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Article 5: the meaning of “the same or a connected project”

1. Article 5(3)(b) of the UN Model addresses the situation of an enterprise that performs services in a Contracting State through employees or other personnel in relation to “the same or a connected project”. There is no guidance in the Commentary on Article 5(3)(b) with

Manual for the negotiation of bilateral tax treaties between developed and developing countries (1979) refers, indeed, to the discussions held within the Group and makes it clear that the majority view must prevail. The following comments indicate that members from developing countries and from developed countries understood that the text retained was requiring a physical presence in the State of source:

“Concerning the time-limit established in paragraph 3, subparagraphs (a) and (b), of guidelines 5, some members of the Group from developing countries said that they would have preferred to remove the time-limit altogether for two main reasons: first, because construction, assembly and similar activities could as a result of modern technology be of very short duration and still result in a considerable profit for the enterprise carrying on those activities; and, secondly, because the period during which the foreign personnel involved in the activities remained in the source country was irrelevant to the definition of

of both the enterprise that furnishes the services and the customer. Following that approach it would be only where it would be clear, from the perspectives of the enterprise and the customer, that no single project exists or that different projects are not connected that one should consider that activities are not performed for the same or a connected project. [The Committee is of the opinion that this approach should be favoured in order to determine if activities would be performed for the same or a connected project.]

Example 1: An enterprise provides services for the maintenance of several medical devices used by a nursing home as well as services for the training of medical staff operating different devices recently sold to that customer. Two contracts have been concluded by two different departments of the supplying enterprise and two different types of services are performed by different employees.

Those services are performed in the framework of two unrelated projects from the perspectives of the supplying enterprise because these projects have no commercial link from the perspective of that enterprise except the fact that the different types of services are furnished to a same customer. From the perspective of the customer, it

Some members of the Committee have, however, expressed the view that services activities performed for different projects may be considered as performed for connected projects because they are performed for a single customer and that no specific interaction between the projects is required in such case.

Example 3: A consultant has been hired to install a new computer system for a bank in State Y. That consultant's activities will take place in the headquarters and in several separate branches of the bank within that State. All the activities are covered by two separate contracts, one of them covering the activities to be performed in the headquarters and the second one covering the activities performed in the branches. In such case, even if one concludes to the existence of two different projects, there is a commercial link between them so that they will be considered to be connected projects.

Example 4: A consultant is hired to install a particular computer system for a bank. At the end of this project, based on a comparison between several estimates established by different professionals, he is hired again by the same company, pursuant to a separate contract, to train employees to use new software unrelated to the computer system that he recently installed. In this case, even though both contracts are concluded between the same two parties, there is no interaction between the two projects, which are therefore not connected neither from the perspective of the consultant nor from the perspective of the customer. Taking into account the fact that the services activities are performed for a single customer, some members of the Committee would, however, consider that the services are performed for connected projects.

Example 5: In June 2010, hardware company XYZ concluded a services contract with a resident of State Y. Pursuant to that contract, XYZ provides a large range of support with respect to any hardware of its own brand used by the customer. The support provided includes expert advice, maintenance and training, those services being performed by different employees. Furthermore, the services contract provides that hardware of another brand can be added to the contract as this hardware comes off support elsewhere. In July 2012, hardware of the brand TILL is added to the contract. In this case, even though the master contract covers activities of a different nature (training and maintenance for instance) performed by different employees and even if additional activities were included later on, all the activities performed by XYZ are performed in the framework of commercially connected projects, since the large and flexible scope of its services contracts is an important sales argument for XYZ.

12.5. The 183-day threshold provided for in Article 5(3)(b) may give rise to abuses. It has indeed been found that some enterprises divide a single project, or connected projects, into several parts, each covering a period or periods of less than 183 days, and attribute parts of those projects to one or more associated companies. Domestic legislative or judicial anti-avoidance rules may apply to prevent such abuses. This issue may, however, also be dealt with in Article 5 of the treaty through a specific provision, which could be drafted along the following lines:

“For the purposes of subparagraph (b) (where an enterprise that is performing services in a Contracting State is, during a period of time, associated with another enterprise that performs substantially similar services in that State for the same or a connected project through employees or other personnel who, during that period, are present and performing such services in that State, the first-mentioned enterprise shall be deemed, during that period of time, to be performing services in that State for that same or connected project through these employees or other personnel. For the purpose of the preceding sentence, an enterprise shall be associated with another enterprise if one is controlled directly or indirectly by the other, or both are controlled directly or indirectly by the same persons, regardless whether or not these persons are residents of one of the Contracting States.”

12.6. According to this provision, the activities carried on in a Contracting State through the employees or other personnel of an associated enterprise for the same or a connected project are taken into consideration in order to determine if the 183-day threshold is met and if the activities carried on in that State by an enterprise of the same Group are deemed to be carried on through a permanent establishment that the enterprise has in that State.

Example 6: Company LAMBDA, a resident of State X, obtains a contract for the maintenance of equipment situated on the industrial site of Company FIR, a resident of State Y. Those activities are supposed to be performed through several employees and

threshold would not be met as far as DELTA is concerned. As a result, the profits attributable to the activities performed by DELTA through its employees would not be attributable to a permanent establishment in State Y and State Y would not have the right to tax those profits even though it would have the right to tax the profits of LAMBDA.³

12.7. Article 5(3)(b) addresses the situation of an enterprise that performs services in a Contracting State through employees or other personnel in relation to a particular project or to connected projects, and this over a substantial period of time. The 183-day threshold referred to in subparagraph b) applies thus in relation to the enterprise and not in relation to the different employees or other personnel through which the activities are performed. A day will be taken into consideration for calculating the 183-day threshold provided, during that day, the enterprise performs its activities through, at least, one of its employees or other personnel or – if the anti-abuse provision suggested in paragraph 5 above is included in the treaty – one of the employees or other personnel of an associated enterprise present in that State. However, a day will count only as a single day regardless of how many employees or other personnel – of the enterprise itself or of an associated enterprise – are present in that State and performing services during that day.

Example 8: Company LAMBDA, a resident of State X, obtains a contract for the maintenance of several equipments situated on several industrial sites of Company FIR, a resident of State Y. Those activities are supposed to be performed through several employees and to last from 15 January 2012 to 31 October 2012 (i.e. 220 days of activities). In such case, the 183-day threshold would be met and Article 5(3)(b) would apply. However, Company LAMBDA and Company FIR agree to split the project into two separate contracts:

f a first contract concluded between FIR and LAMBDA covers the maintenance of

- 12.8 Under Article 5(3)(b) a permanent establishment also exists where services are not carried on through a fixed place of business but are performed in a Contracting State over a substantial period of time for a particular project or for connected projects. Where such is the case, the permanent establishment only encompasses the services performed for the particular project or for the connected projects and does not encompass other services carried on in that State during the relevant period. However, where other services are carried on in that State for unrelated projects and those other services do not of themselves create a permanent establishment but are of the same or similar nature as those effected through the permanent establishment, those other services may also be taxed in that State in accordance with Article 7(1)(c), which provides for a limited force of attraction.
5. While discussing the meaning of “the same or a connected project” some members of