The Residence of the Employer in the '183-Day Clause' (Article 15 of the OECD's Model Double Taxation Convention)*

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I. Article 15 MC

Juridical double taxation means 'the imposition of comparable taxes in two (or more) states on the same taxpayer in respect to the same subject matter and for identical periods'.[1] No rule in International Law prohibits double taxation[2], but it is generally recognized that it must be avoided.[3]

Double Taxation Conventions (DTC) are part of International Law. They limit the content of the tax law of both contracting States.[4] The OECD's Model Convention of 1977 (MC), the structure of which was followed by the UN Model Convention and by several conventions in force, is divided in seven chapters, the most important of which is the third one, which includes rules for avoiding double taxation of income.[5]

Article 15 MC includes a distributive rule for income derived from dependent personal services.[6] According to Article 15 MC such income should be taxed only by the State where the taxpayer resides (State of Residence).[7] This is in line with the systematic approach adopted by the MC, since the State of Residence is likely to be in a more favourable position to make comprehensive use of the right to tax income from both domestic and foreign sources.[8] Also the UN Convention adopted this rule. This may be explained by the fact that payments of this kind made by developing States to developed countries seem to be insignificant.[9]

A limitation to this rule may be found in the *Place-of-Work Principle*[10] (Article 15 (1) (2) MC), according to which the income derived from dependent services should be taxed in the

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[1] *See Model Double Taxation Convention on Income and on Capital, Report of the OECD Committee on Fiscal Affairs*, 1977, at para. 3.

[2] *See* BStBl. II 1975, 497; Vogel, K. *Der räumliche Anwendungsbereich der Verwaltungsrechtsnorm*, Frankfurt/Main, Berlin, Alfred Metzner Verlag, 1965, p. 351–356; Mössner, J.M., *Rechtsprechungs-Report Internationales Steuerrecht*, Herne/Berlin, Verlag Neue Wirtschafts-Briefe, 1991, at 481; Tipke, K. u. Lang, J., *Steuerrecht: ein systematischer Grundriß*, 12. Auflage, Köln, Verlag Otto Schmidt KG, 1989, p. 146.

[3] Rothmann, G.W., *Interpretação e Aplicação dos Acordos Internacionais contra a Bitributação*, S. Paulo, p. 77.

[4] Vogel, K., *Klaus Vogel on double taxation conventions: a commentary to the OECD-, UN- and US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice*, Deventer, the Netherlands, Kluwer Law and Taxation Publishers, 1991 (hereinafter cited as 'DTC-Commentary'), Introduction, at 26.

[5] *See* Vogel, DTC-Commentary, Introd., at 49.

[6] There are special rules for Director's fees and remuneration of top level managerial officials (Art. 16 MC), artistes and athletes (Art. 17 MC), pensions (Art. 18 MC), government services (Art. 19 MC) and students (Art. 20).

[7] Art. 15 MC declares:

> '1. Subject to the provisions of Articles 16, 18 and 19, salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived there from may be taxed in that other State.
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> 2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State shall be taxable only in the first-mentioned State if:
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> a) the recipient is present in the other State for a period or periods not exceeding the aggregate 183 days in the fiscal year concerned, and
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> b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and
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> c) the remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other State.
>
> 3. . . . .'

[8] Vogel, DTC-Commentary, Art. 15 at 7.

[9] Dornelles, F.N., 'O Modelo da ONU para Eliminar a Dupla Tributação de Renda, e os Países em Desenvolvimento', in Tavolaro et all., *Princípios Tributários no Direito Brasileiro e Comparado*, Rio de Janeiro, Forense, 1988, p. 195 (225).

[10] *See*: Mössner, J.M., cit. (FN 2), R. 615.

State where the services are rendered (State of employment). This State must be able to tax an income which is linked to itself. This principle is to be applied when the services are straightly connected to the State of employment.

In the case of a short term activity, however, such straight connection seems not to exist. For this reason Article 15 (2) MC excludes the application of the Place-of-Work Principle in such cases.[11] The '183-day clause' determines that the State of Residence may tax such activities, excluding the right of the State of employment to tax the same income.

According to Article 15 MC, the Place-of-Work Principle is only to be applied if the taxpayer is present in the State of employment for a period or periods exceeding in the aggregate 183 days in the fiscal year concerned, or if his income is paid by, or on behalf of, an *employer* which *is resident in the State of employment*, or if it is borne by a permanent establishment or a fixed base which the employer has in that state.[12]

The question of the determination of a straight connection to the State of the Local of Activity is, thus, regulated by Article 15 (2) MC. Instead of a (always subjective) test of connection to the Local of Activity, the MC adopts objective criteria for the application of the Place-of-Work Principle.

The interpretation of the '183-day clause' is problematic, since the MC contains no definition for many expressions, as 'salaries, wages and similar remuneration',[13] 'dependent personal services'[14] or 'employer'.[15]

For interpreting the expression 'not in (the State of employment) resident employer', the question is of other nature. Article 4 MC defines what 'a person resident in a contracting state' is, and this definition should be valid for the application of Article 15 MC.[16]

Since the application of the '183-day clause' depends on proving that the employer is *not* resident of the State of employment, one could deny its application in any case, when the employer, 'under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature.'[17]

It may occur, however, that according to the multiple criteria fixed by Article 4 (1), the employer would not only be resident of the State of employment, but also of the State of Residence of the taxpayer (employee). Paragraphs 2 and 3 of Article 4 MC solve the case of *double residence*, in order to grant that a person is always to be considered resident of only one state.

If one concludes that Paragraphs 2 and 3 of Article 4 MC are also to be applied in the case of double residence of the employer, then it will be possible to consider an employer as 'not resident' of the State of employment, although he may be liable to tax therein. In this case, the State of employment would not be allowed to tax the income of the employee, according to the '183-day clause'.

On the other hand, one could apply the '183-day clause' from a 'lex-fori' point of view. Such interpretation could be based in Article 3 (2) of the MC. This alternative might imply that no double residence of the employer should be considered, since each State would apply its own criteria for determining the residence of the employer. This might result in different solutions for the same case, depending on the court which would examine it.

Finally, one could try an autonomous interpretation of the '183-day clause'. The criteria for such interpretation should also be discussed.

II. The 'Lex-Fori' Solution: Application of Article 3 (2) MC

DTCs are international agreements. Their interpretation must follow the rules contained in the Vienna Convention on the Law of Treaties of 23 May 1969 (hereinafter referred to as 'VCLT'). Article 3 (2) MC, on the other hand, is a special rule of interpretation, in relation to the rules of the VCLT and as such takes precedence over them.[18]

Unless the context otherwise requires, by force of Article 3 (2) MC, any term not defined

[11] Siefert, B., 'Der Arbeitgeberbegriff im deutschen Abkommensrecht', RIW 1986, 979, expresses the opinion that Art. 15 (2) MC is an exception to the Principle of the Local of Activity.
[12] *See* the positive formel in Vogel, DTC-Commentary, Art. 15, at 12.
[13] *See* Vogel, DTC-Commentary, Art. 15, at 14.
[14] *See* Vogel, DTC-Commentary, Art. 15 at 16.
[15] *See* Vogel, DTC-Commentary, Art. 15 at 27.
[16] *See* Vogel, DTC-Commentary Art. 15, at 13; von Bornhaupt, K.J., 'Lohnsteuerrechtliche Fragen bei Entsendung von Arbeitnehmern ins Ausland und vom Ausland ins Inland,' in *Betriebsberater Beilage* 16/1985, p. 14; for the DTC between Germany and Switzerland, *see* Flick, H., Wassermeyer, F., Wingert, K., Kempermann, M., *Doppelbesteuerungsabkommen Deutschland-Schweiz*, Köln, Verlag Dr. Otto Schmidt KG, Art. 15, at 48.
[17] Art. 4 (1) MC.
[18] *See* Vogel, DTC-Commentary, Art. 3, at 61, 62.

in the MC should have the meaning which it has under the law of the State applying the DTC, concerning the taxes to which the Convention refers.

If one would apply this rule, by interpreting the '183-day clause', one should conclude that a double residence of the employer would never happen, since each State would use its own concept of 'residence'. If the employer is a 'resident' of the State of employment, according to its own internal tax law, then this State might apply the '183-day clause', notwithstanding the fact that the employer might also be a resident of the State of Residence of the taxpayer (employee).

It seems to be convenient to build an example, in order to show the risk of such an interpretation. Suppose a DTC, following the MC, signed between States A and B. The employer X, who is a resident of State A, works for 180 days in the State B. Its employer is a Company, which has its seat in the State A, the place of management of which is in the State B. According to the laws of State A, a Company is *resident* in that State if its seat is located in that State. On the other hand, the State B's laws define the residence of a Company exclusively according to the place of its management. The employer is, thus, resident of both States, according to their internal laws. If Courts in State B applied the rule of Article 3 (2), by interpreting the '183-day clause', they would decide, that the requirements of Article 15 (2) (b) are not fulfilled, since the employer is a resident of the State B, according to the internal law concerning the taxes to which the Convention applies. Courts of State B would therefore conclude that the '183-day clause' should not be applied, and that the State of employment (State B) might tax this income. If the same case would be decided by the Courts of State A, then it would conclude that, according to the meaning of 'residence' valid in State A (place of seat), the employer was not a resident of the State B. Since X was present in the State B for less than 183 days, the Courts would conclude that the requirements of the '183-day clause' were fulfilled, and that *only* State A would be allowed to tax the income.

Similar problems could result, if the employer had its seat in State B, but the place of its management were in State A: The courts of State B would conclude for the application of the '183-day rule' (by denying the residence of the employer according to the criteria of internal law) and would exclude a taxation in State B. On the other hand, the Courts in State A would decide that (according to the meaning valid in State A) the employer was a resident of State B and would therefore exclude the application of the '183-day clause', concluding that only State B might tax this income. A 'double non-taxation' would result in this case.[19]

These problems might be avoided if one would follow the opinion of Avery Jones and his co-authors. They claim that qualifications by the State of Source according to its domestic law are always binding on the State of Residence.[20]

This opinion is based on that the meaning of the expression 'application' in the wording of Article 3 (2) MC should be decisive. These authors claim, that 'the residence State . . . by asking itself whether in the opposite situation it would have taxed the income in the same way as the source State . . . does not apply the convention', since 'it should take the answer for granted'.

However, this reasoning may not be accepted. The exemption (or credit) granted by the State of Residence depends on examining whether the income, 'in accordance with the provisions of this Convention, may be taxed in the other Contracting State'. Such test depends on the application of the distributive rules.[21] In the case of double non-taxation above, for instance, the Courts of State A would have to determine, whether Article 15 allows a taxation by the State of Source (State of employment) and whether this taxation is limited, or not, by the 183-day clause. This would be an 'application' of the distributive rule by the State of Residence.

On the other hand, one should consider that Article 15 (2) MC does not refer to a mere 'residence', but specifically to a residence in 'the other State' (in the State of employment). The interpretation of the '183-day clause' does not depend, therefore, on determining the meaning of 'residence', but on examining whether the 'lex-fori' defines what *residence in the State of employment* means. It is possible to find such definition in the laws of the State of employment, but not of the State of Residence, since the latter would not define the criteria for being resident of a specific foreign country.

[19] *See* Vogel, DTC-Commentary, Introd. at 97; Art. 3 at 60; ibdem. 'La Clause de Renvoi de l'Article 3, Par. 2 Modèle de Convention de l'OCDE' in École Supérieure de Sciences Fiscales (org.), *Réflexions offertes a Paul Sibile*, Bruxelles, Établissements Émile Bruylant, 1981, p. 957.

[20] Avery Jones, J.F. et all., 'The Interpretation of Tax Treaties with Particular Reference to Article 3 (2) of the OECD Model', 1984 BTR 14, 90 (50–54).

[21] *See* Vogel, DTC-Commentary, Art. 3, at 65.

Surprisingly, this confirms the conclusions of which Avery Jones and his co-authors, that the question should not be solved taking into consideration the law of the State of Residence. However, such conclusion is *not* based on the arguments of these authors, and is only valid for the specific question of the determination of the residence of the employer in Article 15 (2) MC. Only the laws of the State of the Activity might be able to determine whether a person is resident in it, or not. The courts of the State of Residence should take this as a fact, not as a juridical question to be decided.

An application of Article 3 (2) MC would depend, on the other hand, that the expression would not be defined in the MC itself. Therefore, the application of the internal law (of the State of employment, exclusively!!) would depend on affirming that the definition of residence, in Article 4 MC would not be applicable for the interpretation of Article 15 (2) MC.

The definition of the term 'resident of a Contracting State' in Article 4 (1) MC is valid 'for the purposes of' the whole convention. According to this rule, residence should be determined according to the verification, whether the person, 'under the laws of that State, is liable to tax therin by reason of this domicile, residence, place of management or any other criterion of a similar nature'.

One should conclude, therefore, that the interpretation of Article 15 (2) MC is not a case of application of Article 3 (2) MC. The expression 'resident in a Contracting State' is defined in the MC, and such definition should be applied.

If the application of the definition of Article 4 (1) would imply that the employer should be considered resident of both the Residence and the Activity State of the taxpayer (employee), then one should determine, whether the '183-day clause' is to be applied, or not. In other words, the question is whether a definition in the MC (Article 4 (1)) is to be applied for the interpretation of a MC's rule (Article 15 (2) (b)). This is an interpretation problem, but which is not included in the scope of Article 3 (2) MC, since this regulates the *meaning of terms* not defined,[22] but it is not a general interpretation rule, which would bring internal criteria of interpretation to the sphere of DTC.[23]

One should conclude, therefore, that Article 3 (2) is not to be applied for the interpretation of Article 15 (2) MC.

III. Not Application of Paragraphs 2 and 3 of Article 4 MC for the Interpretation of Article 15 (2) (b) MC

III.1. Double Residence and the MC

Article 4 (1) MC defines what a 'resident person' is. This concept is important for determining a convention's personal scope of application.[24] This is not the only function of Article 4 MC. Paragraphs 2 and 3 of Article 4 MC rule the case in which a double residence would result from the application of Article 4 (1) MC. A solution of the double residence case would not be necessary, if the objective of Article 4 MC were exclusively defining the personal scope of application of the MC, since Article 1 MC declares that the Convention should apply for persons who are resident of one *or both* of the Contracting States.

For understanding why Article 4 includes rules avoiding a double residence solution, one needs to take into consideration the structure of the MC. The application of the MC depends on determining which is the State of Residence and which is the State of Source. The distributive rules of the MC state whether each type of income is to be taxed exclusively by one ('shall be taxable only in . . .') or whether the State of Source may tax it ('may be taxed in . . .') with exemption or credit by the State of Residence.[25]

These distributive rules take the 'person resident of a Contracting State' for granted. They cannot be applied, therefore, if a person is resident in both States.[26] Take, for instance, Article 14 MC ('Income derived by a resident of a Contracting State in respect of professional services or other activities of an independent character *shall be taxable only* in that State . . .'), which states an exclusive taxation by the State of Residence. The wording

[22] Vogel, DTC-Commentary, Art. 3 at 62; Mössner, J.M., *Neue Auslegungsfragen bei Anwendung von Doppelbesteuerungsabkommen*, Hamburg, Institut für Ausländisches und Internationales Finanz- und Steuerwesen – Universität Hamburg, 1987, p. 18.

[23] Other opinion: Kluge, V., 'Die Auslegung von Doppelbesteuerungsabkommen', RIW 1975, 90 (96); Diehl, W., 'Qualifikationskonflikte im Außensteuerrecht', FR 1978, 517.

[24] *See* the OECD-Commentary cit. (FN 1), Art. 1 at 1.

[25] *See* Vogel, DTC-Commentary, Introd., at 49 ff.

[26] *See* Korn, R., Debatin, H., *Doppelbesteuerung*, München, Beck, Systematik III, at 35b.

'shall . . . only' means that the State of Source must exempt this income.[27] If it were possible that a taxpayer would be considered resident in both States, then one would conclude that a State would tax (as State of Residence) and exempt (as State of Source) the income at the same moment. Of course this does not comply with the objectives of the DTC.

In conclusion, paragraphs 2 and 3 of Article 4 MC have the scope of making it possible to apply a distributive rule, in case of double residence of the taxpayer.

III.2. Article 4(2) and (3) MC and the '183-Day Clause'

According to Article 15 (2) (b) of the MC, the Place-of-Work Principle may only be applied if 'the remuneration is paid by, or on behalf of, *an employer who is not a resident of the other State*'. That means that if the employer of the taxpayer is resident of the State of employment, this State may tax the taxpayer's income, even if the taxpayer's permanence in the State is for an irrelevant period.

The term 'resident' is defined in Article 4 (1) MC, and this definition is valid for the whole MC.[28] The question which must be solved is whether the same rule applies, if the taxpayer's employer is a double resident person, i.e. is a resident of the State of employment, as well as of the State of Residence of the taxpayer.

By the wording of Article 4 (2) and (3) MC,[29] one could conclude that the MC does never admit that the interpretation of the expression 'resident in a Contracting State' results in a double residence of a person. If these paragraphs may also be applied to solve the question of double residence of the taxpayer's employer, one must conclude that his residence should be clearly determined.

The interpretation of an international agreement must be made, though, according to the rules of the VCLT.[30] Of primary importance for solving the question is therefore Article 31 (1) VCLT:

> 'Section 3. Interpretation of Treaties
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> Article 31 – General rule of interpretation
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> 1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to terms of the treaty in their context and in the light of its object and purpose. . . . . .'

The 'ordinary meaning' of the terms of Article 4 (2) and (3) admit both, their application in any case where the application of Article 4 (1) results in double residence of a person (any one), or to limit it to the cases of double residence of the taxpayer. The context[31] of the MC is not enough for solving the question of the limits of application of Article 4 (2) and (3). It is necessary, therefore, to investigate the object and purpose of the MC, in order to solve the

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[27] *See* Vogel, DTC-Commentary, Preface to Arts. 6-22, at 3; Art. 14, at 8.

[28] *See above*, p. 7.

[29] Article 4 MC – Residence:

'1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature. But this term does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.

2. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:

a) he shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident of the State with which his personal and economic relations are closer (centre of vital interests);

b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident of the State in which he has an habitual abode;

c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident of the State of which he is a national;

d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

3. Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident of the State in which its place of effective management is situated'.

[30] *See supra* p. 5.

[31] Paragraph 2 of Art. 31 VCLT limits the meaning of the expression 'context': it includes, besides the text, including its preamble and annexes, only related completing documents made in connection with the treaty.

question of the interpretation of Article 4 (2) and (3) in connection with Article 15 (2) (b) MC.

The object and purpose of the treaty may be found in its preamble. If the 'object and purpose' referred to in Article 31 (1) VCLT were only those declared in the agreement's preamble, though, then there would be no reason for including object and purpose among the interpretative methods, since the preamble belongs to the context of the treaty and should therefore be observed. One must conclude, therefore, that the 'object and purpose' referred to in Article 31 (1) may be other than the expressly mentioned in the preamble of the treaty.

The OECD's Commentary to the MC is of primary importance for determining the object and purpose of a DTC and for determining the scope of its rules.

For States members of OECD, this results from the fact that the OECD Council recommended that the governments of the Member States follow the model 'when concluding new bilateral conventions or revising existing bilateral conventions between them to conform to the Model Convention . . . as interpreted by the Commentaries thereto . . .'. One should conclude, therefore, that the object and purpose of a treaty's rule were known and accepted by the Member States, when they signed a treaty following the MC.[32] This opinion may also be found in courts' decisions in Germany,[33] Great Britain,[34] Switzerland[35] and USA.[36]

In case of DTC between countries which are not all members of the OECD, the use of the OECD's Commentary for investigating the object of purpose of the treaty is not immediate. For such countries, the recommendations of the OECD Council must not be observed. One cannot assume, therefore, that the Commentary was observed by these countries, when they signed the treaty. Despite this, one may assume that if a DTC (signed by a not-OECD member) coincides with the OECD MC, a comparison of this DTC and the MC must be possible. Since the OECD's Commentary is to be observed for the interpretation of the MC, it may also be applied in interpreting DTC which follow the MC. Of course, the circumstances of the individual cases may demand a different interpretation.[37]

The application of the OECD's Commentary for the interpretation of DTC which follow the MC may also be supported by the precept of common interpretation,[38] according to which 'in interpreting tax treaties, . . . an interpretation should be sought which is most likely to be accepted in both contracting States'. It seems to be clear that this 'common interpretation' may be most easily achieved through the observation of the OECD's Commentary to the MC.

The question to be solved is whether the OECD's Commentary explains whether Article 4 (2) and (3) may be used, or not, for solving a case of double residence of the taxpayer's employer.

Of primary importance, here, is Paragraph 7 of the OECD's commentary to Article 4 MC, which declares that the special provisions of Article 4 (2) and (3) are proposed to solve a conflict which results when both States claim that the taxpayer is fully liable to tax.

Problematic is, though, to determine whether these provisions are also to solve a case of a conflict of claims between a State of Residence and a State or Source, or whether their scope is limited to solve a conflict in which two States claim to be the State of Residence. This

[32] Vogel, K., 'Abkommensvergleich als Methode bei der Auslegung von Doppelbesteuerungsabkommen', in *Steuerberater-Jahrbuch* 1983/84, 373 (378); ibdem. DTC-Commentary, Introd. at 81; Strobl, J., 'Zur Auslegung von Doppelbesteuerungsabkommen unter besonderer Berücksichtigung ausländischer Rechtsordnung', in *Handelsrecht und Steuerrecht: Festschrift für Dr. Dr. h.c. Geog Döllerer*, F. Klein (org.), Düsseldorf, IDW Verlag, 1988, p. 635 (651); Ward, D.A., 'Principles to be Applied in Interpreting Tax Treaties', in BIFD 1980, S. 545 (549); Korn/Debatin cit. (FN 26) Systematik III at 131. Considering the OECD's Commentary as preparative work of the treaty, *see*: Mössner, J.M., 'Zur Auslegung von Doppelbesteuerungsabkommen', in Böckstiegel et all. (orgs.), *Völkerrecht, Recht der Internationalen Organisationen, Weltwirtschafts – Festschrift für Ignaz Seidl-Hohenveldern*, Köln, Berlin, Bonn, München, Carl Haymanns Verlag, 1988, S. 403 (412); Klebau, B. 'Einzelprobleme bei der Auslegung von Doppelbesteuerungsabkommen', RIW 1985, 125 (132 ff); only for new treaties which follow the MC, *see*: Höhn, E., *Doppelbesteuerungsrecht – Eine Einführung in das interkantonale und internationale Steuerrecht der Schweiz*, Bern und Stuttgart, Verlag Paul Haupt, 1973, p. 54.

[33] BStBl. III 1966, 24 (27).

[34] 'It is a common ground that in the light of the decision of the House of Lords in *Fothergrill* v. *Monarch Airlines Ltd* [1981] AC 251 the commentaries can and indeed must be referred to as guide to the interpretation of the treaty' – 1984 STC 461 (511).

[35] '. . . la Convention hispano-suisse se fonde sur le modèle de convention en vue d'éviter les doubles impositions que l'OCDE a proposé en 1963 (. . .) Il faut donc interpréter les dispositions de cette Convention à la lumière des commentaires que le comité fiscal de l'OCDE a donnés dans un rapport de juillet 1963.' – BGE 102 Ib 264 (269).

[36] *U.S.* v. *Burbank & Co. Ltd. et al.*, 75-2-USTC.

[37] Vogel, DBA Commentary, Introd. at 82.

[38] Vogel, DTC Commentary, Introd., at 73 ff; Mössner, cit. (FN 32), p. 406–407.

question might be of difficult solution, if one would take into consideration only the (not OECD official) German version of the OECD's Commentary. Accordingly, Paragraph 5 of the commentary to Article 4 MC declares:

> '5. Dies wird besonders deutlich, wenn der Konflikt nicht zwischen zwei Wohnsitzen, sondern zwischen Wohnsitz und Quelle oder Belegenheit besteht. Doch gelten dieselben Erwägungen auch *für den Konflikt zwischen zwei Wohnsitzen.* Die Besonderheit des *letztgenannten Falles* besteht lediglich darin, daß durch die Bezugnahme auf den Wohnsitzbegriff, wie er im innerstaatlichen Recht der betreffenden Staaten gilt, keine Lösung des Konflikts erreicht werden kann. *Für diese Fälle* bedarf es besonderer Bestimmungen in dem Abkommen darüber, welcher der beiden Wohnsitzbegriffe Vorrang hat.'

One could understand that the expression 'für diese Fälle' refers to more than one case. Since the text refers to two different cases of conflicts, i.e., a conflict between two residences, and a conflict between residence and source, one could think that paragraphs 2 and 3 of Article 4 MC are to be applied in both cases.

If one takes into consideration the English version of the same text, the conclusions may be different:

> '5. This manifests itself quite clearly in the cases where there is no conflict at all between two residences, but where the conflict exists only between residence and source or situs. But the same view applies in conflicts between two residences. The special point in *these cases* is only that no solution of the conflict can be arrived at by reference to the concept of residence adopted in the domestic laws of the States concerned. *In these cases* special provisions must be established in the Convention to determine which of the two concepts of residence is to be given preference.'

There is a difference between the English and the German versions. In the English version, the last sentence refers to 'these cases' (plural). But also the previous sentence is in plural, i.e., 'the special point in these cases', not like the German version 'die Besonderheit des letztgenannten Falles'. One should investigate whether the last sentence actually refers to 'den letzen genannten Fall' (the last mentioned case) or to both cases.

This question may be solved, if one takes into consideration the French version of the same text, which declares:

> 'On peut facilement s'en rendre compte lorqu'il y a conflit non pas entre deux résidences, mais entre la résidence et la source ou le situs. Toutefois, les mêmes considérations s'appliquen *en cas de conflit entre deux résidences. Dans ce dernier cas*, il faut cependant noter que l'on ne peut parvenir à une solution du conflit en se référant à la notion de résidence adoptée par la législation interne des Etats considérés. Des clauses spéciales doivent être insérées dans la Convention *pour déterminer à laquelle des deux notions de résidence* il convient d'accorder la préference.'

It is clear in this text, that Article 4 (2) and (3) are intended to solve a conflict between two States, when both claim to be the State of Residence of the taxpayer. The case of a conflict between a State of Residence and a State of source was not, therefore, included in the purposes of this paragraph.

This interpretation may be confirmed by the wording of paragraphs 6 and 7 of the OECD's commentary to Article 4 MC, which refer to a case in which '*both States claim that* (*the taxpayer*) *is fully liable to tax* . . . This conflict has to be solved by the Convention . . . The fact is quite simply that in the case of such a conflict a choice must necessarily be made between *the two claims*, and it is *on this point* that the Article proposes special rules'. No doubt might subsist, that the claims referred to are those of two States of residence (where the taxpayer is fully liable to tax).

Further one has to consider that paragraph 7 of the OECD's commentary to Article 4 declares that this Article does not 'lay down special rules on residence' and that the domestic laws of the Contracting States should not be ignored. Such an affirmation would not subsist, if it were not possible to be there a case conflict, where one should apply the domestic concept of residence, instead of the definitions of paragraphs 2 and 3 of Article 4 MC.

In conclusion, one may affirm that only the first paragraph of Article 4 MC is to be applied for the whole MC. Paragraphs 2 and 3 of this article are proposed only for the case in which there is a conflict of claims between two States, both States claiming to be the State of Residence of the taxpayer.

A comparison between the above mentioned object and purpose of Article 4 (2) and (3) MC and the interpretative question of Article 15 (2) (b) MC results that these last paragraphs of Article 4 MC should not be applied for solving a case of double residence of the taxpayer's employer.

Paragraphs 2 and 3 of Article 4 MC are designed to solve a conflict which would make it impossible to apply the distributive rules of the DTC, because it would not be possible to decide which is the residence State of the taxpayer. This is not the case of the '183-day clause'. The question, here, is whether the taxpayer's *employer* is resident of the State of employment, or not. This employer is not a taxpayer, who is protected from a double taxation by means of the DTC. Even if the employer is a double resident, there will be no doubt about which is the State of Residence of the *taxpayer* (employee). Of course a double residence of the employer may result in a conflict between both States, but this conflict is *not* a conflict about the State of Residence of the taxpayer. Article 4 (2) and (3) MC may not, therefore, solve such conflict.[39]

IV. Limited Tax Liability

The second sentence of paragraph 1 of Article 4 MC states that the term 'resident of a contracting State' 'does not include any person who is liable to tax in that State in respect only of *income* from sources in that State or capital situated therein' (limited tax liability). One should, hereby, verify how far this limitation of the concept of residence applies in the case of the interpretation of Article 15 (2) (b).

The basic question is to verify whether the '183-day clause' is also to be applied, if the taxpayer's employer is limited liable to tax in the State of employment. Basic is however, to know what kind of limited tax liability is meant by Article 4 (1) MC. The wording of this second sentence of Article 4 (1) MC may be interpreted in two different ways, according to the meaning given to the term 'income'. This could be either 'net income', i.e. revenue minus expenses, or 'gross income', i.e. revenue.

There is no definition of the term 'income' in the MC. According to Article 3 (2) MC, this expression should have the meaning which it has under the law of the States concerning the taxes to which the Convention applies. It is very rare, though, that the income tax internal legislations define what 'income' means,[40] since the 'income types' are usually specified and ruled unindependent of a general concept.[41] Since there is no definition in the domestic laws, the interpretation of the word 'income' should be made in light of the treaty itself and its purposes (autonomous qualification).[42] The basic question is, therefore, whether 'gross' or 'net' income seems to be more adequate for applying the second sentence of Article 4 (1) MC, in a case of definition of the residence of the taxpayer's employer, for proposes of Article 15 (2) (b) MC.

The object and purpose of the '183-day clause' are 'to facilitate the international movement of qualified personnel, as in the case of firms which sell capital goods and are responsible for installing and assembling them abroad.[43]

Such facilitation is not interesting for the Contracting States, however, if the State of employment might have financial losses, because the payments made to the installing personnel could be considered business expenses of their employer, reducing the income tax paid by the last-mentioned.[44]

The purpose of the '183-day rule' is, thus, to grant the taxation of the State of employment, if the taxpayer's employer is a resident (and liable to taxation) in this State.[45] If there were no restriction in Article 15 (2) (b) MC, then the State of Activity might have to lose its revenues twice: (1) the employee might not be taxed, due to the Place-of-Work Principle and (2) the employer might deduce the payments made to the employee from his taxable income in the

[39] *See* Vogel, DTC Commentary, Art. 15, at 29; von Bornhaupt, K.J., 'Lohnsteuerrechtliche Fragen bei Entsendung von Arbeitnehmern ins Ausland und vom Ausland ins Inland' in *Betriebsberater – Beilage* 16/1985, p. 14.

[40] Brazilian Código Tributário Nacional defines (Art. 43) the expression 'income', as being the 'product of capital, of labour or of the combination of both of them'. This definition is not enough, though, to determine whether 'gross' or 'net' income is meant.

[41] Germany, for instance, in § 2 of the Einkommensteuergesetz.

[42] Vogel, DTC-Commentary, Introd., at 101; Art. 3, at 74.

[43] *See* OECD's Commentary (cit. – FN 1) to Art. 15, paragraph 3.

[44] Siefert, cit (FN 11).

[45] 'This restriction is designed to ensure that the State of employment retains its taxation if the payment has reduced the profits of an enterprise subject to its tax jurisdiction' (Vogel, DTC-Commentary, Art. 15, at 30). Similar *see* Korn/Debatin, cit. (FN 26) Systematik IV, at 279.

same State. Article 15 (2) (b) is therefore a compensation granted to the State of employment, so it will not have a double loss of revenues.

The second sentence of Article 4 (1) MC should be applied in the interpretation of the '183-day clause', in light of this object of Article 15 (2) (b) MC. The expression 'income' should be interpreted, hereby, in a way to grant that such a double loss by the State of employment will not occur.

If the term 'income' should mean 'net income', then the second sentence of Article 4 (1) would mean that the taxpayer's employer would only not be considered a resident of the State of employment, if his 'net income' were subject to taxation in that State. If the taxpayer received his remuneration from an employer taxed on his net income, then this employer would not be considered a resident of the State of employment and the '183-day clause' would apply: the State of employment might not tax this income. The consequence of this understanding would be that the State of employment would have a double loss, since the remuneration of the employee would not be taxed, but the same remuneration would reduce the tax paid by the employer on the net income. This interpretation is not consistent with the object and purpose of the '183-day clause'.

On the other hand, if the term 'income' should be interpreted as 'gross income', then the employer would not only be a resident of the State of employment, if his tax liability in that State were limited to the 'gross taxation'. In this case, a payment made to an employee would not reduce such liability of the taxpayer's employer. Thus, no double loss would occur.

In conclusion, the second sentence of Article 4 (1) MC must be applied in determining the residence of the taxpayer's employer. The term 'income', however, must be interpreted as 'gross income'. If the employer is subject to tax in the State of employment on his net income (even in limited to some types of income), then he must be considered a resident of this State and the '183-day clause' may not apply.

V. Limited Tax Liability Due to a DTC

Consider the following example:

The employer 'E' carries on his business and has his place of management in State A. The employee 'T' is a resident of the same State A, but is sent to the State B for a 100-day period. According to the laws of State B, E is a resident of that State (and fully liable to tax), because his site is located in that State. E has no permanent establishment in B.

According to paragraph 3 of Article 4 MC, E should be deemed to be a resident of State A, where his place of effective management is situated. If it is true, though, that this paragraph should not be applied for the application of the '183-day rule',[46] then one should consider E resident of the State B, and the remuneration paid to T should be taxed in State B.

This would not be consistent with the object and purpose of Article 15 (2) (b) MC. A short-term-activity does not imply the application of the Place-of-Work Principle, since no straight connection to the State of employment may be affirmed. The limitation of the '183-day clause', to the cases in which the taxpayer's employer is not a resident of the State of employment, is exclusively reasoned on the avoidance of an *undesired double loss* by this State.

By concluding tax treaties, States agree to restrict their substantive tax law reciprocally.[47] If a DTC declares that a type of income of the employer E may only be taxed by State A, there is *no undesired loss* of taxation by State B. This State consciously waives its tax claims. If the discussed limitation of the '183-day clause', for cases in which the taxpayer's employer is not a resident of the State of employment, is aimed to grant that this State does not have an undesired loss, one should conclude that this limitation should not apply, if the loss of the State of employment is not undesired.

The distributive rule applicable to business profits is Article 7 MC. According to this provision, 'the profits of an enterprise of a Contracting State shall be taxable in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein'. Since E has no permanent establishment in State B, this State may only tax the income of E, if E is a resident of this State.

To determine the residence of E, one should apply Article 4 MC. Since E is a resident of both States A and B, according to the rules of Article 4 (1) MC, the 'tiebreaker' rule of Article 4 (3) must be applied. According to this rule, E is deemed to be taxed in State A

[46] See p. 26.
[47] Vogel, DTC-Commentary, Introd., at 45.

(place of its management). That means that State B has *waived*, through the DTC, to tax the income of E.

If State B may not tax E's income, any payment made by E to T implies *no undesired loss* of State B (if State B may not tax E's income, it does not matter to State B, if E reduces, or not, its income). On the other hand, the activity of T, being of short term, implies no significant link of his income to the State of employment. One should conclude, therefore, that the application of the '183-day clause' should result in an exclusive taxation in State A.

Object and purpose of the MC result, therefore, that the expression 'resident' in Article 15 (2) (b) should be interpreted as 'subject to tax on net income'. Exceptuated must be, though, the cases in which the taxpayer's employer is exempted from taxation in the State of employment, due to a distributive rule of a DTC.[48]

It is interesting to note that this conclusion demands the use of the rules of paragraphs 2 and 3 of Article 4 MC, since these rules must be applied to solve the question, whether the taxpayer's employer is exempted to taxation in the State of employment. Despite the fact that these paragraphs are not to be applied in the interpretation of Article 15 (2) (b) MC, they must be applied for interpreting Article 7 MC, which is fundamental in this case.

VI. Conclusion

The expression 'resident' in Article 15 (2) (b) MC should be interpreted as 'liable to tax'. If the taxpayer's employer is not liable to tax, according to the internal law of the State of employment, the '183-day clause' may apply.

If the taxpayer's employer is liable to tax in the State of employment, one should verify if the DTC limits such liability, due to a double residence of the taxpayer's employer. In this case, the taxpayer's employer shall *not* be considered a 'resident' of the State of employment, on applying the '183-day clause'. The State of employment may not tax the income of the taxpayer, in this case.

The interpretative problems discussed herein could be avoided, if the wording of Article 15 (2) (b) were changed, as follows:

> 'b) the remuneration is paid by, or on behalf of, an employer who, in respect of his global net income, or only of income, from which the remuneration may be deduced in the computation of the taxable income, is not:
> I. liable to tax in the other Contracting State, under the laws thereof, by reason of his domicile, residence, place of management or any other criterion of a similar nature; and
> II. to be taxed only by the first mentioned State, due to any provision of this Convention'.

[48] 'Wenn sich der in dem einen Vertragsstaat ansässige Arbeitnehmer nur vorübergehend im anderen Staat aufhält (. . .), soll trotz der Arbeitsausübung die Besteuerung im Tätigkeitsstaat entfallen, *es sei denn, daß diesem Staat aus der Arbeitsvergütung ein Steuerverzicht bei der Unternehmensbesteuerung entstanden ist*' – Korn/Debatin cit. (FN 26) Systematik IV at 279.