bank** acquires notional capital!

UK VAT aims for the moon; **Kenya** returns credit; **Paraguay** taxes transparent entities; and **Italy** avoids the trigger!

But, at the end of the week, the big question is: has **Boris Johnson** got the numbers? We'll soon find out!

Have a great weekend!

Steve

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#AskSteve



Episode 8

To be released on
23 October 2019

Episode 7

Why did you stay at
Deloitte for the whole of
your career?

IN TODAY'S VIDEO PODCAST

(For ITB video subscribers, please log in to access the video and documents/reports)

1. Digital taxation
2. Trade & other global developments
3. Asia Pacific
 - Australia, India, Malaysia
4. Europe
 - ECJ, EU, Germany, Greece, Italy, Luxembourg, Portugal, UK
5. Africa
 - Kenya
6. Americas
 - Mexico, Paraguay, US
7. Treaties
8. Worth reading

WORTH READING

Chetan Vagholkar and Eric Horvitz

["The GILTI High-Tax Exception: The Good, the Bad and the Ugly"](#)

Tax Notes International, Tax Analysts, September 30, 2019 (subscription service)

Mukesh Butani and Tarun Jain

["Reflections on India's Corporate Tax Rate Cuts"](#)

Kluwer International Tax Blog (free service)

Benjamin Satterthwaite

["Nash Bargaining Theory and Intangible Property Transfer Pricing"](#)

Tax Notes Today International, Tax Analysts, October 17, 2019 (subscription service)

INTERNATIONAL TAX QUIZ

ACO is a company which is resident in country **A**. It is an accredited internet domain name registrar authorised by Internet Corporation for Assigned Names and Numbers (ICANN).

BCO is a company which is resident in country **B**.

BCO pays a fee to **ACO** to register its internet domain name.

Is the fee a royalty, as defined in Art. 12 of the A/B double tax treaty?

Please provide separate answers for: (i) assuming the A/B treaty is identical to the 2011 UN model treaty; and (ii) assuming the A/B treaty is identical to the 1996 US model treaty.

Answer in next week's ITB email alert!

[Last week's question & solution](#)

XCO is a company resident in country **X**.

XCO places money on a term deposit with an unrelated **Bank**, which is resident in country **Y**.

The deposit carries a fixed negative interest rate – i.e., **XCO** pays interest to the **Bank**.

The **X/Y** treaty is identical to the 2014 OECD model treaty. Assume that the **Bank** is the beneficial owner of the interest, and that it does not have a **PE** in country **X**.

Question 1: What is the treatment of the interest (which is paid by XCO to the Bank) under the X/Y treaty?

Due to further negative movements in market interest rates, the **Bank** decides to terminate the deposit before its maturity date. This triggers a penalty fee (imposed on the **Bank**) under the terms of the deposit.

Question 2: What is the treatment of the penalty fee (which is paid by the Bank to XCO) under the X/Y treaty?

Question 1:

1. There is no guidance on this issue from the OECD, either in the Commentary or elsewhere. Moreover, although there is some guidance from country tax authorities on aspects of the tax treatment of negative interest (e.g., tax deductibility), there is very little on the characterisation of negative interest for treaty purposes.
2. The relevant part of the definition of "interest" in Art. 11(3) is "income from debt-claims of every kind". This suggests that the income must flow from an asset (being a debt-claim) of the income recipient, and not from a liability. Also, unsurprisingly, the OECD Commentary on Art. 11(3) is written on the assumption that the interest is paid by the debtor to the creditor. The reference to "negative interest" in paragraph 20 of the Commentary refers to bonds which are issued at a premium, which is arguably a different topic from negative coupon interest.
3. It has been suggested that negative interest should be characterised, not as interest, but as a fee charged by the debtor.
4. At present, the better view is that the negative interest is not "interest" as defined in Art. 11(3).
5. As the creditor is a bank, Art. 7(1) should apply to provide an exemption from X tax.

Question 2:

1. The penalty fee is paid by debtor to creditor, and thus the issue considered above does not arise here.
2. But, nevertheless, the question remains: is the penalty fee "income from debt-claims of every kind" (Art. 11(3) definition of "interest")?
3. Again, there is no OECD guidance on this topic, and arguments can be made for and against.
4. If it is "interest", then Y may tax the fee up to a limit of 10% on gross (assuming XCO satisfies the conditions in Art. 11(2) & (4)). X must then provide a credit for the Y tax: Art. 23A(2) or Art. 23B(1).
5. If it is not "interest", then the fee should be exempt in Y (assuming XCO does not have a PE in Y), under either Art. 7(1) or Art. 21(1).

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