

INTERNATIONAL ARTISTES AND SPORTSMEN

ARTICLE 17 OECD MODEL

PROBLEM OF DOUBLE TAXATION

On 23 April 2010 the OECD has published a new Draft Commentary for Art. 17 OECD Model. Below you will find my contribution to the discussion about Art. 17.

1. Introduction

When artistes and sportsmen perform abroad they pay income tax in two countries. Not only in their residence country on their world-wide income, but also in the country of performance. And although tax treaties have been concluded, double (or excessive) taxation very often occurs.

2. Source tax

Most countries levy a source tax on income earned by foreigners in the country. The rates are varying from 15 – 30%. Reasons for this source tax are that countries

- a. want to eliminate the risk of tax avoidance, because the foreigner would not mention the income in its tax return in the residence country or would have moved his residency to a tax haven without income tax, such as Monaco
- b. are not sure whether the foreign artistes will mention the income in their tax return in the residence country

3. Bilateral tax treaties

Bilateral tax treaties have been concluded by most countries, which divide the taxing rights and aim to eliminate double taxation. The general principles of international taxation can be found in the Model Tax Convention of the Organisation for Economic Cooperation and Development (OECD):

- a. companies and self-employed persons are only paying income tax in their residence country, unless when they have a permanent establishment (PE) in the source country (Art. 7 OECD Model)
- b. employees are paying income tax in the country of work, unless when they remain employee in their country of residence, receive their salaries from that employer and work for less than 183 days in the other country. If so, only the residence country is allowed to tax the income (Art. 15 OECD Model)

These two principles follow the idea that someone has to contribute to a country's state budget when he uses the country's infrastructure and facilities on a regular basis.

Double taxation is likely when the source country has the right to tax the income (for companies with a PE or an employee working for an employer in the source state), because the residence

country will also tax this income as part of the world-wide income. The bilateral tax treaties have two ways to eliminate this double taxation:

- tax credit for the foreign tax, or
- tax exemption for the foreign income

The tax credit method is mainly used by the USA and UK, the tax exemption method is more common in continental Europe.

4. Special rules for performing artistes: Art. 17 OECD Model

The member countries of the OECD have decided in the 1960s to create an exceptional rule for performing artistes (and sportsmen). They need to pay income tax in the country of performance, regardless of the general rules for companies, self-employed persons or employees. This is mentioned in the special Article 17 of the OECD Model Tax Convention. Main reason for this special treatment is that top artistes and sportsmen are very mobile and can easily move their residency to a tax haven such as Monaco, which levies no income tax. The OECD believes that without Art. 17 (and the taxing right for the source country) these top artistes and sportsmen would escape from taxation under Art. 7.

5. Elimination of double taxation: Art. 23 OECD Model

To eliminate double taxation the OECD recommends in Art. 23 OECD Model that the residence countries allow its artistes a tax credit for the foreign source tax. Most countries have followed this, also continental European countries, only some countries prefer to use the exemption method for artiste performance income that may be taxed under Art. 17. An example of the latter is Belgium.

6. Problems

With the taxing right of Art. 17 and the tax credit of Art. 23 the taxation of international performing artistes and sportsmen seems very balanced. But unfortunately this is not the reality. The following problems exist in practice:

- a. The country of performance levies tax from the gross performance fee, including all expenses, where the country of residence only allows a tax credit on the net income. An example:

A German classical orchestra performs in Spain, earning € 25.000. The Spanish non-domestic withholding tax is 25% (from gross) and the touring expenses are 60% (= € 15.000). The average German income tax rate for the musicians is 35%:

Spanish withholding tax: $25\% \times € 25.000 =$ € 6.250

German income tax (exempted / maximum tax credit):

Gross earnings – 60% expenses = € 10.000 income x 35% = - 3.500

International double taxation € 2.750

Germany will not allow a higher tax credit than the amount of German tax due on the net income.

- b. But also problems with the tax credit may arise. These problems can be the following:
- The promoter in the country of performance has not issued a tax certificate, so there is no evidence for the tax inspector in the residence country about the source tax
 - The tax certificate is in the name of the group, where the tax credit needs to be obtained by the individual artistes or sportsmen
 - The artistes or sportsmen are employees of the group, receiving a monthly salary, and the tax credit cannot be processed in the monthly salary administration
 - The tax certificate has been issued in the original language of the country of performance (and not in English): see example
 - The foreign tax does not qualify for a tax credit. Examples are French social security contributions, US state tax and German *Künstlersozialversicherung*.

If one of these problems occur, double taxation results, because both source tax in the country of performance and income tax in the country of residence are being paid.

7. Existing solutions

At the moment there are already some solutions for the problems described:

- a. Many tax treaties follow an option in the Commentary of Art. 17 OECD Model, which allows countries to exempt subsidized performances from source tax in the country of performance. The percentage of subsidy may vary in tax treaties, but sometimes this exception may help.
- This solution takes away any risk of double taxation.
- b. Some treaties only tax a part of the performance fee, i.e. the personal income of the performing artistes and sportsmen and exempt the income accruing to others resp. the costs.
- c. The European Court of Justice (ECJ) has ruled in the Gerritse (12 June 2003) and Scorpio (3 October 2006) cases, that under the EC Treaty expenses should not be taxable in the country of performance. This means that within the European Union all countries should only tax the actual income that goes to the performing artistes and exempt the expenses element. The European Commission has become active to force member countries to change their legislation. This has been done by Austria (2008), Germany (2009), Sweden (2010) and Spain (2010), but still needs to be done by countries as Portugal, Italy, Greece, Czech Republic and others.
- These two solutions bring down the source tax and improve the chance that the tax credit in the residence country will be sufficient. But the problems with the tax certificates (and double taxation) may still occur.

8. Administrative expenses

The system of international artiste and sportsman taxation causes much administrative work and expenses. Firstly, an artiste, sportsman or group needs to get an exemption or approval for the deduction of expenses in the source country, and secondly, the tax credit in the residence country needs to be realized. Not only staff members on the payroll, but also external, specialized tax advisers need to be hired to avoid the double taxation. These administrative expenses are a major obstacle.

9. Best practice example: The Netherlands

Per 1 January 2007 The Netherlands has decided to give up unilaterally its source tax on foreign performing artistes and sportsmen, when they live in a country with which The Netherlands has concluded a bilateral tax treaty. This means that The Netherlands is not using its taxing right from Art. 17 anymore. The loss of tax revenue was not more than approx. 5 million euro per year, but also 1,6 million euro in administrative expenses were removed, both with the artistes, sportsmen, promoters as with the tax administration in the two countries. The foreign artistes and sportsmen are now treated in accordance with Art. 7 and Art. 15 of the tax treaties and most often only paying income tax in their residence country.

If all countries would follow this initiative the loss of tax revenue would be nil, because not only the tax earnings would be given up, but also tax credits should not be given anymore.

10. Removal of Art. 17

On 23 April 2010 the OECD has published a new Draft Commentary for Art. 17 OECD Model, in which practical problems have been recognized and solutions are proposed. These are interesting, but do not go in the direction in which I believe Art. 17 should go, i.e. the removal of the article from the OECD Model and the return to the general rules of Art. 7 and 15. That would help everyone in the artiste and sports world, because the administrative obstacles would be taken away as well as the risk of double taxation. And the loss of tax revenue would be nil, as explained in paragraph 9.

Removal of Art. 17 would also take away the risk of double non-taxation in situations where the residence country applies the exemption method and the source country does not levy a withholding tax.

Finally, with the removal of Art. 17 tax avoidance behavior is still counteracted, because source countries will only give up their national withholding tax, if a non-resident artiste, sportsman or company can prove that he is a resident of a country with which a bilateral tax treaty has been concluded (and in which therefore normal taxation is secured).

The OECD has shown with Art. 14 that a removal from the Model Treaty is very well possible. It could improve its Model Treaty by leaving out Art. 17 in the next version.

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