International Environment House 2
Chemin de Balexert 7-9
POB 228, 1211 Geneva 19
Switzerland
Tel.: +41(0)22 791 80 50
E-mail: south@southcentre.int
Website: www.southcentre.int

South Centre Comments on Draft Model Rules for Nexus and Revenue Sourcing

I. Background

The South Centre is the intergovernmental organization of developing countries that helps developing countries to combine their efforts and expertise to promote their common interests in the international arena. The South Centre was established by an Intergovernmental Agreement which came into force on 31 July 1995. Its headquarters are in Geneva, Switzerland.

The South Centre in 2016 launched the South Centre Tax Initiative (SCTI). This is the organisation's flagship program for promoting South-South cooperation among developing countries in international tax matters.

The South Centre offers its comments on the Draft Model Rules for Nexus and Revenue Sourcing. As a procedural matter, the extremely rapid pace of discussions is a matter of great concern for developing countries, a matter also raised by the African Tax Administration Forum (ATAF).[1] While an urgent solution is needed to the taxation of the digitalization of the economy, this must mean one which incorporates the interests of developing countries.

Providing lengthy policy documents to Inclusive Framework delegates for inputs with minimal response time, sometimes just a single day, will have the practical result of the Two Pillar solution reflecting solely the interests of developed countries and snatching away the taxing rights of developing countries. This will further undermine the legitimacy of the Two Pillar solution, which is already on shaky ground, and further encourage developing countries to ignore Pillar One and opt for alternative measures, which they are in their full sovereign rights to do.

The South Centre therefore strongly urges that delegates from developing countries be given adequate response time for documents, and the same principle must be applied for documents provided for public consultation.

II. Specific Comments

The South Centre offers its comments on the Draft Model Rules for Nexus and Revenue Sourcing.

Definition of Intangible Property

The draft definitions of copyright, copyrighted work and intangible property on page 34 exclude computer programs. This aspect of the Model Rules contradicts international law, specifically Article 10 of the WTO Agreement on Trade related

[1] https://www.ataftax.org/itr-global-tax-50-2021-22-logan-wort

SOUTH CENTRE
International Environment House 2
Chemin de Balexert 7-9
POB 228, 1211 Geneva 19
Switzerland
Tel.: +41(0)22 791 80 50
E-mail: south@southcentre.int
Website: www.southcentre.int

Aspects of Intellectual Property Rights and Article 4 of the WIPO Copyright Treaty (1996). It also has implications on existing tax treaties which provide for the taxation of payments for computer software as royalties under Article 12. A total of 474 treaties in force at present tax software payments as royalties, with many of them linking software to copyright. Such an exclusion would undermine such existing treaties and potentially deprive both developed and developing countries of an important source of revenue.

Recommendation: The definitions of copyright, copyrighted work and intangible property should include computer programs.

Services Connected to Tangible Property in International Waters Or International Airspace

The draft rule states that services connected to tangible property are sourced to the place of performance of the service. The reliable indicator says this will be where the tangible property is situated.

Where the service is performed in international waters or airspace, the draft rule then states the tangible property will be "deemed" to be situated at the Location of the Customer when the service is performed. The Commentary will ostensibly confirm that the location of the customer will be based on their tax residence.

The example provided speaks of repairs to an oil rig in international waters.

Applying this rule would then mean that the revenue from such repairs to the oil rig would be sourced to the residence jurisdiction of the company providing the oil repairs. This has negative implications for countries who may lose revenues from economic activities taking place "offshore" or just outside their maritime zones.

Tail End Revenues

The residual revenues from sale of finished goods through an independent distributor after applying the Reliable Indicators and the Regional Allocation Key are the "Tail End Revenues" (TERs). The Model Rules have the right focus on ensuring these should be as small as possible. The higher the TERs, the less accurately revenues will be sourced. These must be even lower than 5%.

However, the draft Rules under Part 3 B do not provide for any penalty if the MNE or the Covered Group fails to take "reasonable steps" to reduce the size of the Tail End Revenues. Thus, there is no real incentive for them to change their behaviour.

SOUTH CENTRE

International Environment House 2
Chemin de Balexert 7-9
POB 228, 1211 Geneva 19
Switzerland
Tel.: +41(0)22 791 80 50
E-mail: south@southcentre.int
Website: www.southcentre.int

Recommendation: The Rules must penalize non-compliant MNEs. Two possible options are retroactive taxation through an amended Amount A filing, or increased revenue sourcing to the Low-Income Jurisdictions.

****