THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2022

MODULE 1

PRINCIPLES OF INTERNATIONAL TAXATION

TIME ALLOWED – 3¼ HOURS

This exam paper has **two** parts: **Part A** and **Part B**.

You need to answer **four** questions in total. You will **not** receive marks for any additional answers.

You must answer:

- **At least two** questions in **Part A** (25 marks each)
- **At least one** question from **Part B** (25 marks each)

Further instructions

- All workings should be made to the nearest month and you must use the appropriate monetary currency, unless otherwise stated.
- As you are using the online method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately a quarter of your time answering each of your four selected questions.
- There is no separate reading time, so you can start typing your answers as soon as the exam begins. However, we recommend that you set aside some time to thoroughly read each question and plan each of your answers.

PART A

You are required to answer AT LEAST TWO questions from this Part.

1. **You are required to prepare a report, outlining whether a person can satisfy the "liable to tax" criterion contained within Article 4(1) of the OECD Model Tax Convention 2017 (OECD MTC 2017), in situations when they have not paid any tax.**

   Your report should include the reasons for your conclusion, together with appropriate references to the OECD MTC 2017 and its Commentary. (25)

2. **With reference to the results of the peer review process, you are required to evaluate the effectiveness of BEPS Action 13 on transparency, exchange of information and reduced opportunities for base erosion and profit shifting.** (25)

3. **You are required to discuss the extent to which the Mutual Agreement Procedure provides for a definitive solution to disputes arising under Article 25 of the OECD Model Tax Convention 2017.** (25)

4. **You are required to prepare a report that considers the allocation of taxing rights under Article 10 of the OECD Model Tax Convention 2017 and Article 10 of the UN Model Double Taxation Convention 2017.** (25)

5. 'Article 21 of the OECD Model Tax Convention 2017 (OECD MTC 2017) is the article of last resort over which the other distributive rules take precedence, and so is of minor importance within the framework of the OECD MTC 2017.'

   You are required to critically evaluate this statement. (25)

PART B

You are required to answer AT LEAST ONE question from this Part.

6. Energio Ltd is a multinational energy company with various subsidiaries around the world, and is tax resident in Country A according to its domestic law. Energio Ltd established a wholly-owned subsidiary, EnerSub Ltd, with $10 million share capital on 10 October of Year One. EnerSub is tax resident in Country B under its domestic law. EnerSub Ltd supplies energy to consumers in Country B and Country B's neighbouring countries (Country C, Country D and Country E).

   EnerSub Ltd sought to construct a new generator, but did not have sufficient funds available to finance the construction. EnerSub Ltd initially approached several commercial lenders in Country B to discuss the possibility of a loan to cover these amounts; none of these discussions were successful. Following lengthy negotiations between the boards of Energio Ltd and EnerSub Ltd, it was agreed on 10 February of Year Two that Energio Ltd would lend EnerSub $30 million in order to enable the construction of the generator by the required date (1 January of Year Three).

   Further contractual terms agreed on the same date included:

   - a three-month loan term (i.e. the loan will be repayable by 9 May of Year Two;
   - an interest rate set at the inter-bank lending rate plus a 4% uplift; and
   - a requirement that the loan will be used to fund the construction of the generator.

   On 10 March of Year Two, Energio Ltd and EnerSub Ltd decided to amend the contractual terms relating to the loan, extending the loan term to six months and increasing the interest rate to the inter-bank lending rate plus 8%. On 10 April of Year Two the loan amount was increased to $60 million and the interest rate was increased to the inter-bank lending rate plus 9%.

   EnerSub Ltd continued to pay the prevailing interest amounts to Energio Ltd throughout the loan period, until the loan matured on 10 August of Year Two. The construction of the generator was completed as planned on 1 January of Year Three.

   EnerSub Ltd has claimed a deduction in its Country B Year Two tax return for all interest amounts owed during the loan term to Energio Ltd in Year Two. The Country B revenue authority (the BRA)'s online filing system raised an alarm in relation to the amounts claimed (both the interest deduction claimed and, upon further investigation, the loan amount) and the BRA has therefore requested further information from EnerSub Ltd regarding the loan details and interest deductions claimed. Energio Ltd has submitted to the BRA a letter from a local Country A bank, outlining the interest rate at which it would lend to EnerSub Ltd during the initial and extended loan periods.

   The BRA has been made aware of other, similar scenarios involving multinationals with subsidiaries in its jurisdiction that have claimed significant interest deductions. It is now seeking advice on how best to address this type of situation effectively.

   All of Country B's double tax agreements (DTAs), including the DTA between Country A and Country B, mirror the OECD Model Tax Convention 2017.

   You are required to prepare a concise report, advising Country B on the DTA consequences of Energio Ltd and EnerSub Ltd entering into the loan agreement.

   You are not required to include calculations in your report. (25)

7. Mykola, a resident of Country U, is employed as a designer by Ultrine Ltd, a large multinational company that is tax resident in Country U and has numerous subsidiaries and branches around the world. Mykola lives with his partner and children in Country U, in a home they both own. He has been employed by Ultrine Ltd since graduating from university fifteen years ago.

Mykola is currently supervising the completion of a large project to redesign a chain of hotels in Country X, which relies upon Ultrine Ltd's combined expertise from a number of different countries. Mykola is expected to be based in Country X for a period of three months, having left for Country X on 1 January of Year One.

Ultrine Ltd entered into the contract for the hotel design project in Country X during the previous year, with the final stage of the project due to end on 31 March of Year One. Ultrine Ltd rents a small office in Country X with several casual staff members who fulfill administrative functions relating to Ultrine Ltd's various projects in Country X. Mykola will spend his time mainly on site at the chain's various hotels, but will also use the Country X office as required.

Mykola is tax resident in Country U under its domestic law. In order to become non-resident under Country U's domestic law, Mykola must be absent for a minimum consecutive period of eight months from the date of departure from Country U. Country U's domestic law also provides that if a person who has been resident leaves the country and then returns to Country U within five years of their departure date, they will immediately and automatically become Country U tax resident again.

Country X operates a 183-day physical presence test for domestic residence, and requires absence for a period of 365 consecutive days before non-resident status is granted. Once satisfied, the Country X physical presence test is backdated to the first day of presence. Both Country U and Country X tax the income of their residents on a worldwide basis, and relieve juridical double taxation by way of the credit method.

Mykola has relatives in Country X and has visited on holiday in the past. He also possesses a bank account that generates interest income and owns an apartment in Country X, which is typically rented out for the majority of the year. However, Mykola tends to visit the apartment when he is in Country X to check on its state of repair and sometimes stays there when it is untenanted. The apartment was tenanted when Mykola arrived in Country X on 1 January of Year One, with the lease due to end on 30 June of Year One. Ultrine Ltd entered into a three-month rental agreement with a provider of short-stay accommodation in Country X, enabling Mykola to be based close to the biggest hotel in the chain.

Soon after his arrival in Country X, Mykola discovered that work had not progressed in line with the contract and immediately advised Ultrine Ltd of the delays, which resulted in him being asked to:

- re-negotiate the various contract terms including costings, resources needed and deadline; and
- stay in Country X until such time as the project is completed.

Mykola agreed to stay on in Country X and renegotiate the project's contract terms. After some negotiation, the revised contract was finally agreed upon on 28 February of Year One. The new completion date for the project was set as 30 June of Year One.

The marketing material aspect of the project was completed by 30 June but, due to numerous shipping delays, the interior design aspect incurred further delays. Mykola was, again, requested by Ultrine Ltd to negotiate a new completion date for the interior design aspect of the project and to stay on in Country X until completion of the project. The completion date for this aspect of the project was extended to 5 September of Year One.

Although both Mykola and his employer had assumed Mykola would stay on in the short-stay accommodation, his tenants decided to vacate his Country X apartment before the lease end date, resulting in the property being vacant from 1 May of Year One. Mykola was able to find tenants to commence a new six-month lease with a start date of 1 September of Year One. He decided to stay in the apartment during the untenanted period (from 1 May until 31 August) so that he could attend to any issues with the property and advised his employer he would no longer need any short-stay accommodation provided. Mykola finally returned to Country U on 5 September of Year One and stayed in a Country X motel near the airport from 31 August until 5 September inclusive.

Country U and Country X have a double tax agreement (DTA) that mirrors the OECD Model Tax Convention 2017. Both countries use the calendar year as the tax year.

You are required to advise Mykola on whether he is likely to be considered a resident of Country U, Country X or neither, for the purposes of the DTA between Country U and Country X in Year One. (25)