

Arvid Aage Skaar

**THE DEPENDENT
SERVICES **CLAUSE**
IN TAX TREATIES
A CASE LAW STUDY**

The Dependent Services Clause in Tax Treaties

Why this book?

This book is a study of court practice dealing with tax treaty provisions concerning cross-border dependent personal services. Which country has the right to tax employees' cross-border earnings such as salaries and similar remuneration for work? Hopefully, the book will be useful for practitioners and for further research.

The author analyses more than 280 court decisions from 24 countries, all dealing in some way with cross-border earnings from employment work. The aim is to support the needs of practitioners and to facilitate further research on these topics.

The court decisions deal with salaries and similar benefits and remuneration from dependent personal services, pensions, savings schemes, severance payments, sickness payments, stock options, government services, frontier workers, hiring out of labour, services aboard ships and aircraft, trucks and trains, sportspersons, artists, musicians, professors and teachers, and more.

In the analysis of these topics, a number of other important tax treaty issues are visited, such as treaty interpretation in good faith under the Vienna Convention on the Law of Treaties, the limits of the tax treaty mutual agreement clause, static vs dynamic interpretation of tax treaties, subject-to-tax provisions, the tax treaty renvoi clause, the other income clause of the tax treaties, the status of the OECD Commentary as a legal source, and exit tax on certain benefits.

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The Dependent Services Clause in Tax Treaties

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A Case Law Study

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Preface

My ambition with this book is limited to presenting an organized case law study. The book does not contain a coherent and holistic analysis of the topic. For the latter purpose, the reader is still referred to Professor Frank Pötgens's doctoral thesis, *Income from International Private Employment* (2006) as the leading work. However, being published in 2006, Professor Pötgens's book does not reflect the case law after 2006. Hence, the present book primarily focuses on the case law during the period 2006-2022.

I have benefited from the IBFD databases, both the case law and treaty databases, which have proven very useful for this purpose. The original versions of many of these court decisions are written in languages I do not command, and I depend entirely on the summaries written by a number of local reporters who have published their summaries in the database. Likewise, most of the treaties are quoted from an unofficial English version in the IBFD database. However, the use of secondary legal sources may create uncertainty, of which the reader should be aware.

I would like to thank the head of the library at the law school of the University of Oslo, Rebecca Josefine Fivie Bergstrøm, for all the support in finding the sources I needed for this book.

22 June 2023
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Terminology

All references to sources in this book are placed in the footnotes. In order to facilitate the reading of the text, the book uses the topic of the tax treaty articles as the “name” of the article, instead of referring to the number of the article, which may vary depending on the treaty. For example, “Article 15 Income from Employment” in treaties based on the OECD Model Tax Convention on Income and on Capital (OECD Model) is named the “employment clause”; and instead of writing in the text of the book: “article 15 of the Nordic Convention (1996)”, the text may be “the employment clause of the tax treaty”,¹ with a specific reference in a footnote (*see* footnote number 1 below as an example).

For readers who find this approach unusual, the following explanation of the most frequently used terms may be helpful:

Clause – article in a model treaty or corresponding articles in bilateral treaties, e.g. the employment clause (article 15 of the OECD Model)

Rule – paragraph in an article in a model treaty or corresponding articles in bilateral treaties, e.g. the exception rule (article 15(2) of the OECD Model)

Test – specific condition in a rule in a model treaty or corresponding articles in bilateral treaties, e.g. the 183-day test (article 15(2)(a) of the OECD Model)

Employment clause – article 15 of the OECD Model and corresponding articles in bilateral treaties

Main rule (the main rule of the employment clause) – article 15(1) of the OECD Model and corresponding articles in bilateral treaties

Exception rule (part of the employment clause) – article 15(2) of the OECD Model and corresponding articles in bilateral treaties

International traffic rule (part of the employment clause) – article 15(3) in an OECD Model treaty and corresponding articles in bilateral treaties

Dependent services clause – *see* employment clause

1. Art. 15 *Nordic Convention* (1996), *Treaties & Models* IBFD.

Independent services clause – article 14 of an OECD Model treaty (before 2000) and corresponding articles in bilateral treaties

Liberal profession clause – *see* independent services clause

Sportsperson and artists clause – article 17 of an OECD Model treaty and corresponding articles in bilateral treaties

Entertainer and sportspersons clause – *see* sportsperson and artists clause

Business clause – article 7 of the OECD Model and corresponding articles in bilateral treaties

Renvoi clause – article 3(2) of the OECD Model and corresponding articles in bilateral treaties

Elimination of double taxation clause – articles 23A and 23B of the OECD Model and corresponding articles in bilateral treaties

Other income clause – article 21 of the OECD Model and corresponding articles in bilateral treaties

Mutual agreement clause – article 25 of the OECD Model and corresponding articles in bilateral treaties

Residence clause – article 4 of the OECD Model and corresponding articles in bilateral treaties

The footnotes:

Please note that this author uses “cf.” in footnotes for references that do *not* directly support the author’s position in the text, but have some relevance or connection to the issue discussed.

The Latin word “con” is used for references that support the opposite view of the author or other sources mentioned in the same footnote.

Chapter 1

Introduction

1.1. Preventing double taxation

The purpose of the employment clause in tax treaties is to prevent double taxation, but not all double taxation. The starting point is that the taxpayer's state of residence under domestic laws has the right to tax income from the taxpayer's employment. However, if the taxpayer is working outside their state of residence, that state (the work state) normally also has a right under its domestic laws to tax the income. Tax treaties establish the threshold for the work state's right to tax the income, and the threshold for the residence state's obligation to grant foreign tax relief (elimination of double taxation). In addition, treaties establish the rules for the allocation of income to the two states once the threshold has been passed.

1.2. Which disputes cannot be solved by tax treaties?

A distinction is often made between juridical and economic double taxation. The tax treaties are designed to prevent the former (juridical double taxation) but not the latter kind of double taxation. Taxation of the same person for the same income and for the same year is harmful and devastating to international business and activities, and is not acceptable. Taxation of the profits of a corporation on the corporation and taxation of shareholders on the dividends paid out by the corporation on the basis of the profits are not considered to be in the same situation.

However, when is the same person taxed for the same income and for the same year? Obviously, juridical double taxation may occur if the tax office claims taxes to be paid by the taxpayer directly, while the employer has already deposited tax directly to the tax office. The tax office cannot demand the employee to pay for the same income, if the employer has already deposited the taxes directly.¹

1. Income Tax Appellate Tribunal (ITAT) High Court of Delhi decision no. 378 of 2007 dated April 23, 2007, cited from IBFD's case law database with comments by Dr Amar Mehta, Case Law IBFD; the decision is primarily dealing with the factual situation.

The disputes to be solved under the tax treaties are limited to cases between a state and a taxpayer – not between the states. Under international law, the state immunity prevents a lawsuit from other states on the issue of that state’s interpretation of a tax treaty (*acta jure imperii*).²

1.3. Who decides what the term “employment” means?

The term “employment” is not defined in the OECD Model Tax Convention on Income and on Capital (OECD Model), although the Commentaries now contain significant guidance, in particular concerning the choice between a “formal” approach and a “material” approach.³ In practice, whether an “employment” exists will normally be a decision by the work state, since the issue of taxation of the individual in the work state is in the interest of the work state. In the process of applying domestic laws in this respect, a distinction has to be made between “employment” covered by the employment clause, and other services covered by other provisions in the tax treaty, such as, for example, independent personal services covered by the independent services clause, if applicable, or the business clause. Since “employment” is not defined in the OECD Model, the meaning of “employment” in the domestic laws of the state that applies the treaty will be used.⁴

Normally, the income from employment is earned and accrued during the same year, the income year. If the income is earned in more than one country, all states will have a right to tax the income, subject to the exceptions established in the employment clause itself.⁵ Income earned over several years and accrued in one year shall also be taxed at source,⁶ if possible.

2. *Hof van Beroep* (Court of Appeals) Brussels in decision 2014/AF/242 dated May 15, 2019, cited from IBFD’s case law database with comments by Bob Michel, Case Law IBFD; this issue was solved by the court of first instance (Leuven).

3. *OECD Model Tax Convention on Income and on Capital: Commentary on Article 15* para. 8.2 et seq. (21 Nov. 2017), Treaties & Models IBFD.

4. The *renvoi* clause, *OECD Model Tax Convention on Income and on Capital* art. 3(2) (21 Nov. 2017), Treaties & Models.

5. Art. 15(2) and (3) *OECD Model* (2017).

6. Paras. 2.2 and 12.1 *OECD Model: Commentary on Article 15* (2017).

1.4. Residence in one of the two states

For a tax treaty to be applicable to solve the question of where the taxpayer's income from employment is subject to tax, the taxpayer has to be resident in one of the two states in question.⁷ The OECD-based tax treaties are worded so that only the state of residence may tax the income from dependent personal services (income from employment), unless the work is performed in another state.⁸ If the work is performed in another state, that other state may tax the income from the work. In reality therefore, the dependent services clause allocates taxing jurisdiction to the source state. Hence, if so, required by domestic laws, the taxpayer has to report the income from employment abroad both to the work state and to the residence state.⁹

7. Art. 1(1) *OECD Model* (2017).

8. *Id.*, at art. 15(1).

9. *Corte Suprema di Cassazione* (Supreme Court) decision 4559/2015 dated March 6, 2015, cited from IBFD's case law database with comments by Teresa Galluccio, Case Law IBFD.

Notes

A series of horizontal dotted lines for writing notes, spanning the width of the page and starting below the 'Notes' header.



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