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## **Business Profits**

### **Discussion Draft for Public Comment**

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Dear Mr. Owens,

Following the Organization for Economic Co-Operation and Development's ("OECD") invitation to comment on the discussion draft on a new Article 7 (Business Profits) of the OECD Model Tax Convention (the "Discussion draft"), you will find below our comments relating to the Discussion draft.

### **General Comments**

As a general comment, we agree with the OECD's revision of Article 7 following the release of the Report on the Attribution of Profits to Permanent Establishments (the "Report"). The revised Article 7 is the reflection of the OECD's "functionally separate entity" approach (the "authorized OECD approach") for attributing profit to a Permanent Establishment ("PE").

As the main purpose of the OECD Model Tax Convention (the "Model Treaty") is to serve as a model for tax treaties entered into by OECD member countries, it is very important to ensure that its language is clear and unambiguous. We believe that the OECD has achieved this goal by revising Article 7.

The new paragraph 3 of Article 7 ensures that if Contracting States use different capital attribution approaches to determine the amount of "free capital", the same amount will be used by both States for the purpose of attributing profit to a PE. We applaud the OECD's attempt to provide taxpayers with additional remedies to eliminate double taxation.

In addition, in paragraphs 53 to 69 of the Discussion draft the OECD discusses the inclusion of an additional paragraph to Article 7, which reads as follows:

*"Where, in accordance with this Article, a Contracting State adjusts the profits that are attributable to a permanent establishment of an enterprise of one of the Contracting States and taxes accordingly profits of the enterprise that have been charged to tax in the other State, the other State shall, to the extent necessary to eliminate double taxation on these profits, make an appropriate adjustment to the amount of the tax charged on those profits. In determining such adjustment, due regard shall be had to the other provisions of this Convention and the competent authorities of the Contracting States shall if necessary consult each other. For the purposes of this paragraph, where the profits that are attributable to the permanent establishment are determined in one State through the use of a method that is provided by the domestic law*

*of that State and that results in profits that are different from those attributed to the permanent establishment in the other State, the first-mentioned State shall be deemed to have adjusted the profits attributable to the permanent establishment.”*

The purpose of this additional paragraph is to provide a corresponding adjustment mechanism following the adjustment of the profits of an associated enterprise in case where the domestic law of a State does not allow it to make an adjustment to eliminate double taxation through the combined application of paragraph 2 and of Article 23A or 23B. We believe that this paragraph should be included in the revised Article 7 as paragraph 3, followed by the proposed paragraphs 3 and 4, which would then become paragraphs 4 and 5. Inclusion of this paragraph in the revised Article 7 and not just in the Commentary on the new Article 7 would ensure that sufficient remedies are provided to taxpayers in order to eliminate the possibility of double taxation.

### **Final Remarks**

We would like to express our gratitude to the OECD for the opportunity to present our comments and we hope that our contribution will help in the future developments of the Model Treaty. We appreciate the work that is done by the OECD to improve the existing Model Treaty and we are looking forward to seeing the new Model Treaty that will better reflect the issues faced by taxpayers in the complex international tax environment.

Yours truly,

**RSM Richter Chamberland LLP**