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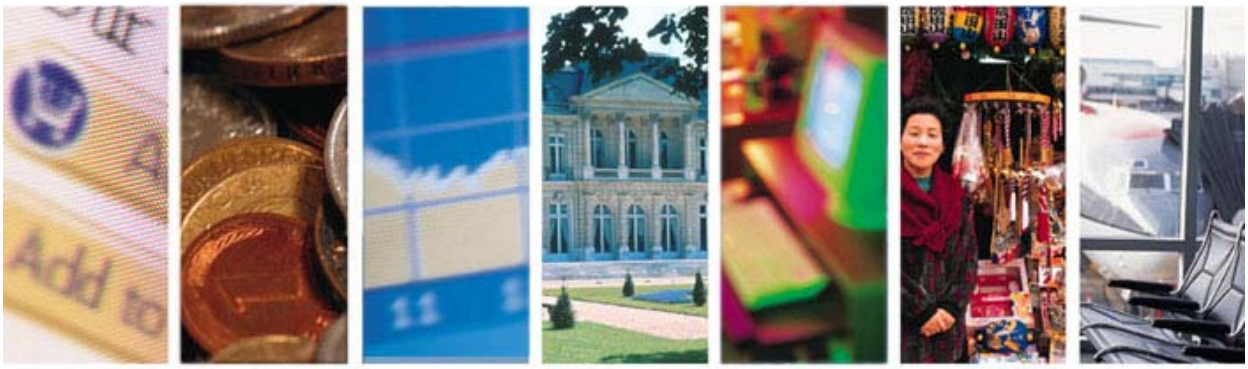

DISCUSSION DRAFT ON TAX TREATY ISSUES RELATED TO COMMON TELECOMMUNICATION TRANSACTIONS

25 NOVEMBER 2009 TO 31 JANUARY 2010

CENTRE FOR TAX POLICY AND ADMINISTRATION

25 November 2009

TAX TREATY ISSUES RELATED TO COMMON TELECOMMUNICATION TRANSACTIONS

Public discussion draft

Various tax treaty issues related to telecommunications have been brought to the attention of the Committee on Fiscal Affairs in recent years through its Working Party 1 on Tax Conventions and Related Questions. These include the taxation of payments to satellite operators, the characterisation of income from granting indefeasible rights over phone lines, the characterisation of roaming payments and payments for spectrum licenses. Some of these issues have given rise to disputes and the Committee on Fiscal Affairs has therefore decided that the Commentary on the OECD Model Tax Convention should clarify the application of treaties based on the OECD Model Tax Convention to income arising from these common transactions.

This public discussion draft includes proposals for additions and changes to the Commentary on the OECD Model Tax Convention that result from the work of the Working Party on these issues.

The Committee is considering the inclusion of these additions and changes in the next update to the OECD Model Tax Convention, which is tentatively scheduled for the second part of 2010. It therefore invites interested parties to send their comments on this discussion draft **before 31 January 2010**. These comments will be examined at the February 2010 meeting of the Working Party, when the Working Party intends to complete its work on the next update.

Comments on this discussion draft should be sent electronically (in Word format) to:

Jeffrey Owens
Director, CTPA
OECD
2, rue André Pascal
75775 Paris
FRANCE
e-mail: jeffrey.owens@oecd.org

Unless otherwise requested at the time of submission, comments submitted to the OECD in response to this invitation will be posted on the OECD website.

This document is a discussion draft released for the purpose of inviting comments from interested parties. It does not necessarily reflect the final views of the OECD and its member countries.

TAX TREATY ISSUES RELATED TO COMMON TELECOMMUNICATION TRANSACTIONS

A. Payments to satellite operators

Add the following new paragraph 5.5 immediately after paragraph 5.4 of the Commentary on Article 5:

5.5 Clearly, a permanent establishment may only be considered to be situated in a Contracting State if the relevant place of business is situated in the territory of that State. The question of whether a satellite in geostationary orbit could constitute a permanent establishment for the satellite operator relates in part to how far the territory of a State extends into space. No member country would agree that the location of these satellites can be part of the territory of a Contracting State under the applicable rules of international law and could therefore be considered to be a permanent establishment situated therein. Also, the particular area over which a satellite's signals may be received (the satellite's "footprint") cannot be considered to be at the disposal of the operator of the satellite so as to make that area a place of business of the satellite's operator.

Add the following new paragraph immediately after paragraph 9 of the Commentary on Article 12:

9.1 Satellite operators and their customers (including broadcasting and telecommunication enterprises) frequently enter into "transponder leasing" agreements under which the satellite operator allows the customer to utilise the capacity of a satellite transponder to transmit over large geographical areas. Payments made by customers under typical "transponder leasing" agreements are made for the use of the transponder transmitting capacity and will not constitute royalties under the definition of paragraph 2: these payments are not made in consideration for the use of, or right to use, property, or for information, that is referred to in the definition (they cannot be viewed, for instance, as payments for information or for the use of, or right to use, a secret process since the satellite technology is not transferred to the customer). As regards treaties that include the leasing of industrial, commercial or scientific (ICS) equipment in the definition of royalties, the characterisation of the payment will depend to a large extent on the relevant contractual arrangements. Whilst the relevant contracts often refer to the "lease" of a transponder, in most cases the customer does not acquire the physical possession of the transponder but simply its transmission capacity: the satellite is operated by the lessor and the lessee has no access to the transponder that has been assigned to it. In such cases, the payments made by the customers would therefore be in the nature of payments for services, to which Article 7 applies, rather than payments for the use, or right to use, ICS equipment. A different, but much less frequent, transaction would be where the owner of the satellite leases it to another party so that the latter may operate it and either use it for its own purposes or offer its data transmission capacity to third parties. In such a case, the payment made by the satellite operator to the satellite owner could well be considered as a payment for the leasing of industrial, commercial or scientific equipment.

B. Roaming payments

Add the following new paragraph 9.1 immediately after paragraph 9 of the Commentary on Article 5:

9.1 Another example where an enterprise cannot be considered to carry on its business wholly or partly through a place of business is that of a telecommunications operator of a Contracting State who enters into a "roaming" agreement with a foreign operator in order to allow its users to connect to the foreign operator's telecommunications network. Under such an agreement, a user who is outside the geographical coverage of that user's home network can automatically make and receive voice calls, send and receive data or access other services through the use of the foreign network. The foreign network operator then bills the operator of that user's home network for that use. Under a typical roaming agreement, the home network operator merely transfers calls to the foreign operator's network and does not operate or have physical access to that network. For these reasons, any place where the foreign network is located cannot be considered to be at the disposal of the home network operator and cannot, therefore, constitute a permanent establishment of that operator.

Add the following new paragraph 9.2 immediately after proposed new paragraph 9.1 (see Section A above) of the Commentary on Article 12:

9.2 Also, payments made by a telecommunications network operator to another network operator under a typical "roaming" agreement (see paragraph 9.1 of the Commentary on Article 5) will not constitute royalties under the definition of paragraph 2 since these payments are not made in consideration for the use of, or right to use, property, or for information, referred to in the definition (they cannot be viewed, for instance, as payments for the use of, or right to use, a secret process since no secret technology is used or transferred to the operator). This conclusion holds true even in the case of treaties that include the leasing of industrial, commercial or scientific (ICS) equipment in the definition of royalties since the operator that pays a charge under a roaming agreement is not paying for the use, or the right to use, the visited network, to which it does not have physical access, but rather for the telecommunications services provided by the foreign network operator.

C. Undersea cables and pipelines

Add the following sentence at the end of proposed new paragraph 9.1 (see Section A above) of the Commentary on Article 12:

Similar considerations apply to payments made to lease the capacity of cables for the transmission of electrical power or communications (e.g. through a contract granting an indefeasible right of use of such capacity) or pipelines (e.g. for the transportation of gas or oil).

Add the following sentence at the end of paragraph 26.1 of the Commentary on Article 5:

An additional question is whether the cable or pipeline could also constitute a permanent establishment for the customer of the operator of the cable or pipeline, i.e. the enterprise whose data, power or property is transmitted or transported from one place to another. In such a case, the enterprise is merely obtaining transmission or transportation services provided by the operator of the cable or pipeline and does not have the cable or pipeline at its disposal. As a consequence, the cable or pipeline cannot be considered to be a permanent establishment of that enterprise.

D. Payments under spectrum licenses

Add the following new paragraph 9.3 immediately after proposed new paragraph 9.2 (see Section B above) of the Commentary on Article 12:

9.3 Payments for the use of, or the right to use, some or all of part of the radiofrequency spectrum (e.g. pursuant to a so-called "spectrum license" that allows the holder to transmit media content over designated frequency ranges of the electromagnetic spectrum) do not constitute payments for the use of, or the right to use, property, or for information, that is referred in the definition of royalties in paragraph 2. This conclusion holds true even in the case of treaties that include the leasing of industrial, commercial or scientific (ICS) equipment in the definition of royalties since the payment is not for the use, or the right to use, any equipment.