SEATINI

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AN ANALYSIS OF THE UGANDA–NETHERLANDS DOUBLE TAXATION AGREEMENT

2018

Countries enter into Double Taxation Treaties (DTTs) or Agreements (DTAs) to facilitate investment and to create fiscal certainty for investors to inform location decisions. In theory, the purpose of DTTs is to eliminate double taxation of cross-border flows by determining which treaty partner can tax different categories of income generated in one treaty state by a resident of the other. The prevalence of DTTs is attributed to a deepening globalization that has led to greater economic interdependence among countries and increased growing cross-border investments, international financial flows, and migration or flows of labour.

In 2017, a study was commissioned by ActionAid with a core objective of highlighting the gaps that exist in the DTTs that Uganda signed with other countries, and to generate a policy guideline that the Government of Uganda, could consider for purposes of future DTT negotiations or renegotiations.

Among the treaties analysed was the Uganda-Netherlands Double Taxation Treaty. The table below reflects an analysis of different clauses within the treaty and highlights recommendations that could be taken on to ensure that the loopholes are closed hence increased and equitable revenue generation for both countries.

An Analysis of the Uganda-Netherlands Double Taxation Agreement

No	Issue / Article	Analysis
1.	Article 5(3) (a)—the time threshold for the creation of a construction PE.	Article 5(3)(a) of the Netherlands treaty is based on the UN Model, which sets a time threshold of 6 months for the creation of a PE for a construction site and supervisory activities connected therewith. ***This needs to be synchronized with the 90 day period set out under s. 78 of the Uganda Income Tax Act Cap 340.***
2.	Article 5(3) (b)—the time threshold for the creation of a service PE.	Article 5(3) (b) of the Netherlands treaty is based on the OECD Model, which sets a time threshold of 4 months for the creation of a PE. ***This needs to be synchronized with the 90 day period set out under s. 78(a) (iv) of the Uganda Income Tax Act Cap 340.***
3.	Article 5(4)—Permanent Establishment (PE) in respect of auxiliary and preparatory activities	Article 5(4) of the Netherlands treaty lacks clarity as to whether each of the activities listed in Para (a) to (e) of Article 5(4) should be of a preparatory or auxiliary status for PE status to be avoided. ***Clarification to this effect is necessary in order to prevent the artificial avoidance of PE status.***
4.	Article 5(5)—Conclusion of Contracts in the Source State	Article 5(5) of the Netherlands treaty is based on the UN Model. Some companies artificially avoid PE status by concluding contracts outside the contracting state, while still generating income from the contracting state. ***Article 5(5) of the Netherlands treaty should be substituted with the language proposed by the BEPS Committee on Article 5(5), which is intended to prevent the artificial avoidance of PE status, by stipulating that a PE may exist in certain circumstances even where no contracts are concluded in the source jurisdiction.***

5.	Article 7—Business Profits	Article 7 of the Netherlands treaty adopts the language of the OECD Model Convention, which does not adopt the "force of attraction" principle. ***This needs to be renegotiated to adopt Article 7(1) (c) of the UN Model, which adopts the "force of attraction" principle in order to maximize the taxing rights of the Source state, which are otherwise reserved to the State of Residence under the OECD Model, in respect of profits from business activities undertaken in the Source state, which are not effectively connected with the PE.***
6.	Article 8—Shipping, Inland waterways transport and air transport.	Article 8 of the Netherlands treaty reserves the taxing right in respect of profits from shipping, air transport and inland waterways transport to the state where the Place of Effective Management is situated. ***This needs to be substituted with an embarkation-based provision as a basis for taxing jurisdiction of the source state, such as is provided for under Section 86 of the Income Tax Act. An embarkation based clause is simpler to comprehend and easier to administer and guarantees that Uganda's tax base, as a source state. The approach under s. 86 of the Uganda Income Tax Act Cap 340 guarantees that the State of Source will tax income arising from international cargo or international passengers embarked at a place in Uganda.***
	Withholding Tax rates on overseas payments under Article 10 (Dividends), Article 11 (Interest), Article 12 (Royalties)	No withholding tax is due on dividends paid by a company in Uganda where a company resident in the Netherlands is the beneficial owner "of at least 50 per cent of the capital of the paying the dividends with respect to investments... made after the entry into force of this convention." Where a company in the Netherlands is the beneficial owner of less than 50 per cent of the capital, 5% withholding tax is payable. • ***The source state should retain the right to tax dividends.*** • ***Tax dividends irrespective of the percentage share in the investment and of up to 10%***
	Article 13 -Taxation of capital gains on sale of shares	Article 13 (5) only applies if the individual who derives the gains has been a resident of the first-mentioned State in the course of the last ten years preceding the year in which the gains are derived and provided that, at the time he became a resident of the other Contracting State, the above-mentioned conditions regarding share ownership in the said company were satisfied. ***The time element should be removed; a capital gains tax should be charged regardless of the period; 10 years is too long*** ***Also, the treaty excludes source Capital Gains Tax on alienation of property associated with a fixed base for providing independent personal services***
7.	Model Article on "Service Fees"	It is proposed to introduce a model Article on Service Fees, to cater for source-State taxation in circumstances where the activities related to the provision of services are not sufficient to give rise to a PE. ***See Annex 1 (Proposed Model Article on Service Fees).***
8.	Article 21—Other Income	Article 21(1)—(*Other Income*) of the Netherlands treaty reserves the right to tax to tax other income (i.e., not covered expressly by the preceding articles of the treaty) to the State of Residence. ***It is important that the State of Source is permitted to tax this income. This is a matter for renegotiation.***
9.	Article 24—Non-discrim-ination	Article 24 of the Netherlands treaty already does not contain clarification that branch/PE repatriated income tax shall not be regarded as a discriminatory tax. ***This needs to be clarified.***
10.	Limitation on Benefits (LOB) Clause	***See Annex 2 for the proposed Limitation on Benefits clause to be inserted as an additional article.***

Conclusion

Developing countries like Uganda face the challenge of ensuring that the different economic measures chosen to support economic development through mobilization of revenue, promotion of trade and investment are efficacious in promoting investment and preventing both tax avoidance and double non-taxation. In a bid to encourage equitable and increased revenue mobilization, Uganda's tax policy should increasingly allow the state to collect tax revenues from production and profits generated in Uganda. The network of double taxation treaties is one of the mechanisms used by companies to avoid paying taxes, leading to illicit financial flows and tax losses for Uganda. Therefore, taking on the recommendations highlighted in this paper is one key step to ensure that Ugandan citizens benefit from investment into Uganda, and the profits that those investors make.

ANNEX I

MODEL SERVICE FEES ARTICLE

1. Service fees arising in a Contracting State which are derived by a resident of the other Contracting State may be taxed in that other State.

2. However, such service fees may also be taxed in the Contracting State in which they arise and according to the law of that State; but where the beneficial owner of such service fees is a resident of the other Contracting State the tax so charged shall not exceed 15% of the gross amount of the service fees.

3. The term "service fees" as used in this Article means payments of any kind to any person, other than an employee of the person making the payment, in consideration for any services rendered by the first-mentioned person.

4. The provisions of paragraphs 1 and 2 of this Article shall not apply if the beneficial owner of the service fees, being a resident of a Contracting State, carries on business in the other Contracting State in which the service fees arise, through a permanent establishment situated therein, and the service fees are effectively connected with such permanent establishment. In such case, the provisions of Article 7 shall apply.

5. Service fees shall be deemed to arise in a Contracting State when the payer is that State itself, a political subdivision, a local authority or a resident of that State. Where, however, the person paying the service fees, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment in connection with which the obligation to pay the service fees was incurred, and such service fees are borne by that permanent establishment, then such service fees shall be deemed to arise in the State in which the permanent establishment is situated.

6. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the service fees paid exceeds, for whatever reason, the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last mentioned amount. In such case, the excess part of the payments shall remain taxable according to the law of each Contracting State, due regard being had to the other provisions of this Convention.

ANNEX II

MODEL LIMITATION ON BENEFITS ARTICLE

1. Except as otherwise provided in this Article, a resident of a Contracting State shall be entitled to the benefits that would otherwise be accorded by this Convention only if such resident is a qualified person.

2. For the purposes of this Article, a resident of a Contracting State shall be a qualified person if the resident is:

a. an individual;

b. that Contracting State, any political subdivision or local authority thereof, the central bank thereof or a person that is wholly owned, directly or indirectly, by that State or any political subdivision or local authority thereof;

c. a company, if the principal class of its shares is regularly traded on one or more recognised stock exchanges;

d. a person other than a company, if its beneficial interests are regularly traded on one or more recognised stock exchanges;

e. a person other than an individual, if residents of that Contracting State that are qualified persons own, directly or indirectly, more than 50 per cent of the beneficial interests of the person;

f. a person other than an individual, if more than 50% of the beneficial interests of the person are owned, directly or indirectly, by persons who are equivalent beneficiaries; or

g. carrying on active trade or business in the Contracting State in which it is resident (other than the business of making or managing investments for the resident's own account, unless the business is carried on by a bank, an insurance company or a registered securities dealer).

4. A resident of a Contracting State that is not a qualified person shall nevertheless be entitled to benefits accorded by this Convention if the competent authority of the Contracting State from which the benefit is being claimed, upon request from that resident, determines, in accordance with its domestic law or administrative practice, that the establishment, maintenance and conduct of that resident's operations in the first-mentioned State are of sufficient economic substance and are considered as not having as one of its principal purposes the obtaining of such benefit.

5. For the purposes of this Article, the term:

f. "equivalent beneficiary" means any person who would be entitled to an equivalent or more favourable benefit with respect to an item of income accorded by a Contracting State under the domestic law of that Contracting State, this Convention or any other international instrument as the benefit to be accorded to that item of income under this Convention, provided that, if that person is a resident of neither of the Contracting States, the first-mentioned Contracting State has a convention for the effective and comprehensive exchange of information relating to tax matters in effect with the state of which that person is a resident;

g. "principal class of shares" means the class or classes of shares of a company which represents in the aggregate a majority of the voting power of the company;

h. "Recognised stock exchange" means any stock exchange established and regulated as such under the laws of any sovereign state.

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