THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

December 2023

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)

You should therefore answer either three questions in Part A and one question in Part B; or two questions in Part A and two questions in Part B.

Further instructions

- You must use the appropriate monetary currency, unless otherwise stated. Any monetary calculations should be made to the nearest whole unit of currency. Any necessary time apportionments in your calculations should be made to the nearest whole month.
- 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 consider the role of countries' stated reservations, observations and positions on the OECD Model Tax Convention 2017 (OECD MTC 2017) and its Commentary.**

   Your answer must include a consideration of the major differences and similarities between these 'departures' from the OECD MTC 2017 and its Commentary. (25)

2. **You are required to evaluate the extent to which the Common Reporting Standard can be described as being effective in promoting global tax transparency and combating offshore tax evasion.** (25)

3. The OECD's Forum on Harmful Tax Practices (FHTP) has been conducting reviews of preferential regimes since its creation in 1998.

   You are required to consider how the global tax landscape has evolved, and thus affected the FHTP's work on harmful tax competition, as well as the challenges faced by the FHTP as its work continues to evolve. (25)

4. **You are required to prepare a report that considers the effectiveness of the OECD Model Tax Convention 2017 in addressing the improper use of tax treaties by preventing tax treaty shopping.** (25)

5. "The UN-led global tax reform initiative would promote greater inclusivity and effective international tax cooperation than that of the OECD."

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

PART B

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

6. Angelica Co. (Angelica) is a company incorporated and tax resident in Fragonia. It carries on a business of both manufacturing and distributing computer products.

   In tax year 1, Angelica began the process of expanding its business into Geronia by sending out Felicity, a member of its Fragonian market research team, to Geronia for one month. Felicity reported back, recommending the commencement of manufacturing operations in Geronia and advising Angelica to hire the services of a real estate agent to assist in finding a suitable site, including a warehouse, to assemble and store the products. Angelica employed the services of an independent real estate agent in tax year 1.

   On the first day of tax year 2, Angelica acquired a warehouse in Geronia for $2 million, its market value at the time, in which Angelica planned to store some of its partly assembled imported products. There was no mortgage on the warehouse. However, as there were delays in importing the partly assembled products into Geronia, Angelica determined to rent out the warehouse for a fee. The warehouse was rented on arm's length terms to an independent third party tenant for the entirety of tax year 2, at a rate of $200,000 per annum. The tenant requested that Angelica provide an all-in price for the rent and the provision of utilities in the warehouse; an additional $20,000 per annum was accordingly charged to the tenant to cover utilities for tax year 2, which cost Angelica $15,000 for the term of the lease.

   In tax year 3, two shipments of partly assembled products were received into Geronia and these were delivered by an independent logistics business to the warehouse. Due to ongoing issues in finding staff with the requisite expertise needed to assemble these products, the partly assembled products were stored in the warehouse but were not fully assembled at that time. Angelica decided to send a number of its Fragonian staff to assemble some of the products in Geronia, and its Fragonia-based sales team found some prospective Geronian customers who advised that they would inspect the products once fully assembled. During a one-month period in tax year 3 (month 1), the warehouse was used both to assemble the products and to store partly and fully assembled products. At the end of month 1, the Fragonian staff returned to Fragonia and, during the remaining 11 months of tax year 3, both the partly assembled and fully assembled products continued to be stored in the warehouse. The prospective Geronian customers did not purchase any assembled products in tax year 3 but advised Angelica that they might be interested in acquiring some assembled products in tax year 4. The market value of the warehouse was $4 million in tax year 3.

   In tax year 4, notwithstanding the possibility that some assembled products may be sold in Geronia, the Board of Angelica determined that expansion into Geronia was not going to be as profitable as they had anticipated and consequently shipped all of the unsold products back to Geronia, placing the warehouse on the market. Angelica sold the warehouse on the last day of tax year 4 for $5 million, its market value at the time of sale.

   Both Fragonia and Geronia:

   - Subject income derived from real property to income tax at 20%.
   - Subject gains derived from the sale of immovable property to tax under their domestic tax law at 20% and define immovable property as "land and all buildings on the land as well as any fixtures".
   - Levy tax on the market value on immovable property on an annual basis at a rate of 10% during the period of ownership. This rate applies whether or not the property is vacant or occupied.
   - Use the calendar year as the tax year.
   - Tax gains under their domestic tax regimes on a realisation basis.
   - Have domestic tax regimes' that determine the tax residency of their companies on the basis of incorporation.
   - Have a double tax agreement (DTA) that is identical to the OECD Model Tax Convention 2017.

   You are required to advise Angelica on the likely tax outcomes under the Fragonia-Geronia DTA in tax years 1 to 4, in relation to the warehouse it acquired in Geronia.

   All monetary amounts and tax rates are used for illustrative purposes, and you are not required to calculate any amounts of tax payable. (25)

7. Country X operates a worldwide basis of taxation, under which Country X tax residents are subject to tax on their worldwide income and non-tax residents are subject to tax on their Country X source income. A non-resident becomes a resident of Country X for tax purposes when that individual has been in Country X for 183 days in a tax year.

Country X actively encourages temporary workers from a range of overseas countries to come to and work on short-term assignments in Country X, including fruit picking and hospitality. Every summer thousands of young people arrive in Country X to take up these short-term assignments. In order to have working rights for these short-term assignments, these individuals must ensure they have the right to work in Country X. Country X provides a range of work visas for foreigners, and the processing fee for these varies depending on the visa.

Zara is a national of Country Y, with whom Country X has a double tax agreement (DTA) that is identical to the OECD Model Tax Convention 2017. Zara has never visited Country X, does not have the right to work in Country X, and holds only a Country Y passport.

Having recently finished their high school examinations, Zara and a group of friends decide to escape the winter season in Country Y and start investigating the types of employment roles they could fulfil in Country X, the hourly rates, the visa costs involved and their likely tax position, to determine whether it makes financial sense for them to make the journey. Zara and her friends discover that they can apply for a special visa for young people like themselves who would not otherwise have the right to work in Country X but wish to come to Country X to work on fruit farms or in tourism.

As the special visa is only available for young people who would not otherwise have full working rights in Country X (i.e. holding a passport from a country other than Country X and not holding a Country X passport), and is only available to people from specified countries outside Country X (including Country Y) and for short assignments, the Country X government keeps the costs of the special visa very low. Zara and her friends discover the hourly rates of pay to work on the fruit farms are reasonable, subsidised employer-provided accommodation is available, and that there are numerous roles available such that they can all be based at the same fruit farm. They also review their putative tax position and determine that:

- Individuals who have full working rights (i.e. those who hold a Country X passport) are subject to tax at a flat rate of 30% and have a tax free threshold of $50,0000. Full working rights are only granted to those who are Country X citizens. This rule is contained within relevant Country X tax legislation.

- Those individuals who are in Country X on the special visa and derive income from their short-term assignments are taxed on their 'special visa income' at a flat rate of 50% and have no tax-free threshold. This rule is contained within relevant Country X tax legislation.

- Country X and Country Y have the same tax year (the calendar year).

- The DTA between Country X and Country Y is identical to the OECD Model Tax Convention 2017 but states that the maximum rate of dividend withholding tax under Article 10(2)(b) is 10%.

- Country X and Y both subject dividends to a flat withholding tax rate of 25% under their domestic tax law.

Zara and her friends are happy with the special visa costs and the rate of pay; they estimate they will earn approximately $50,000 during their stay and now seek to understand their tax position. Zara plans to stay in Country X for 11 months in tax year 2, and her prospective employer has offered to provide subsidised accommodation on the fruit farm for the duration of her stay in Country X. Zara is concerned that she may remain a tax resident of Country Y under its domestic tax laws, as she needs to be absent from Country Y for a minimum of 10 months in the tax year in order to become a non-resident. While Zara has yet to book her flights or make other arrangements, she is clear that if she enjoys living in Country X and is able to extend her visa or obtain a different type of visa she may stay on longer.

Zara's cousin, Maryam, is a national of Country Z, where she lives with her parents. Maryam is considering joining Zara and her friends in Country X, and is exploring her visa options. Maryam's parents, who are also Country Z nationals, have discussed temporarily moving to Country X for the duration of Maryam and Zara's stay. They have never previously visited Country X, nor do they have any pre-existing connections with Country X. Maryam's parents are exploring the idea of purchasing a house for $600,000 in Country X, in which they may live with Maryam and which they may continue to hold as an investment property when they return to Country Z at the end of tax year 2.

Continued

7. Continuation

Country X requires that those without a Country X passport, whilst not prohibited from purchasing residential property in Country X, must pay an additional duty amounting to 10% of the purchase price at the point that the property sale is finalised. The standard level of duty on purchases of residential property is 2% for holders of a Country X passport.

Maryam's grandmother is also a national of Country Z and has never previously visited Country X, nor does she have any pre-existing connections with Country X. She is considering purchasing shares in a Country X resident company, having been advised that the return on investments in Country X is currently stronger than in Country Z and that she may be table to access a withholding tax rate of 10% on any distributed Country X dividends. Country Z subjects dividends to a flat withholding tax rate of 25% under its domestic tax law.

Country X and Country Z also have a DTA that is identical to the OECD MTC 2017; this DTA was entered into two years before the Country X-Y DTA, and states that the maximum rate of dividend withholding tax under Article 10(2)(b) is 15%.

You are required to prepare a report that outlines the likely tax positions of the following:

1) **Zara's likely tax position in Country X in tax year 2, on the basis that she derives $50,000 during her Country X assignment in tax year 2 and stays in Country X for a minimum of 11 months in tax year 2, with respect to the Country X-Y DTA.** (15)

2) **Maryam's parents' likely tax position, with respect to the Country X-Z DTA, in relation to the additional 10% duty on Country X house purchases that applies to those without full working rights in Country X.** (5)

3) **Maryam's grandmother's likely tax position under the Country X-Z DTA if she proceeds with the purchase of the Country X resident company shares, where she is the beneficial owner of the dividends and receives $20,000 dividends from the Country X resident company in tax year 2.** (5)

Total (25)