

Karin Simader\*)

## International Tax Law Summer Conference in Rust: Taxation of CEO Income – Case Study

### INTERNATIONAL TAX LAW SUMMER CONFERENCE IN RUST: DIE BESTEUERUNG VON GESCHÄFTSFÜHRERBEZÜGEN – FALLSTUDIE

Michael *Lang* leitete bei der siebenten International Tax Law Summer Conference (6.–10. Juli 2008) in Rust (Österreich) am 7. Juli 2008 eine Podiumsdiskussion zum Generalthema „Tax Treaties – What Happens When States Disagree? – Qualification and Classification Conflicts in Tax Treaty Law“, an der mit Heinz *Jirousek*, Michael *Wichmann*, Andrew *Dawson* und Elizabeth *Karzon* hochrangige Experten der Abteilungen für Internationales Steuerrecht der österreichischen, deutschen, britischen und US-amerikanischen Finanzverwaltung teilnahmen. Die Experten diskutierten bei dieser Konferenz – nicht in amtlicher Funktion, sondern in privater Eigenschaft – Fallstudien zu DBA-Fragen, die in der Folge auszugsweise wiedergegeben sind.

#### I. International Tax Law Summer Conference 2008

From 6<sup>th</sup> to 10<sup>th</sup> July, 2008, the 7<sup>th</sup> International Tax Law Summer Conference was held in Rust (Austria). At the panel discussion “Tax Treaties – What Happens When States Disagree?” – chaired by Michael *Lang* – various cases on international tax law were presented and discussed from the perspective of experts from the tax administration. Heinz *Jirousek* (Head of the Department for International Tax Law, Austrian Ministry of Finance), Michael *Wichmann* (Head of Tax Treaty Policy Division, German Federal Ministry of Finance), Andrew *Dawson* (Head of Tax Treaty Team, HM Revenue & Customs, UK) and Elizabeth *Karzon* (Branch Chief, Office of the Associate Chief Counsel, USA), participated in the panel discussion, not in their official function, but in their private capacity. This contribution summarizes the main points of the discussion on a selected case.

#### II. Facts of the Case

Ms *Jones* is a resident of state A and the CEO of a corporation which has its seat and place of effective management in state B. She exercises her activities partly in state A and partly in state B.

**Heinz *Jirousek*:** As far as Austria is concerned, the case would be very clear. Of course, the question is which article of the OECD Model Convention is applicable. If the CEO did not have an employment contract, we would apply Art. 14. If the CEO is employed by the company, her income would be covered by Art. 15 unless there is a specific rule, for example in Art. 16. The tax treaty concluded with Germany contains such a rule, which also covers key personnel. However, if there is no specific rule, we would have to apply Art. 15 because Art. 16 would only apply to members of the board of directors who fulfill supervisory functions. As concerns the case at hand, Austria would apply Art. 15 to Ms *Jones*' income from employment. If state A were Austria, we would tax income generated from activities exercised in Austria and give tax exemption for income generated from activities exercised in state B. As far as our treaty policy is concerned, most of our tax treaties do not provide for a specific rule for income of key managerial personnel. There are very rare exceptions, the most important one being Germany.

\*) Mag. Karin *Simader* ist wissenschaftliche Mitarbeiterin am Institut für Österreichisches und Internationales Steuerrecht der Wirtschaftsuniversität Wien.

## Besteuerung von Geschäftsführerbezügen

**Michael Lang:** This position is also supported by a decision of the Austrian Supreme Administrative Court on the tax treaty between Austria and Switzerland, where the Court concluded that only supervisory activities would be covered under Art. 16, referring to the OECD Commentary.

**Michael Wichmann:** Germany seeks to insert a second paragraph, which extends Art. 16 to legal representatives or top managers of a company. The idea is that management activity is performed where the orders of the manager are implemented, which is in line with the continental European concept of the place of effective management being located where the day-to-day management takes place. For example, the second paragraph of Art. 16 can be found in our tax treaty with Austria, which provides for the exemption method for the avoidance of double taxation for income from these activities. Thus, this income is taxed solely in the country where the seat or place of effective management of the company is located. If a tax treaty is concluded in line with the OECD Model, however, Art. 16 would only cover supervisory activities.

Currently, several cases are pending at the Federal Tax Court which concern the taxation of employed top managers under our notably differing tax treaty with Switzerland. The issue is whether this treaty contains a fiction of the place where the work is performed. This is not only relevant for the allocation of taxing rights, but also for the determination of the method for eliminating double taxation because this treaty applies the exemption method for Germany only if the work "*is performed in Switzerland*". It remains to be seen what the outcome will be.

**Elizabeth Karzon:** The US approach is to tax personal services based on where they are performed, whether the services are performed by a director of a company or a CEO. We do not consider services of a director to be performed where the company's place of management is located. So even if Ms Jones carried out some director functions in addition to her CEO functions, if the US were state B, she would be taxed on the portion of her salary attributable to services performed in the US. We do include Art. 16 in our tax treaties, but we only tax services to the extent that they are rendered in a state.

**Andrew Dawson:** Assuming that the CEO is on the board of directors and some of her responsibilities are in her capacity as a director, while other responsibilities are in her capacity of running the company on a day-to-day basis, we would need to split the activities according to that distinction. Para. 2 of the OECD Model Commentary on Art. 16 is clear on this point. In practice, some countries seem to tax everything based on the person being the CEO. But we would tax only those activities which are performed in the capacity as a member of the board, which is the strict wording of the article following the provisions of the Commentary. We would not necessarily limit the scope of Art. 16 to supervisory activities which are not always the same as activities performed in the capacity as member of the board of directors.

**Michael Lang:** I think the Austrian and the German approaches probably go back to their concept of corporate law, which quite often makes a distinction between the management board and the supervisory board. The idea is that members of the supervisory board are covered under Art. 16 and members of the management board are covered under Art. 15 or Art. 14, depending on whether they have an employment contract or not.

**Heinz Jirousek:** As there is no clear definition in the tax treaty, it depends on national law whether or not we are forced to apply Art. 15 or 16 to a certain part of the income. If the UK taxed a certain amount of the income under Art. 16 and if there was double taxation, we would, in principle, be willing to grant a tax credit.

**Michael Lang:** Is the UK forced by its domestic law to apply the approach described before, or is it just how the UK understands the OECD Model concept?

**Andrew Dawson:** We do not seek to expand our taxing rights. We only tax those activities that were performed in the UK. We have no basis to tax the activities if they are performed outside the UK and the person is not a resident. We, therefore, see this provision as having more relevance when UK residents are, for example, directors of subsidiaries of UK companies in other countries.

**Michael Lang:** If somebody is working for a UK corporation, your argument would not depend on domestic law in the UK? It would be a question of treaty interpretation?

**Andrew Dawson:** Yes, we just take the treaty meaning of the expression "*in his capacity as a member of the board of directors*" as explained by the Commentary. So looking at it the other way round, if another country sought to tax a UK resident on the whole of his remuneration received from a company resident in that other country, we would not feel obliged to give relief for amounts that represent work that was carried out outside that jurisdiction in pursuance of functions that were not of a directorial nature. It would be a conflict of interpretation, not a conflict of qualification.

**Michael Lang:** Under the OECD concept of Art. 23, the way how to solve qualification conflicts is to make a distinction between conflicts arising because of differences in domestic law and such arising because of differences in treaty interpretation. It is quite difficult to distinguish between such types of qualification conflicts.

**Heinz Jirousek:** The automatic solution of the conflict by virtue of Art. 23 could only apply if the conflict is caused by differing binding rules of domestic law. If the problem is caused by different treaty interpretation, it can only be solved through the mechanism of a mutual agreement procedure. If it is just a question of facts because the person fulfills different functions, it would not be a problem to split the salary and give a credit for that part.

## Begriff der „genehmigten Geschäftsvorgänge“ im DBA Indien

(BMF) – Zinsen für ein Finanzierungsdarlehen eines indischen Unternehmens unterliegen der beschränkten Steuerpflicht in Österreich, wenn die zugrunde liegende Darlehensforderung auf einer inländischen Liegenschaft des inländischen Darlehensschuldners sichergestellt wird. Der indische Darlehensgeber unterliegt mit den hierfür bezogenen Hypothekenzinsen im Veranlagungsweg der inländischen Besteuerung, die aber gemäß Art. 11 Abs. 2 DBA Indien 10 % des Bruttobetrag der Zinsen nicht übersteigen darf.

Eine Besonderheit ergibt sich aus Art. 11 Abs. 3 lit. b DBA Indien. Nach dieser Vertragsbestimmung erlangt der indische Darlehensgeber Anspruch auf Steuerfreistellung in Österreich, sofern der Geschäftsvorgang, welcher der Forderung zugrunde liegt, von Österreich „genehmigt worden ist“.

Auf österreichischer Seite ist im gegebenen Zusammenhang keine Erteilung einer Einzelgenehmigung der Geschäftsvorgänge durch die Finanzverwaltung vorgesehen. Solange daher auf österreichischer Seite keine anderweitigen Durchführungsanordnungen getroffen werden, wird die Abkommensbestimmung – auf österreichischer Seite – so auszulegen sein, dass alle legalen Geschäftsvorgänge in der genehmigten Sphäre ablaufen. Hierbei ist die „Legalität“ aber nicht nur am österreichischen Steuerrecht, sondern an der gesamten in Österreich in Geltung stehenden Rechtslage zu messen. (EAS 3005 v. 23. 9. 2008)