BAKER & McKENZIE

Baker & McKenzie LLP
815 Connecticut Avenue, NW
Washington, DC 20006-4078, USA

Tel: +1 202 452 7000
Fax: +1 202 452 7074
www.bakermckenzie.com

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Washington, DC

Carol A. Dunahoo
Tel: +1 202 452 7049
Fax: +1 202 416 6952
carol.dunahoo@bakermckenzie.com

February 13, 2012

Grace Perez-Navarro
Deputy Director, CTPA
OECD
2, rue Andre Pascal
75775 Paris
FRANCE

RE: **Comments of the Treaty Policy Working Group on Proposed Changes to the Commentary on Article 5 (Permanent Establishment) of the OECD Model Tax Convention**

Dear Ms. Perez-Navarro:

We write on behalf of the Treaty Policy Working Group, to offer comments on the October 12, 2011 Discussion Draft of proposed changes to the Commentary on Article 5 of the OECD Model Tax Convention. The Treaty Policy Working Group is an association of large global companies that are based throughout the world and represent a broad spectrum of sectors. We have been working together since 2005 to analyze and address tax policy and administration concerns relating to permanent establishment, transfer pricing, and other issues.

Clear guidance reflecting a broad international consensus on permanent establishment issues is critically important to TPWG member companies seeking to avoid double or unexpected taxation and the associated uncertainty and cross-border controversies. Clarity and certainty are especially important where the permanent establishment threshold is concerned, because in many cases that threshold determines whether a taxpayer must file returns and pay income tax on a net basis in a jurisdiction, in addition to bearing applicable withholding or other taxes at source. The provision of clarity and certainty is also consistent with the Working Group's mandate to provide additional guidance to taxpayers and tax administrations regarding the proper application in practice of the current provisions of Article 5.

We applaud Working Party 1 and its Working Group 10 on the definition of permanent establishment for identifying and addressing many of the most important and difficult interpretative issues currently arising in practice under Article 5 of the OECD Model. We are impressed by the speed with which the Working Group developed consensus on most issues and believe that the Discussion Draft proposes many useful clarifications. In some areas, however, we believe that certain modifications or additions to the proposed language are needed to avoid ambiguities that could give rise to controversy. In this letter, we address those proposals of common interest to TPWG members which we believe could most benefit from modification or further clarification.

Meaning of "at the disposal of"

The meaning of the term "at the disposal of" is an important issue for our members, and we applaud the Working Group for endeavoring to provide more clarity regarding the meaning of this expression.

As a threshold matter, of course, a fixed place of business must be found before a foreign enterprise properly may be found to be conducting its business through such a place in a way that gives rise to a permanent establishment under paragraph 1. While it is true that the expression "at the disposal of" does not appear in Article 5 itself, it appears as a standard for the fixed place of business determination in many places in the Commentary, and it has provided useful guidance to taxpayers and tax administrations for many years.

The Discussion Draft notes that the Working Group entertained a suggestion that it should not try to clarify the "at the disposal" concept and instead should focus on the concept "through which the business of the enterprise is wholly or partly carried on". We agree with the conclusion of the Working Group that the "at the disposal" standard remains relevant and could benefit from further clarification. We are aware of various cases in which tax auditors have asserted the existence of a "fixed place of business" PE based on "at the disposal" assertions which are inconsistent with the historic interpretation of the PE standard. While such assertions may not be supported by a fair reading of the Commentary, their prevalence shows the need to examine very carefully the balance of the language used in the Commentary to minimize the possibility that it can be interpreted in an improper way.

The most common contention we are currently encountering in practice is that a nonresident affiliated entity has a PE at the premises of a local affiliate on the grounds that its controlling (or commonly controlled) ownership relationship means that the foreign enterprise necessarily has access to the premises of the local enterprise, and that those premises may, therefore, be regarded as "at the disposal of" the foreign enterprise. We also have encountered some assessments in which it was argued that the local enterprise is conducting the business of the foreign principal or other affiliate and thereby creating a PE at the local enterprise's place of business, merely because it is performing intercompany services for the affiliate there. Such arguments are

fundamentally inconsistent with the provisions of Article 5(7) and with paragraph 42 of the Article 5 Commentary. However, they have been made even in situations not involving construction sites and contractors, including situations in which:

(1) neither the foreign enterprise nor any of its employees has a legal right to access the local premises;

(2) employees of the foreign enterprise are not present at the local premises at all;

(3) employees of the foreign enterprise are present at the local premises but only occasionally for short periods (e.g., not totaling more than 6 months or other applicable threshold period during the taxable period); and/or

(4) employees of the foreign enterprise are present at the local premises, but they conduct only the business of the local enterprise, their compensation is borne by the local enterprise, and they work at its direction and control (sometimes but not always under a written secondment agreement).

Notwithstanding such suggestions, we believe that the "at the disposal" standard, if properly applied, provides an accurate and useful elaboration of the fundamental fixed place of business PE concept as expressed in paragraph 2 of the Commentary. Paragraph 2, which closely reflects the actual language of Article 5 of the Model Convention, states as follows:

> Paragraph 1 gives a general definition of the term "permanent establishment" which brings out its essential characteristics of a permanent establishment in the sense of the Convention, i.e. a distinct "situs", a "fixed place of business". The paragraph defines the term "permanent establishment" as a fixed place of business, through which the business of an enterprise is wholly or partly carried on. This definition, therefore, contains the following conditions:
>
> — the existence of a "place of business", i.e. a facility such as premises or, in certain instances, machinery or equipment;
>
> — this place of business must be "fixed", i.e. it must be established at a distinct place with a certain degree of permanence;
>
> — the carrying on of the business of the enterprise through this fixed place of business. This means usually that persons who, in one way or another, are dependent on the enterprise (personnel) conduct the business of the enterprise in the State in which the fixed place is situated.

This long-standing Commentary makes the essential nature of a "fixed place of business" PE clear: the nonresident enterprise must have a "place" that is "fixed" and through which the

enterprise conducts its own business over an adequate period of time. The expression "at the disposal" describes the relationship of the nonresident enterprise to its premises in a manner that makes clear that the enterprise must exercise a sufficient degree of control over the premises to conduct the range of activities that constitute its business there over time. This confirms that the standard is neither a high bar that requires legal ownership of the premises, nor a low bar that treats the mere availability of premises, with or without restrictions on access, as sufficient.

The Discussion Draft endeavors to further clarify the "at the disposal" standard by adding the italicized sentences below to paragraph 4.2 of the Commentary:

> 4.2 Whilst no formal legal right to use a particular place is required for that place to constitute a permanent establishment, the mere presence of an enterprise at a particular location does not necessarily mean that that location is at the disposal of that enterprise. ***Whether a location may be considered to be at the disposal of an enterprise in such a way that it may constitute a "place of business through which the business of [that] enterprise is wholly or partly carried on" will depend on the extent of the presence of an enterprise at that location and the activities that it performs there. Where an enterprise has an exclusive legal right to use a particular location which is used only for carrying on that enterprise's own business activities, that location is clearly at the disposal of the enterprise. This will also be the case where an enterprise performs business activities on a continuous and regular basis during an extended period of time at a location that belongs to another enterprise or that is used by a number of enterprises. This will not be the case, however, where the enterprise's presence at a location is so intermittent or incidental that the location cannot be considered a place of business of the enterprise. Where an enterprise does not have a right to be present at a location and, in fact, does not use that location itself, that location is clearly not at the disposal of the enterprise; thus, for instance, it cannot be considered that a plant that is owned and used exclusively by a supplier or contract-manufacturer is at the disposal of an enterprise that will receive the goods produced at that plant merely because all these goods will be used in the business of that enterprise (see also paragraph 42 below). It is also important to remember that even if a place is a place of business through which the activities of an enterprise are partly carried on, that place will be deemed not to be a permanent establishment if the only business activities carried on at that place are those listed in paragraph 4***.

We are concerned that these proposed clarifications could be interpreted by auditors to depart from the correct interpretation of the "at the disposal" standard in two respects.

First, the proposed new text suggests that whether a "place" can be considered as being "at the disposal" of an enterprise depends on the "extent of the presence" at that place. This suggestion,

in the first new sentence, seems to refer principally to the passage of time and perhaps to the nature of the business activities being performed there. While such factors may be relevant to other requirements for finding a PE under Article 5(1), they are irrelevant to the threshold determination of whether the enterprise has a place of business that could potentially give rise to a fixed place of business PE. The proposed new sentence should, therefore, be clarified to avoid creating the impression that an enterprise may have a fixed place of business for Article 5(1) purposes based solely on its presence at a location. The discussion of the "at its disposal" term should, instead, make clear that mere presence at a location, without an adequate degree of control over that location, is not sufficient to create a fixed place of business. Given that the focus of Article 5(1) is on activities conducted through a fixed place of business, it should also be confirmed that the relevant type of control for this purpose is operational control over the manner in which such activities are conducted, and not, as is sometimes asserted, mere financial or managerial policy functions (*e.g.*, approval of operating budgets or fixed expenditures incurred by an affiliate with respect to its place of business).

Second, the third new sentence states that an enterprise will be considered to have premises at its disposal when it "performs business activities on a continuous and regular basis". This formulation similarly fails to acknowledge that the mere conduct of business activities at a place is not the determining factor of whether the enterprise has premises "at its disposal". The conduct of business activities clearly is relevant for the third element of the three-part test set forth in paragraph 2 of the Commentary, namely whether the enterprise carries on its business through a fixed place of business. But it does not determine whether the enterprise has a fixed place of business in the first place.

While the proposed new Commentary language on the meaning of "at the disposal of" also contains some helpful clarifications, we are concerned that the proposed addition to Commentary paragraph 4.2 of the two new sentences discussed above could be read to disregard the distinction between the "fixed place of business" standard of Article 5(1) and the alternative "service PE" provisions set forth in paragraphs 42.11 – 42.48 of the Commentary. The latter "service PE" provisions do not require that the enterprise have premises at its disposal. The fixed place of business PE provisions of Article 5(1) do include such a requirement. The two rules simply are different; Article 5(1) describes an actual PE and the alternative provision regarding services describes a deemed PE. The interpretation of Article 5(1) should be kept distinct from that of the deemed PE alternative provision, which applies only if included in the text of the applicable bilateral convention. We believe that these two proposed additions could otherwise seriously confuse what should be a clear distinction between the two standards.

Use of Subcontractors

As noted above, we have seen various controversies arise due to assertions by tax auditors that a nonresident enterprise is somehow present at the location of an associated enterprise, or even an unrelated enterprise, when that second enterprise is performing services for, or is otherwise a

subcontractor of, the nonresident enterprise. These assertions frequently are without merit, as they ignore the requirement that the local premises be at the disposal of the nonresident enterprise itself, as opposed to being controlled by the local contractor or service provider. The OECD has introduced some useful clarifications into the Commentary in recent years to address these issues, most notably the recent revisions to paragraph 42 regarding the provision of management services.

We compliment the Working Group for providing additional clarification on this issue. The Discussion Draft includes important text emphasizing the distinction between the establishment of a nonresident enterprise and the establishment of other persons who may be contractors to or suppliers to the enterprise. The proposed new Commentary paragraph 10.1 helpfully confirms that the fact that an enterprise may be considered to carry on its business through subcontractors does not, in itself, give rise to a fixed place of business simply due to the fact of the contractor relationship.

However, to ensure that this principle is properly applied in practice, we believe that it is important to make conforming clarifications to proposed paragraph 4.5 (current paragraph 4.3) of the Commentary. As proposed, paragraph 4.5 provides an example indicating that a subsidiary's premises will be considered to constitute a PE of a parent company if the parent company has an employee on-site long-term to oversee the subsidiary's performance under a contract it has with the parent and the employee has an office at his disposal. The requirements that an office be at the employee's disposal and it be used for a "long period of time" clearly seem intended to prevent a PE from being deemed to arise automatically whenever an employee is present in such a situation. However, we are concerned that some tax auditors might attempt to argue otherwise, reading the text of proposed paragraph 4.5 together with the indication in proposed paragraph 10.1 that an enterprise may be considered to carry on its business through subcontractors and the general reference in paragraph 4.2 to an enterprise which "performs business activities … at a location". This would create a risk that many contract manufacturing operations and the like, even those conducted by independent entities, could be alleged to give rise to a PE for any principal that engages in regular oversight. As this interpretation would be contrary to the clear intention of proposed paragraph 10.1 and, we submit, the text of Article 5(1), conforming changes to other paragraphs should be made to avoid controversy.

Determination of Whose "Business" Is Being Conducted

We also believe that some caution needs to be expressed about the broad statement in proposed paragraph 10.1 that an "enterprise may also carry on its business through subcontractors". Despite the qualifier "may", without some further elaboration of the circumstances in which this may be true, the statement is too broad to be included in the Commentary without further qualification. The possible unanticipated consequences of the broad statement as drafted in paragraph 10.1 can be seen when read in light of the proposed statement in paragraph 4.2 referring to an enterprise which "performs business activities … at a location". Read together,

those two paragraphs could be misinterpreted to suggest that an enterprise generally will have a PE at any location where it "carries on its business" through subcontractors, without further conditions.

In the normal case, a contractor, even a related party one, should be regarded as simply carrying out its own business, as opposed to the business of the enterprise to which it is providing services. This is consistent with paragraph 42 of the Commentary, in which the case of a management services provider is examined. In that case, the Commentary correctly notes that, as a general matter, the place of business of a service provider is not the place of business of the associated enterprise receiving the services, and the service provider is not conducting the business of the service recipient. If the Working Group believes that circumstances may exist where the contractor should be regarded as performing the business of the enterprise, then specific guidance should be proposed to describe those unusual circumstances.

The question of whether a contractor is carrying on the business of the enterprise, as opposed to carrying on its own business, was raised, but not answered, by the CARCO example set out in paragraph 17 of the Discussion Draft. The Discussion Draft correctly raised, as does the text of existing paragraph 42 of the Commentary, the two key questions of whether the premises of SUBCAR were at the disposal of CARCO, and whether the business of CARCO was wholly or partly carried out at those premises. The Working Group quite properly agreed that in the CARCO example, CARCO did not have a PE in the State of residence of SUBCAR, despite the fact that the foreign enterprise built the industrial plant, and owned the parts, work in process and finished goods at the location of the contract manufacturer. It appears that the Working Group based this conclusion on the assessment that CARCO did not have premises at its disposal. The Discussion Draft unfortunately does not record whether the Working Group also formed a view on the second question: whether CARCO was carrying out its business at SUBCAR's premises.

As a matter of treaty interpretation, it is correct that if the foreign enterprise does not have a "fixed place of business" at its disposal in the State, then it is not necessary to determine whether the activity of the contractor constitutes the conduct of the business of the foreign enterprise or only the business of the contractor or supplier. In some cases, however, the second question of whose business is being conducted by a contractor or supplier is relevant to the analysis (e.g., the "small hotel" example in proposed paragraph 10.1 of Commentary), so it is an appropriate issue for further discussion in the Commentary.

In the CARCO case, it is clear that for purposes of applying the PE standards of the OECD Model, the business activity being carried out at the manufacturing location is the business of SUBCAR, not of the foreign enterprise. It is generally the case that a contractor or service provider which provides goods or services to an enterprise conducts its own business, and not the business of the foreign enterprise, even when the business activities of the two entities are integrally related, as is normally the case in an affiliated group where two entities contract with each other as participants in a single production chain.

Enterprises today commonly divest themselves of manufacturing or other industrial activity in order to concentrate on other functions. A producer of consumer electronics which outsources the production to another enterprise has made a commercial decision not to be in the business of manufacturing. The same relationships should be respected for purposes of PE analysis. Since SUBCAR is engaged in its own business activities, CARCO should not be regarded as conducting its business through the activities of SUBCAR. We recommend that the Final Report also confirm this second point, consistent with paragraph 42 of the Commentary.

Because controversies have already arisen due to contractor business arrangements, we believe that it would be useful for the Commentary to include an example or two of circumstances where the use of a contractor would not give rise to a PE. This could be done in the case of the KCO example set out in paragraph 47 of the Discussion Draft. The Discussion Draft does not indicate whether members of the Working Group believed that the facts of the KCO example create a PE under Art. 5(1). Under the facts as given, it would seem that FCO is conducting its own business activities, not those of KCO. We recommend that the Working Group conclude that even if KCO is regarded as having premises at its disposal in State S, FCO is not conducting the business of KCO for purposes of Art. 5(1).

Similarly, we propose deleting the example of the "small hotel" proposed to be included in paragraph 10.1, at least without more elaboration as to the factors which would determine when a contractor could be regarded as carrying out the business of its principal. As noted above, we believe that considerable further thought needs to be given as to when the activities of a contractor would be regarded as the conduct of the business of its principal, as opposed to the conduct of its own business. For example, if the small hotel owner in proposed paragraph 10.1 engaged an independent hotel management company to manage the hotel, it clearly would be inappropriate to consider that the hotel management company was conducting any business other than its own. Even the guidance on the services PE alternative does not attribute in-country activities to a foreign enterprise that is not closely supervising the manner in which the local person performs the services. It is difficult to see why activities should be attributed to foreign enterprises more broadly. In any event, absent some detailed guidance on that point, it would seem premature and misleading to include this example in the Commentary.

The Discussion Draft (paragraph 45 ff) raises similar issues in the context of a construction site PE under Article 5(3). The Discussion Draft proposes revising paragraph 19 of the Commentary to provide that a general contractor who subcontracts "all or parts" of a comprehensive project could be deemed to spend time on a building site where "the general contractor has overall responsibility for the site and the site is made available to that general contractor for the purposes of carrying on its construction business." Although the proposed language is limited in its application to construction sites, the Working Group suggested in paragraph 50 of the Discussion Draft that the "issue was not restricted to construction sites."

We do not believe that there should be any necessary connection between the guidance expressed for Article 5(3) construction site PEs and the general rules of Article 5(1). Accordingly, we recommend that the final report clarify that the guidance of paragraph 19 of the Commentary is limited to construction site PEs under Article 5(3), and that the examination of whether a nonresident enterprise is conducting business outside the construction context through its fixed place of business for purposes of Article 5(1) is determined solely by the guidance in the revised paragraphs 10 and 10.1, discussed above.

Meaning of "to conclude contracts in the name of the enterprise"

The interpretation of this expression from Article 5(5) is a key issue for members of the TPWG. On this point, we have some specific suggestions for proposed guidance to be included in the Commentary, but also an important general point as to how treaty language should be interpreted. In general, we believe that treaties should be interpreted according to their plain meaning, as is appropriate for the interpretation of a contract between two parties. Accordingly, the terms of Article 5(5) should be applied in each case consistent with the legal relationships actually created by the parties. The Discussion Draft in paragraph 107 frames the issue well: should Article 5(5) apply only when the principal is in fact contractually bound under applicable law and the contracts among the parties, or should the treaty be interpreted to apply in cases where the principal is "economically bound"?

We respectfully suggest that there is no place in the interpretation of Article 5(5) for an "economically bound" concept. While we would agree that appropriately drawn substance-over-form concepts may have a role to play in treaty interpretation, we do not agree that the plain meaning of a treaty should be modified in the normal course through the use of imprecise concepts such as "economically binding".

This issue, of course, has been recently addressed expressly by the highest courts of both France and Norway in their respective *Zimmer* and *Dell* cases regarding commissionaire relationships. In both cases, the Supreme Courts rejected the application of an "economically binding" concept and decided the case on the basis of the actual legal relationships formed by the parties. We believe that this is an important interpretative point, and one that the Working Group should expressly endorse.

Regarding the specific result of the commissionaire cases, we also suggest that the Working Group adopt the view of the French and Norwegian Supreme Courts and conclude that the operation of a civil law commissionaire, in the normal course, does not create a PE of the principal under Article 5(5). Many multinational groups have adopted the commissionaire sales structure for legitimate business reasons, including creating efficiencies in intercompany invoicing, enhanced central control of inventory and receivables, and various other reasons. The protracted controversy over the last decade regarding the application of Article 5(5) to commissionaire relationships has consumed resources of both tax administrations and taxpayers,

and has unnecessarily impeded the adoption and utilization of a commercial structure that has existed in the law of most OECD Member States for many years. In some Member States, the commercial law provisions have remained essentially unchanged since the 19th century. The Working Group now has an excellent opportunity to fulfill its mandate to form and express a consensus among Member States by adopting the approach to the interpretation of Article 5(5) and its application to commissionaire structures that has been confirmed by both European high courts which have addressed the issue.

Part of the controversy over commissionaire structures has been caused by the introduction of language into paragraph 32.1 of the Commentary which deals with common law arrangements, without adequate explanation as to the point of this language. As noted by the French and Norwegian Supreme Courts, the purpose of the existing text of paragraph 32.1 is to address the legal consequences of agents entering into contracts where the agency relationship is governed by the law of common law countries, such as the United Kingdom or the United States. The Working Group has proposed adding further explanatory material to paragraph 32.1, to state that "in some countries, an enterprise would be bound, in certain cases, by a contract concluded with a third party by a person acting on behalf of the enterprise even if the person did not formally disclose that it was acting for the enterprise and the name of the enterprise was not referred to in the contract."

This additional language again apparently is intended to apply only in the context of relationships governed by common law. The proposed language obliquely refers to this limitation, however, by noting that the rule expressed would apply only in "some countries" and in "certain cases". It would be more appropriate in the interests of providing transparent guidance to taxpayers and tax administrators for the Commentary to clearly state that this rule applies only in the common law context, and that the "certain cases" alluded to are those circumstances where the applicable law and the contracts between the parties causes the principal to be legally bound by the acts of the dependent agent.

Finally, we are disappointed that the Discussion Draft declines to provide guidance regarding the application of the contract conclusion standard where standard form or framework contracts are used. Indeed, paragraph 113 of the Discussion Draft could create new confusion with its statement that:

> It was suggested that in cases 2 and 3 [standard form or framework contracts], as long as sales contracts were concluded in the name of a foreign enterprise, the extent to which the person concluding these contracts (e.g. by accepting an order) was using standard contracts or was constrained by a framework contract would not seem to matter.

The passive voice formulation of this statement signals that this was not a consensus view of the Working Group, but gives no indication of whether it was an isolated remark or a widely

accepted view. Absent a consensus view on the issue, it would seem appropriate to delete this language from the report, lest it be misconstrued as the consensus view of Working Party 1**.** If, on the other hand, the Working Party would like to endeavor to reach a consensus view on these issues, or on the treatment of multi-level contract approval, we would be pleased to offer additional recommendations.

Time Requirement for the Existence of a Permanent Establishment

The TPWG notes with some disappointment the Working Group's conclusion, in paragraph 34 of the Discussion Draft, that it will not propose a firmer statement of the minimum time threshold required to form a fixed place of business PE under Article 5(1). We note that the alternative service PE provisions are entirely based on the passage of time. It seems strange, therefore, that the Working Group could not consider that some firmer time threshold would not also be appropriate for business activities other than the performance of services.

Instead, the Working Group's proposals would introduce even more subjectivity into the interpretation of "permanent" by introducing two new exceptions to the "facts and circumstances" approach now set out in paragraph 6 of the Commentary. The Working Group has proposed the following illustrations of circumstances when even stays of less than 6 months in a year could be regarded as "permanent" rather than "temporary":

1. Activities of a recurrent nature: An individual who rents a stand "at a commercial fair" for five weeks each year for 15 consecutive years may satisfy the permanency requirement for a PE under Article 5(1) even though the individual's annual time at the fair falls well below the six-month guideline.

2. Business carried on exclusively in a State: Operating a restaurant for four months during the shooting of a television documentary may satisfy the permanency requirement for an Article 5(1) PE because four months represent the entire operating life of the restaurant. In contrast, operating various catering facilities in a State during a four-week international sports event would not satisfy the permanency requirement if an enterprise otherwise operates a catering business in its home State.

The circumstances that these exceptions presumably are intended to target surely would arise only rarely, and we believe that the potential confusion they could generate would far outweigh their potential benefits. If these exceptions are to be included in the Commentary, certain clarifications would be important to minimize controversy.

First, on the recurrent activity exception, we suggest that the example state that the individual rented a stand "at the same commercial fair" each year. That will confirm the point that this exception is not intended to apply to business arrangements where personnel of an enterprise may make repeated, short-term visits to different client sites in a State.

On the short term business example, the relevant issue under Article 5 should be the level of presence in the host country alone, determined without regard to the extent of the enterprise's presence outside the country. However, if this language is retained, it would be useful to confirm that this exception is not meant to apply to multinational business enterprises, as they necessarily will have other business activities which are conducted outside the State concerned. This would eliminate the potential inference that tax administrators should attempt to compare the levels of presence in-country as opposed to elsewhere, which would present serious administrative challenges and create significant controversy.

Relationship between Delivery and the Sale of Goods in Subparagraph 4 a)

We appreciate the proposed clarification in paragraph 22 of the Commentary that a facility used solely for storage, display or delivery of goods or merchandise will not constitute a PE even if a contract for sale of the goods or merchandise has already been executed by the nonresident enterprise. This is a useful clarification of the exception provided in subparagraph 4 a) of Article 5, as it is common in commercial arrangements for contracts of sale to be entered into with title passing only when the products have been delivered to the purchaser. Under those circumstances, the nonresident enterprise would still own the goods or merchandise located in the storage facility.

We are less sure that the revisions to paragraph 27.1 of the Commentary that are proposed in paragraph 81 of the Discussion Draft make sense. Those proposed revisions apply an anti-fragmentation notion to cases where the enterprise maintains a stock of goods or merchandise for storage, display or delivery in the State, and also is treated as having a deemed "dependent agent" PE in the State under Article 5(5). The proposed Commentary language would state that the enterprise cannot not rely on the exception in subparagraph 4 a), even if the activity of the dependent agent took place at a different location, if the activities of the deemed PE are "not separated organisationally" from the place of storage, display or delivery.

The sole effect of this provision would appear to be to withdraw the exception provided by subparagraph 4 a) whenever a deemed dependent agent PE is found under Article 5(5). We find this result somewhat peculiar, since if the enterprise has a deemed PE under Article 5(5), the enterprise by definition has no actual fixed place of business through which it is engaged in sales activity in the State. Thus, the enterprise's functions, assets and risks which might be attributable to the deemed PE do not exist at the place of storage, display or delivery and there is no second place of business in the State to which the anti-fragmentation principle could be applied. We would have similar concerns if such an analysis were also extended to other types of activities with respect to which a deemed PE may be asserted under Article 5(5).

This analysis may be familiar from UN Model concepts of dependent agent and force of attraction concept but it would seem inconsistent with the text and purpose of OECD Article 5.

We, therefore, respectfully request that it be withdrawn. If the Working Group decides to retain this new rule, we request that the Working Group at a minimum provide a description of the circumstances under which a deemed PE and a facility for storage, display or delivery would be considered as "not separated organisationally".

* * *

The Treaty Policy Working Group appreciates the opportunity to comment on the Discussion Draft. We hope that our suggestions are taken in the constructive spirit in which they are offered and that they assist Working Party 1 in its further deliberations on these important issues.

Sincerely,

Carol A. Dunahoo

Gary D. Sprague

cc: Pascal Saint-Amans, Director, CTPA
Marlies de Ruiter, Head of Tax Treaty, Transfer Pricing & Financial Transactions Division, CTPA
Jacques Sasseville, Head, Tax Treaty Unit, CTPA
Andrew Dawson, Chair, Working Party 1
Aart Roelofsen, Chair, Working Group 10