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Double Taxation Treaties and Transnational Investment: A Comparative Study

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On the national and international levels, fiscal policy plays a crucial role in the mobilizing and channeling resources for economic development. In the domestic sphere, fiscal policy may be the most important among the various means available to a government to mobilize resources and promote economic and social development. Taxation and budgetary allocation serve as the two major tools of fiscal policy.

While a good budgetary system encourages channeling of resources into areas of high development priorities, an appropriately designed tax system can discourage the use of scarce resources in activities of low development priorities. Moreover, taxation can be exploited to encourage a more effective use of more or less idle resources through

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the use, for example, of tax incentives to encourage more labor-intensive method of production, thereby decreasing unemployment and underemployment. Similarly, foreign exchange, often one of the scarcest resources in developing countries, can be increased and directed to priority areas by means of tax policies which favor export transactions.

In the international sphere, the role of taxation receives similar recognition. Economic relations between nations continue to be viewed in terms of economic interdependence, in which the international movement of goods and services and the international movement of factors of production are fundamental.[1] Transnational actors, however, are more concerned with the international movement of factors such as capital and know-how, and the international tax factors which affect transnational corporations (TNCs).

International tax problems have grown in magnitude as transnational corporations continue to expand their activities in the absence of generally accepted principles and adequate intergovernmental institutions dealing with tax matters. There is a widespread feeling, at least in the developing countries, that TNCs are able to obtain unfair tax advantages over other forms of enterprises, to the detriment of most states.[2] Policy makers in these states are, therefore, disturbed by the possible negative economic impact of tax arrangements with TNCs; for example, the unfairness of the distribution of gains as between a TNC and a host state, and the impact on capital accumulation in the host state.

In the taxation of TNCs, there are three main areas of conflict. These are: (1) the allocation of profits between associated enterprises, leading to the classic case of double taxation; (2) trade between associated enterprises (exchange of goods, services, patents and other know-how property, loans, etc.), raising problems associated with tax evasion and avoidance; and (3) the determination of a permanent establishment of TNCs, as a way of avoiding the misuse of tax havens. The types of income or expenditure which pose particular problems in this respect include business profits, interest on loans,

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1. J.D.R. ADAMS & J. WHALLEY, THE INTERNATIONAL TAXATION OF MULTINATIONAL ENTERPRISES IN DEVELOPED COUNTRIES 1 (1977); FOLSOM, GORDON, SPANOGLE, INTERNATIONAL BUSINESS TRANSACTION 2-8 (1986); JACKSON AND DAVEY, INTERNATIONAL ECONOMIC RELATIONS 2-4, 8-10 (1986); CHARLES P. KINDLEBERGER, INTERNATIONAL ECONOMICS (5th ed. 1973); F. ROOT, INTERNATIONAL TRADE AND INVESTMENT (5th ed. 1984).

2. For references to such concerns, *see* ADAMS & WHALLEY, *supra* note 1, at 4; MILLER, *Third World Views of the End and Means of United States Tax Policy*, UNITED STATES TAXATION AND DEVELOPING COUNTRIES (R. Hellawell ed. 1980).

administrative expenses, management fees, royalties and other know-how payments.

This paper examines the legal framework of a number of bilateral double taxation treaties drawn from various regions of the world and from different economic systems in order to see how these fundamental issues are generally treated, and to provide insight into the general nature of these instruments. As a backdrop to our more detailed comparative discussion of the role of double taxation treaties in minimizing these conflicts, this article raises in a general manner the issues of double taxation; tax evasion and avoidance, in particular the problem of transfer pricing and tax havens; and finally, the problem of tax holidays and exemptions. The conclusion summarizes the treatment of the problems of transnational taxation in the agreements discussed.

I. *General Considerations*

A. *Double Taxation*

International double taxation becomes an issue when profit is subject to more than one charge to tax because it is presumptively within the tax jurisdiction of two or more countries.[3] Put simply, international double taxation arises whenever the same profit is liable to tax in two or more countries at the same time.[4] The root of the problem of double taxation is found in the fact that laws designed to serve domestic needs differ significantly among countries regarding the principles of allocating and taxing income and determining permanent establishment. In other words, the territorial scope of tax jurisdiction impacts upon business entities operating in more than one country. National tax systems are based, in varying degrees, on either the source of income, residence or nationality of the corporations concerned, or some combination of these variables.

Apart from the basic jurisdictional problem introduced by the differing principles, the application of the principles themselves fur-

3. ADAMS & WHALLEY, *supra* note 1, at 41. This introductory discussion draws heavily on: ADAMS & WHALLEY, *supra* note 1; J.F. CHOWN, TAXATION AND MULTINATIONAL ENTERPRISE (1974); A.R. PREST, PUBLIC FINANCE (5th ed. 1975).

4. This form of double taxation should be distinguished from "economic double taxation," which is used to describe the phenomenon of the same income flow being subjected to tax in the hands of different taxpayers during the same period under the same domestic tax system. *See* ADAMS & WHALLEY, *supra* note 1, at 41; CHOWN, *supra* note 3, at 54-56.

ther affects the distribution of revenues among capital exporting and importing countries. Under the *source* principle of taxation, a country taxes all income earned from sources within its territorial jurisdiction and generally exempts from taxation income accruing from foreign sources.[5] Under the *residence* principle, a country taxes the worldwide income of persons legally resident within its territorial jurisdiction.[6] For example, if the resident invests in a foreign country and earns profits there, the home country subjects those profits to its income tax. According to the *nationality* principle, taxation is based on the world-wide income of the nationals or citizens of the country concerned, wherever they are resident.[7] This latter principle, however, is applied by only a handful of countries. The more common clash of principles is between taxation at the source of income and taxation on the basis of residence.[8] The United States uses all three principles—source, citizenship, and residence—as a basis for income taxation.

In addition to the differing approaches to territorial jurisdiction, national tax systems also differ in the three basic ways they seek to integrate corporation tax and personal income tax in the form of corporate dividends. Under the *classical* system of corporation tax, profits accruing to a corporation are first subject to corporation tax.[9] In addition, dividend distributions are subject to personal income tax in the hands of the recipients. These distributions are not deductible from the profits of the company for corporation tax purposes. Thus, distributed profits are subject both to corporation tax and personal income tax, whereas undistributed profits are subject only to corporation tax. Under the *imputation* system, on the other hand, profits are subject to tax when they are distributed by way of dividends, as in the classical system. Part of that corporation tax paid by the shareholder, however, is treated as a credit against his liability to personal income tax on the distribution.[10] Under the third system, the *two-rate* system, one rate of corporation tax applies to undistributed profits, and a lower rate applies to distributed profits.[11] Distributed profits are taxed at a lower rate to take account of the

5. ADAMS & WHALLEY, *supra* note 1, at 10-11, 42-43. *See also* TILLINGHAST, TAX ASPECTS OF INTERNATIONAL TRANSACTIONS at 1-7 (2d ed. 1984).
6. *Id.*
7. *Id.*
8. *Id.*
9. ADAMS & WHALLEY, *supra* note 1, at 11, 12, 14, 24-25; MILLER, *supra* note 2, at 234.
10. ADAMS & WHALLEY, *supra* note 1, at 14.
11. *Id.* at 15.

fact that they would also be subjected to personal income tax in the hands of the shareholder.[12]

A further source of differences in national tax practices stems from the fact that countries have different concepts of what constitutes profit for tax purposes. Even when two different countries have the same basic rules for tax computation, they may differ in their interpretation of the facts of particular cases. The upshot of all these differences in national tax systems and practices is that international income flows would normally be subject to double taxation in various respects in the absence of relief arrangements.

In the case of a corporation trading abroad through a subsidiary, the following would be the situation when the tax codes of both states are based on the source principle, each state has a classical system of corporation tax, and there are no double taxation relief arrangements between the states concerned. The subsidiary would be liable for corporation tax on trading profits in the host state because both the source of income and the residence are in the same state. When it pays a dividend to the parent corporation, that dividend would be liable for tax in the host state on the ground that the source, namely shareholding in the subsidiary, is located in the host state. The parent corporation also would be liable to corporation tax in the home state on the dividend received from the subsidiary because it is part of the income of the parent. Additionally, the dividend paid by the parent out of its income would be subject to the personal income tax of the home state in the hands of the recipient shareholders because the latter reside in the home state. Thus, the total tax burden in this case would be two charges to corporation tax and two charges in respect of dividends. In the case of a corporation doing business in an investee state through a branch rather than a subsidiary, its profits also would be liable to taxation in both states.[13] Normally, however, no corporate dividends would be involved in any

12. *Id.*

13. *Id.* at 43. Some countries, however, treat payments from branches to parents as dividends for the purpose of determining withholding tax liability; and a TNC may suffer a withholding tax on branch profits in the host state. But this treatment is the exception rather than the rule. There are additional differences in the tax treatment between branches and subsidiary corporations which tend to make TNCs favor the latter rather than branches. For example, some countries have higher corporate rates on branch profits accruing to a foreign based corporation than on profits of domestic or subsidiary corporations. Branch operations may also render both the parent and the branch liable to tax in each country on the worldwide profits of the entire company. *Id.* at 50-51.

remittances, and withholding taxes on them would not arise.[14]

The nature of the problem posed for international income flows by double taxation seems clear from the foregoing. It has become a general practice for many states to provide some form of relief from this particular consequence of differing tax principles and practices. Double taxation relief may take the form of exemption, credit, or deduction. Under the *exemption* system, the profits of a corporation liable to tax in two or more states are taxed in only one of the states concerned and exempted from tax in the others.[15] The profits may be exempt from tax in the state of source (exemption on a host country basis) or exempt from tax in the state where the recipient resides (exemption on a home basis). Typically, the exemption system exempts income which has already been taxed in a host country from further tax in the home country.

Under the *credit* system, the tax is paid in one state and is then allowed as a credit against tax liability in the other state.[16] This system gives relief from liability in the home country for taxes actually paid in the host country with a direct crediting of taxes paid in one locality against taxes to be paid elsewhere. The tax paid in the home state is the home state tax normally payable minus the foreign tax paid in the host state.[17] The calculation of the tax credit can get very complicated: the credit may take the form of a direct credit for the overseas branch operation or an indirect credit for the foreign sub-

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14. In addition, there may be withholding taxes on payments of interest from the subsidiary to the parent corporation; and, in some cases, withholding taxes on royalties.

15. ADAMS & WHALLEY, *supra* note 1, at 44-45; CHOWN, *supra* note 3, at 17-44, *especially* at 42; TILLINGHAST, *supra* note 5, at 7-8, 45.

16. *See generally*, ADAMS & WHALLEY, *supra* note 1.

17. The following example of the U.S. tax credit system is taken from HELLAWELL, *The Home-Country Tax Credit* 3.22 in 1 NEGOTIATING FOREIGN INVESTMENTS: A MANUAL FOR THE THIRD WORLD (Hellawell & Wallace ed. 1982), [hereinafter HELLAWELL & WALLACE].

> Suppose Acme Shoes, a Delaware corporation which typically earns $10,000,000 a year in the United States, established a branch operation (not a subsidiary) in Taiwan. In 1978 the Taiwan branch earned $1,000,000 and was subjected to a 40% Taiwanese income tax, or $400,000. Acme is of course taxable in the United States on its worldwide income. Assuming for simplicity a 50% U.S. tax rate, Acme's U.S. tax bill before credit would be $5,500,000 ([$10,000,000 U.S. income + $1,000,000 Taiwan income] X 50%). However, Acme would be allowed a credit for Taiwan income tax of $400,000, which would reduce the U.S. tax to $5,100,000. Notice that, in effect, Acme has paid $500,000 on its Taiwan income ($400,000 to Taiwan and $100,000 to the United States). This total rate, 50%, matches exactly the higher rate of the two countries. This is the way the credit should work: it should eliminate double taxation but should not lower the overall rate below that of either one of the countries involved.

In general, the tax credit applies only to foreign income or income-like taxes. It does not apply to such taxes as export taxes, sales taxes, excise taxes, franchise taxes, etc. *Id.* at 3.2B.3.

sidiary.[18] An adverse feature of the credit principle is that the taxpayer ends up paying whichever is the higher of the rates in the states concerned.

With the *deduction* system, the foreign tax levied on the profits is allowed as a deduction from the profit liable to tax in the state concerned.[19] The critical distinction between this system and the credit system is that under the deduction system the foreign tax is deducted from the tax base (i.e., treated as a deductible item from income as computed under the tax system of the taxing state).[20] Under the

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18. The following example is from HELLAWELL & WALLACE, *supra* note 17, at 3.2B.5-3.2B.6:

> Simplex, a Delaware corporation, has a wholly-owned subsidiary organized under the laws of Xanda (X-Sub). In its first year of operation X-Sub earns $100,000 in Xanda, pays 30% Xanda income tax of $30,000 and pays a dividend to Simplex of $70,000.
>
> *Step 1.* Determine the amount of foreign taxes deemed paid by Simplex. This is the portion of the foreign taxes paid to X-Sub which 'the amount of such dividends . . . bears to the amount of such accumulated profits after foreign tax.
>
> $$\frac{\text{Dividend}}{\text{X-Sub Earnings After Taxes}} \times \text{Xanda Tax} = \text{Taxes Deemed Paid}$$
>
> $$\frac{\$\ 70{,}000}{\$\ 70{,}000} \times \$\ 30{,}000 = \$\ 30{,}000$$
>
> *Step 2.* Gross up the amount of the dividend by adding to it an amount equal to the taxes deemed paid under step 1.
>
> Dividend + Taxes Deemed Paid = Amount on which U.S. Tax (before credit) will be computed
> (Step 1)
> $ 70,000 + $ 30,000 = $ 100,000
>
> *Step 3.* Compute U.S. tax on the grossed up amount before credit.
> $100,000 x 50% (U.S. tax on dividend before credit).
>
> *Step 4.* Credit the 'taxes deemed paid' amount against the U.S. tax on the grossed up amount. The result is the net U.S. tax payable by Simplex.
>
> | U.S. Tax on Grossed Up Amount | — | Taxes Deemed Paid | = | U.S. Taxable Amount |
> |---|---|---|---|---|
> | $50,000 | — | $30,000 | = | $20,000 |
>
> Notice that this comes out 'right.' The total bill on the $100,000 of Xanda earnings is $50,000: $30,000 to Xanda and $20,000 to the United States. Thus the total rate is 50%, the same as the U.S. rate.
>
> The process is just the same if the dividend recipient is less than a 100 percent shareholder or if less than all of the earnings after tax are paid out.

19. ADAMS & WHALLEY, *supra* note 1, at 46.

20. Here is a simple example of the deduction system, utilizing a branch operation of Corp X resident in U.S.:

credit system the foreign tax, as assessed by the foreign authority, is accepted as a credit against tax liability in the taxing state. The deduction system would thus give less relief than both the exemption and the credit systems, but it does at least prevent the total tax burden of taxes imposed by the states concerned exceeding 100 percent. The most common solution, and the one used by the United States, is the tax credit system.

B. *Tax Evasion and Avoidance*

The effective tax rate a TNC bears on its global operations may very well differ from the legal tax rate that it should ordinarily account for. Mechanisms which TNCs often use to cause divergence between legal and effective tax rates may be conveniently grouped under tax evasion and tax avoidance. Tax evasion describes the deliberate and illegal non-payment of taxes which are properly due (e.g., by the submission of incorrect business returns or of no returns at all). The important point about tax evasion is that noncompliance with the tax laws is the result of wilful and conscious failure. Tax avoidance, on the other hand, occurs where the taxpayer takes advantage of loopholes in the tax laws or, where doubts exist as to the interpretation of the laws, the taxpayer takes the benefit of the doubt in its favor, provided all this is done within the ambit of the appropriate tax legislation. Tax evasion is considered illegal, while tax avoidance does not technically infringe the law, even though it may be equally damaging to the host state and can be morally reprehensible.

1. *Transfer Pricing*

One of the methods frequently used to avoid or evade taxation is transfer pricing, which is normally facilitated by the misuse of tax havens. Transfer pricing simply refers to the prices used as the

Host State	Home State (U.S.)	
Branch Income $1,000 40% Business Profits tax: $400	Corp X Income from overseas:	$1,000
	Deduction of foreign tax:	$ 400
	Taxable Income:	$ 600
	50% Corporate tax:	$ 300

Total Tax Payable on $1,000 earned overseas:
$400 (host state tax) + $300 (U.S.) = $700

accounting basis for recording intra-corporate transactions (i.e., those between TNC parents and their subsidiaries or branches, or between such subsidiaries).[21] The subject of these transactions covers such things as components manufactured in one country (e.g., by the parent) and transferred or sold to an affiliate (e.g., a subsidiary) for use in a higher stage of production in another country; as well as intangible items such as royalties, know-how, research and development, and the interest rates paid on loans between a parent and subsidiaries. The underlying practice of transfer pricing is to trade intracorporate goods and services at prices that do not correspond to international or competitive prices. The object is to facilitate the functioning of the global system of the corporation at minimum cost to itself through the avoidance or evasion of relatively high rates of taxation, exchange controls, regulations on profit repatriation, or expected losses from impending changes in exchange rates in particular locations of operation.[22]

The basic financial structure of the relationship between subsidiary and parent lends itself to similar manipulation. A TNC may, for example, attempt to withdraw most of the profits accruing to a subsidiary by setting it up with a heavily financed loan from the parent. In this case, the profits are transferred in the form of repayment of loans and interest. Alternatively, the parent may borrow from the subsidiary as a way of moving profits to a low tax host state. Intracorporate dividends also may be converted into capital gains as a way of remitting profits with tax savings. In this case, retention of profits by the subsidiary (if located in a low tax area), followed by liquidation of the subsidiary, may give the parent considerable tax savings owing to the taxation of the capital gains on a

21. ADAMS & WHALLEY, *supra* note 1, at 161; S.H. ROBOCK & K. SIMMONDS, INTERNATIONAL BUSINESS AND MULTINATIONAL ENTERPRISE 509-510 (3rd ed. 1983); U.N.C.T.C., Intrafirm Trade, *Transnational Corporations in World Development* (1983 ST/CTC/46) at 160-62.

22. Two examples of transfer pricing would suffice. Corporation A is located in an African state where it produces a given product. The Corporation could sell this product directly in London for £ 100 and increase its total sales figure attributable to the business in the African state and hence increase its tax liability in that state. Instead, it forms a subsidiary corporation in a tax haven in the Mediterranean and sells the product to the latter for £ 90. The interposed corporation then resells the product in London for £ 100, thus making a tax-free profit of £ 10 and depriving the entity in the African State, corporation A, of that extra amount.

In another example, let us think of a Corporation B, which is a parent located in the U.S. It could sell directly to its subsidiary Y located in an African State, its product at $100 and make a reasonable profit. However, B forms another subsidiary (Z) in a tax haven in Central America and sells the product to it for $90. Z then resells the product to Y for $110, at a much higher profit than B would have realized if it had dealt directly with Y.

realization basis, and the avoidance of dividend withholding taxes. In some countries, however, capital gains in the hands of a corporation are taxed as ordinary profits.

The consequences of transfer pricing for the host or investee state are manifold. One consequence is the reduction of exports through the overpricing of company goods, with a consequent unfavorable impact on the balance-of-payments of the host state. Imported inputs, which are overpriced with a view to reducing profits from operations in that state and moving them to more favorable tax jurisdictions, affect the balance-of-payments as well. Underpriced affiliate imports (under invoicing) affect the volume of import duties and undermine domestic capital formation through price undercutting. Furthermore, overpriced affiliate imports (overinvoicing) facilitate otherwise unauthorized repatriation of funds. In sum, this results in increased outflow of funds from the country in which the affiliate operates, thereby affecting the balance-of-payments situation in many respects.

C. *Tax Holidays and Tax Remission*

From the standpoint of host states, there are two basic aspects to the subject of taxation of TNCs. The first aspect lies in the consideration of ways to frustrate the attempts of TNCs to minimize their tax liability in the host state. This falls within the area of tax evasion and tax avoidance discussed above. The second aspect, however, involves various policies to encourage TNCs to invest in or carry on their projects. The issues of relief from double taxation and direct tax incentives addresses this latter aspect.

There are several forms of tax incentives, of which the following are perhaps the more prevalent: (1) corporate income tax holiday, be it partial or total; (2) capital allowances (e.g., accelerated depreciation); (3) carrying forward of losses for tax deductions; (4) tax-free dividends to shareholders; (5) tax deduction for research and development expenditure; (6) employment tax credit; (7) exemption from property tax (land, mining, and forest dues, etc.); (8) exemption from indirect taxes such as turnover tax, capital gains tax, patents tax, sales tax, excise duty, and purchase tax; (9) waiver or deduction of import duties on equipment, spare parts, and raw materials; (10) export incentives (such as waiver of export tariff, elimination of import duties on intermediate goods for the manufacture of export products, export subsidies, and tariff protection); (11) deferment of corporate registration fees and stamp duties; and (12) tax-free status for salaries of expatriate employees and tax-free interest on loans.[23]

The general rationale for these and other tax incentives is to assist an industry during the initial years of its operation, when there are recognized hardships, including unfair competition from older enterprises. While many recognize and appreciate this purpose, it is disturbing to note that many host states are too willing to grant tax incentives which, at least in the short-term, can have adverse effects on their revenues and balance-of-payments position. In their haste to grant incentives, host states become entangled in a self-defeating competition which enable TNCs to play off one country against another in the siting of projects. In some cases, a tax holiday may not even benefit the subsidiary in the investee state, but merely may swell its tax liability in, and hence increase the tax revenue of, the home state. This would indeed be the case with the United States as a home state, since it does not accept the practice of "tax sparing."[24]

The problems posed by double taxation, tax evasion and avoidance, and tax incentives, can be dealt with unilaterally (i.e., exclusively by one state under its sovereign powers), or under reciprocal treaty obligations, which could take the form of bilateral or multilateral agreements. There is some debate as to the true value of these

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23. OCRAN, *The Legal Framework of Foreign Investments in Africa*, 12 ZAMBIA L.J. 1, 4-6 (1980). *See also* United Nations, *Tax Incentives for Reinvestment*, TAX TREATIES BETWEEN DEVELOPED AND DEVELOPING COUNTRIES, THIRD REPORT, at 92-104 (U.N. Sales No. E.72 XVI.4 1972).

24. Tax sparing becomes relevant where the host state provides some sort of tax holiday or tax reduction as an incentive to a foreign investor. In that case, the home state would grant credit for the full amount of foreign tax which would have been charged on the foreign source income if there had been no tax incentive program. Without complementary tax sparing provisions in the income tax system of the home state, the entire objective is defeated. "In effect, the U.S. investor loses the tax benefit of the incentive and, instead, the U.S. Treasury gets a tax windfall." HELLAWELL, *supra* note 2, at 98.

The following is an example from HELLAWELL & WALLACE, *supra* note 17, at 3.2C3, 3.2C4:

> Suppose a United Kingdom company (UKCO) is operating a branch in a developing country (LDC) which has granted it a five year tax holiday on all income and withholding taxes. And suppose a comprehensive tax sparing provision is in the tax treaty between the two countries. In year three of the holiday UKCO earns £ 1,000,000 in LDC. It pays no LDC tax because of the tax holiday. U.K. tax law is like the United States tax law in that U.K. resident companies (we assume UKCO is such) are taxable on foreign earnings, subject to a tax credit much like that of the United States. Thus, UKCO would normally be subject to full U.K. tax on the £ 1,000,000 earnings. Moreover, it would normally not be able to credit any foreign tax because it paid none. The tax sparing article provides that UKCO may take a tax credit against U.K. taxes (subject to normal limitations *et al.*) in the amount of taxes it would have paid to LDC if there had been no tax holiday.

As Anthoine notes, tax sparing is widely accepted by Britain in its taxation treaties with developing countries, but is rejected by the United States. *See* Anthoine, *Provisions in Tax Laws of Developed Countries* (1982); HELLAWALL & WALLACE, *supra* note 17, at 3.2D16, 3.2D17.

treaties, since national legislation may actually provide a solution to double taxation. Indeed, it has been suggested that tax treaties play only a marginal role in relieving double taxation, and that the major thrust of tax treaties is to limit taxation by the source country through the concept of permanent establishment. Hellawell notes that if there is no "permanent establishment, then only the country of taxpayer's residence may tax the income; the other state may not tax even though the income plainly has its source in that state."[25] It should be remembered, however, that the problems go beyond the relief of double taxation, and involve matters which can be dealt with more effectively through international cooperation.[26] Most authorities regard unilateral measures for eliminating excessive tax burdens and harmonizing taxable income as insufficient, and hold that the satisfactory reconciliation of the conflicting tax claims is more probable through treaty arrangements.[27]

Based on this premise, the United Nations has been promoting the conclusion of tax treaties since 1967. An Ad Hoc Group of Experts on Tax Treaties Between Developed and Developing Countries was set up in 1968 composed of tax officials and independent experts. This Group was given the mandate to explore ways and means of facilitating the conclusion of these treaties either bilaterally or multilaterally and to formulate possible guidelines for use of the treaties.[28] In 1974, the Group of Eminent Persons set up by the United Nations Secretary-General to study the impact of TNCs on world development and international relations also took up the theme of tax treaties and

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25. Hellawell, *Tax Treaties*, in HELLAWELL & WALLACE, *supra* note 17, at 3.2C1; Owens, *United States Income Tax Treaties: Their Role in Relieving Double Taxation*, 17 Rutgers L. Rev. 428 (1963).

26. OWENS, *supra* note 25, at 430.

27. For an account of the development of tax treaties as an answer to the deficiencies of unilateralism, *see* VOGEL, *Double Tax Treaties and Their Interpretation*, 4 INT'L. TAX & BUS. LAW., 10-13 (1986). *See also*, ADAMS & WHALLEY, *supra* note 1, at 44-45, 71.

28. The Group of Experts was established under ECOSOC Resolution 1273, 1967. The Group doubted whether the time was ripe for a multilateral tax agreement, either in an all-embracing form or on specific tax issues. The mandate of the Group was subsequently broadened by ECOSOC Resolution 1765 of 18 May 1973.

There are, however, examples of multilateral tax agreements which have been successfully negotiated. For example, the OECD Model Convention, the Double Taxation Agreement concluded in 1966 by the Member States of the African and Malagasy Common Organization, the Convention for the Avoidance of Double Taxation within the Andean Group adopted in 1966 by the Commission of the Cartagena Agreement. For other models of such agreements, *see* The Draft Multilateral Agreement prepared by the Nordic Group and the European Free Trade Association, *and* the Guidelines Formulated by the UN Group of Experts, *reprinted in* ADAMS & WHALLEY, *supra* note 1, at 79-111; VOGEL, *supra* note 27, at 11-13.

There may be areas of multilateral co-operation which do not require formal multilateral agreements, *e.g.*, a forum for sharing technical experience in the field of tax administration.

concluded that if the provisions of bilateral treaties were standardized with only a small number of clauses to be negotiated in particular cases, they would in fact amount to an international agreement on taxation.[29] As it turned out, double taxation treaties stopped at the bilateral or regional levels; no global multilateral double taxation treaty has ever been concluded. The United Nations effort has been limited to the development of a model for use in treaty negotiations between developed and developing countries.[30]

A number of fundamental issues must be addressed in a double taxation treaty, regardless of whether the treaty is bilateral or multilateral. One of these relates to the bases for the assumption of tax liability of transnational investors. As explained earlier, tax liability may be founded either upon the source of income, residence, or nationality, or some combination of these. Lack of agreement on the appropriate basis could become a source of confusion and unfairness for the investor, the home state, or the host state. Other fundamental issues involve the category of persons and taxes covered by the agreement, the specific arrangement or scheme for the elimination of double taxation among the contracting parties, provisions against tax avoidance and evasion, non-discrimination as to the treatment of nationals of contracting states, and procedures for handling tax complaints from taxpayers.

II. Transnational Taxation Issues in Double Taxation Treaties

Analytically, perhaps the easiest way to present and explain the framework of bilateral double taxation treaties is to group them into models by a process of comparison, and by a further comparison of the models *inter se*, much in the same way as comparisons have been made between the OECD Model Double Taxation Convention on Income and Capital (1977), the United Nations' Model Double Taxation Convention Between Developed and Developing Countries (1980), and the U.S. Department of Treasury Model Income Tax Treaty (1981). The main tendencies in the practices of the home states of

29. *The Impact of Multinational Corporations on Development and on International Relations*, (UN Doc. No. E/5500/Rev.1) (1974).

30. UN Model Double Taxation Convention Between Developed and Developing Countries (1980) (ST/ESA/102). *See also Guidelines for Tax Treaties Between Developed and Developing Countries*, (UN Doc. No. ST/ESA/14) (1974). The UN has published subsequent reports on the subject.

the major TNCs emerge from the following discussion.[31]

Among the elements found in double taxation treaties are provisions on the types of persons and taxes covered. A perusal of any of these treaties makes clear that they cover persons other than transnational corporations as well as incomes other than those of TNCs. Since this article focuses on corporations in general and TNCs in particular, issues will be analyzed essentially in reference to them, without implying that they are the only persons so covered.

A. *Agreed Basis for Taxation*

Tax treaties cover different bases for taxation, such as residence and permanent establishment. Key phrases, used as terms of art, are common in this area (including such concepts as center of vital interest, permanent home, habitual abode, and place of effective management).

The relevant provisions of the United Kingdom-United States Convention[32] serve to illustrate most of the pertinent concerns applicable to other treaties. First, the agreement defines residency for a corporation: a corporation is resident in the United Kingdom if its business is managed and controlled there, while a corporation is resident in the United States if it is determined to be a United States corporation under United States domestic law.[33] In general terms, the phrase "permanent establishment" might seem self-explanatory. The treaties, however, go to some length to minimize any ambiguity because of the importance of the concept in the area of double taxation. In the United Kingdom-United States Convention, the term refers to a fixed place of business through which the business of an enterprise is wholly or partly conducted.[34] It includes, but is not limited to: (1) a branch, office, factory, workshop; (2) a mine, oil or gas well, a quarry, or other place of extraction of natural resources; and (3) a building construction or installation project which exists for more than twelve months.

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31. For an article by article comparison of the texts of the OECD Model treaties (1963 and 1977), the U.N. Model Treaty (1980) and the U.S. Model Treaty (1981), see K. Van Raad, *Model Income Tax Treaties* (1983).

32. Tax Convention with the United Kingdom of Great Britain and Northern Ireland, Dec. 31, 1975, Great Britain-United States, 17 I.L.M. 836. [hereinafter United Kingdom-United States Convention].

33. *Id.* art. 4. Such domestic criteria are considerably broader using such factors as place of incorporation and management.

34. *Id.* art. 5.

On the other hand, a fixed place of business used solely for one of the following purposes is not a permanent establishment: (1) the storage; display, or delivery of goods belonging to the enterprise; (2) maintenance of a stock of goods belonging to the enterprise for the purpose of storage, display, or delivery; (3) the maintenance of goods belonging to the enterprise for the purpose of processing by another person; (4) maintenance for the purpose of purchasing goods or collecting information for the enterprise; (5) maintenance for the purpose of advertising, supply of information, for scientific research, or for similar activities which have a preparatory or auxiliary character, for the enterprise; or (6) a building or other installation which does not exist for more than twelve months. The agreement also provides that the carrying on of business in another state through a broker, general commission agent, or any other agent of independent status, where such persons are acting in the ordinary course of business, is not considered as having a permanent establishment in that state.[35]

A corporation may be resident in one place and yet be considered as not having a permanent establishment in the place of residence (e.g., a U.S. corporation which is resident by virtue of the residence definition in the Convention, but has no permanent establishment in the United States). The basic principle of residency in the United Kingdom-United States Convention is found in Article 7. Business profits of an enterprise are to be taxed only in the state in which it is resident. Where the enterprise concerned carries on business in the other contracting state through a permanent establishment situated there, however, the profits may be taxed in that other state to the extent of the proportion of profits attributable to that permanent establishment.

The treaty also deals with the basis for taxation of dividends. Dividends from a corporation resident in one state derived by a resident of another state is taxable in the second state (i.e., the state of residence of the income-receiver).[36] On some occasions, the country of source also may tax the dividends, but this is exceptional.

In the original United Kingdom-United States Convention provision, dividends from a corporation resident in one state derived by a resident of another state were to be taxed in the second state (the

35. *Id.* art. 5, para. 5.
36. *Id.* art. 10.

recipient's state of residence).[37] The country of source, however, might also tax the non-resident beneficial owner, except that in that case the tax is limited to a certain percentage of the gross amount of the dividends. Under Article 10(5) as amended, dividends from a corporation resident in one state and paid to a corporation resident in the second state cannot be taxed by the first state, even if the dividends consist wholly or partly of profits or income arising in that state—except insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or fixed base situated in that state.[38] The second state, however, can tax the dividends in the hands of the recipient corporation even if the corporation paying the dividends is a resident of both states. Interest income derived from one state by a resident of the other state is exempt from tax by the first state and taxed by the resident state. Royalties derived from one state by a resident of the other state is also exempt from tax by the first state (the country of source). Hence, they are taxed only by the resident state.[39]

The Netherlands-Singapore Convention[40] is similar to the United Kingdom-United States Convention. Under Article 3(1), a resident is a person (legal or natural) who, under the law of that state, is liable to taxation, whether by reason of domicile, residence, place of management and control, or similar criterion. Thus, it allows for differing ways for determining residence and leaves open the possibility of one being a resident in both states on account of the application of different criteria. Article 3 clarifies the case of a corporation which, according to the definition of resident in the convention,[41] is a resident of both states. It provides that in such a case, the corporation is deemed a resident of the state in which it is managed and controlled. Thus, in comparison with the United Kingdom-United States Convention, this clause treats the issue of residency in a less equivocal manner. In the United Kingdom-United States Convention, the issue of dual residence is left unresolved by saying that the convention does not apply to dual residency in most respects.

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37. United Kingdom-United States Convention, *supra* note 32, art. 10.
38. *Id.*
39. *Id.* art. 11. Note that royalties and interest are characteristically straight-forward cases of tax-exemption or waiver, as distinguished from tax credits. *See id.* art. 12.
40. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Income and on Capital (with protocol), Feb. 19, 1971, Netherlands-Singapore, 801 U.N.T.S. 27, art. 3, para. 1 [hereinafter Netherlands-Singapore Convention].
41. *Id.* art. 3, para. 1.

Article 4 of the Netherlands-Singapore Convention employs a permanent establishment provision identical to the United Kingdom-United States Convention. The same is true for business profits,[42] dividends,[43] and interest.[44] Some differences exist, however, in the case of interest: Where interest is taxed by the first state (the state of source), the tax cannot exceed a given percentage of the amount of the interest. As with the United Kingdom-United States Convention, royalties are payable only in the country of residence of the recipient. This, however does not cover royalties paid for use of copyright of literary or artistic work, including motion picture films and tapes for television or broadcasting.[45]

The Denmark-Trinidad Convention,[46] is similar to the Netherlands-Singapore Convention. The issues of dual residency and permanent establishments are dealt with in the same manner as the Netherlands-Singapore Convention.[47] This is also true for the basis for taxation of business profits, dividends, and interest income.[48] Royalties are normally taxable in the country of residence of the recipient. However, where the country of source taxes these items, the amount cannot exceed a certain percentage of the gross amount of the royalties.[49]

The France-Morocco Agreement[50] deals with the issue of the basis for taxation.[51] Income from industrial, mining, commercial, or financial enterprises are taxable only in the state in which a permanent establishment is situated. Where an enterprise is permanently established in both contracting states, each state may tax only the income from operations of the permanent establishments situated in its territory.[52] Limitations on such taxable income, however, do exist. "The taxable income may not exceed the amount of the industrial,

42. *Id.* art. 7.
43. *Id.* art. 10.
44. *Id.* art. 11.
45. United Kingdom-United States Convention, art. 12, para. 6.
46. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and the Encouragement of International Trade and Investment, June 20, 1969, Denmark-Trinidad & Tobago, 801 U.N.T.S. 257 [hereinafter Denmark-Trinidad & Tobago Convention].
47. *Id.* art. 4, para. 3; art. 5.
48. *Id.* arts. 7, 10, 11 respectively.
49. *Id.* art. 10, para. 4.
50. Agreement for the Elimination of Double Taxation and the Establishment of Mutual Administrative Assistance with Respect to Taxes (with protocol and exchange of letters), May 29, 1970, France-Morocco, U.N.T.S. 329 [hereinafter France-Morocco Convention].
51. France-Morocco Convention, *supra* note 50, art. 10.
52. *Id.* art. 10, para. 2.

mining, commercial or financial profits realized by the permanent establishments, including profits or advantages derived indirectly from that establishment or allotted to third parties either by increasing or decreasing purchase or selling prices or by any other means. Part of the overhead expenses of the head office is charged against the earnings of the various permanent establishments in proportion to their turnover.[53] Where this method of apportioning profits is not feasible, "the amount of profits taxable by each state is calculated by apportioning the total earnings between the two states in proportion to their turnover realized in their respective territories.[54] If a permanent establishment in one state realized "no turnover, or if the business carried on is not comparable to that in the other state, the competent authorities of the two states shall consult to resolve the situation.[55]

In the United States-USSR Convention,[56] Article 2 provides that residency is determined according to each country's laws. Article 3 provides that income derived from the following sources within one Contracting State by a resident of the other Contracting State are subject to tax only in the other contracting state: (a) rentals, royalties,[57] or payments for equipment, knowledge, experience, or skill; (b) gains from the sale or exchange of any such rights or property; (c) gains from the disposition of property received by inheritance or gift; (d) income from engineering, architectural, designing, and other technical services furnished at one location in connection with an installation contract with a resident of the first contracting state and less than 36 months in duration;[58] (e) income from the sale of goods or services through a broker, or agent acting in the ordinary course of business; (f) reinsurance premiums; and (g) interest on indebtedness connected with the financing of trade between the United States and the USSR except where received by a resident of the other contracting state from a general banking business in the first contracting state.[59]

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53. *Id.* art. 10, para. 3.
54. *Id.* art. 10, para. 4.
55. France-Morocco Convention, *supra* note 50, art. 10, para. 4.
56. Convention Between the United States of America and the Union of Soviet Socialist Republics on Matters of Taxation, June 20, 1973, United States-U.S.S.R., 12 I.L.M. 899 [hereinafter United States-U.S.S.R. Convention].
57. United States-U.S.S.R. Convention, *supra* note 56, art. III, para. 1, at 900.
58. *Id.* art. III, para. 1, subd. d, at 900.
59. *Id.* art. III, para. 1, subd. g, at 900. Income arising in connection with certain activities is not to be attributed to taxable income (when such activities are conducted within one contracting state by a resident of the other contracting state); the purchase of goods or

Several agreements deal with the issue of residency and resolve the dual residency contingency in a manner unlike the United States-USSR Convention resolution: West Germany-Morocco Convention,[60] Denmark-Sweden Agreement,[61] Belgium-Italy Convention,[62] West Germany-Singapore Agreement,[63] France-Brazil Convention,[64] Brazil-Denmark-Portugal Convention,[65] Denmark-Malaysia Agreement,[66] and Finland-France Convention.[67] These agreements provide, generally, that a resident of a contracting state is a person whose income is liable to taxation in that state by reason of domicile, residence, place of management, or similar criterion.[68] As to the residence of persons other than individuals, these agreements provide that where such persons are residents of both contracting states, they will be considered residents of the state of their place of effective management.[69]

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merchandise; the use of facilities for the purposes of storage or delivery of goods or merchandise belonging to the resident of the other contracting state; the display of goods or merchandise belonging to the resident of the other contracting state, and also the sale of such items on termination of their display; advertising by a resident of the other contracting state, the collection or dissemination of information, or the conducting of scientific research, or similar activities, which have a preparatory or auxiliary character for the resident. *Id.* art. III, para. 2, at 900.

60. Convention for the Avoidance of Double Taxation with respect to Income and Capital (with final protocol and exchange of letters), June 7, 1972, West Germany-Morocco, 966 U.N.T.S. 207, art. 4 [hereinafter West Germany-Morocco Convention].

61. Agreement for the Avoidance of Double Taxation with Respect to Taxes on Income and Fortune, Nov. 16, 1973, Denmark-Sweden, 927 U.N.T.S. 61, art. 4 [hereinafter Denmark-Sweden Convention].

62. Convention for the Avoidance of Double Taxation and the Regulation of Certain other Matters With Respect to Taxes and Income, Oct. 19, 1970, Belgium-Italy, 924 U.N.T.S. 201, art. 4 [hereinafter Belgium-Italy Convention].

63. Agreement for the Avoidance of Double Taxation with Respect to Taxes on Income and Capital (with protocol) Feb. 19, 1972, West Germany-Singapore, 922 U.N.T.S. 213, art. 2 [hereinafter West Germany-Singapore Convention].

64. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes and Income (with protocol), Sept. 10, 1971, France-Brazil, 857 U.N.T.S. 3 [hereinafter France-Brazil Convention].

65. Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, April 22, 1971, Brazil-Portugal, 834 U.N.T.S. 3 [hereinafter Brazil-Portugal Convention].

66. Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (with exchange of notes) Dec. 4, 1970, Denmark-Malaysia, 860 U.N.T.S. 19 [hereinafter Denmark-Malaysia Convention].

67. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Fortune, Sept. 11, 1970, Finland-France, 818 U.N.T.S. 29 [hereinafter Finland-France Convention].

68. West Germany-Morocco Convention, *supra* note 60, at art. 4; Denmark-Sweden Convention, *supra* note 61, at art. 4; Belgium-Italy Convention, *supra* note 62, at art. 4; West Germany-Singapore Convention, *supra* note 63, at art. 2.

69. Where, by virtue of the initial determination of residency, an individual is a resident of both states, these agreements use a five step procedure to resolve the problem of dual residency. First, the individual is deemed a resident of the contracting state in which he has a permanent home available to him. Second, if he has a permanent home available to him in

Numerous other agreements have similar formats. The Japan-Switzerland Convention[70] provides that a resident is any person who, under the laws of that contracting state, is subject to taxation by reason of domicile, residence, place of head or main office, place of management, or any other similar criterion. The term "resident" does not include any person liable for tax in that contracting state solely because it derives income from sources therein. Furthermore, in the case of Switzerland, the term includes partnerships created or organized under Swiss law.[71] Where dual residency arises under the provisions of the treaty, the competent authorities are to determine by mutual agreement the contracting state of which the individual will be a resident for the purposes of the convention. A corporation or other legal person considered a resident of both contracting states by applying the provision above, shall be deemed a resident of the contracting state in which its head or main office is situated.

The Japan-Singapore Convention[72] resolves the dual residency issue by having the competent authorities of the contracting states determine by agreement the residency of a person for the purpose of the convention.[73] This is also the case in the Japan-Korea Convention.[74] For this latter agreement, however, the mutual agreement mechanism is to be used only where an individual is considered a dual resident. The agreement goes into some detail to provide criteria determining the basis of taxation of a permanent establishment.[75] The Netherlands-

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both contracting states, he shall be deemed to be a resident of the contracting state with which his personal and economic relations are closest (center of vital interests). Third, if the contracting state in which he has his center of vital interests cannot be determined, or if he has not a permanent home available to him in either contracting state, he shall be deemed to be a resident of the contracting state in which he has a habitual abode. Fourth, if he has a habitual abode in both contracting states or in neither of them, he shall be deemed to be a resident of the contracting state of which he is a national. Fifth and last, if he is a national of both contracting states or of neither of them, the competent authorities of the contracting states shall settle the question by mutual agreement. *See e.g.*, West Germany-Morocco Convention, *supra* note 60, art. 4.

70. Convention for the Avoidance of Double Taxation with Respect to Taxes on Income (with exchange of notes) Jan. 19, 1971, Japan-Switzerland, 827 U.N.T.S. 111 [hereinafter Japan-Switzerland Convention].

71. *Id.* art. 4.

72. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (with protocol and exchange of notes), Jan. 29, 1971, Japan-Singapore, 827 U.N.T.S. 213 [hereinafter Japan-Singapore Convention].

73. *Id.* art. 4, para. (2).

74. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (with protocol and exchange of notes), Mar. 3, 1970, Japan-Korea, 799 U.N.T.S. 247, art. 3, para. 3 [hereinafter Japan-Korea Convention].

75. *Id.* art. 4.

Indonesia Agreement,[76] the United Kingdom-Barbados Agreement,[77] Denmark-Kenya Convention,[78] Great Britain-Zambia Agreement,[79] and Belgium-United States Convention,[80] in most respects, treat the issue of dual residency in the same manner as the group of agreements above.

Under the China-Japan Convention,[81] a resident of a contracting state means any person who, under the laws of that contracting state, is liable for tax by reason of domicile, residence, place of head or main office, or similar circumstance.[82] Where a person is a dual resident (a resident of both contracting states), then the contracting states will agree upon the residence of that individual. When a person other than an individual is a dual resident, they shall be considered a resident of the contracting state of their head or main office.

Under Article 5 of the China-Japan agreement, a permanent establishment is a fixed place of business through which the business of an enterprise is wholly or partly conducted. The term includes a place of management, a branch, an office, a factory, a workshop, and a mine, an oil or gas well, a quarry or other place of extraction of natural resources. Also, a building site, a construction assembly or installation project, or supervisory activities connected with these activities constitute a permanent establishment if the site, project, or activities continue for more than six months. An enterprise of a contracting state is considered to have a permanent establishment in the other contracting state if it furnishes, outside that contracting state, consultancy services through employees or other personnel,

76. Agreement for the Avoidance of Double Taxation and Fiscal Evasion with Respect to Taxes on Income and on Capital (with protocol), Mar. 5, 1973, Netherlands-Indonesia, 969 U.N.T.S. 375 [hereinafter Netherlands-Indonesia Convention].

77. Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Tax on Income and Capital Gains, Mar. 26, 1970, Great Britain-Northern Ireland-Barbados, 767 U.N.T.S. 61 [hereinafter Great Britain-Barbados Convention].

78. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, Dec. 13, 1972, Denmark-Kenya, 896 U.N.T.S. 245 [hereinafter Denmark-Kenya Convention].

79. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, Mar. 22, 1972, Great Britain-Northern Ireland-Zambia 915 U.N.T.S. 45 [hereinafter Great Britain-Northern Ireland-Zambia Convention].

80. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, July 9, 1970, Belgium-United States, ____U.N.T.S. ____, 23 U.S.T. 2687, T.I.A.S. No. 7463 [hereinafter Belgium-United States Convention].

81. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes and Income, Sept. 6, 1983, Peoples Republic of China-Japan, 23 I.L.M. 120, art. IV [hereinafter China-Japan Convention].

82. *Id.* art. V.

other than an independent agent. Merely carrying on business in the other contracting state through a broker, general commission agent, or any other independent agent does not accord permanent establishment status to an enterprise, provided that the agents are acting in the ordinary course of their business. Unless an enterprise carries on business in the other contracting state through a permanent establishment, profits of an enterprise of a contracting state are taxable only in that contracting state.[83] Profits earned through a permanent establishment in the other contracting state may be taxed in that other contracting state, but only attributable to the permanent establishment.

Dividends paid by a resident corporation of one contracting state to a resident of the other contracting state may be taxed in that other contracting state. The dividends also may be taxed in the contracting state of which the corporation paying the dividends is a resident. If, however, the recipient is the beneficial owner of the dividends, the tax charged must not exceed ten percent of the gross amount of the dividends.[84] Royalties and interest income are treated similarly.[85] The United States-Trinidad & Tobago Convention[86] sets forth as the general rules for taxation that a resident of one of the contracting states is taxable by the other contracting state only on income derived from sources within that other contracting state.[87]

II. Arrangement for Elimination of Double Taxation

Conceptually, arrangements for the elimination of double taxation could provide that certain classes of income are wholly exempt from tax in the source country (so that they can be taxed fully in the country of residence); assessed at reduced rates of tax in the source country (with the consequent differential payable in the country of residence); or taxed fully in the source country (and the amounts involved credited to or deducted from any taxes otherwise payable at the residence).[88]

83. *Id.* art. 7.
84. *Id.* art. 10.
85. *Id.* arts. 11, 12.
86. Convention for the Avoidance of Double Taxation, the Prevention of Fiscal Evasion with Respect to Taxes on Income, and the Encouragement of International Trade and Investment (with proces-verbal exchange of ratifications), Jan. 9, 1970, United States-Trinidad & Tobago, 22 U.S.T. 164, T.I.A.S. No. 7047 [hereinafter United States-Trinidad & Tobago Convention].
87. *Id.* art. 3, para. 1.
88. Adams & Whalley, *supra* note 1, at 41. Compare this with the approach of the

Although the net results of relevant treaty provisions are often quite similar, the language used to achieve these results varies from treaty to treaty. The Japan-Korea Convention provides that Korea must allow a Korean resident or corporation a "credit" against Korean tax, for "the appropriate amount of tax paid or to be paid to Japan."[89] Japan is also to allow the same credit treatment to a Japanese resident or corporation for tax payable in Korea. The Korean tax credit, however, cannot exceed that proportion of Korean tax which the income from sources within Japan bears to the entire income subject to Korean tax.[90]

Another treaty, between Brazil and Portugal,[91] utilizes the deduction method. Here, where a resident of a contracting state derives income which may be taxed in the other contracting state, the first contracting state allows as a "deduction" from the tax on the income of the resident an amount equal to the tax paid in the other contracting state.[92] Like the Japan-Korean Convention, however, this deduction on the tax payable must not exceed that part of the tax of the first state, as computed before the deduction is given, which is appropriate to the income taxed in the other state.[93] Interest income is not subject to these provisions.[94]

The France-Morocco Agreement treats the elimination of double taxation rather thoroughly.[95] Treatment of double taxation depends upon the particular source of the income.

OECD Model Convention for the Avoidance of Double Taxation with Respect to Taxes on Income and Capital, reprinted in ADAMS & WHALLEY, *supra* note 1, at 80, which provides that where a resident of one state carries on business in another state, the profits of that business shall be taxable only in *the state of residence*, unless the person carrying on the business has a permanent establishment in the other state. "Permanent establishment" is defined to mean a fixed place of business in which the business of the enterprise is wholly or partly carried on. Where a resident carries on a business in another state through a permanent establishment, the state of permanent establishment can tax the business profits attributable to that establishment. If double taxation results from this process, and the two states concerned practice the exemption system, the profits of that entity will be taxable in state II where it carries on business, but exempt in state I where the company itself is resident. If the two states have the credit system contained in the treaty, the profits will be liable to tax in state II (the investee state) and that tax will be a credit against the company's liability to tax in state I (the resident state) in respect of these profits.

89. Japan-Korea Convention, *supra* note 74, art. 18, para. 1.
90. *Id.* at art. 22.
91. Brazil-Portugal Convention, *supra* note 68.
92. *Id.* art. XXII, para. 1.
93. *Id.* art. 22.
94. *Id.* art. XXII, para. 2.
95. France-Morocco Convention, *supra* note 50.

> Income from immovable property, including profits from agricultural and forestry enterprises, shall be taxable only in the state in which the property is situated.[96]
> Income from industrial, mining, commercial, or financial enterprises shall be taxable only in the state in which a permanent establishment is situated.[97]
> Where an enterprise maintains permanent establishments in both contracting states, each state may tax only the income derived from the operations of the permanent establishments situated in its territory.[98]

The agreement delineates the treatment to be accorded other forms of income, including, but not limited to, dividends, interest, director's emoluments and percentages, royalties, and pensions and annuities.[99]

Two agreements contain provisions similar to those of the Japan-Korea Convention on the elimination of double taxation. The Japan-Switzerland Convention states that subject to the provisions of the laws of Japan regarding the allowance as a credit against Japanese tax, Swiss tax payable, in respect of income arising in Switzerland, is credited against the Japanese tax payable for that income.[100] As for dividend income paid by a company which is a Swiss resident to a company which is a Japanese resident, and which owns not less than twenty-five percent either of the voting or total shares of the company paying the dividend, the credit shall include the Swiss tax payable by the first-mentioned company in respect of its profits.[101]

Furthermore, this agreement includes a clause generally found in many of the other agreements. This provision reserves for Switzerland an effectively higher rate of tax for residual income taxable in Switzerland in accounting for income taxable in Japan by applying the rate of tax which would have been applicable if the exempted income had not been exempted.[102] The Japan-Singapore Convention deals with these issues in a similar fashion.[103]

The United Kingdom-United States Convention also details the arrangement for double taxation controls.[104] The United States allows

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96. *Id.* art. 9.
97. *Id.* art. 10, para. 1.
98. *Id.* art. 10, para. 2.
99. *Id.* arts. 13-17.
100. Japan-Switzerland Convention, *supra* note 70, art. 23, para. 1.
101. *Id.*
102. *Id.* art. 23, para. 2.
103. Japan-Singapore Convention, *supra* note 72, arts. 21-22.
104. United Kingdom-United States Convention, *supra* note 32, at art. 23.

resident corporations a credit against United States tax for the amount of tax paid to the United Kingdom for partial business carried out in the United States. As for the payment of dividends by United Kingdom corporations to United States corporations, where the United States corporation owns at least ten percent of the stock of a United Kingdom resident corporation, the United States allows a tax credit for the amount of tax paid to the United Kingdom by the United Kingdom corporation on profits out of which the dividend is paid.[105] Tax credits are not to exceed the limitations provided for by United States law for the taxable year.[106] The United Kingdom reciprocates by allowing similar tax credits for like profits.[107]

The net effect of this tax credit arrangement is that the appropriate tax is first paid to the tax authorities of the state where the tax liability arises (i.e., the source of the income). The amount of tax paid is then credited against the overall tax payable to the authorities of its state of residence or nationality. From the source country's standpoint, this is certainly not a case of tax exemption.

As already noted, certain other agreements do not employ the tax credit scheme.[108] Rather, these agreements allow a deduction against tax payable to the country of residence or nationality up to the amount of tax paid to the authorities in the country which is the source of the income. The Netherlands-Singapore Convention further exemplifies this difference in treatment. In computing the taxable income of its residents, the Netherlands includes income or capital earned in the other state and taxable by the latter.[109] Part of the tax which bears the same proportion as the income from the other state already included in its computation of the taxable income, and paid to the other state, is allowed as a deduction from the taxes collected by the Netherlands.[110] Singapore, on the other hand, adopts the tax credit system: Tax payable in the Netherlands is allowed as a credit against Singapore tax payable in respect of that income.[111]

Under the Denmark-Trinidad & Tobago Convention, both states use the credit system of double taxation avoidance,[112] unlike the

105. *Id.* art. 23.
106. *Id.*
107. *Id.*
108. Netherlands-Singapore Convention, *supra* note 40.
109. *Id.* art. 24, para. 1.
110. *Id.* art. 24, para. 2.
111. *Id.* art. 24, para. 6, subd. a.
112. Denmark-Trinidad & Tobago Convention, *supra* note 46, art. XX.

separate schemes adopted by The Netherlands and Singapore.[113] The United States-USSR Convention provides for the elimination of double taxation through tax deductions.[114]

The Peoples Republic of China-Japan Convention provides for deductions and tax credits.[115] Expense deductions against profits of a permanent establishment are allowed to the extent that they are incurred for the purposes of the permanent establishment, including executive and general administrative expenses, regardless of where the expenses actually arose.[116] In other respects, China and Japan employ a tax credit system.[117] Where a resident of the first state derives income from the other, second contracting state, the amount of tax payable to the first contracting state on that income is allowed as a credit against the tax imposed by the second contracting state on that resident.[118] Treatment of dividends is also reciprocal.[119] Except where income derived from Japan is a dividend paid by a company which is a resident of Japan to a company which is a resident of China and which owns not less than ten percent of the shares of the company paying the dividend, the credit will take into account the Japanese tax payable by the company paying the dividend in respect of its income. Conversely, the percent of ownership required of a Chinese company receiving dividends from a Japanese resident company is twenty-five percent of the voting shares (or total shares issued) of the paying company.[120]

The West Germany-Singapore Agreement on the elimination of double taxation closely resembles the China-Japan Convention.[121] In computing the tax on a West German resident, income derived from, and capital situated within Singapore, which may have been taxed in Singapore, is excluded from the basis upon which West German tax is imposed; subject, however, to West Germany's reserved right to take into account in the determination of its rate of tax the items of income and capital so excluded.[122] Dividends receive typical treatment; a twenty-five percent ownership stake is required of the West

113. Netherlands-Singapore Convention, *supra* note 40, art. 24.
114. United States-U.S.S.R. Convention, *supra* note 56, art. IV.
115. China-Japan Convention, *supra* note 81.
116. *Id.*
117. *Id.*
118. *Id.* art. 23, para. 1.
119. *Id.* art. 23.
120. China-Japan Convention, *supra* note 81, art. 23.
121. West Germany-Singapore Convention, *supra* note 63, art. 23.
122. *Id.* art. 23, para. a.

German company of the Singapore company's stock.[123] Income derived in Singapore, for which tax payments can be credited against the West German tax on this same income, include certain dividends not covered in the discussion above (i.e., certain interest, royalties, and other remuneration).[124] The tax credits accorded under these provisions are not to exceed that part of the West German tax, as computed before the credit is given, which is appropriate to these items of income.[125] Tax credit treatment for Singapore residents is much the same as for West German residents.[126] Similar arrangements are provided for the Finland-France Convention.[127] The Denmark-Kenya Convention, too, is very similar in providing for tax credits.[128]

The Denmark-Malaysia Agreement uses a deduction and credit combination.[129] Subject to relevant Malaysian laws, Danish tax payable, whether directly or by deduction, for income derived from Denmark, is credited against Malaysian tax payable in respect of that income.[130] When the income is a dividend paid by a company, which is a Denmark resident, to a Malaysian resident, the tax credit will take into account Danish tax payable on the income of the company paying the dividend.[131] Where, however, a Danish resident derives income subject to Malaysian tax (in accordance with the convention), Denmark will allow as a deduction from the payable Danish tax for the income subject to tax in Malaysia.[132] Certain restrictions limit the extent of tax credits granted regarding certain types of income and the ceiling of the tax credit.[133]

The Denmark-Sweden Agreement uses a deduction method of eliminating double taxation in respect of income for fortune.[134] Again, the tax credit must not exceed that part of the income or fortune tax, calculated in the absence of a deduction, which corresponds to

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123. *Id.*
124. *Id.* art. 23, para. b.
125. *Id.*
126. West Germany-Singapore Convention, *supra* note 63, art. 23.
127. Finland-France Convention, *supra* note 67, art. 23.
128. Denmark-Kenya Convention, *supra* note 78, art. 25.
129. Denmark-Malaysia Convention, *supra* note 66, art. 21.
130. *Id.*
131. *Id.*
132. *Id.*
133. *Id.*
134. Denmark-Sweden Convention, *supra* note 61, art. 25. Where a resident of one state receives income or owns fortune which, according to this agreement, may be taxed in the other contracting state, the first contracting state shall allow as a deduction from the income tax or fortune tax of the person in question an amount corresponding to these taxes paid in the other contracting state.

the income or fortune that may be taxed in the other contracting state.[135] Profits are afforded similar tax credit treatment. The United Kingdom-Barbados Agreement uses a tax credit arrangement regarding both income and dividends.[136]

The agreements between Germany and Morocco[137] and Belgium and Italy[138] also exhibit similarities. In the former convention, West German residents having income arising in Morocco are to have this income exempted from West German tax.[139] West German authorities can still take this income into account in calculating its own rate of income tax.[140] For dividends, the exemption only applies where the dividends are paid by a Moroccan resident company limited by shares, to a joint stock company, which is a resident of West Germany and which directly holds at least twenty-five percent of the voting stock or voting shares of the first mentioned company.[141] West Germany, furthermore, provides a tax credit for Moroccan taxes paid on certain income.[142] Similar reciprocal treatment is granted by Morocco in all major respects.[143] The Belgium-Italy Convention is quite similar.[144] It provides, however, that where losses of an enterprise in one state having a permanent establishment in the other state have been effectively deducted from the profits of the enterprise for the purpose of taxation in the first state, no exemption applies in the first state to the extent that profits have been exempted from tax in the other state because they are offset by the losses.[145]

The Great Britain-Zambia Convention summarily disposes of the issue of avoiding double taxation.[146] Where, in accordance with the convention, a person is relieved from tax in a contracting state, and that person is subject to tax in the other contracting state on the same income, the relief from tax allowed under the agreement in the first state will apply only to the amount remitted or received.[147]

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135. *Id.* art. 24.
136. Great Britain-Barbados Agreement, *supra* note 77, art. 22.
137. West Germany-Morocco Convention, *supra* note 60, art. 23.
138. Belgium-Italy Convention, *supra* note 62, art. 23.
139. West Germany-Morocco Convention, *supra* note 60, art. 23.
140. *Id.*
141. *Id.*
142. *Id.*
143. *Id.*
144. Belgium-Italy Convention, *supra* note 62, art. 23.
145. *Id.*
146. Great Britain-Northern Ireland-Zambia Convention, *supra* note 79, art. 6.
147. *Id.*

The Netherlands-Indonesia Agreement uses a deduction method to eliminate double taxation.[148] First, in imposing tax on one of its residents, each state may include in the basis upon which taxes are imposed the items of income or capital which, according to the agreement, may be taxed in the other state.[149] For the Netherlands, the deduction from the amount of tax (computed in conformity with the provision immediately above) is to be equal to that part of the tax which bears the same proportion to this tax as the part of the income or capital which is included in the basis.[150] Additionally, the agreement stipulates rules for deductions for the various types of royalties and dividends, and provides reciprocal provisions for Indonesia.[151]

Three other agreements use a tax credit arrangement for the elimination of double taxation: United States-Trinidad & Tobago Convention,[152] France-Brazil Convention,[153] and Belgium-United States Convention.[154] By way of example, the France-Brazil Convention provides that where a Brazilian resident derives income taxable in Brazil according to its domestic laws, and the income is taxed in France in accordance with the agreement, Brazil will allow a tax credit equivalent to the tax paid in France.[155] The tax credit is not to exceed that part of the Brazilian tax which is appropriate to the proportion the income bears to the total income taxable in Brazil.[156] Dividends also receive limited tax credit treatment.[157]

III. Provisions Against Tax Avoidance and Evasion

International tax treaty provisions covered under this topic include allocation of expenses, secrecy covenants, apportionment of profits, and information exchange. The United Kingdom-United States Convention serves as a useful archetype for analytical purposes.[158] The "apportionment of profits" clause effectively states that where a resident enterprise in one state carries on business in the other

148. Netherlands-Indonesia Agreement, *supra* note 76, art. 24.
149. *Id.*
150. *Id.*
151. *Id.*
152. United States-Trinidad & Tobago, *supra* note 86, art. 4.
153. France-Brazil Convention, *supra* note 64, art. 22.
154. Belgium-United States Convention, *supra* note 80, art. 23.
155. France-Brazil Convention, *supra* note 64, art. 22.
156. *Id.*
157. *Id.*
158. United Kingdom-United States Convention, *supra* note 33, art. 7, para. 2.

contracting state through a permanent establishment (branch or subsidiary), each state must attribute to that permanent establishment the profits which it would be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities.[159] In other words, states are to estimate and then allocate to the permanent establishment in the second state those profits which it would make if it were wholly independent.[160] This is commonly referred to as the arm's length principle requiring fair dealing in trade and profits allocation.[161]

Just as the profits are allocated on a pro rata basis, so too, are the expenses associated with the permanent establishment.[162] Expenses incurred for the purposes of the permanent establishment are treated as viable deductions against the profit allocated to the establishment.[163] These expenses include reasonable executive and administrative expenses, research and development expenses, and interest.[164]

The next major issue in the United Kingdom-United States Convention deals with problems of transfer pricing as an aspect of tax evasion. Article 9 provides that where an enterprise resident in one state is associated with an enterprise in another state, and the two enterprises would have paid taxes on income in the first state but for commercial or financial conditions imposed between the two entities which differ from those which would have been made between independent enterprises, then any income or payments affected by the conditions may be taken into account in computing the profits or losses of that enterprise in the other state.[165] The latter state must, however, make such adjustments as may be appropriate to the amount of tax charged on those points.[166] Any disagreements as to the amount taken into account in the computation process will be resolved by mutual agreement between the parties.[167]

Another principal clause in the United Kingdom-United States Convention details the exchange of information and mutual administrative assistance.[168] Authorities of each state are to exchange in-

159. *Id.*
160. *Id.*
161. *Id.*
162. *Id.*
163. United Kingdom-United States Convention, *supra* note 32, art. 7, para. 2.
164. *Id.* art. 7, para. 5.
165. *Id.* art. 9.
166. *Id.*
167. *Id.*
168. United Kingdom-United States Convention, *supra* note 32, art. 26.

formation available under their respective tax laws to execute the transforming provision, prevent tax fraud, and administer statutory provisions against legal avoidance of taxes.[169] Certain limitations are imposed on this exchange; no information which would divulge a trade or business or industrial secret shall be exchanged. For administrative assistance, the parties are to consult with each other for the purpose of cooperating and advising on any action to be taken in implementing the exchange of information provision.[170] Naturally, the treaty provides for the resolution of disagreement over the amounts taken in account in computing the taxable profits and losses by requiring the parties' mutual agreement.[171]

The Singapore-Netherlands Agreement employs provisions very similar or identical to the United Kingdom-United States Convention.[172] The Peoples' Republic of China-Japan Convention also contains provisions on these issues.[173] First, profits are to be allocated (and taxed accordingly) to the subsidiary or branch operation on a pro rata basis as if it were a wholly independent enterprise.[174] Expenses attributable to the branch also are to be appropriately deducted from the allocated profits.[175] The treaty contains language controlling the allocation of profits where, but for existing conditions on commercial or financial relations, the enterprises would be considered separate entities and their profits would be taxable.[176] The profits are, therefore, allocated and taxed as if the enterprises were wholly distinct.[177] Information is to be exchanged to carry out the provisions of the agreement, enforce the local tax laws of the respective states, or to prevent evasion of taxes covered by the agreement.[178] The information is accorded confidential status and may be disclosed only to persons involved in the collection or assessment of the pertinent taxes.[179] Restrictions prevent disclosure

169. *Id.*
170. *Id.*
171. *Id.* art. 9.
172. Netherlands-Singapore Convention, *supra* note 40. For subsidiaries or branches, *see* art. 7, para. 2; for associated enterprises and arm's length treatment, art. 9; and for information exchanges and administrative assistance, art. 27.
173. China-Japan Convention, *supra* note 81, art. 7.
174. *Id.* art. 9.
175. *Id.*
176. *Id.*
177. *Id.*
178. China-Japan Convention, *supra* note 1, art. 7, para. 1.
179. *Id.*

of trade, business, industrial, or commercial secrets or information, as that would be contrary to public policy.[180]

The Denmark-Malaysia Agreement[181] and the Denmark-Kenya Convention[182] are also similar with respect to tax avoidance and evasion. Information is to be exchanged to carry out the agreements' provisions, prevent fraud, prevent underpayment of taxes for reasons other than fraud (i.e., other fiscal evasion), or to administer statutory provisions against legal avoidance.[183] Both conventions declare any information exchanged to be treated as secret; only persons concerned with the assessment or collection of the taxes shall have access to the information.[184]

Article 27 of the Great Britain-Zambia Convention[185] contains provisions quite similar to the two Danish agreements. Additionally, information which would disclose any trade, business, industrial, or professional secret or any trade process may not be exchanged.[186] Five other conventions treat these issues in nearly identical fashion: Japan-Singapore Convention,[187] France-Brazil Convention,[188] West Germany-Morocco Convention,[189] West Germany-Singapore Agreement,[190] and Netherlands-Singapore Convention.[191] Using the Japan-Singapore Convention as a basis for discussion, note that the contracting states are to exchange any information as is necessary for (1) carrying out the convention's provisions, (2) preventing fraud, or (3) the administering statutory provisions against tax avoidance.[192] Information exchanged is to be accorded secrecy status and cannot be disclosed to any person other than those, including a court, concerned with the assessment and collection of the tax or the determination of appeal in relation thereto, and in the case of the West Germany-Morocco Convention, to the judicial authorities for the purpose of criminal prosecution in respect of such taxes.[193]

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180. *Id.* art. 26, para. 2, subd. c.
181. Denmark-Malaysia Agreement, *supra* note 66, art. 22.
182. Denmark-Kenya Convention, *supra* note 78, art. 28.
183. *Id.*
184. *Id.*
185. Great Britain-Northern Ireland-Zambia Convention, *supra* note 79, art. 27.
186. *Id.*
187. Japan-Singapore Convention, *supra* note 72, art. 24.
188. France-Brazil Convention, *supra* note 64, art. 26.
189. West Germany-Morocco Convention, *supra* note 60, art. 26.
190. West Germany-Singapore Convention, *supra* note 63, art. 26.
191. Netherlands-Singapore Convention, *supra* note 40, art. 26.
192. Japan-Singapore Convention, *supra* note 72.
193. West Germany-Morocco Convention, *supra* note 60.

In no case should these treaty provisions be construed to impose the following obligations on a contracting state: (1) to carry out the administrative measures at variance with the laws or administrative practice of that or of the other contracting state; (2) to supply particulars which are not obtainable under the laws or in the normal course of administration of the contracting states; (3) to supply information which would disclose any trade, business, industrial, commercial, or professional secret or trade process, or information, the disclosure of which would be contrary to public policy.

Two other agreements deserve review. The France-Morocco Agreement covers information exchange and administrative assistance.[194] The two states are to assist and support each other in the collection of taxes to which the agreement relates, and of any tax increases, surcharges, overdue payment penalties, interest and costs pertaining to the said taxes, with the exception of those of a penal nature, where such sums are finally due under the laws or regulations of the requesting state.[195] Documentation must accompany the assistance requests as required by the laws of the requesting state. The documentation serves as evidence that the sums to be collected are finally due.[196] Once the requested state receives the documents, it is to serve writs and take measures so as to satisfy the collection and recovery of taxes due.[197]

The Belgium-Italy Convention also contains information exchange provisions aimed at discouraging tax avoidance or evasion.[198] Article 26 provides that the competent authorities of each state shall exchange information as is necessary for carrying out the convention and the domestic laws of each contracting state to the extent that the domestic laws deal with taxes covered by the agreement and taxation is effected in accordance with the agreement.[199] Information exchanged pursuant to the agreement must be treated as a secret.[200] Other than the taxpayer or his agent, the information can be disclosed only to the person or authorities concerned with the assessment or collection of the taxes which are the subject of this convention, and to the judicial

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194. France-Morocco Convention, *supra* note 50, art. 29, at 1.
195. *Id.* art. 29, para. 1.
196. *Id.* art. 29, para. 2.
197. *Id.* art. 29, para. 3.
198. Belgium-Italy Convention, *supra* note 62, art. 26, para. 1.
199. *Id.*
200. *Id.*

authorities.[201] The agreement contains the usual provisions aimed at safeguarding certain information.[202]

The Denmark-Sweden Agreement contains a provision governing the issue of associated enterprises[203] regarding the possibility of transfer pricing. The convention provides that where an enterprise of one contracting state participates directly or indirectly in the management, control, or capital of an enterprise of the other contracting state, and conditions are imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, any profits which, but for those conditions would have accrued to one of the enterprises, may be included in the profits of that enterprise and taxed accordingly.[204] The agreement also provides that where a question relevant to the issue arises in one of the contracting states, the competent authority of the other state must be informed with a view to making the necessary adjustment in connection with the calculation of the profits of the enterprise which is a resident of that other state.[205] Apportionment of profits can be arranged by special agreement of the contracting state.[206] This is reminiscent of the provision in the United Kingdom-United States Convention on associated enterprises.[207]

IV. NONDISCRIMINATION

The subject of non-discrimination involves several interrelated issues. First, the treaties deal with the determination of which persons are accorded the non-discriminatory protection of the treaties; whether as nationals, citizens, mere residents, or stateless persons. Second, the conventions deal with protection in respect of permanent establishments as well as foreign-owned or foreign-controlled enterprises. Third, the instruments refer to the kinds of exemptions and reliefs to which nationals of the other contracting state are entitled. As the following treaties evidence, most bilateral double taxation treaties grant national treatment. Occasionally, however, one encounters most-

201. *Id.*
202. Belgium-Italy Convention, *supra* note 62, art. 26, para. 1.
203. Denmark-Sweden Convention, *supra* note 61, art. 9.
204. *Id.* art. 9, paras. a, b.
205. *Id.*
206. *Id.*
207. United Kingdom-United States Convention, *supra* note 32, art. 9.

favored-nation (MFN) treatment for nationals of the other contracting state.

The Brazil-Portugal Convention,[208] France-Brazil Convention,[209] and Japan-Switzerland Convention[210] contain provisions defining the meaning of a "national" for the respective countries. In the case of the Brazil-Portugal Convention, national means:

> (1) all individuals possessing the nationality of a contracting state;
> (2) all bodies corporate deriving their status as such from the law in force in a contracting state; and
> (3) all entities which, not being bodies corporate, are treated as such, for tax purposes, by the legislation of a contracting state.[211]

The France-Brazil Convention uses identical language.[212] The Japan-Switzerland Convention also defines nationals in respect of each contracting state in similar terms.[213] All three treaties provide that nationals of one contracting state must not be subject to any taxation or connected requirements more burdensome than the taxation and connected requirements to which nationals of that other state in the same circumstances are or may be subjected.[214]

The Brazil-Portugal Convention[215] and France-Brazil Convention[216] contain nearly identical provisions dealing with non-discriminatory, national treatment for permanent establishments in the other state, where the enterprise carries on the same activities as national establishments.[217] Neither agreement, however, obliges a contracting state to grant residents of the other contracting state any personal allowances, reliefs, and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.[218] Similar nondiscriminatory protections are granted to enterprises of a contracting state whose capital is wholly or partly owned or controlled by one or more residents of the other contracting

208. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 2.
209. France-Brazil Convention, *supra* note 64, art. 24, para. 2.
210. Japan-Switzerland Convention, *supra* note 70, art. 24, subd. 2.
211. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 2.
212. France-Brazil Convention, *supra* note 64, art. 24, subd. 2.
213. Japan-Switzerland Convention, *supra* note 70, art. 24.
214. Brazil-Portugal Convention, *supra* note 65, art. XXIII; France-Brazil Convention, *supra* note 64, art. 24; Japan-Switzerland Convention, *supra* note 70, art. 24.
215. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 3.
216. France-Brazil Convention, *supra* note 64, art. 24, para. 3.
217. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 3; France-Brazil Convention, *supra* note 64, art. 24, para. 3.
218. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 3; France-Brazil Convention, *supra* note 64, art. 24, para. 3.

state.[219] Taxation or connected requirements cannot be different (or more burdensome) than those to which national enterprises are subject.[220]

The agreements between Denmark and Kenya,[221] West Germany and Morocco,[222] Great Britain and Zambia,[223] and Peoples' Republic of China and Japan[224] all provide similar protections through nearly identical language. The Finland-France Convention also treats the outlined issues in a similar manner.[225] Some notable exceptions, however, do exist. The most significant distinction is the provision found in the latter agreement dealing with stateless persons.[226] Stateless persons are not to be subject in either contracting state to any taxation or any connected requirement which is more burdensome than that treatment accorded nationals of the other contracting state in the same circumstances.[227]

The Japan-Singapore Convention and West Germany-Singapore Agreement also resemble the model agreements discussed insofar as non-discriminatory treatment is concerned.[228] Some minor distinctions include the use of the words "citizens or nationals" in the former agreement, and only "citizens" in the latter.[229] Thus, unlike those agreements examined above where nationals also receive national treatment, in some other agreements, only citizens receive such treatment. In the Japan-Singapore Convention, however, this provision granting national treatment to citizens or nationals of the other contracting state is not to be construed as obliging Singapore to grant to nationals of Japan, who are not resident in Singapore, those personal allowances, reliefs, and reductions for tax purposes which are by law available only to citizens of Singapore.[230] Likewise, the provisions granting national treatment to permanent establishments

219. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 4; France-Brazil Convention, *supra* note 64, art. 24, para. 4.
220. Brazil-Portugal Convention, *supra* note 65, art. XXIII, para. 4; France-Brazil Convention, *supra* note 64, art. 24, para. 4.
221. Denmark-Kenya Convention, *supra* note 78.
222. West Germany-Morocco Convention, *supra* note 60, art. 24.
223. Great Britain-Northern Ireland-Zambia Convention, *supra* note 79, art. 25.
224. China-Japan Convention, *supra* note 81.
225. Finland-France Convention, *supra* note 67, art. 24.
226. *Id.* art. 70, para. 3.
227. *Id.*
228. Japan-Singapore Convention, *supra* note 72, art. 22; West Germany-Singapore Agreement, *supra* note 63, art. 24, para. 1.
229. Japan-Singapore Convention, *supra* note 72, art. 22; West Germany-Singapore Agreement, *supra* note 63, art. 24, para. 1.
230. Japan-Singapore Convention, supra note 72, art. 22, para. 1.

in the other contracting states are not to be construed as obliging either state to grant to citizens, nationals, or residents (depending upon the particular treaty) of the other contracting state those personal allowances, reliefs, and reductions for taxation purposes which are by law available only to residents of the first contracting state or available on account of civil status or family responsibilities or any other personal circumstances which the contracting state grants to its own residents.[231]

In most respects, the Denmark-Malaysia Agreement and United Kingdom-Barbados Agreement are similar to the two preceding agreements.[232] The Belgium-United States Convention generally accords, with one difference.[233] Although permanent establishments are granted national treatment in either contracting state, this national treatment protection is not wholly unconditional. Belgium has reserved the right to tax the total profits attributable to a permanent establishment which is maintained in Belgium by a United States corporation, or any unincorporated entity which is a United States resident, at a rate equal to the highest rate at which the profits of a Belgium corporation may be taxed.[234]

The Denmark-Sweden Agreement also includes the same type of national treatment protections to nationals, permanent establishments, and foreign-owned or foreign-controlled enterprises of either state.[235] Article 25 of the agreement provides:

> The provision on permanent establishment, however, do not imply the right to exemption in a contracting state from taxation on dividends paid or other payments made to a company which is a resident of the other contracting state.[236]

Furthermore, where the permanent establishment belongs to a joint-stock company or company assimilated to a joint stock company in the other contracting state, either contracting state may tax income derived from the permanent establishment in accordance with the rules of that state's own legislation.[237] This taxation must correspond to the tax on undistributed profits levied on joint stock companies which are residents of the other contracting state.[238]

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231. *Id.* para. 2.
232. Denmark-Malaysia Agreement, *supra* note 66, art. XXIV; Great Britain-Barbados Agreement, *supra* note 77, art. 26.
233. Belguim-United States Convention, *supra* note 80, art. 24.
234. *Id.*
235. Denmark-Sweden Agreement, *supra* note 61, art. 25, para. 2.
236. *Id.*
237. *Id.*
238. *Id.*

The United States-Trinidad & Tobago Agreement also contain limits on the national treatment accorded permanent establishments, as do most conventions.[239] The France-Morocco Agreement contains a national treatment formula[240] and provides that nationals of one contracting state liable for taxation in the territory of the other state are entitled to, under the same conditions as nationals of that other state, such exemptions, relief, rebates, and reductions of any taxes or charges whatsoever, as may be granted in respect of family dependents.[241] The Belgium-Italy Convention also entitles certain individuals to these exemptions and abatements.[242] The agreement includes provisions covering national treatment for stateless persons, nationals, and permanent establishments of the other contracting state.[243]

One agreement in particular, the United States-USSR Convention, ensures both MFN and national treatment to citizens of one state who are residents of the other contracting state.[244] The MFN treatment provides that citizens will not be subject to taxes more burdensome than are generally imposed in the other contracting state on citizens or representatives of residents of third states carrying on the same activities.[245] Where, however, tax benefits are granted to citizens or representatives of third states pursuant to special agreements, one contracting state is not obliged to grant to citizens or representatives or residents of the other contracting state the same benefits.[246] In all other material respects, the agreement is similar to the agreements discussed above.[247]

V. Procedure for Handling Tax Complaints From Corporate Taxpayers

The procedures by which corporate taxpayers complain or object to taxation levied upon them are comparatively similar in most double taxation treaties. Among the relevant provisions dealt with in the conventions, the following prove noteworthy: (1) resolution of tax-

239. United States-Trinidad & Tobago, *supra* note 86, art. 6.
240. France-Morocco Agreement, *supra* note 50, art. 5.
241. *Id.* art. 5, para. 2.
242. Belgium-Italy Convention, *supra* note 62, art. 24.
243. *Id.* paras. 3, 5.
244. United States-U.S.S.R. Convention, *supra* note 56, art. V.
245. *Id.*
246. *Id.*
247. *Id.*

ation discrepancies through mutual agreement; (2) preservation of national remedies; (3) resolution of difficulties associated with convention interpretation or application; (4) statute of limitations; and (5) details for further communication between the two contracting states.

The United Kingdom-United States Convention provides that where a corporation feels that the actions of one or both states will result in taxation which is not in accordance with the Convention, the corporation may present its case to the competent authority of the state of which it is a resident.[248] In evaluating this provision, two points of primary importance come to mind. First, one must look elsewhere in the convention to determine precisely what constitutes "taxation which is not in accordance with the convention." Second, the complaining corporation presents its objection to the state of which it is a resident.

Upon the corporation's presentation of the objection, the receiving state, if it feels that the corporation's objection is justified, and it is unable to resolve the issue on its own, must endeavor to resolve the case by mutual agreement with the appropriate authorities of the other contracting state.[249] Resolution of the case is accomplished by taking measures to avoid unlawful taxation. Refunds of taxes paid are to be made where necessary. This procedural facility is not the exclusive remedy for the corporation; the corporation preserves rights under applicable national laws. Authorities of the two contracting states are also required to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. This effort is particularly important with respect to the attribution of income, deductions, credits, and allowances of an enterprise to its permanent establishment.[250]

The Netherlands-Singapore Convention and Denmark-Trinidad-Tobago Agreement employ nearly identical language on all of the above matters.[251] Numerous other treaties also contain very similar provisions. The Denmark-Sweden Agreement, West Germany-Singapore Agreement, and Netherlands-Indonesia Agreement serve to illustrate these similarities.[252] First, as in the treaties discussed above, where

248. United Kingdom-United States Convention, *supra* note 32, art. 25.
249. *Id.*
250. *Id.*
251. Netherlands-Singapore Convention, *supra* note 40, art. 25; Denmark-Trinidad & Tobago Convention, *supra* note 46, art. XXI.
252. Denmark-Sweden Convention, *supra* note 61, art. 26; West Germany-Singapore Convention, *supra* note 63, art. 25; Netherlands-Indonesia Convention, *supra* note 76, art. 25.

the corporation (or resident) considers that measures or actions of one or both of the contracting states will result in taxation not in accordance with the agreement, the resident may, without affecting its remedial rights available under national laws of the party states, present its case to the competent authority of the contracting state of which it is a resident.[253]

If the objection is considered to have merit and the competent authority is unable to arrive at a satisfactory or appropriate solution, that authority must endeavor to resolve the case through mutual agreement with the competent authority of the other state with a view to the avoidance of taxation not in accordance with the agreements.[254] Beyond this resolution of declared taxation disputes, the agreements provide that the states are to resolve disputes or difficulties as to interpretation or application of the agreements.[255] As for avoiding double taxation not provided for in the agreements, the competent authorities may consult with each other to reconcile possible differences.[256]

The West Germany-Morocco Convention,[257] Japan-Switzerland Convention,[258] Japan-Singapore Convention,[259] Great Britain-Zambia,[260] United States-USSR Convention,[261] and Finland-France Convention[262] treat these issues in like fashion, except that the Finland-France Convention is not so specific; it contains a clause providing that the competent authorities of the contracting states shall settle the *mode of application* of the convention.[263] The Denmark-Malaysia Agreement and France-Brazil Convention are similar in all relevant respects to the more typical of these provisions.[264]

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253. Denmark-Sweden Convention, *supra* note 61, art. 26; West Germany-Singapore Convention, *supra* note 63, art. 25; Netherlands-Indonesia Convention, *supra* note 76, art. 25.
254. Denmark-Sweden Convention, *supra* note 61, art. 26, para. 2; West Germany-Singapore Convention, *supra* note 63, art. 25, para. 2; Netherlands-Indonesia Convention, *supra* note 76, art. 25, para. 2.
255. Denmark-Sweden Convention, *supra* note 61, art. 26, para. 3; West Germany-Singapore Convention, *supra* note 63, art. 25 para. 3; Netherlands-Indonesia Convention, *supra* note 76, art. 25 para. 3.
256. Denmark-Sweden Convention, *supra* note 61, art. 26, para. 4; West Germany-Singapore Convention, *supra* note 63, art. 25 para. 4; Netherlands-Indonesia Convention, *supra* note 76, art. 25 para. 4.
257. West Germany-Morocco Convention, *supra* note 60, art. 25.
258. Japan-Switzerland Convention, *supra* note 70, art. 25.
259. Japan-Singapore Convention, *supra* note 72, art. 23.
260. Great Britain-Northern Ireland-Zambia Convention, *supra* note 80, art. 26.
261. United States-U.S.S.R. Convention, *supra* note 56, art. XI.
262. Finland-France Convention, *supra* note 67, art. 25.
263. *Id.* art. 25, para. 5.
264. Denmark-Malaysia Convention, *supra* note 66, art. 25; France-Brazil Convention, *supra* note 64, art. 25.

The France-Morocco Agreement deals with the issues in somewhat different language.[265] Under the agreement, if a taxpayer asserts that certain actions of the other contracting state are not in accordance with the convention, it may submit an objection to the competent authorities of the other state, not necessarily the state of which it is a resident.[266] Obviously, an objection against the actions of the state of which it is a resident would be filed in that same state.[267] The rest of this agreement is much like the others discussed above.

The Belgium-United States Convention,[268] Brazil-Portugal Convention,[269] Denmark-Kenya Convention,[270] Belgium-Italy Convention,[271] and China-Japan Convention,[272] although similar in most respects to the treaties discussed above, include statutes of limitations clauses. The Belgium-United States Convention allows a corporation to present a complaint or objection within two years from the date of notification or collection of taxes.[273] The remainder of the agreement follows the other conventions above. The Brazil-Portugal Convention provides that a resident's application must be submitted within two years from the date of notification of the tax which has given rise to the objection; or, in the case of taxation in both states, from the date of notification of the second taxation; or, in the case of a tax payable by deduction at the source, from the date of payment of the income which has been taxed even if the objection relates to the second taxation.[274] The Denmark-Kenya Convention stipulates that the case must be brought within three years of the date of the disputed action, or the latest of the disputed actions as the case may be.[275] The Belgium-Italy Convention provides that written application by a complaining resident must be submitted within two years from the date of notification or of deduction at the source of the second taxation.[276] Lastly, the China-Japan Convention allows two years for the presentation of an objection, provided that a complaining per-

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265. France-Morocco Convention, *supra* note 50, art. 31.
266. *Id.* art. 31, para. 1.
267. *Id.*
268. Belgium-United States Convention, *supra* note 80, art. 25.
269. Brazil-Portugal Convention, *supra* note 65, art. 27.
270. Denmark-Kenya Convention, *supra* note 78, art. 27.
271. Belgium-Italy Convention, *supra* note 62, art. 25.
272. China-Japan Convention, *supra* note 81, art. 25.
273. Belgium-United States Convention, *supra* note 80, art. 31.
274. Brazil-Portugal Convention, *supra* note 65, art. XXIV para. 1.
275. Denmark-Kenya Convention, *supra* note 78, art. 27, para. 1.
276. Belgium-Italy Convention, *supra* note 62, art. 25, para. 1.

son's case comes under the scope of national protection.[277]

VI. COMMENTARY

This article has attempted to outline the importance of taxation in international capital flows and domestic capital formation; the problems posed by differing tax systems and policies for international investment; and the types of income or expenditure which create the greatest source of conflict among capital importing and capital exporting countries. In addition, this article has discussed in some detail the issues of double taxation and tax evasion and avoidance, especially the manner in which the latter are promoted by the use of transfer pricing and tax havens. This article also touched briefly on the nature, rationale, and dangers of tax incentives, such as tax holidays, as a way of promoting TNC investment. The article does not discuss another equally important aspect of the analysis of tax treaties; namely, their formal interpretation, which lies outside the framework of our present concern.[278]

With respect to the problem of double taxation, the interest of host states requires increased efforts to conclude bilateral and regional tax treaties in which the principle of source of income would be enshrined as the basis for the assumption of tax liability by TNCs. This would cover various types of incomes such as business profits, interest on loans, management fees, and other payments for intellectual property, to the extent that they either arise from, or are used in, local operations.[279] Indeed, the Group of Experts on Tax Treaties (the Group), in the main thrust of its formulations, favored the primacy (though not the exclusivity) of the principle of source as the

277. China-Japan Convention, *supra* note 81, art. 25, para. 1.

278. For an excellent treatment of this topic, see VOGEL, *supra* note 27, at 29.

279. Most developing countries as host states are unlikely to be faced with many situations in which their own nationals would have greater income from foreign sources, than foreign nationals would have from sources in such host countries. Thus, such countries would tend to lose if the trend were to move from tax assessment on a "source" to a "residence" basis.

Thus, the domestic tax laws of host states could be so framed that business profits are deemed to have their source in the host state to the extent that they arise from or through a branch or a permanent establishment such as a subsidiary; from contracts entered into or carried out in the host state; and from the operations of dependent agent in that state. Interest paid on loans could be deemed to have a source in the host state if a loan is used by the borrowing subsidiary and claimed as a deduction in the host state, irrespective of where the loan is in fact borrowed. Management fees paid by a subsidiary to its overseas parent could by deemed to have a local source in the host state and to be assessed at full corporation rate in the hands of the parent. Finally, royalties and other payments for know-how could also be deemed to have a source in the host state when deducted by the subsidiary TNC in arriving at its assessable income in that state.

basis for the assumption of tax liability.[280] At the same time, the Group emphasized that such a principle should take into account certain considerations: expenses allocable to the earning of the income, so that such income would be taxed on a net basis; the appropriateness of the sharing of revenue with the capital exporting country; and the desirability of tax rates which are not so high as to discourage investment.[281]

To deal with tax avoidance and evasion, a number of measures could be adopted. Tackling the transfer pricing of TNCs entails a basic practical problem: how to find and substitute a fair domestic price for the price that an overseas parent corporation has charged its local subsidiary for goods and services. The problem posed here is that, in a majority of cases, a "fair" or "appropriate" price is largely indeterminate; yet, whatever price is charged would have considerable impact on the tax calculations involved. Empirical research work in this area is very difficult. Ideally, not only must the researcher have access to detailed information about the intra-corporate deals of a TNC, but he or she also needs the expert assistance of valuers to be able to ascertain whether a price charged in each intra-corporate transaction was artificially low or high.

International practitioners may best benefit their clients by consulting trade journals listing prices of, or discounts on, commodities, as well as prices paid by independent companies. Quite often, however, the practical problem lies in finding adequate and reliable sources. Exchange of information on prices pursuant to double taxation agreements is a potentially effective approach. But, here again, remains the problem that where the parent corporation located in a contracting state deals directly with its subsidiary located in another contracting state (the typical situation), the home state may not feel inclined to supply information on overpricing if that would adversely affect its own tax revenues. Exchange of information is more likely to be forthcoming where the revenues of both home and host countries have been adversely affected by corporations interposed in a tax haven.

Transfer pricing is indeed one of the most troublesome aspects of the allocation problem of TNC financial operations viewed in their

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280. *Tax Treaties between developed and developing countries, 7th report; Report of the Group of Experts on Tax Treaties between Developed and Developing Countries on the work of its 7th meeting* at 28-45, U.N. Doc. ST/ESA/79, U.N. Sales No. E.78.XVI.1 (1978).
281. *Id.*

global perspective. The clearly emerging solution is that home and host states should enforce arm's length prices wherever appropriate (i.e., prices charged between competitive or independent buyers and sellers in a free market without collusion). The Group of Experts on Tax Treaties, in its Seventh Report, also adhered to the principle of arm's length allocation and devised a framework for procedural arrangements.[282] Among the methods mentioned in that report for the ascertainment of the arm's length price are the uncontrolled market price method, the resale price method, and the cost-plus method.[283]

In commodities where arm's length or competitive prices do not exist (as in the case of monopolistic markets), TNCs could be required to pay prices linked to the prices of the final product on the world market. In any other situation, and in non-commodity areas such as royalties and know-how where, again, competitive prices may be non-existent or difficult to establish, TNCs would pay prices which are objectively fair and equitable. In essence, this entails the use of whatever methods are likely to achieve a reasonable approximation to an arm's length price. Some of the methods mentioned in this regard include the division of gross or net profit between manufacturing and marketing units of the TNC on the basis of factors such as sales, assets, and payrolls; comparison with foreign customs valuation; and a unilateral price selected by tax authorities on the basis of its own research or intelligence network.[284]

Mention has been made of artificial intracorporate transactions not involving commodity trading, such as interest on loans, management fees, and royalties. The basic approach to obviously excessive claims under any of these headings would be either to disallow the payments as items deductible as a cost for tax assessment purposes, or to allow them only up to some set percentage. In particular, tax on interest could be assessed at the greater of non-resident withholding tax on the gross interest or ordinary corporation tax rates on the net income from the interest if the payee (the external lender) is an associate of the payer (the local subsidiary borrower). In calculating the net interest, charges (e.g., interest the payee paid to itself) could be deductible. Management fees could be assessable at the full corporation rate in the hands of the parent.

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282. *Id.*
283. *Id.*
284. *Id.*

Administrative expenses (i.e., expenses incurred in the administration of the world wide operations of the particular group of corporations) also need to be considered. A parent corporation may seek to claim in a particular country a proportion of the head office administrative expenses, which were in fact incurred overseas, as being applicable to the operations carried on in that particular country. While defensible in principle, this sort of claim always raises a question as to the fairness of the apportioning method. The host state could reasonably resolve the issue by allowing a deduction for a proportion of head office administrative expenses based on a percentage of the local gross receipts. At periodic intervals, claims of this nature could be checked, and a stipulation made for a certificate by external auditors of the parent office giving such details as the itemized list of the expenses included in the claim,[285] local receipts, and total receipts for the enterprise as a whole. There is also the possibility of apportioning administrative expenses on the basis of the proportion that local expenses (rather than local receipts) bear to the total or global expenses. As far as royalties paid between associates are concerned, these could be assessed at the greater of non-resident withholding tax on the gross royalties and ordinary corporation rates on the net. Know-how payments (e.g., payments for technical or commercial services), also could be assessed in the same manner as royalties when paid between associates.

Branches of TNCs are often treated rather differently from subsidiaries in various tax codes, the theory being that a subsidiary is legally a different entity from its parent company. It is therefore argued that when a branch and a parent office situation is involved, internal payments or credits should be ignored for tax purposes. The practical effect would then be that interest payable by the branch on its head office account should neither be deducted by the paying branch nor assessable to the payee parent office. A portion of the interest payable, however, may be allowable against the branch operations. Internal payments or credits for royalties, know-how payments, management fees, and the like could be allowed if they represent the bare cost of providing these services, but should be discounted if they contain a profit element.

The abuse of tax havens is obvious from the above description of the modalities of transfer pricing. A tax haven is defined as a tax

285. The list would show the expenses did not include any capital or other items not normally deductible for tax purposes, and that they did in fact cover administering operations of the kind carried out in the host state concerned.

jurisdiction with zero or extremely low tax rates. A parent corporation may always seek to avoid or defer its liability to tax on profits of its foreign enterprise by using transfer pricing and other methods to augment the profits in a foreign subsidiary located in a tax haven or in a place which, although not a tax haven, has lower tax rates than the home country. To combat this misuse of tax havens, bilateral and multilateral treaties should establish clear guidelines for assigning a permanent establishment to an entity situated in a tax haven and interposed between related entities located in the countries which are parties to the treaties. More importantly, tax treaties should contain provisions on exchange of information which would form the basis for obtaining information on the dealings between the related entities in the treaty states and the tax havens.

Other methods of tax evasion and avoidance take much less subtle forms than transfer pricing and the other artificial transactions just addressed. Particularly in the case of tax evasion, this is often accomplished by direct and outright misrepresentation of the operations of the business to the tax authorities, in areas such as the level of profits and the value of imports and exports. In these cases, the tax authorities could be empowered to impose their own tax assessments on the basis either of assets or gross income. The tax authorities would also need to monitor the operation of business enterprises within their jurisdiction more closely, with a view to collecting more adequate information on them.

Indeed, the whole issue of tax evasion and tax avoidance cannot be divorced from the availability of adequate information. The point already made about exchange of information in relation to tax havens applies equally well to the entire subject of taxation. Exchange of information could take the form of an automatic exchange of information, information supplied on demand, or information on facts deemed by the supplying state to be significant for taxation purposes in another state. There should be machinery in place to afford a full and complete disclosure of the financial transactions of TNCs not only to make sure that they pay their full tax bills in the home and host states, but also to allow the opportunity of comparing these bills with corresponding ones in other countries. In the final analysis, it is only through comparative information among countries that an appropriate distribution of tax benefits among them can be attained. This would also lay the foundation for more effective international cooperation in the detection and punishment of tax crimes.

Conclusion

In assessing the utility and impact of tax incentives, two essential questions must be raised constantly. First, to what extent do such incentives really motivate TNC investment? Put another way, would TNCs not make the particular investment in the absence of such incentives? Second, what are the trade-offs of tax incentives in terms of the loss of public revenue and increased public expenditure? Before incentives are granted, careful thought should be given to costs and benefits. It must be clear that economic benefits would be obtained which would not otherwise arise in the absence of such grants. The procedures of each state should provide a mechanism for a review of the benefits. Furthermore, there should be a policy of harmonization of tax incentives in countries comprising the same economic region.

In various ways, the different approaches to the issues addressed in this paper reflect a need for international co-operation (bilateral, subregional, regional, and interregional) in the resolution of problems of international taxation. This implies not only procedures for overcoming the complexities of tax laws and differences in bases of taxation which make comparability difficult, but also the development of principles of equity in international income allocation. International legal practitioners, their clients, and national interests can only stand to gain from agreements which heed such concerns.