

Tax Treaties, Transfer Pricing and Financial Transactions Division  
OECD/CTPA

Comments on “OECD Model Tax Convention: revised discussion draft  
on the definition of “permanent establishment””

The following are the comments of the Accounting & Tax Committee of the Japan Foreign Trade Council, Inc. in response to the invitation to public comments by OECD regarding “Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention.” The Japan Foreign Trade Council is a trade-industry association with trading companies and trading organizations as its core members, while one of the main activities of its Accounting & Tax Committee is to develop the trade environment by submitting specific policy proposals and requests to government authorities concerning tax matters. (Member companies of the Accounting & Tax Committee of JFTC are listed at the end of this document.)

Issue 2. Meaning of “ at the disposal of ”	
Para. 4.2 2 <sup>nd</sup> Sentence	Revised proposal
	“...that enterprise <i>having the effective power to use that location as well as</i> the extent of the presence of the enterprise...”
	Comments on the revised proposal
	✓ In this revised draft, the concept of “effective power to use that location” is stressed. We are concerned that, based on

	<p>this concept, it could be interpreted that a mere fact that an enterprise are controlled by the other enterprise (even if there is no legal right to use) constitutes a situation where the controlling enterprise has effective power to use the location that belongs to the controlled enterprise.</p> <p>✓ In this respect, the OECD Model Tax Convention specifies in paragraph 7 of Article 5 that “The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other”. So that this statement is not overlooked, we suggest inserting that the following sentences in this commentary.</p> <p><i><u>“A fact that an enterprise controls the other enterprise shall not of itself constitute a situation where the controlling enterprise has effective power to use the location that belongs to the controlled enterprise”.</u></i></p> <p>✓ In addition, we consider that “power” in the context of this paragraph should be power that is clearly agreed between the parties. Therefore, we suggest that, as well as using a term “exclusive legal right” in the paragraph 4.2, the commentary replaces “effective power” with “effective <u>legal</u> power”.</p>
<p>Para. 4.2 5<sup>th</sup> Sentence</p>	<p>Revised proposal</p>
	<p><i>(e.g. where employees of an enterprise have access to the premises of associated enterprises which they often visit but without working in these premises for an extended period of time).</i></p> <p>Comments on the revised proposal</p> <p>✓ We understand that the purpose of adding this example is to provide some guidance for interpretation of the meaning of “intermittent or incidental”. However, if it is the purpose, we consider that it would be necessary to provide further clarification on the definition of “for an extended period of</p>

	<i>time</i> ".
Issue 3. Can the premises of a (converted) local entity constitute a permanent establishment of foreign enterprise under paragraph 1 ?	
Para. 3.1	Revised proposal
	<p><i>It is also important to that the way in which business is carried on evolves over the years so that the facts and arrangements applicable at one point in time may no longer be relevant after a change in the way that the business activities are carried on in a given State. Clearly, whether or not a permanent establishment exists in a State during a given period must be determined on the basis of the circumstances applicable during that period.</i></p>
	<p>Comments on the revised proposal</p> <p>✓ We agree with the Working Party's conclusion that no distinction should be made in the application and interpretation of Article 5 based on whether or not the facts and arrangements relevant to determination of a permanent establishment resulted from a business restructuring. However, it appears to us that the new paragraph doesn't explain directly relationship between such business restructuring and determination of a permanent establishment. Therefore, to make clarification on this point, we suggest the following sentence is added after the second sentence of the new paragraph.</p> <p><u><i>"For example, cross-border transfer of functions, risks and/or assets between associated entities does not necessarily constitute a permanent establishment for the transfer in the country in which the transferee exists."</i></u></p>
論点 6. Time requirement for the existence of a permanent establishment	
Para. 6.1 4 <sup>th</sup> Sentence	Revised proposal
	<p><i>An enterprise of State carries on drilling operations at a remote arctic location in State S. The seasonal conditions at that location prevent such operations from going on for more than three months each year but the</i></p>

	<p><i>operations are expected to last for 5 years.</i></p> <p><b>Comments on the revised proposal</b></p> <p>✓ We appreciate that, the commercial fair case is deleted and instead the drilling operations case which would be more realistic one is added in the illustrations of the revised draft, We believe that the important factor for determination of a permanent establishment in a situation where the activities are of a recurrent nature is whether the operation period is “clearly” expected “at the beginning of the activities”. In this respect, we suggest adding some words into the second sentence as follows (see the underlined part).</p> <p><i>“The seasonal conditions at that location prevent such operations from going on for more than three months each year but the operations are <u>clearly</u> expected to last for 5 years <u>under a specific contract or similar legal arrangements at the beginning of the activities.</u>”</i></p>
<p><b>Issue Additional work on a construction site 11.</b></p>	
<p><b>Para. 19.1 9<sup>th</sup> Sentence</b></p>	<p><b>Revised proposal</b></p>
	<p><i>Depending on the circumstances, however, any subsequent work (including work done under a guarantee) performed on the site during an extended period of time may need to be taken into account in order to determine whether such work is carried on through a distinct permanent establishment.</i></p> <p><b>Comments on the revised proposal</b></p> <p>✓ For the last sentence, as discussed in the public consultation meeting on September 7, 2012, we suggest that the following sentences are added to clarify the meaning of the “<i>distinct permanent establishment</i>”.</p> <p><i>“<u>This determination should be made separately from determination of a permanent establishment for the original construction work. Therefore, even if such subsequent work constitutes a permanent establishment, it shall not be deemed retrospectively that the original construction work constituted a permanent establishment.</u>”</i></p>

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