PART E

FUTURE

CHAPTER 14

HOW TO IMPROVE ARTICLE 17 OF THE OECD MODEL

14.1. Problems with international artiste taxation need solutions

The study for the first aim of this thesis has shown in the preceding chapters that the taxation of international performing artistes is very often problematic. This chapter will list the options are available for improvement, leaving the general approach of source taxation in the country of performance as it is, but adding modifications to either the text of Article 17 or to the Commentary or to the approach by the tax treaty partners. Some options come from the official Commentary on Article 17 of the OECD Model, while others can be taken over from other tax treaties, from European rules and directives or from national practice. Implementation at short notice is often possible.

14.2. Reintroduction of the limited approach for Article 17(2)

Paragraphs 2.12.-2.14. have discussed the change from the limited approach for Article 17(2) to the unlimited approach in the 1992 Commentary to Article 17 of the OECD Model. This had the effect that all payments to any third party became taxable in the country of performance. Three countries, Canada, Switzerland and the United States, did not agree with this change, added reservations on this reversal and decided to use Article 17(2) only in abusive situations.[1] The United States has expressed its restricted view on Article 17(2) with a deviating text in its 1996 US Model.[2]

The conclusion has been drawn in 9.3.2. that the unlimited approach of Article 17(2) hits the wrong target. This was explained with four examples in 9.2.3. Many theatre companies, orchestras, dance companies and others

1. Paragraph 16 of the Commentary on Article 17 of the OECD Model.
2. See 2.14.

cannot escape the wide scope of Article 17(2) and find that any payment to them for performances is taxable in the country of performance, regardless of to what extent salaries for performing artistes or taxable profit for the company are involved. These parties are normally based in treaty countries and are subject to normal taxation in their residence country or are exempt from corporation tax because of their specific cultural activities. But the source taxation following from the unlimited approach of Article 17(2) is so heavy that they can very easily suffer excessive taxation.

The examples showed that at the same time the top artistes, who live (or pretend to live) in tax havens and try to place their performance income offshore, are not taxed more securely with the unlimited approach. Their total performance income was already fully taxed with the limited approach and this remains the same after the reversal to the unlimited approach. This was explained with example C in 9.2.2. The conclusion must be that the change to the unlimited approach for Article 17 has been a mistake.

A good and directly available option for the improvement of Article 17 of the OECD Model would be the reintroduction of the limited approach for Article 17(2). This can be realized by a change of Paragraph 11 of the Commentary on Article 17. With the active attitude of the OECD towards the Model Treaty and the regular adjustments of the Commentary such a change could be realized at short notice.

However, given the broad scope of the provision itself, it would be preferable if the OECD were to adopt the text of Article 17(2) of the 1996 US Model and make the limited approach of the article clear and evident in its text.

14.3. Change in Paragraph 10 of the Commentary

The neutral position of the OECD towards the deduction of expenses and the suggestion of gross taxation, even though at a low tax rate, in Paragraph 10 of the Commentary on Article 17 of the OECD Model has brought many countries to their current, protective tax system. Although the OECD does not consider Paragraph 10 of the Commentary as a recommendation, it is adopted as a justification by most countries in the world. See chapter 6 for an overview of the national artiste tax rules.

But after the *Arnoud Gerritse* decision of the European Court of Justice[3] the 25 Member States of the European Community (EC) and 3 (out of 4) Member States of the European Free Trade Association (EFTA) can no longer accept this neutral position of the OECD. They must allow the deduction of expenses by artistes from other Member States, because the ECJ did not find any justification for the unequal treatment resulting from gross taxation. Any uncertainties or different views that exist after the *Arnoud Gerritse* decision should be clarified in the pending ECJ cases of *FKP Scorpio Konzertproduktionen GmbH*[4] and *Centro Equestre da Leziria Grande Lda*.[5]

The overview in 6.2. shows that countries such as the United States, Australia, New Zealand, the Netherlands, the United Kingdom and Switzerland already accept the deduction of expenses at the time of the withholding tax, while Canada, Austria, France and Norway levy a gross withholding tax and accept the deduction of expenses in an income tax return at the end of the year, where the normal tax rates apply on the net profit.

The OECD should change its neutral position in Paragraph 10 of the Commentary into a positive recommendation for the deduction of expenses at source before the performance, and raise a withholding tax on the net income at a flat tax rate of between 20% and 30%. The OECD can benefit from the experience of countries such as the United Kingdom, the Netherlands, the United States and others, which have set up special tax offices for non-resident entertainers and allow the deduction of expenses before the tax is calculated and deducted. There is no longer any need for the old-fashioned gross withholding taxation, because broad practical experience is available.

This change could be also realized at short notice, given the active attitude of the OECD towards the Model Tax Convention and the regular adjustments of the Commentary.

3. See 11.4.
4. See 11.6.
5. See 11.7.

14.4. Normal income (or corporation) tax returns

In addition, the OECD could also recommend, either in Paragraph 10 or in another paragraph of the Commentary, that countries should offer the option for non-resident artistes to file normal income or corporation tax returns at the end of the year. This income tax settlement could be optional, as in the Netherlands, or obligatory, as in the United Kingdom, Canada, the United States and Australia.[6] But it would in any case lead to fairer taxation and non-discrimination, which is required under the EC Treaty[7] but and is also important under Article 17 of the OECD Model Tax Convention. Artistes can be treated in the same manner as others with active income, who are normally entitled to an income tax settlement after their visit to another country.

This change could be achieved at short notice by inserting a recommendation in the Commentary on Article 17 of the OECD Model.

14.5. Special provisions for small artistes (the *de minimis* rule)

The overview of the national artiste tax rules in chapter 6 shows that some countries have made special provisions for small non-resident artistes. They need not file an application if their earnings are below a certain threshold. This avoids administration for both the small artiste and the tax administration in cases where earnings do not exceed the expenses for the performances.

The United Kingdom does not levy tax if gross fees do not exceed GBP 1,000 per year, the Netherlands considers EUR 136 per artiste per show as deemed expenses, Belgium has set the threshold at EUR 400 per artiste per show, and Germany introduced the *Staffelbesteuerung* (Bracket Tax System) with lower tax rates under EUR 1,000 per artiste per performance and an exemption if gross fees are under EUR 250 per person per show. But the clearest allowance for small artistes is the *de minimis* rule of USD 20,000 in the 1996 US Model, which has been taken over in many US tax treaties, although sometimes at a lower level.[8]

6. See 6.6.
7. Especially after *Arnoud Gerritse*, 12 June 2003, C-234/01, and *Biehl-I*, 8 May 1990, C-175/88, and *Biehl-II,* 26 October 1995, C-151/94.
8. See 5.6.2. for an overview of the 65 US tax treaties.

Special provisions for small artistes take away the administrative burden for the category of taxpayers that suffers relatively the most from the source taxation in the country of performance. The OECD should recognize this element. A good option would be for the OECD to adopt the recommendation of a USD 20,000 *de minimis* rule per artiste per taxable year from the 1996 US Model. If gross earnings remained under this threshold the taxing right would remain exclusively with the country of residence. This would help many smaller international performing artistes.

Such a change would have to be accompanied by a proper exchange of information about the performance fee, so that the tax authorities in the country of residence were able to include the gross earnings in the worldwide income of the artistes. This exchange of information can be established during the application procedure for the exemption, when the tax authorities in the residence country have to confirm the residence status of the taxpayer.

The introduction of the USD 20,000 *de minimis* rule can best be accompanied by the use of the tax credit method in the country of residence, as recommended in Paragraph 12 of the Commentary on Article 17 of the OECD Model.

Negative aspects to the implementation of a *de minimis* rule may be that it needs to be clarified what the definition of gross earnings is for the USD 20,000 limit and that countries may want to allow the use only after the year-end, which creates cash flow disadvantages for the artiste and an administrative procedure for the refund. But the practical experience with the *de minimis* rule in the US tax treaties up to now has been quite good and these negative aspects do not occur frequently.

It is possible to implement this change at short notice. The OECD could add a recommendation to its Commentary on Article 17 for a *de minimis* rule of e.g. USD 20,000 per artiste per taxable year, and it could also make a connection between the *de minimis* rule and the tax credit method. Countries could follow this recommendation unilaterally in their national tax legislation without changing their bilateral tax treaties.

Furthermore, the OECD could make the recommendation stronger by adding the *de minimis* amount of USD 20,000 to Article 17(1) of its Model

Tax Convention. Countries could follow this change in the (re)negotiations for their bilateral tax treaties.[9]

14.6. Restrict Article 17 to business activities, exempt employees

Another available option for improvement is the provision offered in Paragraph 2 of the Commentary on Article 17 of the OECD Model. This option suggests restricting the scope of Article 17(1) to business activities only, i.e. the earnings that would normally fall under Article 7 of the OECD Model. With this restriction the earnings of artistes/employees would be taxed in accordance with Article 15 of the OECD Model and they could make use of the exception of Article 15(2) and in many cases achieve exclusive taxation in the country of residence.

This option was discussed in 5.3. Earlier, in 2.9., it was noted that Germany used this restrictive provision in its tax treaty practice in the 1950s and 1960s, but later adopted the recommendations of the OECD Model Treaty. But some of the older German tax treaties have still not been renewed. An example is the 1959 Germany–Netherlands tax treaty, under which both German and Dutch music, theatre, dance and other productions that employ artistes, can perform in the other country without any deduction of source tax, either on the salaries for the artistes or on the reimbursement for expenses and on the profit, if any, because the old treaty does not contain a clause comparable to Article 17(2). Under the Germany–Netherlands tax treaty, these production companies and their artistes are taxable only in the country of residence.

This option does not seem to be directly available, because it must be specified in the text of a bilateral tax treaty. At present most treaties have the same wording as the OECD Model, saying: “Notwithstanding the provisions of Article 7 and 15 …” To make use of the option of Paragraph 2 of the Commentary, Article 17 in a bilateral tax treaty needs to be changed. As a minimum the reference to Article 15 (Income from employment) has to be deleted, but it would make the article clearer if the text explicitly mentioned that artistes/employees were excluded from Article 17 and fell under Article 15.

9. And consideration could be given to increasing the amount of USD 20,000 every year by a specific percentage to compensate for inflation.

To avoid the reimbursement for expenses and the profit element for the production company remaining taxable after this change, this measure should be accompanied by the reintroduction of the limited approach of Article 17(2).[10] With this measure the total performance fee would become exempt in the performance country and taxable only in the residence country.

Only self-employed artistes, including those using their own limited company, would remain taxable in the source country.

Even though the OECD mentions this option in its Commentary on Article 17, tax treaty practice shows that only a few countries use this exception. The survey in 5.3. lists only 16 tax treaties with this exception, of which 6 are old German tax treaties from the 1950s and 1960s, and only 2 are more recent than 1980, i.e. Bulgaria–Malta (1986) and Indonesia–Russia (1997). And because the text of Article 17 in a tax treaty needs to be changed, which normally happens just after a general renegotiation of the treaty, the chances of this option being used actively and becoming common treaty policy are slim.

This could change if the OECD transferred the option from Paragraph 2 of the Commentary to the official text of Article 17(1). Then the option would become an outright recommendation, instead of a mere option, and it would then be followed more often by OECD Member countries.

The risk that this restriction to business activities and exclusion of artistes/employees from source taxation might create new options for tax avoidance schemes with rent-a-star companies does not seem imminent. First, the proposed exemption would be inserted in a bilateral tax treaty and not in the national tax rules of the source country. These treaties are normally not concluded with countries/tax havens in which rent-a-star companies are constructed. And without a tax treaty the national tax rule of the source country still applies and the full performance income of the rent-a-star company can be taxed.

Secondly, with an application procedure for the use of the exemption provision it can be certified that the artistes are real employees of the non-resident company. Otherwise the taxing right remains with the source country, because the performance is considered to be a business activity.

10. See 13.2.

14.7. Exemption for equivalent part of fixed salaries

A variation on the option in the preceding paragraph is the possible exemption for an equivalent part of fixed salaries, as mentioned in Paragraph 11(b) of the Commentary on Article 17 of the OECD Model. The Commentary states that "if individual members of a team, orchestra, etc. are paid a fixed periodic remuneration and it would be difficult to allocate a portion of that income to particular performances, countries may decide, unilaterally or bilaterally, not to tax it". This option could be used directly, without the need to change the text or interpretation of a tax treaty. It is interesting to note that the suggestion is made that countries should apply this exemption unilaterally.

It is also interesting that no country seems to use this possible exemption, even though the practical difficulties occur frequently. For every classical orchestra, theatre or dance production, whether very well-established and publicly funded or dependent on commercial earnings, with artistes on the monthly payroll, it is very difficult to allocate a portion of that income to specific performances. This issue is very often ignored because countries just tax the gross performance income without any deduction for expenses or allocation between the individual artistes and the company involved. They just take a bite from the total pie, regardless of who is involved. This simplified approach very often not only leads to excessive taxation but also to tax credit problems. Without tax certificates dividing the income between the individual artistes and the production company the residence country can easily disallow applications for tax credits.[11] This may lead to double taxation for both the individual artistes and the production company.

The option of an exemption for an equivalent part of fixed salaries, combined with the limited approach for Article 17(2), would remove this risk of double taxation. But although it looks as if this measure could be introduced directly by just changing the Commentary, it may be that – if it was introduced – a difference would exist between the reference to Article 15 in the opening text of Article 17 and the interpretation of the article in Paragraph 11(b) of the Commentary. This could lead to discussions with

11. This was discussed in 7.5.5.

the tax authorities in either the country or performance or the home country and fail to make Article 17 clearer and more reliable.[12]

14.8. Addition of Article 17(3) to the official text of Article 17

As the survey in chapter 5 shows, many countries use the option of Paragraph 14 of the Commentary on Article 17 of the OECD Model to allocate the taxing right for artistes who are supported by public funds not to the country of performance but to the country of residence. The figure of 66% of the tax treaties in the survey using this special provision is a big surprise. The option is most often inserted in an additional third paragraph to Article 17.[13]

The content of Article 17(3) is not always the same. In a minority of tax treaties the exemption in the country of performance is based on the existence of a cultural exchange programme or a cultural agreement or only applies to non-profit organizations.[14] But most often the condition for Article 17(3) is that the artiste company needs to be supported by public funds, although the requirements for the level of funding vary from "mainly" to "wholly".

Setting aside the criticism of and possible problems[15] with the option supported in Paragraph 14 of the Commentary on Article 17(3), the broad use of Article 17(3) in the tax treaty policy of most countries cannot be ignored. If two thirds of the tax treaties in the world contain an "Article 17(3)" it should be included by the OECD in its Model Tax Convention and added as the official third paragraph to Article 17. This would then give the OECD the chance to offer a more extensive explanation of the

12. But Article 17 in its current form is already unclear with regard to the allocation of an equivalent part of the fixed salaries to the country of performance. Many countries still use the tax exemption method to eliminate double taxation, but sometimes question whether the taxing right for fixed salaries is allocated to the country of performance. This means that they do not allow a tax exemption in the country of residence. See the different decisions of tax courts in the Netherlands in Rijkele Betten, "Netherlands Ice Skater not Eligible for Relief for Foreign Training Days", 45 *European Taxation* 6 (2005), at 259.
13. See 5.1. for the results of the survey and 5.5. for the explanation of "Article 17(3)".
14. See for the variations in Article 17(3) the example in 5.6.3., where all tax treaties of the Netherlands were listed.
15. See 5.5.3. to 5.5.6. and 12.5.

scope of this third paragraph, remove uncertainties with regard to elements such as the level of public funding and offer a justification for its discriminatory character. It would also be good if the OECD were to make an official choice about whether the paragraph can be extended to variations such as cultural exchange or agreement or exemption for non-profit organizations.

The official addition of Article 17(3) to the OECD Model Treaty would convert the tax treaty practice of many countries into an official recommendation by the OECD and would lead to more harmonization of bilateral tax treaties. But this requires a change in the article and in many bilateral tax treaties, which means that a complete direct effect at short notice should not be expected.

14.9. Change to tax exemption or full credit would give a better balance

The OECD recommends the tax credit method to the country of residence of the artiste to eliminate double taxation.[16] The OECD has chosen not to recommend the full tax credit but the ordinary tax credit, which limits the compensation for the foreign tax to the tax which is due on the income item in the residence country. Calculations show that this very often leads to excessive taxation, because many performance countries do not allow the deduction of expenses when they tax performance income, while residence countries tax only the net profit (after expenses) from the foreign activities. And with high expenses the foreign tax can easily exceed the income or corporation tax in the residence country. But many other problems can stand in the way of actually achieving the tax credit in the country of performance, as explained in 7.5.

This leads to the conclusion that the tax credit method can at best give an exact compensation, but can never give a benefit to international performing artistes, and will be very likely to lead to excessive taxation because part or the full amount of the foreign tax is not accepted as a credit in the residence country. This gives an unfair balance. In 12.8. it was discussed that the ordinary tax credit method was inconsistent and therefore might be incompatible with the equal treatment and freedom principles of the EC Treaty. This led to support for the exemption method,

16. See 7.3. and Paragraph 12 of the Commentary on Article 17 of the OECD Model.

which can produce either positive or negative results for the artiste and the country of performance.

Another development within the European Community is that within an internal market without borders the full tax credit method may have to apply to foreign-source income. In that situation the tax credit would not be limited to the amount of tax due on the income in the country of residence, but a refund would be given for an excess tax credit. A few small steps have been taken in this direction, with two ECJ decisions and the 2003 Savings Income Directive, but the full tax credit it is still far from broader use.[17]

The option of changing the method for the elimination of double taxation to the tax exemption method can be applied directly and only needs a change in the Commentary on Article 17 of the OECD Model. But this change in the Commentary will unfortunately not work in every residence country, because many bilateral tax treaties contain the credit method for Article 17 and some countries, such as Australia, the United Kingdom and the United States, use only the ordinary tax credit method in their national tax law as relief for double taxation. These countries can improve their credit system by applying the basket system (instead of the per-country system)[18] and allowing the carry-forward of excess credits.[19]

The change to the full tax credit method is a more fundamental change, because Article 23B of the OECD Model Treaty is restricted to an ordinary tax credit. This is the same in the typical tax credit countries which were mentioned above.

14.10. Conclusions

Many of the problems with the taxation of international performing artistes can more or less be avoided with measures which are already available. Some of these can be activated at short notice, while other measures need more action to become effective. All measures leave the general principle of source taxation in the country of performance intact, but try to rein back the extravagant elements of the existing tax system.

17. This was discussed in 12.8.4.
18. See 7.4.
19. See 7.6.

The first available option is to reintroduce the limited approach for Article 17(2), as was originally intended at the introduction of the paragraph in 1977.

Another directly available option would be a change of Paragraph 10 of the Commentary on Article 17 of the OECD Model into a recommendation for the deduction of expenses and normal net taxation. To this recommendation it can be added that non-resident artistes should be allowed to file a normal income tax return after the end of the taxable year and make use of normal tax rates.

Special provisions for small artistes would reduce the administrative burden, which affects these artistes relatively harder than bigger artistes. The OECD could consider adopting the USD 20,000 *de minimis* rule of the 1996 US Model as the general recommendation for Article 17(1) of the OECD Model Treaty.

Two options from the Commentary on Article 17(2) would exclude the salaries of performing artistes/employees from taxation in the source country, i.e. the restriction of Article 17(1) to business activities of Article 7 of the OECD Model and the exemption of fixed salaries of artistes/employees from source taxation in the country of performance. Unfortunately, the negative side of the latter option is that it would be problematic to calculate which part of the salaries could still be taxed.

The option of Paragraph 14 of the Commentary to exempt artistes from source taxation if their performance is supported by public funds is already frequently used by countries in their tax treaty negotiations. The OECD could consider adding this option as an official Article 17(3) to the text of Article 17 of the OECD Model, although it needs to be aware of the discriminatory character of this measure.

The recommendation in the Commentary to use the ordinary tax credit method seems to be unfair to international performing artistes because they can at best be normally compensated but can very easily end up suffering excessive taxation. A change to the exemption method or the full tax credit method would create a better balance of responsibilities between artistes and the tax authorities.

The implementation of the available options would lead to a much lower risk of excessive taxation for international performing artistes. More artistes could be exempted in the country of performance and return to exclusive taxation in the country of residence. But this would also bring up new discussions about the qualification for the conditions for the exemptions and it would make the use of Article 17 more difficult.

But the general conclusion from this chapter needs to be that if the OECD took the options in its own Commentary more serious, a considerable proportion of international performing artistes would be better off.