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INTERNATIONAL DOUBLE TAXATION: DSOUBLE TAXATION AGREEMENTS (DTA)

Summary

As a result, present taxation, avoidance of double taxation and Double Taxation Agreements (DTA) are important elements of international trade relations. All states are interested in harmonizing tax systems to expand trade and other ties with each other. Thus, importance of double taxation agreements (DTA), structure of these treaties nneds to be resarched and stuidied in that article.

Key words: *taxation, history of double taxation, avoidance of double taxation, double taxation agreements, mechanics of double tax avoidance*

Intorduction

Economic activities cross national borders, whereas the power to tax is bound to the nation state. One of the problems resulting from this incongruity is double taxation, which stems from an overlap of jurisdiction to tax between a residence state — the country where a taxpayer lives — and a source state — the country where the taxpayer’s income was generated. If both countries exert to the full their power to tax, then the tax burden for international investments is much higher than for national investments. In order to prevent this, governments engage in efforts to avoid double taxation. The institutional form of international double tax avoidance, however, exhibits several remarkable features that are in need of explanation.

The most remarkable feature of international cooperation to avoid double taxation is the fact that double tax agreements (DTAs) are predominantly bilateral. This bilateralism contrasts with many other international regimes in the economic sphere. Most prominent among these is the GATT/WTO — a multilateral regime with a commitment to achieving progressive, coordinated trade liberalization in simultaneous negotiations. Unlike the GATT/WTO, for example, cooperation in double tax avoidance is organized bilaterally, and negotiations take place sequentially.

International double taxation is subjecting direct to the same tax and taxable materials for the same period of time, by the public authorities from different countries. The advent of double taxation is due to the manner in which criteria are applied to the taxation of income or wealth. Generally, the situations in which double taxation (economic or legal) appears, are determined by the fact that the Governments of various States apply to taxes on income made in the Territories concerned by subjects of taxation local and foreign, and on the other subject to taxes and the income from its own citizens abroad.

Since double taxation affects the efficiency and competitiveness of exports of foreign goods, the removal of international double taxation is a necessity in order to ensure an economic developments of relations at the international level. Why international elimination of double taxation is a concern of all States, and amid its legal abolition is the development of international tax conventions called Conventions for avoidance of double taxation.

In international practice, for the avoidance of double taxation were enshrined certain principles on which the conventions concluded lays down the methods of settlement and collection of taxes. Double taxation tax may constitute an obstacle to optimal allocation of capital investments and productive activities and precisely why it is believed that removing them is a fundamental economic policy side and the tax of Governments. In international practice, for the avoidance of double taxation have been devoted to certain principles, on the basis of which shall be determined by conventions concluded by settlement and methods of tax collection.

The development of foreign trade in value of the materials and international economic cooperation, among other measures required and to find appropriate means in order to avoid double taxation of operations with revenue made of outbound, which ensure their normal development and flourishing reciprocal partners in promoting and improving international cooperation in further.

External, international elimination of double taxation in order to represent a necessity to ensure an improvement of the economic relations at the international level. Why international elimination of double taxation is a concern of all States, and amid its legal abolition is the development of international tax conventions called Conventions for the avoidance of double taxation. Double taxation tax may constitute an obstacle to optimal allocation of capital investments and productive activities and precisely why it is believed that removing them is a fundamental economic policy side and the tax of Governments.

A significant role of a double tax agreement (DTA) between two or more countries is to remove the double taxation, which is an impediment to cross-border trade in goods and services, and the movement of capital and people between countries. Many countries have now entered into scores of comprehensive DTAs with other countries to assist in the avoidance of double taxation.

The second purpose of a DTA is the prevention of fiscal evasion, which can reduce a country's tax base where a taxpayer has economic connections with more than one country. In this general context, it is particularly important to know how DTAs come about and how they are used for the benefit of taxpayers, which embark upon transactions or economic events that have international tax ramifications, and for the benefit of tax administrations in different countries, which are charged with the responsibility of protecting their state's tax base.

1. The History of Double Tax Avoidance

The history of the double tax regime goes back to the beginning of the last century, when a few continental European states signed bilateral double tax treaties, mostly with their neighbors. The issue became more prominent in the 1920s when the League of Nations appointed economists to address the problem of double taxation, and convened several conferences of technical experts and government officials (League of Nations 1923, 1927). The objective during the "League years" was to draft a multilateral treaty. While governments persistently rejected this, they were nonetheless very supportive of developing a model convention (MC) that could be employed as a template for bilateral negotiations. They insisted on keeping the model convention non-binding, because that would allow the necessary flexibility to make nationally differing tax systems compatible to one another. The work of the League resulted in the model conventions of 1928, 1935, 1943 and 1946. (4)

In the 1950s and 1960s the Organisation for Economic Co-operation and Development (OECD) has taken over the position of the League of Nations (and briefly the United Nations) as the main multilateral policy forum for discussions of international tax issues. Countries' positions remained unchanged. They expressed their opposition to a multilateral treaty, but were supportive of further developing and adapting the MC. The OECD published its first MC and commentary in 1963, followed by a revised version in 1977. In 1991, the OECD decided to publish the model convention in loose-leaf format, in order to be able to better adapt it to changes in the economic environment. Since then the MC has been updated continuously, with consolidated versions being published in 1992, 1994, 1995, 1997, 2000, and 2003.then the MC has been updated continuously, with consolidated versions being published in 1992, 1994, 1995, 1997, 2000, and 2003. (3)

The growth rate of bilateral treaties increased strongly after the OECD MC was concluded. In 1958, 263 treaties were in force, gradually increasing to 333 by 1963 and 600 as of 1978. After the conclusion of the 1977 MC — and with the further liberalization of capital markets and increasing tax ratios in industrialized countries, which made the problem of double taxation more prevalent — the number of treaties increased rapidly to 1582 in 1998. (5)

Even though countries are not obliged to use the MC in their bilateral negotiations, almost all of the more than 2000 tax treaties that are in force today follow it. Bilateral treaty making basically consists of the treaty partners agreeing on the MC and adapting some provisions to their needs.

Despite these successes in confronting the issue of double tax avoidance, the development was not without conflict. The most important conflict among governments is that between the residence and source principle of taxation. In general, developed countries are in favor of the residence principle, whereas developing countries prefer the source principle because it allocates a larger share of the transnational tax base to them. The conflict has accompanied the entire history of international tax cooperation. One embodiment of this conflict is the existence of different model conventions that accord different weights to both principles. Since the OECD MC accords greater weight to residence taxation, the United Nations (UN) developed a competitor model that leans toward source taxation. (6)

Over time, the arrangement of a non-binding multilateral model convention as template for bilateral treaty negotiations has become firmly institutionalized. The Commission on Fiscal Affairs (CFA) of the OECD — a body of government officials and tax experts, the same persons negotiating bilateral treaties for their countries — meets on a regular basis. The CFA is the global forum for countries to cooperate in matters of taxation, and non-OECD member countries also participate in these negotiations. In an ongoing process the CFA strives to modernize and adapt the MC. Often technical innovations that come up in bilateral treaties are integrated into the model; other innovations are developed within the CFA. In the process a common understanding of bilateral tax treaty making and interpretation is developed. These common understandings and remaining dissent are published in the commentary that accompanies the MC, which enjoys considerable authority with courts, lawyers and other tax practitioners. Unlike the OECD, the UN has not devoted many resources to international taxation and thus did not become a potent rival of the OECD as the main policy forum in international taxation. (1)

The jurisdiction to impose income tax is based either on the relationship of the income (tax object) to the taxing state (commonly known as the source or situs principle) or the relationship of the taxpayer (tax subject) to the taxing state based on residence or nationality. Under the source principle, a State's claim to tax income is based on the State's relationship to that income. For example, a State would invoke the source principle to tax income derived from the extraction of mineral deposits located within its territorial boundaries. Source taxation is generally justified on the ground that the State has contributed to the creation of the economic opportunities that allow the taxpayer to derive income generated within the territorial borders of the State. Of course, jurisdiction to tax is also about power, and a State generally has the power to tax income if the assets and activities that generated it are located within its borders. (3)

2. Methods of avoidance double taxation

In international practice, for the avoidance of double taxation have been devoted to certain principles, on the basis of which shall be determined by conventions concluded by settlement and methods of tax collection.

In 1963, and then in 1977, the Organization for economic cooperation and development has released models of the Convention reviewed and improved. Within the framework of that Convention contained some model solutions applicable in relations between the countries, solutions that are retrieved in the form you want concrete under conventions concluded between countries. (1)

Featured solutions take into account, inter alia, as the imposition profits achieved by economic operators should be carried out by the country in which they were made and these subjects have a fixed establishment, and proceeds in the form of coupons associated with bonds, promissory notes or other evidence of debt, in the form of fees for use of copyrights patents, trademarks, or trade secret formulas, processes or etc., as well as in the form of dividends to be taxed by both countries, in proportions agreed by them. (3)

Another measure imposed by international conventions proposes that the taxation of the income derived from the performance on your own professional free (architect, doctor, lawyer, accountant, engineer, professional artist, professional sports, etc) to be carried out either in the country of origin when their beneficiary has a fixed establishment for the free pursuit of the occupation, either in the country in which the beneficiary of the income when it has no registered residence in the foreign country. (3)

For the avoidance of double taxation conventions shall apply to taxes on income and wealth, levied on behalf of each of the Contracting States. Fall within the scope of the Convention all taxes on income and wealth, regardless of the system in which they are used: the imposing at source, surcharges, additional odds.

In the case of indirect taxes there is no question of double taxation of foreign citizens whereas international support, as buyers, same taxes included in the price of the goods purchased with the citizens of the country.

Of course, such a tax in question only if the residents of a country achieves revenue or have properties in other countries. Because, in the case of payment of taxes once, but two or more fiscal authorities juxtaposed in the same country (and parallel), double, triple or multiple taxation (exaggerated materially) is a reality (pressing), but this is not considered in the theory of public finance a triple double, or multiple legal enforcement, but one of an economic nature, which in fact is reflected in the increase in average fiscal pressure borne by the taxpayer in question in its own country. (5)

Administrative point of view, in the analysis of double taxation must keep in mind the difference between financial authorities and the overlying juxtaposed (parallel). Such double taxation occurs only where it is caused by juxtaposed authority.

In connection with the "multiplication" of taxation, we appreciate that in international practice may not be detained than double taxation, since the imposition of a particular topic should be judged against the criteria of taxation of incomes and estate, which country they use in relation to different country, viewed in isolation, the country with the country. (2)

The emergence of double taxation is due to the way in which the criteria are applied which underlie the imposition of income or wealth. International tax practice criteria which underlie the imposition of income or wealth are:-the criterion of residence (or the tax residence), according to which the imposition of income or property shall be carried out by the tax authority in the country to which it belongs, regardless of whether the resident's income wealth, or subject to taxation are obtained or is in the territory of that country or outside;

-the criterion of nationality, according to which a country impose its residents, carrying out of income or owns property in the country concerned, whether or not they live in their country; (5)

- revenue-origin criterion (territoriality), according to which the imposition of the tax authorities of the country in whose territory they were produced or revenue, regardless of their wealth or nationality of recipients of income. (5)

Double taxation can be avoided either by unilateral legislative action, either by the conclusion of bilateral or multilateral agreements between different countries. Avoidance of double taxation by unilateral legislative action is more difficult, because every country is interested in how to achieve higher tax revenue.

Within the framework of conventions concluded between parties to international tax avoidance of double taxation or of clarification regarding the way in which the concrete will be imposed with reference to precise definition scope of applicability of the Convention in regard to the subjects of taxation, but in all of the residence and citizenship; (10)

-the laying down of profit taxation of businesses and ways or/and limits the deduction of expenses arising from parent firms to management only to daughters, which operates in other countries; (10)

-tax rates that we can use the country of origin of income in the form of interest, royalties and dividends. (10)

Taking into account these elements, in the international tax practice has been accepted following 4 methods or technical procedures for the avoidance of double taxation:

1. total relief-according to this method, income derived by a resident in a foreign country and subject to taxation in that country shall be deducted from the taxable income of the bulk in the country of residence shall take into account all revenue earned by taxpayers. To this end, the relationship is used: (3)

2. Exemption involves a progressive taxation income separately in each of the signatory countries of the Convention. But, in the context of taxation revenues, a non-resident abroad shall be added to taxable income in the country of residence shall be the taxable income earning overall depending on the progressive rate is to be determined for a fixed amount and/or progressive. They shall be used, and then only for the calculation of the tax on the income in the country of residence. In essence these remedies are on the one hand, allowing the use of appropriate tax in that State, and on the other hand reducing the tax paid abroad from taxable income in that State. (3)

3. Crediting ordinary lies in that foreign country tax paid for income received in the territory by a resident of another country shall be deducted directly from the tax calculated total in the country of residence. This tax is calculated taking into account the overall taxable income obtained by the sum of the taxable income in both countries (according to the previous method). Tax paid abroad shall be deducted only up to the limit of the internal tax that would be due to an income equal to that achieved abroad. Therefore, if the calculated tax in the country of residence is less than that paid abroad, the taxpayer will incur a higher total tax corresponding to that which would be incurred if all the taxable income would have been obtained in his/her country of residence. (3)

4. Crediting removes integral a previous method, meaning that the tax paid abroad shall be deducted in full from the total calculated tax in the country of residence, regardless of its size. Of the two methods of relief, the more advantageous it is outright, and between the two methods of \"lending\" best value for the taxpayer's total exemption method. Advantages and disadvantages of taxpayers shall be without prejudice, but it depends on the statement included in the Convention concluded between the countries concerned-on the method or process that will be used for the avoidance of double taxation and international taxation. (3)

3. Double tax agreements

Double tax agreements, double tax treaties or, in short, DTAs represent a complex area in the field of international tax. Therefore this article does not purport to comprehensively cover the topic; it merely aims to provide a highlevel overview of DTAs, with a special focus on the concept of ‘permanent establishment’. (2)

As the name suggests, a double tax agreement is an agreement or a contract regarding double taxation or, more correctly, the avoidance of double taxation. In the Malaysian context, a DTA is usually signed by a cabinet minister (or sometimes by the prime minister) representing his country. Thus, it is an agreement between two sovereign states (separate and distinct political entities). It has the status of a ‘treaty’ – hence, its alternative name of double tax treaty. (2)

A DTA is therefore a contract signed by two countries (referred to as the contracting states) to avoid or alleviate (minimise) territorial double taxation of the same income by the two countries. Any amendment or addition to such an agreement is known as ‘a protocol’.

A typical DTA will contain ‘articles’ (ie chapters or parts) covering various areas. When a DTA is mooted, the two countries will start off with a model convention, which is a template containing the standard articles and clauses of a DTA. Each country will come to the negotiating table with its list of conditions or ‘must-haves’. The treaty that is ultimately signed is therefore the culmination of rounds of negotiations, compromises and trade-offs. This is the reason why every treaty is unique and the particular treaty must be referred to whenever an issue arises pertaining to the two countries. The OECD (Organisation for Economic Co-operation and Development) model convention is one of three main ones; the other two are the UN (United Nations) and the US model conventions. (9)

4. The Mechanics of Double Tax Avoidance: Residence vs. Source

Double taxation results from an overlap of jurisdiction to tax between a residence state, where the recipient of income lives, and a source state, where the income was generated. If both exert their power to tax to the full extent, the total burden on transborder economic activities is prohibitively high. In order to obtain the benefits of liberalization, governments have a common interest in avoiding such double taxation. In principle, there would be two solutions to this problem. Countries could delegate the power to tax international income to an international authority (conjoint taxation) or they could agree on some rule to share the jurisdiction to tax between them. Leaving aside the European Union, the first option has never seriously been contemplated and is generally believed to be utopian. (5)

According to tax treaty rules, the residence country is obliged to provide relief from double taxation in cases of full or limited source taxation. This can either be done by allowing a credit for the tax paid at source on the tax due in the home country or by exempting the income taxed at source from home tax altogether (Article 23 of the OECD MC). Importantly, however, basically all countries already provide for relief of double taxation unilaterally. Their national tax codes contain provisions for either exempting foreign income from taxation, or granting a credit for taxes paid on such income in the source country. In those cases, double taxation is already effectively prevented. In a few cases, the national rules only foresee partial tax relief. (7)

5. Conclusion

In summary, international double tax avoidance takes place on three interrelated levels: the unilateral, bilateral and multilateral levels. For one, all countries relieve double taxation in their national tax laws, that is, on the unilateral level. In effect, they give up entirely or partially their right to tax foreign source income, in order to avoid interfering with other tax systems. Second, in bilateral negotiations, countries conclude double tax treaties which mainly deal with the cooperative avoidance of double taxation and the division of taxing rights. Third, international tax policy takes place on the multilateral level. Technical experts, national tax administrators, and scientific advisors cooperate in international organizations to develop model conventions, disseminate information on treaty practices, standardize the bilateral treaties, and monitor the treaty network. The resultant MCs are legally non-binding, but are quite influential in practice. Basically all existent double tax treaties are based on the MC.

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