

Improving Tax Treaties by Allowing Limited Double Taxation

Jeroen Lammers

jl.lammers@cbs.dk

CBS  **COPENHAGEN
BUSINESS SCHOOL**

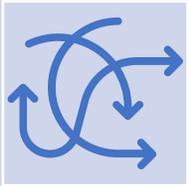
Tarcísio Diniz Magalhães

Tarcisio.DinizMagalhaes@uantwerpen.be



University of Antwerp
| Faculty of Law

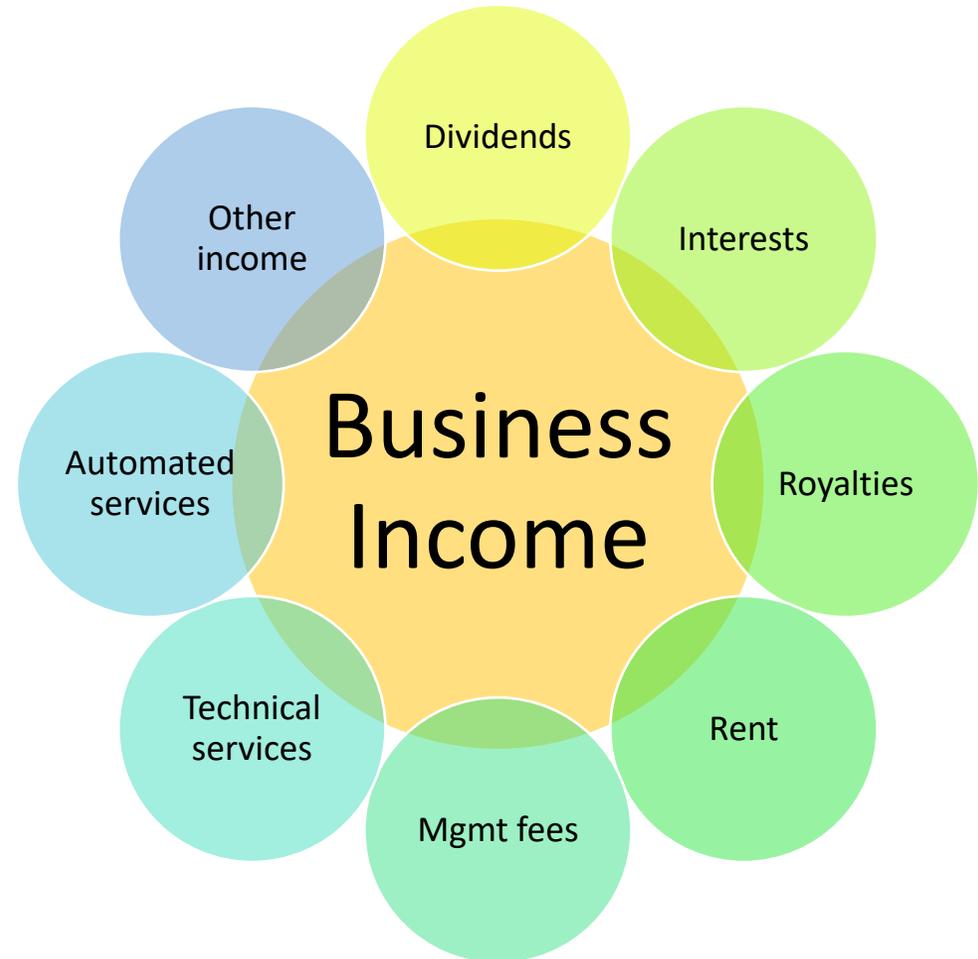
What's wrong with tax treaties?



Schedular structure: complex, costly, and risky for double nontaxation.



Pro-capital exporting states: treaties shift from a system that is source-based by default to a system that is residence-based by design.



What about double taxation?

Are treaties needed to prevent double tax?

- Unilateral measures (FTC/exemption) already provided by most residence states.

Does double tax restrict FDI?

- Literature on tax treaties & FDI: largely inconclusive.
- Literature on FDI determinants: rule of law, infrastructure, labor costs/human capital, consumer market, R&D, conflicts/corruption.
- Studies on int'l double tax & FDI: what matters is the overall burden (better to be taxed 10 times at 1% than 1 time at 20%).

Is double tax normatively bad?

- Assets are often multiple taxed.
- Unfairness is about unequal/discriminatory taxation (horizontal equity) or excessive/confiscatory taxation.
- Single tax can lead to “double dipping” and “free riding” by MNEs.

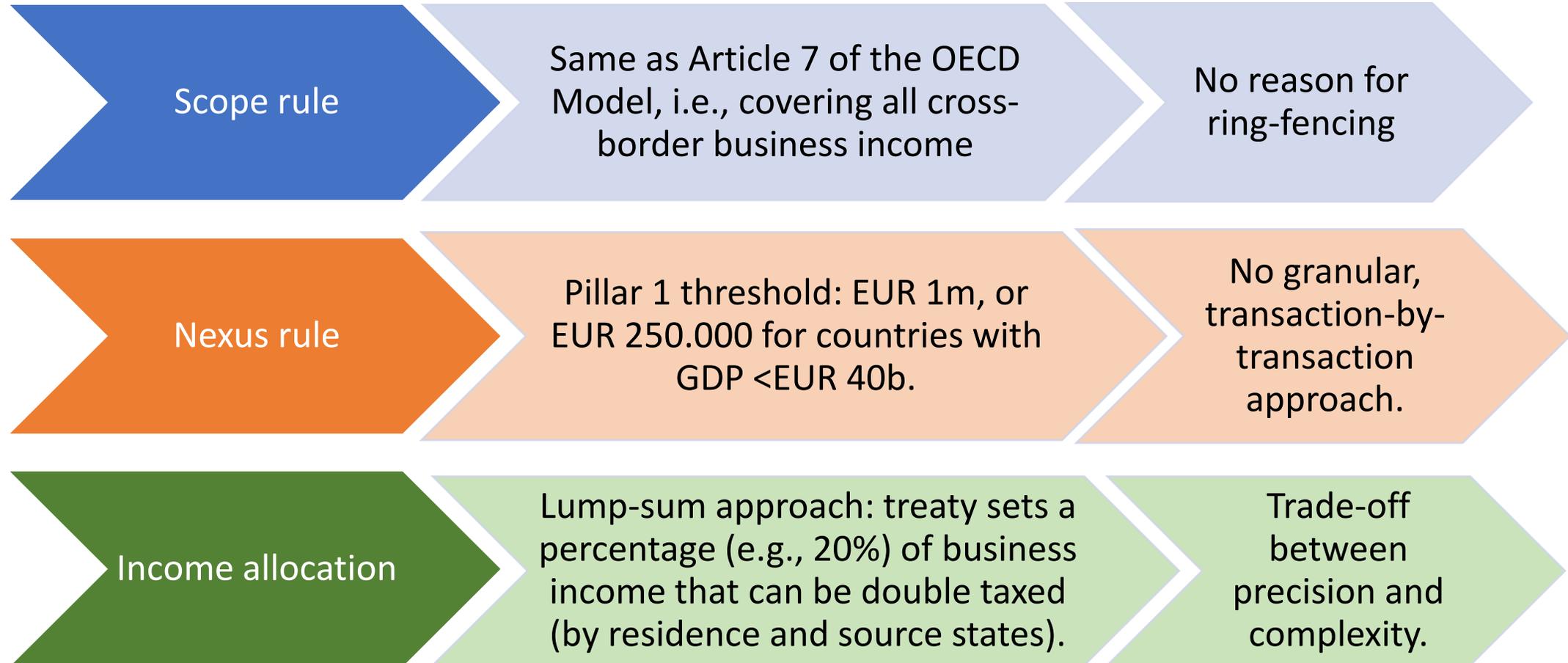
A simplified mechanism

Treaty partners agree to a reduced percentage of the company's relevant profits (e.g., 20%) to be always allocated to source without reducing the percentage of the profits that is allocated to residence.

Why?

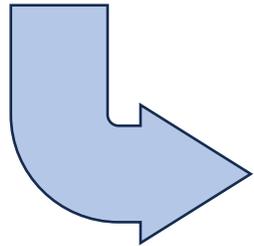
- Source states wouldn't have to depend on PE to tax.
- Pillar 1 is too complex while gains for developing countries are uncertain.
- Formulary apportionment requires new system that is unlikely in the near future.
- Simplifying existing treaties increases legal certainty and reduces costs.

Rule design

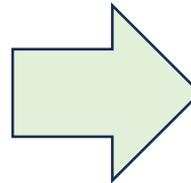


Legal certainty

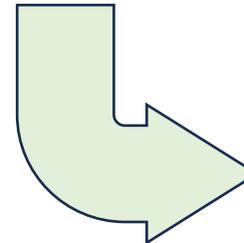
The mechanism should be as **clear and unambiguous** as possible.



The allowed double taxation **may not exceed** the agreed upon percentage on a global level.

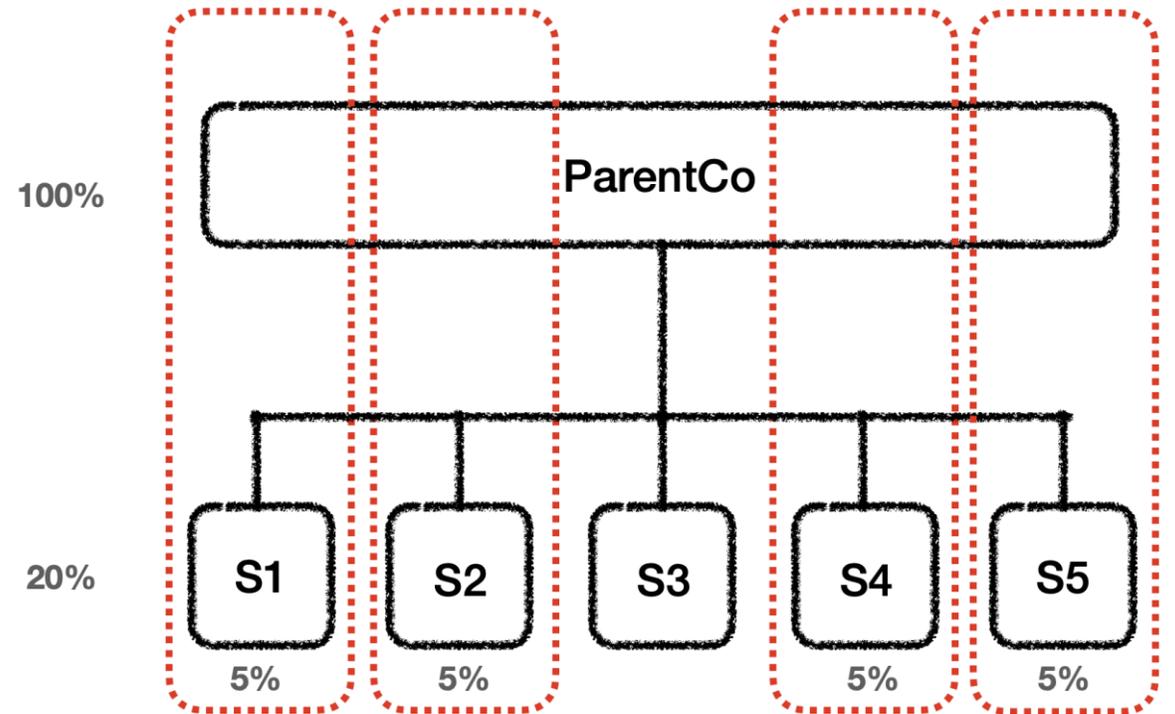
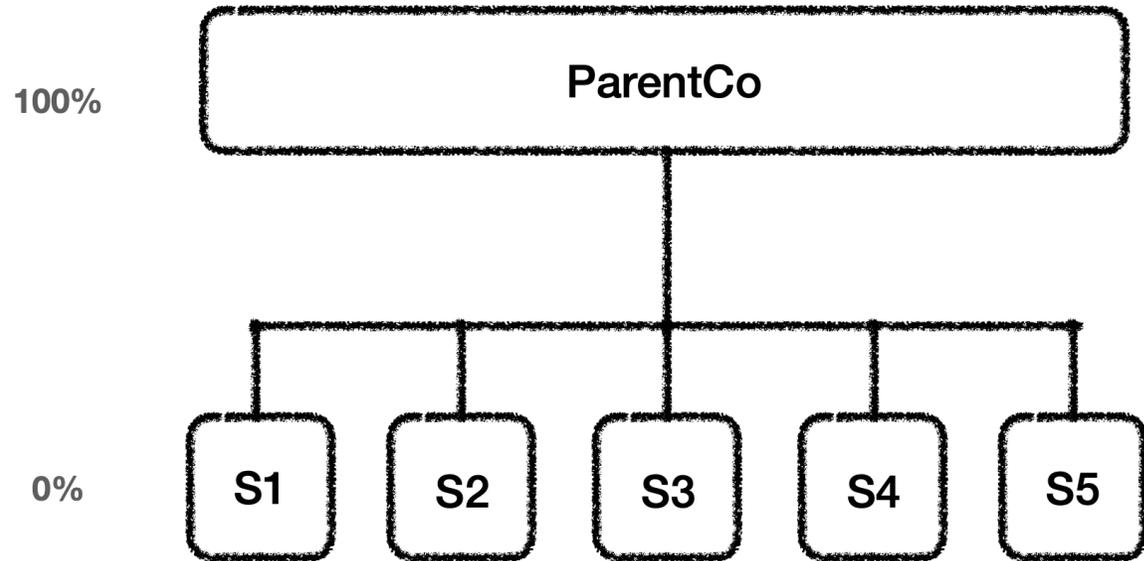


Eligible Source jurisdictions share the extra 20% of the tax base equally.



Equal sharing is based on pragmatic and theoretical considerations.

Simplified example



Double taxation should not be an
obstacle for making tax treaties fairer
and easier to apply.

