

Research Paper



DOUBLE TAX TREATIES: AN EMPIRICAL ANALYSIS

Nandini N. Math¹

¹Research Scholar, Department of Studies & Research in Commerce, Gulbarga University, Kalaburagi -585106, Karnataka, India

Dr. Basavaraj C.S²

²Professor, Department of Studies & Research in Commerce, Gulbarga University, Kalaburagi -585106, Karnataka

ABSTRACT

In the present paper the researchers have empirically analysed the purpose and impact of Double Tax Avoidance Agreements by studying 194 respondents – tax consultants and experts. The researchers have highlighted the structure of UN and OECD Model Tax treaties. In their analysis the researchers have categorised the issues for the study as general issues relating to Double Tax Treaties and General issues relating to Double Tax Treaties vis-à-vis India. The study reveals that the Double Tax Treaties are the essential features of International Tax Structure in the globalised era and they serve a positive role in enhancing international economic transactions. The researchers suggest that Double Tax Treaties signed prior to the globalisation of Indian economy need to be modified so as to make them more suitable for the present day requirements.

KEY WORDS: Double Tax Avoidance Agreements, UN Model Convention, OECD Model Convention, Domestic Tax, International Economic Transactions.

INTRODUCTION

Globalization has become one of the defining buzzwords of our time - a term that describes a variety of accelerating economic, political, cultural ideological and environmental process that are rapidly altering our experience of the world¹. Globalisation leads to technological advancements which have supported communication and travel across the world, has helped the gradual disappearance of boundaries that existed worldwide geographically. People coming together from different parts of the world have increased international interaction and economic transactions. Increase in international trade leads to overlapping of tax system of multiple countries resulting into the problem of double taxation. The problem of double tax can be solved with the help of Double Tax Avoidance Agreements (DTAAs). The vital role of double tax treaties is to remove the problem of double taxation. Tax treaties represent an important aspect of the international tax rules of many countries. Over 3,000 bilateral income tax treaties are currently in effect, and the number is growing. The overwhelming majority of these treaties are based in large part on the United Nations Model Double Taxation Convention between Developed and Developing Countries (2011)². DTAAs help in free flow of income earned in international market by avoiding double tax. Generally, Tax Treaties are based either on OECD or on UN tax treaty models.

Every country has their own tax laws where as tax treaty is a legal agreement between countries agreeing to distribute taxing rights among themselves at international horizons. Tax treaties are also called as double taxation avoidance agreements which are signed as unilateral, bilateral or multilateral.

IMPORTANCE OF DOUBLE TAX TREATIES

The significance of DTAA mainly offers following benefits

1. DTAAs lead to more defined investment strategy for investors.
2. Tax payers will be completely confident about their tax liability.
3. DTAAs help in the free flow of income in international market by avoiding tax complications.
4. DTAAs help in the growth of international economic activities.
5. DTAAs distribute taxing rights among the countries participating in tax treaty and avoid confusion of taxing rights and thereby avoid double tax.

OBJECTIVES OF THE STUDY

The objectives of the study are:

1. To observe the UN and OECD model of tax treaties.
2. To study the purpose of double tax treaties.



3. To study the basic aspects concerning Indian DTAA's.
4. To draw conclusions.

METHODOLOGY

The researcher collected primary data from 194 respondents. The respondents are advocate tax consultants and chartered accountants. Questions were designed to examine various double taxation avoidance articles of double taxation treaties in India. Questions have been prepared in close ended form to retrieve optimal information for the targeted objectives. In order to examine retrieved data for better analysis and justification, the responses were collected on the basis of 5 point Likert's scale ('Strongly disagree', 'Disagree', 'Neither agree nor disagree', 'Agree' and 'Strongly Disagree'/'Highly Dissatisfied', 'Dissatisfied', 'Neither Satisfied Nor Dissatisfied', 'Satisfied', 'Highly Satisfied').

The study uses statistical tools like percentage, mean standard deviation, graphs and charts.

The Study:

Here the authors have presented the structure of UN and OECD tax treaty model, the opinion of respondents to the statements based on general issues concerning DTAA's and respondents' opinion about the general aspects relating to Indian DTAA's.

Structure of UN and OECD Tax Treaty Models

A) UN Model of DTAA

The typical structure of UN tax treaties is most easily seen from the scheme of chapters and articles contained in the UN Model (2011),³ which is presented below. The model DTAA consists of seven chapters; divided into 30 articles.

CHAPTER I: SCOPE OF THE CONVENTION

Article. 1 Person Covered

Article. 2 Taxes covered

CHAPTER II: DEFINITIONS

Article. 3 General definitions

Article. 4 Resident

Article. 5 Permanent establishments

CHAPTER III: TAXATION OF INCOME

Article 6 Income from immovable property

Article. 7 Business profits

Article. 8 Shipping and air transport

Article. 9 Shipping, inland waterways transport and air transport (alternatives A and B)

Article. 10 Dividends

Article. 11 Interests

Article. 12 Royalties

Article. 13 Capital gains

Article. 14 Independent personal services

Article. 15 Income from employment

Article. 16 Directors' fees

Article. 17 Artistes and sportsmen

Article. 18 Pensions

Article. 19 Government Service

Article. 20 Students

Article. 21 Other income

CHAPTER IV: TAXATION OF CAPITAL

Article. 22 Capital

CHAPTER V: METHODS FOR ELIMINATION OF DOUBLE TAXATION

Article. 23 A Exemption method

Article 23 B Credit method

CHAPTER VI: SPECIAL PROVISIONS

Article. 24 Non-discrimination

Article. 25 Mutual agreement procedure

Article. 26 Exchange of information

Article. 27 Assistance in the collection of taxes

Article. 28 Members of diplomatic missions and consular posts

CHAPTER VII: FINAL PROVISIONS

Article. 29 Entry into force

Article. 30 Termination⁴

B) Structure of OECD Model of DTAA

The typical structure of OECD tax treaties is most easily seen from the scheme of chapters and articles contained in the OECD Model (2010),⁵ which is presented below. The model DTAA consists of seven chapters; divided into 31 articles.

CHAPTER I :SCOPE OF THE CONVENTION

Article. 1 Person Covered

Article 2 Taxes covered

CHAPTER II :DEFINITIONS

Article. 3 General definitions

Article. 4 Resident

Article. 5 Permanent establishments

CHAPTER III :TAXATION OF INCOME

Article 6 Income from immovable property

Article. 7 Business profits

Article. 8 Shipping and air transport

Article. 9 Shipping, inland waterways transport and air transport (alternatives A and B)

Article. 10 Dividends

Article. 11 Interests

Article. 12 Royalties

Article. 13 Capital gains

Article. 14 (Deleted)

Article. 15 Income from employment

Article. 16 Directors' fees

Article. 17 Artistes and sportsmen

Article. 18 Pensions

Article 19 Government Service

Article 20 Students

Article 21 Other income

CHAPTER IV :TAXATION OF CAPITAL

Article 22 Capital

CHAPTER V :METHODS FOR ELIMINATION OF DOUBLE TAXATION

Article. 23 A Exemption method

Article 23 B Credit method

CHAPTER VI :SPECIAL PROVISIONS

Article. 24 Non-discrimination

Article. 25 Mutual agreement procedure

Article. 26 Exchange of information

Article. 27 Assistance in the collection of taxes

Article. 28 Members of diplomatic missions and consular posts

Article. 29 Territorial extension

CHAPTER VII :FINAL PROVISIONS

Article. 30 Entry into force

Article. 31 Terminations⁶

The UN and OECD Model conventions cover almost every aspect of a person’s international transactions. It may be a business/ profession or any other the coverage is adequate. The structure has been evolved over a period. Almost every country has followed either of the models in structuring their own model.

C) Double Tax Treaties : General Issues

The respondents were made to present their opinion on issues as regards to the primary aspects concerning the need and significance of DTAA’s, in general. There are in all five statements based on regulatory, relieving and restricting role of DTAA’s. The other two statements relate to the unanimity in UN and OECD DTAA’s structure and need to have international judicial authority to handle double tax issues around the world.

Table 1: Respondents opinion about General issues vis-avis the Double Tax Treaties

General issues relating Double Tax Treaties	Mean	Std. Dev
DTAAs regulate the relations between persons and states.	3.613 (72.26%)	1.043
DTAAs are primarily relieving in nature and do not impose tax.	3.608 (72.16%)	1.043
DTAAs can restrict the amount of domestic tax and not increase the domestic tax.	3.551 (71.20%)	1.086
There is no much difference between OECD and UN Model Conventions.	3.659 (73.18%)	0.985
There is a need to establish International Judicial Authority to interpret double tax treaties.	4.020 (80.4%)	1.007

**Source: Primary Data*

In this study, it has been found that the 72.26% of the respondents have agreed that DTAA’s regulate the relations between persons and states (M=3.613, SD=1.043). 72.16% of respondents also affirmed that Tax treaties are primarily relieving in nature and do not impose tax, while the domestic tax law seeks to impose tax in specific circumstances (M=3.608, SD=1.043). A treaty specifies general taxing principles to avoid double taxation. Moreover, as the life of a treaty can be very long it must be flexible enough to adapt to changes in the domestic law while continuing to reflect the original negotiated balance of obligations and concessions. This study has revealed an interesting fact that through double taxation treaties, domestic tax can be restricted and domestic tax does not increase 71.20 % of respondents have consented (M=3.551, SD=1.086).

Observing classical agreements or policies and the recently signed agreements, it has been found that there is no much difference in policy and related constraints which have implications for taxation law and economic outcomes, despite the OECD portray the UN Model as nearly a reproduction of the OECD Model 73.18 % (M=3.659, SD=0.985). A major fraction of respondents i.e. 80.4 % stated that there is a need to establish International Judicial Authority to interpret double tax treaties (M=4.020, SD=1.007) and award decisions. Since, each state have different rules, hence differing results and imperfect legal relationships are not understood to people easily in such cases they required judicial authority establishment.

Graph: 1

General issues of the Double Tax Treaties



Figure 1: Respondents’ opinion about General issues of the Double Tax Treaties



D) General issues of the Double Tax Treaties in India

In the present study respondents were asked to provide their opinion about Indian DTTAs with reference to statements like DTAA override domestic tax law in India, Indian DTAAs are always implemented in good faith, India has succeeded in allocating taxing rights and providing relief if

double taxation arises, Indian tax treaties are sound enough to tackle the issues of tax avoidance, Indian courts have taken literal view in interpreting tax treaties than being liberal and Indian DTAAs are sound in structure, language, coverage and purpose and is fairly ahead in providing the treaty advantages to its citizens/residents

Table-2. General Issues of the Double Tax Treaties vis-a-vis India

General Issues of Double Tax Treaties in India	Mean	Std. Dev
DTAAs override domestic tax law in India.	2.958 (59.16%)	1.203
Indian DTAAs are always implemented in good faith.	3.933 (78.66%)	0.734
India has succeeded in allocating taxing rights and providing relief if double taxation arises.	3.582 (71.64%)	0.925
Indian tax treaties are sound enough to tackle the issues of tax avoidance, in general.	3.484 (69.68%)	0.998
Indian courts have taken, in interpreting tax treaties, literal view than being liberal.	3.314 (66.28%)	1.076
Indian DTAAs are sound in structure, language, coverage and purpose.	3.639 (72.78%)	0.889
India is fairly ahead in exploiting the treaty advantages to its citizens/residents.	3.773 (75.46%)	1.033

*Source: Primary Data

The OECD draft itself defines ‘Treaty Override’ as a situation where the domestic legislation of a State overrules the provisions of a single treaty or all treaties hitherto having had effect in that state (OECD Draft)⁷ the study has revealed that DTAAs override domestic tax law in India (59.16%) (M=2.958, SD=1.203). Respondents also revealed that DTAA are structured from assessee’s point of view. It is positively accepted that Indian DTAAs are always implemented in good faith, with 78.66% of consent (M=3.933, SD=0.734). In the present empirical analysis it has been found that though being geographically diverse nation, India has succeeded in allocating taxing rights and providing relief in case of double taxation (71.64%) (M= 3.582, SD=0.925). 69.68% respondents agreed that Indian tax treaties are sound enough to tackle the issues of tax avoidance (M=3.484, SD=0.998). It is also revealed

that a few treaties framed during preliberalisation are old formatted and require equipping with present day business conditions while considering economic values, competition and practical economic environment. The respondents have revealed that there is a need for modifications and development in tax treaties to cope up with the recent changes in business environment by considering major international business structure. With 66.28% respondents are of the opinion that the courts to interpret tax treaties, in literal view than being liberal (M=3.314, SD=1.076). India has 88 countries, but presently 85 are in force. The respondents suggest International Judicial Authority to interpret double tax treaties, (72.78%) (M=3.639, SD=0.889). Respondents also revealed that government is working towards it making DTAAs beneficial to the assessee, (75.46%) (M=3.773, SD=1.033).

Graph: 2

General Issues of the Double Tax Treaties vis-a-vis India

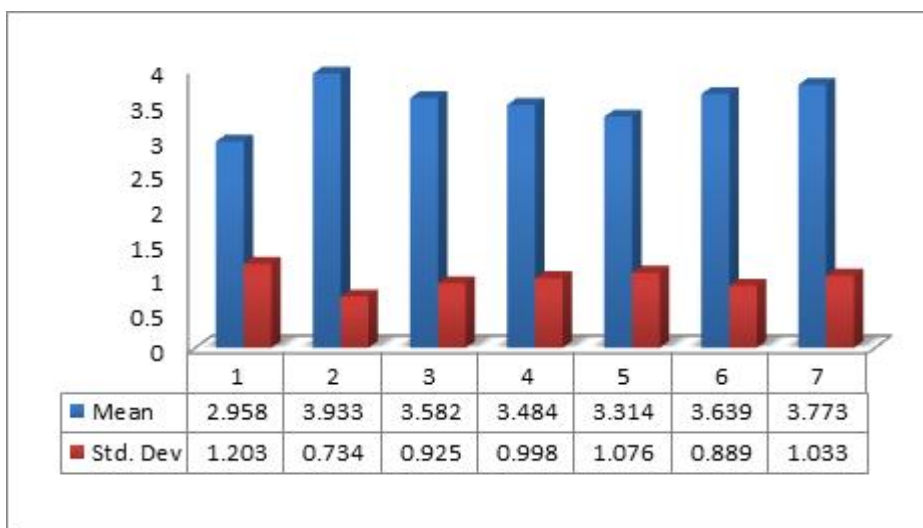


Figure 2: Respondents opinion about General issues of the Double Tax Treaties in India

CONCLUSION

In the cotemporary economic environment DTAAAs play a very effective role in ensuring sound taxation principles like certainty and equity, to the tax payers, more specifically, to the persons with international economic transactions. DTAAAs are the pillars of international taxation across the world. The findings revealed by the present study clearly indicate the significance of the DTAA. The government should make still rigorous efforts in modifying the older DTAAAs with different countries to make them suit to the present needs of the tax payer, the government and the economy. The developments like “exchange of information” clause in DTAAAs will go a long way not only in facilitating the stakeholders but also curbing the black money emanating from international economic transactions.

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3. United Nations Model Double Taxation Convention between Developed and Developing Countries (2011).
4. *Ibid.*
5. ARTICLES OF THE OECD MODEL TAX CONVENTION ON INCOME AND CAPITAL [as they read on 22 July 2010]
6. *Ibid.*
7. OECD Model Treaty, *supra* note 50, art. 7(1).