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Natural Resource Protection through Double Tax Agreements in the East African Community

A critical analysis of whether Kenya, Tanzania and Uganda have sufficiently protected the taxing rights over natural resources within their Double Tax Treaty Network.

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ABSTRACT

Kenya, Tanzania and Uganda are countries that are in rich natural resources. The two resources which these states are the most economically reliant upon are that of arable land and minerals. It is these two resources which hold the most potential for these three states in terms of further economic growth. This makes it important for these two valuable resources to be afforded the best possible protection through the Double Tax Agreements (DTAs) that the three states have negotiated.

This dissertation determined whether sufficient protection exists within the DTA networks of Kenya, Tanzania and Uganda by analysing two important Articles that have a major impact on the ability of the "source State" to tax the exploitation of natural resources. These two Articles are the income from immovable property Article and the permanent establishment (PE) article (Article 6 and Article 5 of the OECD Model Tax Convention respectively). The Articles overlap to some extent making it important for the authorities within the three states to effectively negotiate both Articles in such a way to offer sufficient protection of arable land and minerals. The deciding factor that causes certain proceeds to fall under either article is the relative importance that immovable property plays in the income earned.

Within the DTA networks of these three states, some protection exists for both arable land and mining. However, it is submitted that such protection is insufficient. The income from immovable property Article is, at times, not included in a treaty. In terms of the PE article, there is a lack of consistent protection for the resources of arable land and minerals. The null hypothesis at the start is that the PE article should effectively cover the industries of agriculture and mining. However, it was found that no uniformity existed within the wording of the two relevant Articles resulting in inconsistent protection of valuable natural resources. Although Kenya has taken steps to protect itself in the case of agriculture and Uganda has, in some of its DTAs, provided for better protection to its mining industry, more needs to be done by all three states to ensure better protection.

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ABBREVIATIONS AND GLOSSARY

DTA/treaty	Double Tax Agreement / Double Tax Convention
E.A.C.	East African Community
GDP	Gross Domestic Product
OECD	Organisation for Economic Co-operation and Development
OECD MTC	OECD Model Tax Convention on Income and on Capital
OECD Commentary	Commentary on the OECD Model Tax Convention on Income and on Capital
MTC	Model Tax Convention
The three states	Kenya, Tanzania and Uganda
UN MTC	United Nations Model Double Taxation Convention between Developed and Developing Countries
VCLT	Vienna Convention on the Law of Treaties

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CHAPTER 1

INTRODUCTION

1.1 The importance of DTAs for Africa

It is certainly a well known fact that the African continent is well endowed with valuable natural resources. These resources have been shown to be an important springboard for economic growth because, where there are economically viable resources to exploit, there exists the potential for foreign investment to be drawn to the state which possesses them. Yet vast amounts of these resources remain under-developed and still many African states are of the poorest in the world. Questions as to why this is the case have been asked. A variety of factors have contributed to this state of affairs. Nonetheless there are two important contributors to economic growth and subsequent wealth creation which are closely related to one another; namely tax and investment. An African State must balance the twin aims of trying to attract foreign investment through the offer of natural resources, while at the same time ensuring that it has sufficient taxing jurisdiction over foreign exploitation of these resources. Care must be exercised to not dissuade foreign investment through an overly onerous taxing regime.

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Double taxation is a major deterrent to foreign investment and also a major contributor to an onerous taxing regime. The means by which states ensure that their taxing regimes encourage investment, while at the same time ensuring that its taxing rights upon foreign activities are sufficiently protected, are through the conclusion of Double Tax Agreements (DTAs). DTAs are vital for African states seeking to maintain strong economic progress. The effective functioning of DTAs will make Africa both an investor friendly environment and ensure sufficient protection for the states right to tax. However, whether or not such DTAs function “effectively” is the crucial issue. Only when a states’ natural resources are being sufficiently protected, can it be said that the DTAs concluded are functioning effectively. It is only right that states, which are rich in natural resources, should be placed in a strong position to tax foreign activities involved in the exploitation of such resources.

This dissertation seeks to determine whether or not sufficient protection exists in the DTAs of the three major African states which make up the original members of the East African Community (E.A.C): Kenya, Tanzania and Uganda with reference to their key natural resources. As a result, the analysis will focus on two important articles that exist in the DTA network and which are modelled on the OECD MTC. These two articles are the “permanent establishment” article[1] and the “income from immovable property” article.[2] Therefore, the analysis of whether or not the three East African states have sufficiently protected themselves can be more specifically stated as; an analysis of whether or not these two articles offer adequate scope for those states to be in a strong position to tax the exploitation of their key natural resources.

1.2 Structure and research question

This dissertation seeks to answer the following question: Are the permanent establishment (“PE”) and income from immovable property articles, as used in the Double Tax Agreements of the original partner states of the East African Community, sufficient to protect the taxing rights over their natural resources? Each chapter in this dissertation facilitates the answering of this question.

In chapter 2, an economic overview of Kenya, Tanzania and Uganda is provided, which demonstrates on which natural resources these states are most dependent. The aim of this analysis is to justify the selection of resources which are subsequently used as the basis for answering the research question. It also allows for the determination of the industries involved in these resources so as to make a better judgement on the protection offered within the selected two MTC articles.

In chapter 3, the methodological approach is discussed. This is done by outlining the interpretational position which will be applied to the DTA network of each of the three states. The need for an international approach to interpreting DTAs is justified and the basis for the use of commentaries is explained. The concluded approach stated in this chapter will be the means by which the two articles are understood and tested.

[1] Article 5 of the OECD MTC
[2] Article 6 of the OECD MTC

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Chapter 4 serves to unpack and determine the full implications of both the PE article and the income from immovable property article in the context of the OECD MTC. Both articles are noted for their applicability to natural resources. The impact and overlap that both articles have on each other is analysed. This chapter serves as the theoretical basis for the analysis in the subsequent chapter.

Chapter 5 seeks to answer the main research question. It is within this chapter that the two relevant articles are examined, as contained in the specific DTAs entered into by Kenya, Tanzania and Uganda, in order to determine whether or not the three states have sufficiently protected their natural resources. This is done by identifying the areas within the two articles which are inadequate and offering suggestions as to where special inclusions could be added to expand the scope of the two articles to provide adequate protection over the specific natural resources.

The final chapter provides outlines the conclusions reached from this study.

1.3 Limitations to the study

This dissertation has not consulted the domestic tax legislation of Kenya, Tanzania and Uganda. The approach found in this study has been that of applying the international DTA literature, as informed by the OECD Commentary and supported by recognised tax scholars, to the DTAs found within the three states' natural resources. Therefore no attempt has been made to determine whether the domestic legislation of the three states applies the taxing rights granted in terms of the two articles analysed. Furthermore, the use of international interpretational methodology is justified on the basis that this study is a comparative analysis of three independent states.

In addition, this dissertation is limited to those DTAs concluded by Kenya, Tanzania and Uganda that were in force as at 31 January 2011.

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CHAPTER 2

ECONOMIC OVERVIEW AND NATURAL RESOURCE DEPENDENCE

2.1 Introduction

In order to answer the question as to whether or not Kenya, Tanzania and Uganda have sufficiently protected themselves within their DTA networks, it is first of all necessary to determine on which natural resources these three states are most dependent. In this chapter, an overview of each State's economic climate is briefly discussed after which particular attention is focussed upon those natural resources which are significant contributors to each of these states' economies. This chapter will aid the analysis that follows by gaining a better understanding as to which natural resources are in most need of protection.

2.2 Kenya-Overview

Kenya is known to possess one of the most diverse economies in Sub-Saharan Africa (Youngblood-Coleman, 2010a). It is rich in natural resources such as: Limestone, soda ash, salt, gemstones, fluorspar, zinc, diatomite, gypsum, wildlife and hydropower (Singh 2010). Kenya has also long been thought of as the hub of East Africa with a population of 39 million (International Monetary Fund, 2010), and it is said to possess the region's best trained personnel. Nairobi, the capital city, has good and continuingly improving communication and financial facilities with the region's best transportation linkages, though it is supposed that this advantage is steadily decreasing (U.S. Department of State, 2010a). Kenya has shown a steadily improving growth in real GDP at the turn of the millennium with growth rates of 5.1%, 5.9%, 6.3% and 7.1% in the years 2004 – 2007 respectively. However, real GDP growth contracted to a mere 1.6% as a result of decreased demand for Kenyan exports due to the global financial crisis and political violence in early 2008 (Central Bank of Kenya, April 2010). There are positive signs that the economy could be improving with the Central Bank reporting a provisional growth rate of 2.6% of real GDP for 2010.

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2.2.1 Resource Dependence

Notwithstanding Kenya's abundance in natural resources and its growing skilled labour force, agriculture remains the dominant driving force behind the Kenyan economy. Arable land is therefore their most precious resource with the bulk of their economy highly dependent on agriculture and its products. This makes the Kenyan economy extremely susceptible to exogenous shocks such as a severe lack of rainfall, a problem that severely affected the agricultural sector in early 2008. Agriculture is said to account for the majority of Kenya's GDP and employs about 75% of the labour force (Youngblood-Coleman, 2010a). The Central Bank of Kenya estimated that agriculture contributed 24.4% to GDP during 2009 (Central Bank of Kenya, April 2010).

The products from this sector and upon which the economy is so dependent are that of coffee, tea, horticultural products and sugarcane. These products contributed approximately 75% of total agricultural GDP for 2008 (Kenya National Bureau of Statistics). Coffee, tea and horticultural products together constitute 37% of the value of exports (Central Bank of Kenya, April 2010) and therefore, as far as natural resources are concerned, are the most in need of protection. It is somewhat surprising that mineral exports do not play more of a significant role and that mining as an enterprise hasn't developed into a major economic driving force. The exportation of such commodities is negligible when compared to the agricultural sector. Iron and Soda Ash contributed roughly 3% and 2% respectively to the value of exports for 2007 (Export Promotion Council, 2008). It is a widely held belief that Kenyan mineral deposits remain largely un-explored or un-developed and therefore possess large potential for future growth prospects. The potential for minerals to be exploited through foreign enterprise involvement make it deserving of protection.

Agriculture as reflected through its major industries producing coffee, tea and horticulture will be a main focus of this paper. This industry is of major importance to the Kenyan economy and is also the industry that exploits the dominant share of Kenya's most precious resource namely, arable land. The Kenyan Government would do well to ensure that its DTAs offer sufficient protection of this resource by

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catering for the nature and structure of this industry.

2.3 Tanzania-Overview

Tanzania has long struggled with being labelled as one of the poorest countries in sub-Saharan Africa. Its economy is heavily reliant on agriculture which is responsible for the large majority of its labour force (Youngblood-Coleman, 2010b). Industrial development is constricted due to consistent weaknesses in infrastructure such as bad roads and poor water supply, all of which does little to assist the Tanzanian economy's battle against its deep poverty problems. Tanzania is estimated to possess a population of 43.7 million with a matching total GDP of only 22.31 in US$ billion compared with Kenya's 32.72 US$ billion, which possess a population of 39 million (Babb, 2010a). Notwithstanding the massive challenges that the Tanzanian economy faces, real GDP growth has on the whole been positive, estimated to have reached as much as 5.6% for 2009 and 7.1% in 2008 (Babb, 2010b), which is all the more encouraging after the economy was feeling the after effects of a drop in demand for its exports on the back of the global financial crisis in early 2008 and the rise in the fuel prices.

2.3.1 Resource Dependence

Tanzania has large quantities of natural resources. The mineral potential that exists for its economy is vast. The resources include hydropower, tin, phosphates, iron ore, coal, diamonds, gemstones, gold, natural gas, nickel and arable land (Singh, 2010). However, the main contributing sector to GDP is still agriculture which contributed approximately 25% to GDP (Bank of Tanzania, 2010).[3] Within this sector lies the so-called "traditional exports", which includes: coffee, cotton, tobacco, cashew nuts, tea and cloves. These exports, according to the Bank of Tanzania, is said to have made up 19.2% of total exports an 2008 and 18% in 2009 (Bank of Tanzania, 2010). Horticultural products are said to contribute just 1.5% of total exports with fish and its

[3] This is a position which is sure to improve as Tanzania is viewed as possessing Africa's greatest mineral potential for foreign investment. Gold has of late been the driving force behind this optimism, with there being the belief that Tanzania holds Africa's greatest gold reserves after South Africa and is the third largest producer after both South Africa and Ghana.

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products contributing just over 5% in 2008. This suggests, in similar fashion to Kenya, that land and territorial waters remain valuable resources for the Tanzanian economy with fish also making a noticeable contribution to exports. All of which points to an economy struggling to shake of its socialist past.

However, there is much optimism that this will no longer be the case because of the growing potential of a class of resources of which Tanzania is certainly not in short supply. Unlike its neighbour Kenya, minerals play a substantial role in the area of exports. It is noticeable that the mining industry currently contributes less than 3% to national output; however, it is noted by Babb that the sector has great importance as an earner of foreign exchange through the exportation of gold (Babb, 2010b). Gold exports constituted 32% of total exports for 2008 (Bank of Tanzania, 2010). It is further pointed out by Babb (2010b: 2) that other mining products such as coal and uranium as well as other base metals, diamonds, ferrous minerals and gemstones (incl. Tanzanite[4]) offers further growth potential to this sector. Commercial production of uranium and coal is becoming a real possibility which, if it should eventuate, will bring it closer to the government's aspired 10% contribution of this sector to GDP. Tanzanian minerals and metals are believed to include gold, diamonds, tanzanite, nickel, copper, cobalt, tin, iron ore and coal. Exports remain, for 2009, concentrated in gold. It is believed that gold could have contributed as much as 40% of exports in 2009, increasing in the past year as a result of increased production as well as an increase in gold prices.

If Tanzania is going to realize its growth prospects and future potential in the development of these industries, the respective DTAs with the major trade partners will need to allow enough scope to cover the taxing of the exploitation of these minerals. This makes it important to identify whether or not Tanzania's DTAs sufficiently protect its mineral sectors. The same could be said for its "traditional exports" (outlined above). Although secondary in terms of contribution to overall exports, it is no less in need of protection.

[4] This gemstone is found nowhere else in the world except on the foothills of Mount Kilimanjaro and after processing turns a royal blue adding to its value and necessary protection in order to maximise its benefit to the economy.

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2.4 Uganda-Overview

Out of the three original East African Community states, Uganda has within its territory the richest of natural resources. The country has substantial resources including fertile soils, regular rainfall and sizable mineral deposits of copper and cobalt, and has deposits of limestone, salt and gold (Youngblood-Coleman, 2010c). This all contributes to Uganda possessing significant potential for growth. With a population of 30.7 million, Uganda is said to have a GDP of 15.74 US$ Billion and extremely positive growth rates estimated for 2009 and 2010 to be 7.1% and 7.3% respectively (Babb, 2010a). It has long been the belief amongst developed nations that Uganda appeared poised for rapid economic growth and development at independence in 1962 (U.S. Department of State, 2010b). However, it was the consistent political instability since independence coupled with poor economic management that has as its result a state that remains among the world's poorest and least-developed countries. Notwithstanding this predicament, there still remains much about which to be positive concerning the prospects of the Uganda economy.

2.4.1 Resource Dependence

Uganda, unlike neighbouring Kenya and Tanzania does not have the agricultural sector as the main contributor to GDP, with the services sector enjoying the majority of 46.4% (Bank of Uganda, 2009). Nonetheless it does play an important role, with the Bank of Uganda estimating a contribution of approximately 22% of GDP. However, in similar fashion to that of Kenya, it shares a favourable climate for coffee production, making it a major exporter. This commodity continues to be the main foreign reserves earner for the economy, where the latest figures out of the Bank of Uganda have coffee exports at 14% of its total exports for May 2010 (Bank of Uganda, 2010). The other 3 commodities which make up the so called “traditional exports”, namely: cotton, tea and tobacco make up 12.8 % of total exports. This is followed by gold and other base metals at 10.5% and fish and its products with 10% of exports. Maize as a food crop and horticultural cash crops each make up approximately 3.6% of exports.

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According to the U.S. Department of State there have been significant discoveries of oil in the Albertine Rift in western Uganda in 2008. This would clearly be a very exciting prospect for the Uganda economy and for its development. However, this would also pose a major challenge to the government to ensure that it has implemented sufficient protection.

It is understood that “as of late 2009, the private sector had invested considerably in the oil sector, but production had not yet begun pending further feasibility studies on the funding and construction of the necessary infrastructure to support the industry” (U.S. Department of State, 2010b). This is very positive for Uganda and it is hoped that increased foreign direct investment would result through foreign company involvement.

It is evident that Uganda is the most diversified in its natural resource based exports out of the three East African states. However, this brings with it its own challenges in ensuring that its DTAs go far enough to protect the taxing rights on natural resource exploration and exploitation. The most important industries, therefore, upon which protection would need to be granted is that of coffee, tea, tobacco, cotton, fish and minerals (including gold). The future prospects for oil exploration and exploitation will also soon play a role in this regard.

2.5 Conclusion

As is evident from the above, these three states are certainly in no short supply of natural resources. Kenya has the ideal climate for coffee, tea and horticulture production and hence possesses the fertile land to support its production. Tanzania is endowed with a treasure chest of minerals which is beginning to reflect in the prominence which it plays in terms of its exports. Uganda has a diverse range of resources upon which its economy relies, including fertile land, minerals and potentially oil due to its discovery in late 2009. For these reasons the industries of agriculture and mining will form the main focus of this dissertation as it is those industries, in that order of importance, upon which all three states are dependent. The analysis of whether or not the DTA networks of the three states have gone far

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enough to protect these industries will provide an answer as to whether or not their natural resources are being adequately protected.

CHAPTER 3

INTERPRETATIONAL APPROACH

"'To interpret' is to unfold a text, to bring it to be understood."[5]

3.1 Introduction

The purpose of this chapter is to outline the methodological approach that will be followed in this dissertation. This will be outlined in the context of the interpretational rules applicable to the various Double Tax Agreements (DTAs) of the three East African states. Since this dissertation is not concerned with the analysis of the domestic laws of the respective states and that this is an international comparative study, an international approach to treaty interpretation will be sought to be applied to the relevant DTA Articles which will in turn provide an answer to the main question which this dissertation seeks to answer.

3.2 The International Approach

There is much authority which upholds the position that an international approach should be taken in the interpretation of DTAs.[6] This is because a DTA is an international agreement, the interpretation of which should take place in an international context (Olivier, 2004: 343). The basis of the interpretational approach to all DTAs can be found in the Vienna Convention on the Law of Treaties ("VCLT"). That the Vienna Convention rules are seen to constitute customary international law and used today as a basis for the Interpretation of DTAs, even with regards to states who have not yet ratified the Vienna Convention, is beyond dispute.[7]

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[5] Vogel,1997

[6] See in this regard the Indian case of *CIT v Visakhapatman Port Trust* 144 ITR 146 where it was said: 'In view of the standard OECD Models which are being used in the various countries, a new area of genuine 'International Tax Law' is now in the process of developing.' And also the remarks of Baker (2010:E-2): 'A clear majority of courts in a number of countries have now accepted that double taxation conventions are to be interpreted in accordance with the rules of public international law applicable to the interpretation of treaties, and not by application of the rules applicable to domestic tax legislation.'

[7] See Vogel (1997:35) and the authority cited therein.

In terms of the VCLT,[8] the text of a treaty is of primary importance; the treaty is to be interpreted according to the ordinary meaning of the terms in its context. Subordinate to the textual interpretation is "purposive" interpretation of the treaty. Purposive interpretation assesses the text of the treaty in the context of its objective. However, Vogel (1997:37) provides that such an approach merely gives "light" to the terms of the treaty but should not be applied as an *independent* method of interpretation (i.e. to the exclusion of the textual interpretation). In this regard, according to the OECD Commentary on its general remarks concerning the interpretation of treaties outlined by Olivier (2008: 43):

> "tax treaties aim primarily at the avoidance of double taxation and the prevention of fiscal evasion but also the objective of allocating tax revenues equitably between two Contracting states. Thus, any interpretation achieving these objectives would be preferable to one leading to double taxation or to an inappropriate double exemption".

The intention of the parties to the agreement also plays a role but only if it is supported by the text of the agreement itself as per Article 31(4) of the VCLT. If this approach still leaves the interpretation of an Article ambiguous, obscure or leads to a result which is unreasonable,[9] then cognisance can be taken of other means of interpretation such as the preparatory work of the treaty and the circumstances of its conclusion.[10]

3.3 Basis for the use of the Commentaries

The use of the OECD and UN MTCs and their Commentaries can find its application based upon Article 31(4) of the VCLT.[11] This article states that a special meaning shall be given to a term if it is established that the parties so intended. The reasoning for this is that if the meaning in the Commentaries is different from the

[8] Specifically Articles 31 and 32.
[9] As per Article 32 of VCLT.
[10] See the English case of *IRC v Commerzbank AG* 1990 STC 285 where this principle was confirmed in the context of DTAs.
[11] Though the exact legal foundation of this is uncertain. Possibilities exist which could place the basis for using the Commentary as being an instrument made in connection with the conclusion of the treaty in terms of Article 31(2) or that its use is a supplementary means of interpretation under Article 32. It is submitted that the most persuasive is that adopted above. For a more detailed discussion see Vogel (1997:44).

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ordinary meaning of the words in their context, it is easy to say that the parties, being familiar with the Commentaries, intended that the meaning in the Commentaries should apply and so, in the context, the special meaning merges with the ordinary meaning (Lang 2001: 364).[12]

This principle is also confirmed by the simple fact that MTCs and their Commentaries play an important role in the international tax arena. This is confirmed in the introduction to the OECD MTC Commentary where the following is said in this regard:

> "…the worldwide recognition of the provisions of the Model Convention and their incorporation into a majority of bilateral conventions have helped make the Commentaries on the provisions of the Model Convention a widely-accepted guide to the interpretation and application of the provisions of existing bilateral conventions. This has facilitated the interpretation and the enforcement of these bilateral conventions along common lines. As the network of tax conventions continues to expand, the importance of such a generally accepted guide becomes all the greater".

It seems that the OECD itself never intended for the Commentaries to have a limited role. It is argued by Uckmar (2006:159) that in the case of the interpretation of DTAs concluded between two OECD member states, the OECD MTC and Commentary should be considered as primarily as part of the context. He goes on to argue that the OECD Commentaries will be less significant for treaties between an OECD member and non-member and between two non-member countries. However as far as the OECD MTC serves as the basis for the negotiations of a DTA, it should be considered as part of the "context" as well. Therefore where it is clear that a certain DTA is based on a MTC it will be presumed that the parties intended for the interpretation given in the Commentaries to apply unless a provision differs from the

[12] In the Australian case of *Thiel v FCT* 21 ATR 531 it was said that there is no reason why the OECD Tax Model and Commentary should not be regarded as having been made in connection with and accepted by the parties to a bilateral treaty subsequently concluded in accordance with the framework of the MTC.

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Model in which case the Commentaries will not be considered.[13]

3.4 The use of later versions of the Commentaries

The issue with respect to the existence of Commentaries in existence after a DTA is negotiated is by no means clearly settled. The OECD Committee on Fiscal Affairs (CFA) has stated in its introduction to the OECD MTC (par 33-35) that existing Conventions should, as far as possible, be interpreted in the spirit of revised Commentaries even if those existing Commentaries do not include the precise wording of the newer OECD MTC. However the CFA states further at par 35 that:

> "…amendments to the Articles of the Model Convention and changes to the Commentaries that are a direct result of these amendments are not relevant to the interpretation or application of previously concluded conventions where the provisions of those conventions are different in substance from the amended Articles. However, other changes or additions to the Commentaries are normally applicable to the interpretation and application of conventions concluded before their adoption, because they reflect the consensus of the OECD member countries as to the proper interpretation of existing provisions and their application to specific situations".

It seems that many academic writers are not all in agreement on this point and hold that reference to later commentaries is not permissible.[14] It would be impossible for the purposes of this dissertation to undertake a detailed analysis on this issue considering the divergence of views on this question. However, it is submitted that the comments of Arnold, quoted by Mössner, are extremely helpful on the topic, mainly due to their simplicity:

> "…interpretation is not a simple procedure with rigid rules leading to doubtless results. In this process the Commentary plays an important role as a supplementary means of interpretation, and later changes of or amendments to the Commentary could have an influence on the interpretation as far as they are compatible with the wording of the treaty"

[13] Vogel (1997 Introduction para 35) confirms this principle that Commentaries may be used on the basis that treaty negotiators who use a term contained in the Model Tax Conventions are assumed to have intended to follow the same meaning of the term as used in the MTC.
[14] See Baker (2010:E16) and the sources cited under footnote 1.

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(Mössner 2010:18).[15]

Baker (2010: E-18) states the following, with reference to a possible approach, in this regard:

> "In a pragmatic sense, both the version of the Commentaries existing at the time of the conclusion of the specific treaty and subsequent versions of the Commentaries may be relevant: the former indicating the interpretation which prevailed at the time the convention was concluded, and the latter indicating any change in approach. Both may be relevant, but simply with different weight attaching to the versions".

It is submitted that this represents the correct approach to this issue. Later Commentaries are relevant to the interpretative process. To limit oneself only to the Commentary which existed at the time the specific treaty was concluded is to forget that a DTA is intended to remain in force for some years. It is also to forget that an interpretation of an OECD or UN MTC would develop either in a change of understanding or in clarification. Admittedly one will have to be extremely sensitive to the terms contained in the treaty itself and reference can only be taken of later Commentaries to the extent which the wording of the specific treaty allows. This would serve to indicate that the terms of a provision have a different meaning than that proposed by the Commentary.

A neat summary as to the approach that is followed in tax treaty interpretation can be found in the case of *Memec Plc v IRC* 1996 STC 1336 where it was held that:

- The approach should be purposive and international;
- Regard should be had to the Vienna Convention;
- Recourse may be had to supplementary means of interpretation;
- Subsequent commentaries and decisions of foreign courts have persuasive value only; and
- Recourse to supplementary means of interpretation, international case law and the writing of jurist is discretionary and not mandatory.

[15] Note also the remarks of Avery Jones (Lang 2001: 365): 'I expect that the courts will be willing to look at later Commentaries but if there has been any substantial change in the Commentary since the date of the treaty, they are not likely to pay much attention to them.'

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3.5 Conclusion

The interpretational approach which will be adopted in this dissertation is discussed above. The DTA will be examined firstly by giving the ordinary meaning to the terms which exist. This will be done in the light of the DTAs purpose so as to place its terms in its context. Then, secondly, the ordinary meaning of the DTAs terms' will be confirmed and expressed in the light of either the OECD or UN Commentary depending on which MTC the specific DTA follows. However, meaning will be derived from the Commentaries only as far as the wording of the DTA allows, by taking note of divergence away from the respective MTCs. It follows then that this is the basis upon which the investigation into whether the three states have gone far enough to protect its natural resources, in terms of the Articles, is conducted.

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CHAPTER 4

RELEVANT MTC ARTICLES AND THEIR INTERACTION

4.1 Introduction

Article 6 (“the immovable property article”) of the OECD MTC covers income that is earned from immovable property. It is identical in wording to the UN MTC. All three states that are the subject of this dissertation contain, in almost all their treaties concluded,[16] an Article dealing with income from immovable property which follows similar, if not identical, wording to the OECD MTC Article on immovable property. The immovable property article is highly relevant for purposes of this dissertation since exploitation of natural resources necessarily involve the use of immovable property. This is especially true for agriculture, upon which all three states are economically reliant, and has a direct impact on a valuable natural resource, namely arable land. The same can also be said for mining. The mining for minerals also directly involves the use of immovable property. This is perhaps not as obvious as is the case with agriculture since there are varying degrees in which the immovable property will be involved in a mining enterprise. Nonetheless, the enterprises involved therein, which are in turn directly involved in the states natural resources, may be affected by the immovable property article. It is for this reason that the immovable property article needs to be examined and understood in the context of the Permanent Establishment principle and therefore what follows is an overview of this (the immovable property) article and thereafter the relationship which it has with Articles 5 (“the permanent establishment article”) and 7 (“the business profits article”) of the MTCs.

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[16] The exception being in the treaties concluded with Zambia. All three states have concluded treaties with Zambia but have not negotiated an Article dealing specifically with Income from immovable property, along the same lines as the OECD MTC. Rather, provision has been made to deem income from immovable property to have been derived from a source where the immovable property is situated. See below for the discussion on the DTAs negotiated with Zambia.

4.2 Overview of the Income from Immovable Property Article

The income from immovable property Article entrenches the well established *situs* principle. It is the *situs* of the immovable property (its location) which establishes a close economic connection with the state in which the property is situated and therefore it is accepted worldwide that any income earned from immovable property should be taxed at source.[17] Article 6(1) of the OECD MTC provides the following:

"*Income derived by a resident of a Contracting State from immovable property (including income from agriculture or forestry) situated in the other Contracting State may be taxed in that other State".*

This Article makes taxation at the place of *situs* the priority over all the other distributive rules in the OECD MTC (Vogel 1997:370). In other words all income from immovable property is taxed according to Article 6, including income from business property used in commerce and industry[18] or for independent personal services,[19] even if the enterprise has no permanent establishment situated in the *situs* state. It is important to note that this article only applies to cross-border income. It only applies when a resident of a contracting state derives income from immovable property situated in the other contracting State.[20] When income is earned from immovable property that is situated in the contracting state of which the taxpayer is a resident or in a third state, Article 6(1) does not apply.[21]

The term "immovable property" is to be defined according to the domestic law of the contracting state in which the property is situated.[22] The paragraph nonetheless outlines the type of property which would constitute "immovable property" to provide

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[17] Article 6(1) MODEL CONVENTION and the OECD Commentary (OECD MODEL CONVENTION) par 1 of Article 6. See the whole of Article 6 quoted in the appendix as a reference to this discussion.
[18] Article 6(4).
[19] Though the application of Article 6(1) and (3) to income from independent personal services has since been removed (1992) from the MTC, on only two occasions has the equivalent paragraph in the DTA network for this dissertation been negotiated by omitting personal services.
[20] This is contrary to the OECD MTC of 1963 which stated that: '"Income from immovable property may be taxed in the Contracting State in which such property is situated." The change was brought about in the OECD MTC of 1977.
[21] Such income would fall under Article 21(1) (Vogel 1997:370).
[22] Article 6(2).

for those domestic laws which may apply an unnecessarily narrow definition. This includes property which is accessory to immovable property, livestock and equipment used in agriculture and forestry, certain corporeal rights treated as rights in immovable property and rights to mineral resources in whatever form. Although there is an indication as to what the term "immovable property" encompasses, the term "income **derived** […] **from** immovable property" has no such indication. A definition will also have to be sought under domestic law in order to determine what constitutes income from immovable property.[23] There is an indication that it includes, in terms of Article 6(1), income from agriculture and forestry and in terms of Article 6(3), income derived from the direct use, letting, or use in any other form of immovable property. What is in mind with this Article is the taxation of income from exploiting land or from permitting the occupation of land (Baker, 2010:6-2) and that the *situs* principle applies to any form of use of immovable property.[24]

4.3 Interaction between Article 5, 6 and 7

It is important at this stage to discuss the relationship that Article 6 (income on immovable property) has with Article 7 (business profits) and Article 5 (permanent establishment) since there is indeed much overlap that will occur in certain situations. Both Article 6 and Article 7 can be applied to the same income and therefore an understanding of how these two Articles interact in the context of the MTCs will assist in the analysis of the DTA networks of the three states. Below is a brief overview of Article 7, followed by an overview of Article 5 (as far is relevant to the natural resources considered in this dissertation) and an analysis of the overlap that Article 6 has with Article 5 and 7.

4.4 Overview of Article 7

Article 7 determines which business profits of a non-resident may be taxed in another

[23] Vogel (1997:376) He suggests that the question is not governed by the law of the situs state by Article 3(2) of the MTC which makes it subject to the law of the state applying the treaty.
[24] Paragraph 3 of the MTC Commentary of Article 6: "Paragraph 3 indicates that the general rule applies irrespective of the form of exploitation of the immovable property."

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state.[25] This can only occur if the non-resident carries on business through a permanent establishment (PE) in the other state and if the business profits can be attributable to the PE. In addition, Article 7 also contains in its remaining provisions, general rules or principles for computing the profits that are attributable to a PE.[26] There is extensive literature on Article 7, both in the Commentaries and in that of academic writers, all of which is unnecessary for present purposes to outline. Suffice it to say that Article 7 permits taxation of income attributable to the PE, the "business profits", on a net-basis. Article 5, which defines the term "permanent establishment", acts as a threshold requirement before the state in which the PE is situated may tax the attributable business profits and other types of income.[27] Critical to the application of Article 7 is the determination of the existence of a PE in terms of Article 5.

4.5 Overview of Article 5

Article 5(1) of the OECD MTC, identical in the UN MTC, defines a PE as a fixed place of business through which an enterprise carries on its business, wholly or in part. This is what is commonly referred to as a basic-rule PE definition. Essentially this basic-rule describes 1 of the 3 ways in which a PE can be said to exist. The two other ways in which a PE may be found to exist is if it is found that there is a construction

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[25] Since the term "business profits" is not defined in the MTC, domestic law will have to determine what constitutes "business profits" applicable under Article 7.

[26] These principles include the so called "arms-length" principle (Art 7(2)) which is used to calculate the profits of the PE and the net basis taxation principle (Art 7(3)) which allows the deduction of PE expenses from the profits of the PE. Note in this regard the changes brought about to the wording of Article 7 and its Commentary by the OECD MTC 2010 to bring it in line with the OECD Transfer pricing guidelines. See the preliminary remarks to Art 7 of the OECD Commentary (2010) where it is stated that these changes were brought about in order to bring in a degree of uniformity in the interpretation of Art 7 amongst OECD member states and also to establish a better approach to the attribution of profits to PEs. This approached is proposed to be used in the negotiation of new treaties and the re-negotiation of existing treaties. However, as most states will have an Art 7 based on the old wording, a revised Commentary has also been submitted with the 2010 Commentary based on the old wording.

[27] Such as dividends, interest, royalties and other income which contain "throw-back" rules (i.e. Arts. 10(4), 11(4), 12(3) and 21(2)) with the effect that those types of income are taken out of their respective Articles and made subject to Article 7. See Arnold (2006:6) who regards them not as "throw-back" rules but deeming rules, i.e. deeming income to be business profits even though they are not so for purposes of Article 7.

PE[28] (Art 5(3)) or an agency PE (Art 5 and 6[29]). The basic-rule PE can be divided into three criteria, all of which must be present before a PE can be said to exist in terms of the basic-rule. Firstly there needs to be a **place**; secondly this place must be **fixed**; and lastly there needs to be a **business carried on through** that place, wholly or in part.[30]

4.5.1 Basic-Rule PE

Firstly there must be a "place" of business. It is apparent that there must be some physical presence in the contracting state. The place of business is a tangible asset of a substantial nature which could be in the form of premises or equipment that is used in the business. A "place" which qualifies as a place of business is broadly interpreted as being any "place" in the ordinary sense of the word (Sasseville and Skaar: 2009:24).[31] The OECD Commentary states at paragraph 4.1 that: "the mere fact that an enterprise has a certain amount of space at its disposal which is used for business activities is sufficient to constitute a place of business. No formal legal right to use that place is therefore required". However the OECD Commentary does state that the mere presence of an enterprise at a particular location does not necessarily mean that the location is at the disposal of the enterprise.

Secondly, such a place of business must be a "**fixed**" place. This is generally understood to imply both physical permanence (or a "link between the place of business and a specific geographic point") and temporal permanence (or a certain degree of permanency, i.e. "if the place of business is not of a purely temporary nature").[32] This means that the place of business must stay in the same place for a sufficient length of time.

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[28] However this seems only to be true as far as the UN MTC has been followed with regards to the construction Article. It is argued by Sasseville and Skaar (General Report: 45) that the Construction Article according to the UN MTC seems to be a deeming PE provision. This according to the language used. However the same cannot be said for the same article in the OECD MTC. In other words the basic-rule PE will still need to be met as well as the time period.
[29] In the UN MTC it is Art 5 and 7.
[30] This is the criteria in the OECD Commentary at par 1 to Article 5.
[31] The authors list as examples: Any open air place, e.g. in a forest where logging equipment is demonstrated; the wharf of a shipping enterprise; the place where a drilling ship or rig is located; substantial machinery and equipment; mines quarries and underground pipelines.
[32] Larking (1998:266); quoting from Par. 5 and 6 of the OECD Commentary respectively.

As mentioned, the first implication of the word “fixed” is the need for permanence as seen between the place and a specific geographic point.[33] This does not mean that the place must be fixed in the sense of attaching itself at one particular point on the soil. Rather, the OECD Commentary suggests that a place of business can be held to be fixed where there is a location, within which the activities of the enterprise move, which, due to the nature of the business undertaken, can be identified as constituting a coherent whole **commercially** and **geographically**.[34] Both need to be present before a certain area can be held to constitute a place of business. The OECD Commentary provides an example for geographic and commercial coherence, relevant for purposes of this dissertation, of a mine, clearly constituting a single place of business even though the business activities move from one location to another in what may be a very large mine (Par 5.2 OECD Commentary on Art. 5).

The second implication of a place of business being fixed looks at the degree of permanence which exists between the foreign taxpayer and the place. A PE will not be held to exist where the presence at the place is of a purely temporary nature. However, a PE can still be said to exist if, due to the nature of the business, it exists only for a short period of time (Holmes 2007:151). The OECD Commentary itself recognises the difficulty in drawing this distinction. It does state that short periods of permanency would constitute a PE where the activities performed therein were of a recurrent nature or where activities constituted a business that was carried on exclusively in that country.[35]

Then lastly, the enterprise must carry on a **business** (wholly or partly) **through** the fixed place in order for that fixed place to constitute a PE.[36] This last requirement raises four questions that need to be answered in the affirmative before a PE can be said to exist: Is the activity a “business activity” under the laws of the state applying the treaty and under the treaty itself? Is the business activity the taxpayer’s

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[33] Par 5 of the OECD Commentary of Article 5(1). The emphasis here is on there being a distinct place.
[34] Par 5.1 of the OECD Commentary of Article 5(1).
[35] Par 6 of the OECD Commentary on Art. 5.
[36] This leg of the PE test is commonly known as the “business activity” test.

business?[37] Are the business activities that are conducted "core" business activities and not merely "preparatory" or "auxiliary" activities?[38] Is the business conducted "through" the place of business?[39] Holmes states the following in this regard (2007:151): "The concepts 'permanent establishment' and 'carrying on business' are inextricably bound up together. The carrying on of a business involves the carrying on in a country of virtually any activity related to the business of the enterprise". The place of business of the foreign taxpayer must serve its business activity, as opposed to other income generating activities, and the business activities of the taxpayer must be connected to the fixed place of business. The remarks of Sasseville and Skaar (2009:44) are also to be noted:

> "It can clearly not be required that the entire core business is carried out through the place of business; it is not always required that a core business activity is carried out through the place of business at all. The rationale of this practice is that it is sufficient for the business connection test that an auxiliary business activity is carried on through a place of business, and a core business activity, which is supported by the auxiliary activity, is carried on within the same jurisdiction (but outside the place of business)".

4.5.2 Examples of PEs

The OECD MTC then goes on, in Art. 5(2), to list six examples of PEs or places of business which are *prima facie*, PEs. The article is worded in the following way:

> "The term 'permanent establishment' includes especially:
>
> (*a*) A place of management;
>
> (*b*) A branch;
>
> (*c*) An office;
>
> (*d*) A factory;
>
> (*e*) A workshop;

[37] For example where an enterprise sub-contracts a business activity to somebody else in another country. This would normally not be enough for a PE to exist in that other country unless the foreign enterprise is present in that country and doing business there. (Sasseville, Skaar: 2009:39).
[38] This is illustrated by the "preparatory" or "auxiliary" activities listed in the excluded activities of Art. 5(4) of the OECD and UN MTCs.
[39] Also known as the "business connection" test.

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(*f*) A mine, an oil or gas well, a quarry or any other place of extraction of natural resources".

From the wording of the provision it seems clear that this Article is not there to deem these six places as PEs.[40] The OECD Commentary in par 12 on Art. 5 states the following: "This paragraph contains a list, by no means exhaustive, of examples, each of which can be regarded, *prima facie*, as constituting a permanent establishment". This means that if a foreign enterprise has one of these places at its disposal it will be presumed that it has a PE in the other state unless shown otherwise from Art 5(1). Therefore the basic rule still needs to be met before a PE can be said to exist. Or to put it more succinctly, the business of the enterprise would still have to be "carried on in whole or in part at or through" the relevant place (Holmes 2007:152). In addition to this, the above list is not exhaustive of places which can constitute a PE.[41]

4.6 Overlap between Article 5, 6 and 7

As mentioned at 4.3 above, both Article 6 (income from immovable property) and Article 7 (business profits) can be applied to the same income earned by a non-resident in another contracting state. This happens when the following two eventualities occur: Firstly, when immovable property also qualifies as a PE under Article 5; and secondly when the income from immovable property also constitutes business profits attributable to the PE (Arnold 2006:6).

4.6.1 Immovable property constituting a PE

In terms of the first eventuality, as outlined above (4.5.1), the basic rule defines a PE as a fixed place of business through which the business of an enterprise is wholly or partly carried on. And although the definition of immovable property is left up to the domestic law of the *situs* state, this term will invariably include land, buildings and

[40] This is supported by the OECD Commentary par 12 of Article 5. See also the (Sasseville and Skaar, 2009: 32): "[…] treaties based on the OECD model convention should be interpreted so that the positive list requires the basic rule conditions to be met, unless a state has made an observation to the commentary in this respect".

[41] See Sasseville and Skaar (2009:32): "the positive list may be seen as an illustration of what may constitute a PE if the other conditions in the basic rule are met, but any other facility that meets the general definition in the basic rule may also constitute a PE".

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rights to natural resources.[42] As per the basic-rule definition of a PE, it seems clear that immovable property will be seen as a “fixed place”. The very nature, of even the narrowest definition, of immovable property points to the fact that such property would normally have a degree of permanence at a distinct place. The same can be said when viewed from a different angle. Naturally, when one looks at the examples of PEs in Art 5(2), the places listed there, such as an office, factory, workshop, mine, oil or gas well, quarry, or any other place of extraction of natural resources, all of these will invariably involve the use of immovable property except in special circumstances.[43]

Therefore even at this point it can be said that an overlap between Art 6 and the PE definition often occur. However, this is not enough to make all immovable property a PE. In addition to there being a fixed place, there also needs to be a business that is carried on through that fixed place in order for there to be a PE. This is important in order to understand the extent of the overlap since it is possible for a non-resident to own or lease out immovable property without such person ever carrying on a business through the immovable property. The obvious example where a business is being carried on through immovable property would be a farming enterprise. Land and buildings are in this case being directly used in the farming operations, making that place a PE. Therefore the key question is whether or not there is a business being carried on through the immovable property. Since “business” is left un-defined in the OECD MTC,[44] according to Art 3(2), it would have the meaning that it has under the domestic law of the State applying the treaty. Income from immovable property that is not considered to be a business will result in their being no overlap with Art 7 and only Art 6 would apply. However, when a business is held, under domestic law, to be conducted through the immovable property, then the possibility of

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[42] Article 6(2) of the OECD Model Convention
[43] As a “special circumstance” Arnold (2006:footnote 23) uses the following example: “[…] a ship performing seismic surveys in an assigned area in a country’s territorial waters can be considered to be performing services at a fixed place (the assigned area), but that area of the territorial waters is unlikely to be considered immovable property, although the seabed itself would be”.
[44] Arnold (2006:9) states that for some countries this question is irrelevant since the only thing that matters in this regard is characterisation of the income as “business profits”. This question is what follows above.

the income falling under both Art 6 and 7 will occur.

4.6.2 Income from immovable property as "business profits" attributable to a PE[45]

The difficulty in applying Article 6 to a certain type of income lies in the uncertainty of the term "income from immovable property" situated therein. It is not clear to what extent income can be said to be derived from immovable property and when income is removed far enough from the use of immovable property to exclude it from the scope of Art 6. The Commentary also does not assist in determining the boundaries between what constitutes "income from immovable property" and "business profits". Since "income from immovable property" is un-defined, domestic law will need to determine the meaning. However, Art 3(2) states that the context of the treaty may limit the definition of the term found in domestic law. As outlined in 4.2 above, Article 6 does give one the idea of what income from immovable property includes i.e. income from immovable property includes income from agriculture and forestry; it applies to the use of immovable property in any form; and it also includes income from immovable property of an enterprise. Therefore Art 6 does serve to limit any definition of "income from immovable property" that is found under domestic law. The difficulty arises when the domestic law of a state regards certain income from immovable property as "business profits".[46] An example would be the case of income being earned from an agricultural enterprise.

The implications for classifying income from agricultural activities as business profits are that if the characterisation of the income was determined exclusively under domestic law, there would be no overlap between Art 6 and 7. However, since this is not the case, income can often fall within the scope of Art 6 even though, under domestic law, the income is not considered to be income from immovable property. Arnold (2006) summarises the position at 10:

[45] As discussed in the above it seems that this constitutes a different situation when the two Article overlap simply because some states place a bigger emphasis on the characterisation of the income.
[46] An analysis of the approach of Kenya, Tanzania and Uganda in the characterisation of certain income from immovable property is, although helpful, beyond the scope of this dissertation. For a neat summary of some general trends see Arnold (2006:9).

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> "Because the treaty meanings of income from immovable property and business profits may differ from the domestic law meanings, an item of income may be covered by both Art. 6 (as income from immovable property located in a country) and Art. 7 (as profits from a business attributable to a PE in the country). This would often be the case if income from immovable property within the meaning of Art. 6 (not domestic law) is considered to be business profits under domestic law".

Therefore the above two situations reflect the overlap that is likely to often occur between Art 6 and 7. In the event of the above situation occurring, the approach that needs to be followed is essentially the determination of which Article takes preference and to what extent that Article should apply to the exclusion of the other Article.

4.6.3 Approach to the Article 6 and 7 overlap

In the event of both Article 6 and 7, through the application of Article 5, being applicable to the same income, the result will be that Article 6 applies exclusively to that income. The dominance of Article 6 over the PE concept is derived from Article 7(7), which provides that where profits include items of income which are dealt with separately in other Articles of the Convention, the provisions of those Articles shall not be affected by the provisions of this Article.[47] Therefore, in the example of an agricultural enterprise (which is specifically mentioned in Article 6(1)), the profit that is earned by a non-resident in the other state will be taxed according to Article 6. This is due to the fact that agriculture primarily involves the use of land and income

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[47] Although this is not certain. See in this regard Raul-Angelo and Saccardo (2002:516) who suggest that the provisions of Article 7 can never apply to income from immovable property and therefore it is Article 6(4) with its Commentary which takes all income from immovable property out of the provisions of Article 7 with the result that Article 7(7) has no consequence for the overlap between Article 6 and 7. It is submitted that Arnold (2006) who states at 6 (footnote 7) that this approach is incorrect since it reads into Article 7 a rule that excludes all income from immovable property that constitutes business profits under domestic law, reflects the correct position.
However I am in disagreement with Arnold who states that the implication of this is that Article 6(4) is unnecessary. Rather it is my view that Article 6(4) is relevant in that it clarifies, beyond doubt, that the situs principle takes precedence over the PE principle. Irrespective of whether or not the immovable property is part of the PE, the state in which the property is situated will be entitled to 'primary taxation' (Vogel 1997:386). It still allows income from immovable property to be included under the PE's income, but the right to tax is based on Art 6. Taxing the income under Art.6 has practical consequences in terms of the computation of income; taking it away from being calculated according Art 7(2) – (6) of the Model Convention (2008) and leaving it entirely up to the domestic law of the situs state (Vogel 1997:387).

therefrom should fall under Article 6 despite it being in the context of an enterprise (Vogel 1997:371). However, many other businesses make use of immovable property, especially in the case of industries involved in the exploitation of natural resources. This can be seen with regards to mining (relevant for present purposes). The question which needs to be answered is whether or not, in this case, all the profits of a mining enterprise should fall under Article 6 or whether or not all or some of the income remains within the scope of Article 7.

The answer to this appears to come down to the extent of the role which the immovable property plays in the enterprise. In this regard, the remarks of Arnold (2006:10) are pertinent:

> "The importance of the land in generating the profits of the business varies depending on the nature of the business. Except perhaps in the case of rental income or profits from the sale of immovable property, it is difficult to argue that all the profits of a business are derived from the immovable property used in the business. Even in a farming or forestry business, where immovable property is clearly an essential asset, other assets and labour are also important.
>
> […] The less important the immovable property is to the business, the more unreasonable it would appear to be to include in Art. 6 all of the profits from the business. Although it is clearly unreasonable to include in Art. 6 all of the income from businesses that involve the use of immovable property, no matter how insignificant, neither Art. 6 nor the Commentary provides any basis for making a distinction between businesses using immovable property".

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It appears that Article 6 does not cover all income that is earned in an enterprise that involves the use of immovable property, but rather depends on the significance of the use of the immovable property. Even in the case of an agricultural enterprise, where land is clearly an important contributor to the earning of income, it can be argued that there is some income which is sufficiently removed from immovable property to warrant it not falling under Article 6. It is important to remember that Article 6 gives the *situs* state an uninhibited ability to tax the income. It gives the *situs* state the freedom to compute the income attributable to immovable property entirely according to its domestic law. This is different to Article 7 which provides that the income is to

be attributed on a net-basis i.e. allowance is to be made for expenses incurred of the PE.[48] This is why it is unreasonable to include under Article 6, all income from businesses that merely involve immovable property, without taking into account the extent of use of such property.

Although most, if not all, natural resource extraction or exploitation involve the use of immovable property, Article 5 and 7 are still relevant in including that income which is sufficiently removed from Article 6 but still effectively connected to natural resources. Therefore the concept of a PE (and the attribution of the business profits) remains relevant to natural resources.

In order to determine whether an item of income is “sufficiently removed” from Article 6, domestic law will need to be consulted. Since more specific guidance is needed from domestic law, further conclusions as to how certain income will be treated and distributed between Article 6 and 7 is beyond the scope of this dissertation. No guidance is afforded in the OECD MTC or in the associated Commentary. Therefore, an allocation would need to be made of the income in order to distribute it amongst the two Articles. However, it is difficult to determine how this would operate practically. Both Article 6 and 7 do not provide clear guidance as to where that line between the two Articles is situated, which would serve as the basis for making such a distribution.

4.7 Conclusion

This chapter has demonstrated the content and overlap of Articles 5, 6 and 7 of the OECD MTC. It has been shown that although Article 6 gives the *situs* state an unlimited right to tax the income derived from immovable property of an enterprise, such unlimited right depends on the extent to which the immovable property plays a role in the derivation of such income. Therefore, instances remain in which Article 7 must be applied to income earned by the enterprise, notwithstanding the fact that immovable property is involved in its operations.

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[48] Article 7(3) OECD MODEL CONVENTION (2008).

It is difficult to draw a clear line between Article 6 and 7. Much will depend on domestic law to bring clarity to such terms as “income from immovable property” when derived in the context of a business.

Since Article 6 does not apply to all income of enterprises operating from immovable property, Articles 5 and 7 remain relevant to income derived from the extraction or exploitation of natural resources. The PE principle is still important in the determination of whether Kenya, Tanzania and Uganda have gone far enough in terms of its DTAs to protect the right to tax income earned by foreign enterprises utilising their natural resources.

An analysis of the DTA networks of those three states against the Articles discussed above follows. This analysis is performed in the context of the industries identified in chapter 2 and considering the interaction (demonstrated above) between Articles 6 and 7 (with 5). This analysis will determine whether or not these states have protected their taxing rights over their natural resources.

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CHAPTER 5

DTA NETWORK ANALYSIS

5.1 Income from immovable property article

5.1.1 Agriculture

In terms of agriculture, it was noted that Article 6 envisages income earned from such an enterprise to be covered under this Article. This is seen in the addition of the bracketed words “including income from agriculture and forestry” within Article 6. This was added to the OECD MTC of 1977 but should not be taken to mean that any change in meaning was intended from the OECD MTC of 1963 which did not include these words. Out of the 25 DTAs situated within the network, 13 have an income from immovable property article expressed along similar lines as that found in the 1963 OECD MTC and therefore make no specific reference to “income from agriculture and forestry” being included. However, income from agriculture is clearly included since the 1963 OECD MTC defined “immovable property” as including livestock and equipment used in agriculture and forestry and also, according to Article 6(3), income derived from the direct use is also deemed to be income from immovable property. These 13 DTAs include the above paragraphs[49] which suggest that, to a large degree, income derived by foreign enterprises from agricultural activities carried on in one of the applicable states would fall within the Article regardless of the fact that the language used is similar to the 1963 OECD MTC.

Therefore, in the case of agriculture, where immovable property plays a very important role in the earning of income, the taxing rights on the income earned from this industry is given to the three states based on the income from immovable property article. This means then that Kenya, Tanzania and Uganda have, in a DTA context, sufficiently protected the taxing rights over their arable land (as a natural

[49] The exception to this is the DTA concluded between Kenya and Sweden which includes the equivalent of Art. 6(2) but not that of Art. 6(3). However, it is submitted that the position would remain the same since Art. 6(2) on its own is sufficient to justify this submission.

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resource) by the operation of the income from immovable property article.

Out of all 25 DTAs which Kenya, Tanzanian and Uganda (hereafter “the three states”) have concluded, only 3 DTAs do not have separate income from immovable property articles equivalent to that found in the OECD MTC. Those 3 DTAs which do not have such an Article were those concluded with Zambia in 1968.[50] Other than this peculiarity, all three states have this far-reaching Article.

As discussed above at 4.6.3, it is advantageous to the source state for income to be classified as income from immovable property. The income from immovable property article (Article 6) grants the source state the freedom to determine its own mechanism or policy for taxing this type of income under its domestic law. It is not a restricted distributive rule, unlike business profits in terms of Article 7.

Article 6 also does not require the foreign enterprise to have a PE in the state and therefore, as long as the income earned by the foreign enterprise can be defined as “income from immovable property” under the domestic law, the income will fall within the source State’s taxing jurisdiction.

Since this Article has largely been adopted by the three states, it is submitted that Kenya, Tanzania and Uganda have placed themselves in a suitable position as regards the right to tax the proceeds from those foreign enterprises extracting their natural resources to the extent that the income is derived from the use of immovable property. Certainly the industry of agriculture inherently involves the extensive use of immovable property and is likely to be incorporated in the scope of Article 6.

5.1.2 Mining

In terms of mining, however, the position in the context of Article 6 is less straightforward. As outlined earlier (see chapter 4 above) as regards the overlap between Article 6 and 7, much depends on the role that immovable property plays in the enterprise, which serves to distinguish the two articles from each other. In the

[50] See the discussion on this below.

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case of mining, clearly immovable property (the mine with its mineral deposits) plays an important role in a mining enterprise. However, it would be unreasonable to include under Article 6 all income earned by a mining enterprise no matter how remote the connection between the immovable property and the income. This is a question of domestic law since it would be the domestic law of Kenya, Tanzania and Uganda that would determine what constitutes "income from immovable property" under Article 6(1) of the MTC or its equivalent in the DTA network.

The income from immovable property article has an important role to play in the case of mining, especially for those foreign enterprises whose income earning operations within the three states is closely linked with immovable property. For example: a foreign enterprise whose income is derived solely from leasing out land used for mining; or where a foreign enterprise receives fixed or variable payments as consideration for the working of mineral deposits owned by it in the source state. These types of foreign enterprise activities carried out in any of the three states would be adequately covered by the income from immovable property article. Therefore, the fact that all three states have included within their DTA network an income from immovable property article ensures the right to tax the income from that type of foreign involvement in their mineral resources without the foreign enterprises involved necessarily having much of a presence in their territories.

5.1.3 Conclusion

In summary, Kenya, Tanzania and Uganda have, for the most part, included an article in their DTA network in similar fashion to that found in the MTC. This means that sufficient protection exists, at a primary level,[51] for its arable land and minerals. However there is the peculiar situation of the DTAs which all three states concluded with Zambia. This deviation is considered below.

[51] The word "primary level" is used to categorise that type of foreign involvement which exists in the three states where the link between immovable property and the income earned is strong; such as is the case with the examples mentioned above. See below the discussion on the level of protection which the three states have in the context of the PE Article. The PE article would seek to protect the three states at a secondary level, where certain income earned by a foreign enterprise is sufficiently removed from immovable property causing it to fall under the business profits article.

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5.1.4 An exception - DTAs concluded with Zambia

As mentioned at 5.1.1, the DTAs that all three states have concluded with Zambia do not contain a specific Article dealing with income earned from immovable property as per the OECD MTC. Rather there is an Article (XV(4)) within the three DTAs which states the following:

> "For the purposes of the present Convention: Income from immovable property (including income derived from the alienation of such property) and royalties paid in respect of the operation of a mine, oil well, quarry or of any other place of extraction of natural resources, shall be treated as derived from sources within the Contracting State in which such immovable property, mine, oil well, quarry or place of extraction of natural resources is situated".

What is important to note in this paragraph is that it seeks to deem income from immovable property to be from a **source** within the state where the property is situated. There is no other mention of income from immovable property and therefore no clear link exists between this deeming rule and another distributive rule encompassing income from immovable property. For example, one would have expected a separate article (dealing with income from immovable property) which incorporated the concept of source in one form or another. Rather, the source concept seems to be linked to a paragraph in the business profits article which prohibits industrial or commercial profits from being attributed to a PE if from a *source* outside the PE state.[52]

The function of Article XV(4) appears to be that it ensures that income from immovable property situated within the PE state will always be attributed to the PE. This suggests that income earned by a resident of Zambia, from immovable property situated in one of the three state, will be treated as business profits and will need to fall under that Article's requirements. There appears to be no distributive rule dealing specifically with income from immovable property. The lack of such a rule implies that

[52] This is found in Art IV 2(b) of the three DTAs. There is also reference to source in Art. VI 3 dealing with dividends; prohibiting tax on dividends being levied by the state in which the source of income is earned by a resident of the other state.

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the *situs* principle does not apply. Rather there will need to be a recognised PE, as defined, before the three states will be in a position to tax the income earned by Zambian residents on immovable property situated in the other three states.

This state of affairs negates the advantages that an article drafted along the lines of the MTC offers. Namely, the ability for the *situs* state to determine its taxation rules exclusively under its domestic law without being limited by a distributive rule itself, and the right to tax this type of income not being dependant on the existence of a PE in the *situs* state. The result then seems to be that income from immovable property earned by a Zambian resident will be dealt with under the business profits article and subject to that distributive rule's mechanism for determination.

This is certainly not desirable from the point of view of Kenya, Tanzania and Uganda especially in its protection of land. The income from immovable property article of the OECD MTC enables the source state to be placed in a strong position to tax the income earned from immovable property. Since agriculture is covered by Article 6 (see above), the three states will lose the benefit that this article offers. Moreover, before Kenya, Tanzania or Uganda can be placed in a position to tax any income earned of its land, a Zambian enterprise would need to qualify as a PE under the treaty making it more burdensome for them to be placed in a position to tax such proceeds. This results in less protection being offered to the taxation of income from arable land.

The DTAs concluded with Zambia will also result in less protection being offered in the area of mining for the three states. Zambian enterprises that are involved in the three states' mineral deposits will need to have a significant presence in the form of a PE. The advantage of catching this involvement within the tax net of the three states has been lost because a Zambian enterprise will not require a presence within their territory. In addition, the three states have foregone the advantage of determining its taxing regime exclusively under its domestic law, separate from the distributive rule in the DTA. This is seen in the business profits article where all income which originates out of the mining industry will fall under the business profits distributive rule. The business profits rule prescribes the method of attribution of profits and the deduction

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of business expenses.[53] Although this is seen as a legitimate restriction in international tax on the source country's taxing mechanism in the context of business profits, it could be argued otherwise when dealing with income from immovable property. Since there is a close economic connection between immovable property and the state in which it is situated, it could be argued that the source state should be able to determine exclusively under its domestic law the taxing regime applicable to income earned from immovable property. This advantage Kenya, Tanzania and Uganda possess in the bulk of the DTAs which they have negotiated except in the DTAs concluded with Zambia.

It is recommended that the DTA concluded with Zambia be re-negotiated to take hold of the advantages that a separate income from immovable property would provide for the three states, as outlined above. Perhaps the fact that the DTAs concluded with Zambia are the oldest within the three states DTA network point to the fact that this DTA would need to be re-visited to bring it in line with the MTCs.

5.2 PE Article Analysis

The Permanent Establishment principle is relevant for the purposes of this dissertation because the income from immovable property article does not apply to all income earned by a foreign enterprise that makes use of immovable property. The less important the role played by immovable property in a foreign enterprise, the less likely all the income earned will be included under the income from immovable property article. However, it is difficult to draw an exact dividing line between the two articles since the phrase "income from immovable property" in Article 6(1) of the MTC is to be defined according to domestic law and it will also be applied to a multitude of different business models that could exist in the three states. The remarks of Arnold (2006:10) express the solution aptly:

> "If it is inappropriate to apply Art. 6 to all of the profits of businesses using immovable property and inappropriate to exclude from Art. 6 all of the profits of businesses using immovable property, the only alternative is to allocate some of the profits of such a business

[53] Art IV (2), (3) and (4) of the respective DTAs concluded with Zambia.

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to the immovable property for purposes of Art. 6".

There would need to be an apportionment of an amount between the two articles in order for the effects of those two articles to take their course. It is difficult to determine how this will be done since much will be dependent on the facts and circumstances of a particular case. However, what is important to maintain is that the PE Principle still plays a very important role for Kenya, Tanzania and Uganda. It needs to be determined whether or not the DTAs negotiated cast the tax net sufficiently wide enough to include income from foreign enterprises using natural resources which will not be included in the scope of the income from immovable property article. This analysis will take place by looking at the PE articles within the DTA network of the three states. The specific question to be answered in this section is whether or not the language of the PE articles' offers further protection to the three states resources of land and minerals.

5.2.1 Basic Rule PE

All 25 DTAs concluded by Kenya, Tanzania and Uganda contain the basic rule definition of a PE along the same lines as the OECD and the UN MTCs. As outlined above in the overview of Article 5, the existence of a PE is dependent on three conditions being satisfied: there needs to be a place, that place must be fixed (both in terms of physical attachment to the land and temporal permanence of the activity) and there must be a business activity carried on through that place.

All foreign enterprises that conduct agricultural activities within the three states, whereby immovable property such as land, buildings and agricultural equipment are naturally being used, will meet these conditions and generally be considered to constitute PEs. Agricultural activities conducted in this way are inherently "places of business", "fixed" and would constitute a "business activity" in the source state. The same can obviously be said for most mining enterprises which conduct activities at a mine situated within one of the three states. The assumption here is that the place where the extraction of certain minerals is taking place is at a fixed place (in terms of both forms of permanence) and that core business activities are being conducted through that place.

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However, there may be situations where the basic principles of the PE definition do not offer sufficient protection to the resources of fertile land and minerals. There may indeed be foreign activities involved in these resources which might escape the basic rule definition of the PE. It is to these resources that attention is focussed below. An examination of the possible shortcomings of the basic rule definition with regards to the industries of agriculture and mining is performed below to determine whether or not specific protection has been provided within the DTA network.

5.2.2 Agriculture

The economic overview earlier demonstrated that agriculture is a vital industry for all three states. It is submitted that every effort should be made to ensure that any significant foreign enterprise earning income from the use of these states arable land should generate a PE for such enterprise. However, there is value in making the PE article clear, through the wording of a specific treaty that agricultural activities are to constitute a PE. This is needed in the eventuality of certain agricultural activities, perhaps lacking geographic or commercial connection in the states or conducting only preparatory or auxiliary services, preventing a PE from being recognised in terms of the basic definition. The negotiators of a treaty can agree to include agricultural activities specifically under the equivalent of Art 5(2) of the MTCs within a DTA. This would be a positive move since the special inclusions article regards places listed as constituting *prima facie* PEs. Prima facie PEs are those places listed in the special inclusions article which are presumed to constitute a PE unless there are factors which show otherwise. Factors which would show otherwise would be those elements of the basic rule definition (outlined above at 4.5.1) that serve to qualify a place as a PE. Therefore the implication is that the basic rule definition still needs to be met. However, including agricultural activities within the special inclusions article remains important. It is because, through this Article, an intention is communicated on behalf of the negotiators that activities related to agriculture are generally regarded as fixed places of business which would go a long way to

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alleviate the uncertainty regarding the permanence of the activity.[54]

This has occurred in some instances within the DTA networks of Kenya, Tanzania and Uganda. With regards to the PE Article found in the Kenyan DTA network, of the 8 DTAs concluded, in every situation except for one,[55] there was the provision: “a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on”, listed under the inclusion list of the PE article. In terms of Tanzania, there has not been a blanket inclusion as was the case in Kenya. However, in the DTA concluded with India the following provision was listed in the equivalent of Article 5(2): “a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on”. In the DTAs concluded with Italy and Zambia, a similar provision was provided, namely”: “a farm or plantation”. Apart from these three instances, out of the 9 DTAs concluded, no further provision was made to protect its arable land. Uganda has on only 2 occasions[56] specifically provided for a farm or plantation as an example of a PE.

This lack of clear inclusion of agricultural land as a PE creates a potential for the State to lose taxing rights, particularly for Tanzania and Uganda. Since arable land is such a valuable resource for all three states, one would expect there to be a blanket specific inclusion of agricultural activities across the whole DTA network. The specific inclusion of: “a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on”, offers greater protection than the briefly worded: “a farm or plantation.” This is because the former version is worded in broader language. Not only would a farm or a plantation be considered *prima facie* to constitute a PE but also other places where agricultural or related activities are carried on. This extends the protection that the basic rule definition offers the three states in terms of its arable land and would serve to catch those activities allied to

[54] See above where Holmes (2007:152) seems to suggest that often the only aspect of the basic rule PE that would still need to be determined is whether or not the business of the enterprise is “carried on in whole or in part at or through” the relevant place. It is submitted that Holmes is not suggesting that the permanence enquiry falls away. Rather it would provide a strong presumption in favour of such a place being permanent within the source state.

[55] The exception being in the DTA concluded with Zambia where, under the examples of PEs provision, there is simply the phrase:”a farm or plantation”.

[56] India and Zambia. Zambia with the simple: “a farm or plantation”.

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farming which perhaps don't make use of a "fixed" farm or plantation in the ordinary sense. The short version of "farm or plantation" appears for the most part superfluous since such a place would, in any event, constitute "fixed" places of business under the basic rule definition. This is perhaps because of the time when the DTAs were negotiated. The older treaties for the most part contain the short version and therefore the inclusion is perhaps there merely for clarification purposes as to what constitutes a PE.

Kenya has managed to negotiate 7 of its 8 DTAs with the broader version which puts them in a favourable position as far as its arable land is concerned. Both Tanzania and Uganda have only provided for the broader version in one DTA, in each case being the DTA concluded with India. It is the treaties that all three states have concluded with Zambia and the DTA between Tanzania and Italy which contain the short version. It would be in the interests of Tanzania and Uganda to follow the example of Kenya and adopt the broader version within its DTA network more extensively. It would also be to all three states advantage if they re-negotiated the old DTAs (concluded in 1968) which all three have concluded with Zambia.[57]

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5.2.3 Mining

Similar to agriculture, mining activities carried out in a normal way appear included in the basic definition of a PE. Where a foreign enterprise establishes a fixed mine within the territory of the three states and engages in the extraction of minerals for a significant period of time (i.e. not of a purely temporary nature), this will be a PE in the source State. The OECD Commentary confirms that although such activities may not take place at one specific point within the source state but are often moved between neighbouring locations, the place where such activities occur can still be regarded as "fixed":

> "A mine clearly constitutes a single place of business even though business activities may move from one location to another in what may be a very large mine as it constitutes a

[57] Specific mention was made of this need above in the context of the Income from Immovable Property Article.

single geographical and commercial unit as concerns the mining business".[58]

Nonetheless, as was the case for agriculture, it would still be necessary for all three states to ensure that all activities concerning the exploitation of its mineral resources, regardless of how they are conducted, should be brought within the PE definition. This is because it is by no means certain that all mining activities will operate in the same manner. Treaties of these states should make it clear that all places that are engaged in the exploitation of mineral resources are considered PEs despite the fact that they may lack the geographic coherence to make the place "fixed" under the basic rule definition. Simply put; the three states cannot rely on the principles encompassed in the basic rule definition alone. They would need to expand the definition. This, as was the case with agriculture, has been done in some of the DTAs concluded by these states (but not all the DTAs).

All three states have included Art. 5(2) (f) of the OECD MTC within their DTA network. The paragraph is as follows: "The term 'permanent establishment' includes especially: *f)* a mine, an oil or gas well, a quarry or any other place of extraction of natural resources". The OECD Commentary on this paragraph states the following: "The term 'any other place of extraction of natural resources' should be interpreted broadly. It includes, for example, all places of extraction of hydrocarbons whether on or off-shore".[59] The rich variety of minerals which the three states possess would be covered by this interpretation and therefore all activities which are focussed upon mineral extraction found within the territory of the three states would be covered by this inclusion.

Nonetheless, there are 7 treaties which have gone further than this by having a special inclusion as follows: "an installation or structure used for the exploitation of natural resources". Uganda has in 5 of its 8 DTAs made such an inclusion, whereas Tanzania made only one such inclusion in its DTA concluded with South Africa (see Analysis Tables). It is not certain whether or not this deviation from the OECD MTC has a significant impact of the broadening of the PE concept. There is no guidance in

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[58] Par 5.2 on Art. 5.
[59] Par 14.

the Commentaries regarding the use of the word "exploitation" and therefore an understanding of the term will have to be derived from the plain meaning of the term. Perhaps by adding the word "exploitation" a source state is not restricting itself to the core business activity of extraction but to any activity which seeks to take advantage of a source states' natural resources. Therefore the term is possibility widening the application of the traditional Art. 5(2) (f) as found in the MTC. This could serve to provide a source state with better protection regarding its natural resources and is perhaps an advisable inclusion, particularly for the three states, when seeking to ensure that its PE definition is flexible enough to cover all forms of exploitation of natural resources.

What is a less certain position is that of exploration activities conducted by foreign enterprises before the actual extraction activities commence. The exploration for minerals is an important part of the production process with foreign enterprises often spending considerable periods of time engaged in exploration activities long before access to the ore body is constructed and mining commences. For this reason, foreign enterprises may have already maintained considerable presence within the three states without having engaged in any activities of extraction and therefore, with all likelihood, not having a PE within the territory. This is because exploration activities are preparatory in nature and what Art 5(2) (f) has in mind are core business activities of extraction. Sasseville and Skaar (2009:42) state the following in this regard:

> "A distinction should be made between extraction of natural resources (oil, natural gas, etc.) for own (or somebody else's purpose) on the one side, and exploration activities for own purposes on the other side. Exploration for own purposes should be considered a preparatory or auxiliary activity with the consequence that no PE exists under treaties based upon the OECD Model Convention. However, exploration carried out for third parties qualifies as a core business activity (for the party carrying out the exploration, but of course not for the other party)".

It is not only the fact that exploration activities may not be considered to be core business activities which may disqualify them under the basic rule. In addition, the fact that such activities are often not conducted at one specific geographic point but

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move between different locations, would cause there to be a lack of geographic coherence under the basic rule.[60] Therefore, if the three states are to ensure tax from such operations, it would do well to make a special inclusion of such activities within its examples of PEs paragraph.

Unfortunately this inclusion of "exploration" of natural resources in the PE definition does not exist throughout the DTA network of the three states. In only three treaties has there been included: "an installation or structure used for the exploration […] of natural resources" as an example of a PE. These three inclusions were only concluded by Uganda with Mauritius, South Africa and the United Kingdom respectively. It would be necessary for such a paragraph to be the norm throughout the DTA network so as to make it clear (through the plain language of the terms used) that it was within the intention of the negotiators to a treaty for such activities to constitute a PE. Minerals are far too a valuable resource for all three states to run the risk of allowing exploration activities to escape the "PE net".

What becomes immediately apparent when analysing the DTA network of the three states is the lack of uniformity in its specific inclusions with regards to mining. Again, as was the case with agriculture, one would have expected for the three states to ensure in all its DTAs that activities focused upon its minerals would be covered. Perhaps the fact that mining makes up only a small share of Kenyan GDP is a reason for there being no special inclusion of mining activities within its DTA network. However, this fact alone cannot justify this state of affairs since Kenya's mineral potential is vast and untapped and therefore attention will undoubtedly increase in this area by foreign enterprises. Kenya should re-visit and perhaps re-negotiate their existing treaties as regards the exploitation and extraction of mineral resources.

Perhaps what's most surprising is that Tanzania with all its reliance on its minerals (mostly gold) for its export earnings have not made more inclusions apart from that

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[60] The OECD Commentary itself, at par. 15 of Art. 5, recognises the uncertainty regarding exploration activities. It suggests that states, if so agreed, deem such activities to either be carried on through a PE or not so.

found in the treaty concluded with South Africa. This treaty was concluded in 2005, the latest within its DTA network. However, the other DTAs which it has concluded are relatively old with 7 out of 9 being concluded between the years 1968 and 1979. It is submitted that Tanzania should update its negotiated DTAs along the same lines as that concluded with South Africa.

Uganda has in 5 of its DTAs sought to increase the protection of its minerals through the term "exploitation". This is a positive step and should be followed by the other three states. However Uganda would do well to re-negotiate its other DTAs which do not do likewise in order to continue this trend. The issue of including exploration activities is significant for all three states, particularly for Tanzania and Uganda who rely heavily upon mineral production. Although Uganda has sought to list exploration activities as an example of a PE in three of its treaties, it should seek to include such activities in all of its treaties. The same would apply for Tanzania who have made no such mention.

5.3 Conclusion

This section has highlighted the areas where the DTA networks of Kenya, Tanzania and Uganda have failed to offer sufficient protection for their natural resources in the context of the income from immovable property article and in the PE article. Although it has been seen that there is a certain level of protection which exists when viewed against the backdrop of the basic principles of the OECD MTC, there is nonetheless significant room for further extending such protection of key natural resources (as identified). The income from immovable property article cannot be solely relied upon to protect the three states' resources (of arable land and minerals). The PE article plays an important role in including those activities not considered to be "income from immovable property". Moreover, the basic rule definition of a PE, as informed by the OECD Commentary, is also not a sufficient means of protection of natural resources. It was submitted that the three states negotiate additional inclusions to its PE articles in order to widen the net of activities which would be brought under the PE principle.

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CHAPTER 6

CONCLUSION

This dissertation has sought to answer the question of whether or not the PE article and income from immovable article ("the two articles") adequately protect the three states natural resources. The analysis has sought to answer this question through exploring the implications that these two articles have for the resources of arable land and minerals. This was done not only on the basis of how the two article are worded according to the OECD MTC but also as they have been worded within the DTA network of the three states.

Based on the analysis, it is submitted that although there is protection in the clauses in existing DTAs, it is by no means sufficient. It was shown that since the resources of arable land and minerals are vitally important for the three states, greater protection would need to be granted through the wording of the two articles. The two articles, as worded by the OECD MTC, are insufficient in and of themselves to offer the kind of protection that Kenya, Tanzania and Uganda require. It was therefore proposed that these three states seek to re-negotiate those treaties which are lacking in terms of protection. The most notable treaty which needs to be re-negotiated is the treaty that all three states concluded with Zambia. It is the oldest of the treaties within the DTA network and is largely outdated and out of step with current international DTA standards.

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Although there were some innovative inclusions which the states had negotiated within the two articles, which would serve to broaden either the income from immovable property article or the PE article, it was surprising that these inclusions were not adopted throughout the DTA network. The protection which existed was largely inconsistent. This could be due to a two related factors:

Firstly, it could be that Kenya, Tanzania and Uganda has a "weak" position at the negotiation table. That is to say that they were unable to influence the negotiation of their treaties with the other states in a more favourable manner as far as their natural

resources are concerned. Secondly, yet related to the first, one has to question whether the treasury departments of these three states possess the necessary international tax knowledge which is required to properly guard against foreign exploitation of natural resources without strong taxing rights. Perhaps it is due to the fact that these states have in the past been ill-equipped to remain abreast of the ever changing international tax landscape and therefore the ability to successfully negotiate DTAs that sufficiently protect their natural resources have been weakened. There are signs that this could be about to change with some of the more recent DTAs negotiated containing the more innovative provisions which serve to expand the scope of the two article relevant for this dissertation. It is hoped that this will continue for the sake of greater protection in the future.

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APPENDIX A

ARTICLE 5 OF THE OECD MODEL TAX CONVENTION

Permanent establishment

1. For the purposes of this Convention, the term “permanent establishment” means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term “permanent establishment” includes especially:

a) a place of management;

b) a branch;

c) an office;

d) a factory;

e) a workshop, and

f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

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ARTICLE 6 OF THE OECD MODEL TAX CONVENTION

Income from Immovable Property

1. Income derived by a resident of a Contracting State from immovable property (including income from agriculture or forestry) situated in the other Contracting State may be taxed in that other State.

2. The term "immovable property" shall have the meaning which it has under the law of the Contracting State in which the property in question is situated. The term shall in any case include property accessory to immovable property, livestock and equipment used in agriculture and forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources; ships, boats and aircraft shall not be regarded as immovable property.

3. The provisions of paragraph 1 shall apply to income derived from the direct use, letting, or use in any other form of immovable property.

4. The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise.

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APPENDIX B

Analysis table for specific protection in the PE examples paragraph for Kenya

No	1	2	3	4	5	6	7	8
Country	Canada	Denmark	Germany	India	Norway	Sweden	U.K.	Zambia
Conclusion date	27-Apr-83	13-Dec-72	17-May-77	12-Apr-85	13-Dec-72	28-Jun-73	31-Jul-73	27-Aug-68
'an installation or structure used for the exploitation of natural resources.'	No	No	No	No	No	No	No	No
'a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on.'	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No
'a farm or plantation.'	No	No	No	No	No	No	No	Yes
an installation or structure used for the exploration of natural resources.'	No	No	No	No	No	No	No	No

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Analysis table for specific protection in the PE examples paragraph for Tanzania

No	1	2	3	4	5	6	7	8	9
Country	Canada	Denmark	Finland	India	Italy	Norway	S.A.	Sweden	Zambia
Conclusion date	15-Dec-95	06-May-76	12-May-76	05-Sep-79	07-Mar-73	28-Apr-76	22-Sep-05	02-May-76	02-Mar-68
'…any other place for the … exploitation of natural resources'	No	No	No	No	No	No	Yes	No	No
'a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on.'	No	No	No	Yes	No	No	No	No	No
'a farm or plantation.'	No	No	No	No	Yes	No	No	No	Yes
an installation or structure used for the exploration of natural resources.'	No	No	No	No	No	No	No	No	No

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Analysis table for specific protection in the PE examples paragraph for Uganda

No	1	2	3	4	5	6	7	8
Country	Denmark	India	Mauritius	Netherlands	Norway	S.A.	U.K	Zambia
Conclusion date	14-Jan-00	30-Apr-04	19-Sep-03	31-Aug-04	07-Sep-99	27-May-97	23-Dec-92	24-Aug-68
'an installation or structure used for the exploitation of natural resources.'	Yes	No	No	Yes	Yes	Yes	Yes	No
'a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on.'	No	Yes	No	No	No	No	No	No
'a farm or plantation.'	No	No	No	No	No	No	No	Yes
an installation or structure used for the exploration of natural resources.'	No	No	Yes	No	No	Yes	Yes	No

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