THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

December 2020

MODULE 1

PRINCIPLES OF INTERNATIONAL TAXATION

TIME ALLOWED – 3¼ HOURS

This exam paper has **two** parts: **Part A** and **Part B**.

You need to answer **four** questions in total.

You must answer:

- **At least two** questions in **Part A** (25 marks each)
- **At least one** question from **Part B** (25 marks each)

Further instructions

- All workings should be made to the nearest month and you must use the appropriate monetary currency, unless otherwise stated.
- As you are using the online method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately a quarter of your time answering each of your four selected questions.
- There is no separate reading time, so you can start typing your answers as soon as the exam begins. However, we recommend that you set aside some time to thoroughly read each question and plan each of your answers.

PART A

You are required to answer AT LEAST TWO questions from this Part.

1. "The standard of 'foreseeable relevance' is intended to provide for exchange of information in tax matters to the widest possible extent and, at the same time, to clarify that Contracting States are not at liberty to engage in 'fishing expeditions' or to request information that is unlikely to be relevant to the tax affairs of a given taxpayer."

   OECD, Update to Article 26 of the OECD Model Tax Convention and its Commentary 2012, 3. Now contained within Commentary on Article 26[1], [5].

   You are required to discuss this statement. Your answer must include references to developments in the area of exchange of information. (25)

2. **You are required to answer both parts of this question:**

   1) Summarise how taxing rights related to royalty income are allocated across jurisdictions under the OECD Model Tax Convention (OECD MTC) 2017 and the UN Model Tax Convention (UN MTC) 2017. (15)

   2) Discuss recent developments relating to the taxation of royalty payments in an international context. (10)

   Total (25)

3. **Consider the extent to which you agree with the proposition that the manner in which 'offshore indirect transfers' (OITs) (i.e. transfers that involve a Country B resident selling an entity that owns immovable property located in Country A) are taxed is of particular significance to developing countries.** (25)

4. **Discuss the extent to which you consider international rules affecting direct taxation on the one hand, and trade on the other, to have evolved in similar ways. To what extent can they be said to have similar goals?** (25)

5. **Write a report for a revenue authority that evaluates the effectiveness of the mutual agreement procedure as a tax treaty dispute resolution mechanism.** (25)

PART B

You are required to answer AT LEAST ONE question from this Part.

6. Antonio (A) and Bao (B) are employed by Finesse Ltd (Finesse), a company which is a tax resident of Leonia. Both individuals are tax residents of Zantra. A and B are both sales managers of different teams within Finesse. A and B travel to Leonia for sales meetings every quarter but are otherwise based in Zantra. A and B also receive dividends from a company resident in Leonia (Leralo Ltd) and have recently been awarded some Finesse stock options as a reward for meeting their sales targets. These stock options must be exercised before employment with Finesse ceases and are non-transferable.

A is now close to the Zantran retirement age and Finesse is aware of this fact. B is planning to move overseas to Colonia to take up a position at a rival company, Clarisse Ltd, which is tax resident in Colonia, but has yet to hand in her notice to Finesse.

In the relevant tax year, A and B each:

- derive \$100,000 in salary;
- derive \$8,000 in dividends; and
- receive stock-options that have a market value of \$15,000 and \$25,000, respectively.

Leonia and Zantra entered into a double tax agreement (DTA) in 1964. It contains articles that mirror the OECD Model Tax Convention (OECD MTC) 2017, with the exception of the following article that permits residents of both countries to claim foreign tax credits (FTCs) for tax withheld on dividends derived in the other state, provided tax has been paid in the other state:

(a) In respect of individuals who are resident in Zantra and who receive income from movable property that has been effectively subject to withholding tax (WHT) in Leonia, the tax due on the net amount of the income following withholding tax in Leonia is reduced with an FTC that can be used offset tax payable in Zantra under conditions fixed by Zantra law, provided that such percentage is not less than 15% of the net amount.

(b) In respect of individuals who are resident in Leonia and receive income from movable property that has been effectively subject to WHT in Zantra, the tax due on the net amount of the income following withholding tax in Zantra is reduced by way of an FTC of 15% that can be used to offset tax payable in Leonia.

Zantra subjects the net dividends (i.e. net of Leonia WHT received by A and B) to personal income tax at a rate of 25%. On their respective Zantra tax returns, A and B have claimed an FTC that represents 15% WHT paid in Leonia. However, Zantra has refused to provide A and B with an FTC to cover the tax paid in Leonia, because Zantra's domestic law changed quite substantially in 1988. The relevant change removed the ability of individual taxpayers resident in Zantra to access FTCs on dividends derived overseas, and also reduced the overall personal income tax rate.

Upon further inquiry it becomes evident that:

- Leonia withholds tax at 15% and there have been no rate changes since the Leonia-Zantra DTA was entered into; and
- Zantra's domestic tax regime was amended in 1988.

The relevant amendments in Zantra include reductions in the personal income tax rate, as well as the non-availability of FTCs on dividends from non-resident companies from 1988 onwards.

You are required to discuss the grounds, if any, upon which Leonia and/or Zantra can assess to tax A's and B's salaries, dividends and stock options.

You must include a consideration of whether it is possible for A and B to appeal against the Zantra revenue authority's claim that they are not entitled to an FTC for tax paid in Leonia on dividends derived therein. (25)

7. Karl is 70 years old. He is a citizen of Gelia but has lived in Halonia for the past 15 years and is a permanent resident of Halonia for immigration purposes. Karl receives pension payments from his previous employer, the Gelia Department of Statistics, with whom he was employed as a civil servant for 30 years. Karl retired 15 years ago and has received monthly payments since then. The pension fund, out of which the payments are made, is a public fund. Recently, Karl has been approached by a financial advisor who suggests that Karl should move his pension into a private fund.

Karl rents a property on a long lease in Halonia, where he lives with his partner and their cat. He maintains a bank account at Gelia National Bank Ltd in Gelia, which generates approximately $20,000 gross interest per annum (of which 10% is withheld as tax).

Karl visits his family in Gelia every summer, where they stay together in a beach house that he owns. While on holiday in Gelia, Karl attends the annual general meeting of a company in which he used to own shares. He attends the meetings in his capacity as non-executive director and is paid $15,000 per annum for his role. Outside the summer season, Karl rents out the house on the open market, usually finding tenants on a local writers' retreat website.

Gelia and Halonia have a double tax agreement that mirrors the OECD Model Tax Convention (OECD MTC) 2017. Both countries operate worldwide bases of taxation for individual resident taxpayers.

You are required to advise Karl on the appropriate tax treatment of the relevant income amounts in the above scenario. (25)