

Paris, October 25, 2011

Re: Comments on Discussion Draft – Tax Treaty Issues Related to the Trading of Emissions Permits

Dear Jeffrey,

This letter is in response to the request by the OECD Committee on Fiscal Affairs for comments on its discussion draft, released on 31 May 2011, concerning the preliminary conclusions of Working Party 1 concerning tax treaty issues related to the trading of emissions permits.

BIAC believes that the draft paper correctly concludes that emissions permits are commodities to be consumed through their use and not property or rights that can be leased or licensed. Thus, the paper correctly posits that the typical tax treaty issue is treatment of the income from the alienation of such permits by a resident of a Contracting State. Among the possible interpretations set forth in the paper, we believe that gain on the sale of the permit is properly the subject of either Article 7 (Business Profits) or Article 13 (Capital Gains) and thus subject to tax in the state of residence unless attributable to permanent establishment in the other state. Although the paper discusses the possible application of Article 6 (Immovable Property), Article 8 (Shipping, Inland Waterways Transport and Air Transport), and Article 12 (Royalties) taxation under any of these articles seems incorrect if the emissions permits are properly characterized as commodities. BIAC believes that the OECD should endorse the treatment of profits from the alienation of emission permits as either business profits or capital gains. Further, BIAC believes that it would be helpful to provide the amount of such income should be determined pursuant to the generally applicable transfer pricing rules.

The European Commission is preparing a proposal to enhance the framework for market oversight of the EU Emissions Trading Scheme (ETS).¹ The two main options under consideration are i) to classify carbon certificates as financial instruments under the Markets in Financial Instruments Directive (MiFID), which currently only covers derivatives of carbon certificates and ii) to design a separate tailor-made regime for the carbon certificates. It is important that whatever the outcome of this proposal, it should not affect or determine the tax treatment proposed above.

BIAC strongly recommends that the paper explicitly address the taxation of traders or dealers in emission permits. If trading in emissions permits is wide spread, then, like other commodities, traders and dealers will be involved in making that market. Thus, the taxation of the gains of traders and dealers will be important. Consistent with the treatment suggested above, we believe gain from the sale of the emissions permits by traders and dealers should be analyzed as either business profits or capital gains.

BIAC also recommends that the paper be broadened to cover both certified emission reduction (CER) credits and emission reduction units (ERUs). We do not see any distinction that would be relevant for tax purposes between emission permits more generally and CER and ERUs. The same tax treaty rules should, therefore, be applicable to gains from trading in all forms of emissions permits.

Thank you again for the opportunity to comment on this important project. We would welcome further consultation on the project, and would be pleased to receive any questions that you may have on our submission.

Sincerely yours,



Chris Lenon
Chair, BIAC Committee on Taxation and
Fiscal Affairs

Mr. Jeffrey Owens
Director, CTPA
OECD
2, rue André Pascal
75016 Paris