

Sent by email: taxtreaties@oecd.org

Tax Treaties, Transfer Pricing and Financial Transactions Division
OECD Centre for Tax Policy and Administration
2, rue Andre Pascal
75775 Paris Cedex 16
France

28 May 2021

RE: Public Consultation Document – Proposed Changes to Commentary in the OECD Model Tax Convention on Article 9 and on Related Articles

Dear Sir/Madam,

The International Bar Association would like to take this opportunity to comment on the Public Consultation Document entitled Proposed Changes to Commentaries in the OECD Model Tax Convention on Article 9 and on Related Articles dated March 29, 2021 (the Consultation Document).

The International Bar Association (IBA), the global voice of the legal profession, includes over **[45,000]** of the world's top lawyers and **[197]** Bar Associations and Law Societies worldwide. The IBA is registered with OECD with number **1037 55828722666-53**.

We are submitting our comments on behalf of the IBA Taxes Committee which has **[1,037]** members from around the world. This committee formed a Working Group to respond to the Public Consultation.

The comments made in this report are the personal opinions of the Working Group participants and should not be taken as representing the views of their firms, employers or any other person or body of persons apart from the IBA Taxes Committee of which they are members.

The comments are enclosed with this letter.

Sincerely yours,

Francesco Gucciardo

*International Organization Liaison Officer
IBA Taxes Committee
Canada
Partner
Aird & Berlis LLP*

Torsten Engers

*International Organization Liaison Officer
IBA Taxes Committee
Germany
Partner
Flick Gocke Schaumburg*

Working Group Participants:

Laura Salviano Almeida da Costa

Machado Meyer Advogados

Brazil

Nikolaj Bjørnholm

Bjornhalm Law

Denmark

Pedro Angel Palma Cruz

Sanchez Devanny

Mexico

Barbara Gangl

Binder Grösswang

Austria

Pedro Gasparetto

Machado Meyer Advogados

Brazil

Ryan Rabinovitch

Fasken

Canada

Fernando Tonanni

Machado Meyer Advogados

Brazil

Christian Wimpissinger

Binder Grösswang

Austria

Below we address certain of the proposed changes to the commentary to the OECD Model Tax Convention set out in the Consultation Document (the Comentary).

Proposed Changes to the Commentary on Article 9

Paragraph 2

The amendment to paragraph 2 of the Commentary to Article 9 does not acknowledge that some countries have not fully adopted the arm's length principle in their domestic laws, which leaves multinational enterprises operating in such jurisdictions at a material disadvantage if the prescriptive and remedial elements of the Convention were limited solely to the extent that the non-adjusting State considers the adjusted profit to correctly reflect what the profits would have been if the transactions had been at arm's length.

This is the case, for example, in Brazil whose transfer pricing methods involve the use of fixed margins without a transfer pricing study or functional analysis. The mismatch in domestic approach (e.g. arm's length principle versus fixed margins or other methodologies) creates the potential for economic double taxation. Accordingly, it may be prudent to acknowledge that not all OECD member countries currently adhere to the arm's length principle and that if the remedy under Article 9 is limited solely to adjustments made in accordance with the arm's length principle, there is still scope for a remedy and the alleviation of double taxation under Article 25, which is reflected in the new paragraph 12.1 of the Commentary to Article 25. We believe that it is important to note within the Commentary to Article 9 itself that if the scope of Article 9 is to alleviate economic double taxation to the extent of an adjustment made on the basis of the arm's length principle, other instances of economic double taxation that arise as a consequence of adjustments that are not made on the basis of that principle still can and should be alleviated using the methodology set out in Article 25.

Paragraphs 3 & 3.1

We interpret the intention of paragraphs 3 and 3.1 of the Commentary to Article 9 as merely providing observations on the application of domestic law in pricing and/or characterizing transactions in order to provide context.

Paragraph 3 of the Commentary to Article 9 notes that in considering whether a purported loan should be regarded as a loan or as another kind of transaction, the State making the determination will do so taking into consideration factors discussed in its domestic laws, as well as those in the OECD Transfer Pricing Guidelines. It may be worthwhile to acknowledge and note that the lack of a single internationally recognized and unified concept of "debt" and "equity" is more likely to give rise to cases of economic double taxation where the domestic approaches among States differ. The Commentary itself might then encourage States to follow international standards so as to further the taxpayers' objective of achieving certainty. This could be accomplished by adding the following sentences to the end of paragraph 3 of the Commentary to Article 9:

"Instances of economic double taxation are more likely to arise when States apply materially different standards and approaches in determining whether a purported loan should be regarded as a loan or as another kind of transaction, which gives rise to a considerable amount of uncertainty for taxpayers. States are encouraged to apply uniform, internationally acceptable standards, such

as those outlined in Actions 4, 8-10, including section B of the February 2020 guidance in accurately delineating an advance of funds, for example.”

Turning to paragraph 3.1 of the Commentary to Article 9, it appears that the words “as long as there is conformity with the requirements of other provisions of this Convention” derogates from mere observation and context-setting by imposing a precondition on the instances in which a State’s domestic law should be applied to determine how allocated profits are to be taxed. As it currently reads, the first sentence of paragraph 3.1 of the Commentary to Article 9 suggests that it is not for the domestic law of each Contracting State to determine how allocated profits should be taxed if there is not conformity with the other provisions of the Convention. We question whether the words “as long as there is conformity with the requirements of other provisions of the Convention” are meant to impose a condition, and suspect that the concept of conformity with the other provisions of the Convention is the preferred and recommended approach. Accordingly, we would suggest revising the first sentence in paragraph 3.1 of the Commentary to Article 9 so as to read as follows (changes underlined):

“Once the profits of the two enterprises have been allocated in accordance with the arm’s length principle, it is for the domestic law of each Contracting State to determine whether and how such profits should be taxed, preferably in conformity with the requirements of other provisions of the Convention.”

Paragraphs 6 & 6.1

We believe that paragraphs 6 and 6.1 of the Commentary to Article 9 represent an improvement relative to the predecessor text. We believe the wording in the first sentence of paragraph 6 of the Commentary to Article 9 could be improved further and made clearer (and more consistent with the proposed wording to paragraph 59 of the Commentary to Article 7) if it were written as follows (changes underlined):

“It should be noted, however, that an adjustment is not automatically to be made in State B simply because the profits in State A have been increased; State B is obliged to make an appropriate corresponding adjustment but only to the extent that State B considers that the figure of adjusted profits correctly reflects what the profits would have been if the transactions had been at arm’s length.”

As noted above with reference to paragraph 2 of the Commentary to Article 9, the Commentary to this prescriptive and remedial measure should likely also acknowledge and contemplate that not all OECD member countries currently adhere to the arm’s length principle and that some form of adjustment may nonetheless be warranted so as to alleviate economic double taxation.

Proposed Change to the Commentary on Article 7

No additional comments other than, perhaps, a similar acknowledgement as highlighted above in respect of States that do not fully adhere to the arm’s length principle.

Proposed Change to the Commentary on Article 25

No additional comments on the proposed new paragraph. However, as a general comment, which is equally applicable to Articles 7 and 9 and any other provision contemplating an adjustment so as to alleviate economic double taxation that may arise following an adjustment by one State, the Commentary should recommend that States, in general, agree bilaterally and in the applicable convention on the rules and procedures for effecting an adjustment or, at the very least, provide taxpayers with guidance on the expected general procedure followed by the particular State via an enactment in its domestic law. A uniform understanding, consistent rules regarding proceedings, and the involvement of the taxpayer may lead to an increase in procedural efficiency, shorter process duration and fewer instances of economic double taxation.