

LECTURE 2: PRINCIPLES OF INTERNATIONAL TAX LAW

Treaties

- The definition of a treaty is an agreement between two sovereign nations, which serves as a bridge between tax systems and contracting states.
- Two types of Model Treaties OECD Model Treaty and UN Model Treaty, main difference is that UN Model Treaty imposes fewer restrictions on taxes that may be imposed by developing countries.

Sources of Public International Law

- (a) international conventions establishing rules expressly recognised by states,
- (b) international custom, as evidence of a general practice accepted as law,
- (c) the general principles of law recognised by civilised nations, and
- (d) certain judicial decisions and legal teachings.

Double Taxation

Refers to both (i) the **right of legislation** and (ii) **the right of enforcement**. A State cannot enforce what it cannot legislate. However, the reverse may be true. A State may legislate, even when it is unable to enforce.

2 schools of thought:

- a.) No restriction on a state's right to tax and is exercised without regard to other states.

THEREFORE, no need to have a legal connection / link with a jurisdiction, PROVIDED there is a **valid nexus** with that state.

- b.) Sovereign right to tax confined to a territory having a "*legally relevant connection*" with State and taxpayer.

Both views accept connecting factors give a state right to tax. The connecting factors link taxpayer personally to a particular tax jurisdiction. They include personal links with the home State by virtue of residence, domicile or citizenship (national person), place of incorporation / location of a registered office, management & control for legal persons.

Domestic Law in countries usually apply the:

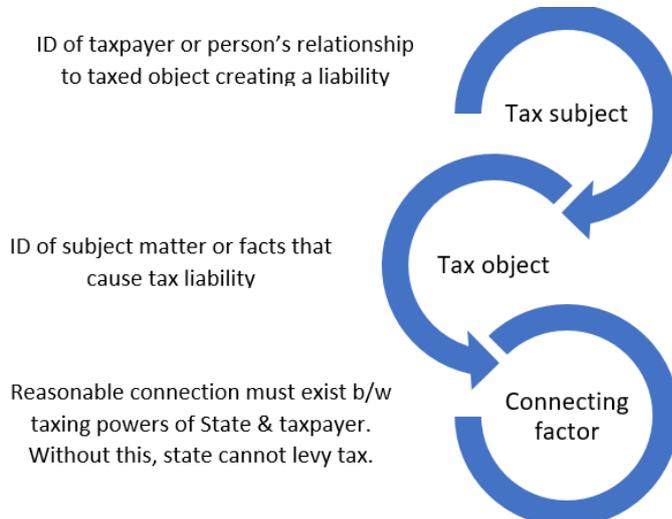
- **Residence rule:** Unlimited tax rights are granted here due to personal attachment May apply World-wide income tax rules.
- **Source rule:** Limited taxation rights granted to country of source due to economic attachment. Only tax what is derived from economic activity in territory.

Could land-up double taxing a taxpayer, there are 2 categories of double taxation:

Economic double taxation: double tax same income in different hands.

Juridical double taxation: same tax object & same tax subject. This can also lead to double non-taxation / exemption. However, these conflicts are usually resolved by DTAs.

There are three key components of a taxable transactions



2 types of constitutional principles / approaches of countries making treaty obligations have the force of domestic law:

Monistic principle: municipal law linked / subordinated to intl. law under "doctrine of incorporation".

Dualistic principle: regards international & municipal laws as separate & requires specific domestic legislation under "doctrine of transformation".

Two groups of countries:

- (i) Direct effect:
- (ii) Indirect effect:

Is International Tax Law Enforceable?

- Countries have legislative powers, don't have enforcement rights over foreign jurisdictions.
- International tax law = only permits enforcement by a country of its tax laws within its legislative jurisdiction.
- Forbids executive / administration acts & enquiries by foreign tax authorities cannot without consent of host country. E.g collect documents, tax evidence or legal documents served without consent. Tax authorities must follow principles of intl. law when they enforce the dom. Law.
- Art 26 OECD Model of Treaty, there is exchange of information.

In order to understand enforcement of International Tax Law, one needs to look at principles that govern:

1. Bilateral Investment agreements;
2. WTO Disputes; and
3. State Responsibility.

Is International law enforceable? In your answer give your understanding of WTO obligations, BIT obligations and State Responsibility obligations?

International tax law usually only permits enforcement of a country within its legislative jurisdiction. They do not have enforcement rights over a foreign jurisdiction. However, review what is stated below about state responsibility actions.

In terms of the WTO obligations three items are relevant to tax areas:

- i. Non-discrimination principle
- ii. Wide definition of prohibited / actionable subsidies
- iii. General Agreement on Trade in Services

All of these three obligations are what both parties have to try and adhere to when engaging in activities with each other, these three obligations is meant to be upheld by the country that seeks investments into their country. Once again, not subject to the procedural laws of any state.

In terms of BIT "Bilateral Investment Treaties" these serve the purpose of investment protection for the investor and if a potential investor enters into these BITs and the country falls foul of their provisions as per the BIT, the aggrieved party can seek international arbitration usually submitted to ICSID as the arbitrations are not subject to the procedural laws of any state. The obligations include ones against discrimination and the application of the most favoured nation clause.

Lastly in terms of State Obligation responsibility, States are responsible for ensuring taxes are correctly imposed under the domestic law that governs that state. This means that state obligation responsibility in respect of the international arena is established if the international law requirements are met irrespective of the domestic requirements for establishing state responsibility, and vice versa.

State responsibility at the international level requires a breach of an international obligation by a State. This would include the breach of a treaty provision, or the failure to adhere to *jus cogens* (a peremptory international norm – such as transgressing unjust enrichment, overstepping tax audit powers without permission of another State). Failure to apply the most favoured nation clause in a BIT, or GATT and GATS, would be the failure to adhere to treaty provisions, giving rise to a state responsibility action, between States, but only once all court processes in the offending jurisdiction have taken place.