



What is the current International Tax Practice regarding the taxation of non-resident entertainers and sportspersons and will the new South African Tax Legislation, S47A – S47K, be effective in the taxation of non-resident entertainers and sportspersons in South Africa?

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I hereby declare that I have read and understood the regulations governing the submission of *Postgraduate Diploma in Income Tax Law* dissertations, including those relating to length and plagiarism, as contained in the rules of this University, and that this dissertation conforms to those regulations.

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Introduction

In the ever expanding world of sports and entertainment a lot of money circulates amongst artistes, entertainers and sportspersons. This is of great economic relevance given the fact that, as with any business activity, the resources of the country in which they perform are used to earn these monies; as such these countries should have a right to reap some form of payment, through taxation, for the use of their resources. Given the large quantum circulating amongst these performers, it is a fairly lucrative source of economic revenue for the respective countries' tax authorities.

In South Africa it is of considerable importance that the Commissioner of SARS (CSARS) ensures that he has access to this form of tax revenue, especially given the fact that the recent growth in the sports and entertainment industries in South Africa have been greater than the rest of the world. As such the CSARS must ensure these performance incomes form part of his tax base. Not only have international musicians and artistes taken a liking to touring and performing in South Africa, but the awarding of the right to host various Sports' World Cups are also significant contributors to this increasing tax base.

As we are dealing with the taxation of non-residents in South Africa, the focus of this paper is within the realms of international law, specifically dealing with international tax practice. There is no international tax act governing International tax practice, as such it is more customary law based and is derived from the international tax agreements entered into between countries in order to clarify which country has the right to tax certain forms of income earned by a resident of either contracting country. More specifically with regards to international artistes, entertainers and sportspersons the current practice is to tax these performers on the income received from their performances in the country of performance. The CSARS also follows this practice, but due to practical difficulties, the taxation of these performance incomes is not as effective as it should be, in turn eroding the CSARS's tax base. This loss of tax revenues has lead to the recent introduction of Sections 47A - 47K, effective from 01 August 2006, in the South African Income Tax Act No. 58 of 1962, to try and mitigate these losses.

Each year these losses of revenues continue to increase, and given the future growth of these revenues in South Africa, particularly looking towards the 2010 Soccer World Cup, the CSARS needs to ensure they try and minimise these losses. According to Grant Thornton the 2010 World Cup is expected to earn ZAR7.2 Billion in taxes¹, so should the CSARS not have effective legislation in place, they could sacrifice a large proportion of these prospective revenues; this is a material amount of money to throw away due to practical ineffectiveness. The focus of this paper is therefore to evaluate whether the new legislation will in fact help towards improving the CSARS's ability to collect his revenues from the use of South African resources by international performers.

This paper is an interpretive guide to the practice of the taxation of non-resident artistes, entertainers and sportspersons in South Africa. There is no greater focus on the artiste, the entertainer or the sportsperson as they are rather seen as one for the purposes of this paper and as such will be collectively referred to as performers.

This paper takes the following approach in reaching a conclusion on whether the new South African Tax Legislation, S47A – S47K, will be effective in the taxation of non-resident performers in South Africa:

- Current international practice
 - ↳ Double Tax Agreements and the OECD and UN Taxation Model Conventions
 - ↳ Article 17
 - ↳ Current Issues/Problems
 - ⊗ The Definitions
 1. Sportsmen
 2. Residence
 3. Performer
 4. Source
 5. Performance Income
 - ⊗ The Deductibility of Performance Expenses
 - ⊗ Elimination of Double Taxation and Non-Discrimination

¹ <http://www.polity.org.za/pdf/WorldCup2010.pdf>

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- Explain current practice in South Africa
 - ↻ Prior to the new legislation: Practice, Issues and Problems
 - ↻ The new legislation
- Conclusion: Shortfalls and Recommendations

➤ Current International Practice

The fundamental question to ask in deciding whether a person's income is taxable in any country is whether there is a jurisdictional link between the income and the country in question.

In most countries their residents, as defined per their relevant domestic tax legislation, are taxed in their resident country on their worldwide income, irrespective of the originating source of such income (residence jurisdiction). In the same country non-residents are taxed on any income deemed to be from a source of that country (source jurisdiction). This is common international tax practice to mix the two practices, however the problem arises when a resident is taxed on his worldwide income but part of this income is from a source in another country which taxes the non-resident on this source income, bringing to a fore the infamous scenario of jurisdictional double taxation. Although jurisdictional double taxation is not illegal in terms of international law, it is harmful in an economic sense in that it negatively effects the movement of goods, capital and persons between countries. Accordingly, to avoid this scenario many countries enter into bilateral double taxation agreements (DTA's) to clarify which of the contracting countries has the right to tax the income being taxed twice, the other country thus waiving its right to tax the income.

↳ DTA's and the OECD and UN Taxation Model Conventions

In preparing these bilateral agreements, there are currently two taxation model conventions which are used as guidelines, namely the Organisation for Economic Development (OECD) and the United Nations' (UN) Taxation Model Conventions. The OECD model is geared to developed countries; whilst the UN Model is geared towards implementation in developing countries. Both model conventions are very similar, with slight differences to adapt to the different economic environments. The UN model is viewed as not making a significant contribution to many international tax treaties². Neither form part of customary international law³, as they do not meet the rules of *opinion juris* and *usus* internationally to be accepted as such, but they do

² Olivier, L and Honiball, M ; International Tax: A South African Perspective 2005. As such reference will only be made to the OECD taxation model convention in the rest of this paper.

³ Olivier, L and Honiball, M ; International Tax: A South African Perspective 2005.

have significant interpretive persuasion when there is a conflict regarding the taxing rights conferred by DTA's. One has to stress at this point that DTA's do not impose or extend a country's right to tax, but rather limit one country's domestic taxing rights when a double tax scenario arises and the other contracting country also has the right to tax the income in terms of the DTA.

Looking to a scenario where a country wishes to tax a non-resident on income from a source within that country where at the same time the non-resident will be taxed on this world-wide income in his country of residence. One will always first look to the domestic legislation to seek relief for the double taxation, then to any DTA entered into between his resident country and the source country, which will clarify which country has the right to tax the income, if no relief is available in the domestic legislations. As stated these DTA's use the respective model conventions as guidelines, which do follow the general international tax principles of residence and source jurisdiction taxation, but more importantly also have specific articles which tax certain forms of income exclusively at the income's source or in the taxpayer's resident country.

↳ Article 17

Specific to this paper with respects to the taxation of non-resident performers is Article 17 of the OECD taxation model convention. Article 17 was introduced as an anti-avoidance mechanism against schemes implemented by performers to under-report foreign-earned income in their country of residence, and to not report any income to the country of performance. This created the under-taxation of the performance incomes and the loss of tax revenues in the country of performance.

The first paragraph to Article 17 (below) was inserted into the model convention in 1963, although subsequently amended; the Article fundamentally implies that non-resident performers are liable for tax on the income earned from their performances in the specified country of performance.

1. Notwithstanding the provisions of Articles 7 and 15, income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as a sportsman, from his

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*personal activities as such exercised in the other Contracting State, may be taxed in that other State.*⁴

Although the implementation of the first paragraph closed the initial avoidance loophole, many top performers were still able to avoid such taxation by having the income from their performances not accrue to them, but rather to a company controlled by them ('Star-Company') also a non-resident of the country of performance, who then in turn paid the performer a basic salary but the performer also shared in the profits. As such the salary and profit sharing was not taxable in the country of performance as the first paragraph is interpreted as applicable only to direct receipts of performance income. To remedy this, in 1974 the second paragraph to article 17 (below) was added to overcome such avoidance practice, creating the 'look-through approach'.

*2. Where income in respect of personal activities exercised by an entertainer or a sportsman in his capacity as such accrues not to the entertainer or sportsman himself but to another person, that income may, notwithstanding the provisions of Articles 7 and 15, be taxed in the Contracting State in which the activities of the entertainer or sportsman are exercised.*⁵

Initially paragraph 2 was applied in accordance with its original object and purpose to prevent these 'Star Company' schemes, a so-called limited 'look-through approach'. However performers, the top-ranking and the relatively unknown alike, were continuing to avoid taxes by forming 'Slave Companies' etc., which lead to worldwide mistrust of international performers by the relevant tax authorities in both their resident country and countries of performance. To counteract these new avoidance schemes, commentaries were issued on Article 17 of both the OECD and UN model conventions. These changes amounted to the change in interpretation to an unlimited 'look-through approach'. This unlimited approach ended the limitation of paragraph 2 to 'Star Companies' and made more use of the wording '*accrues not to the entertainer or sportsman himself but to another person*'. Not only 'Star Companies' but also incorporated teams, troupes, etc., should fall within the scope of

⁴ Article 17(1); OECD Model; July 2005 and UN Model; 1999

⁵ Article 17(2); OECD Model; July 2005 and UN Model; 1999

paragraph 2. The implication being that in addition to the performers' salaries for their personal performance, the profits attributable to performances of the (separate) legal entity were also taxable in the country of performance. Thus, even without having a permanent establishment in the source country, a separate production company or legal entity could be taxed in that country, even though it was not itself performing.

However when it comes to the application of paragraph 2, international and various countries' domestic courts have helped in the application of the 'look-through' approach regarding the application of the relevant DTA between the contracting countries. Although some countries have domestic tax legislation to 'look through' so-called 'star companies', many countries are not as flexible⁶. Of fundamental relevance is what the courts adjudged, thus creating international tax practice precedent, on the application of the 'look-through approach'. There are court decisions of various countries relating to the application of the 'look-through approach' to respective DTA's entered by the countries.

The most influential court decisions relating to the 'unlimited approach' are those of the Tax Court of Canada and the Central Economic and Administrative Court of Spain. The first case was *Sumner (aka Sting) v The Queen (Canadian Tax Administration)*⁷, in which the performer, Sting, performed in Canada. He was paid via a Dutch company in the form of a fixed salary and he was entitled to 95% of the profits. The performer only declared his salary to the Canadian Tax Administration, and held that the profits were only taxable where the Dutch Company's permanent establishment resided. The court however referred to the 1992 commentary on Article 17(2) of the OECD Taxation Model Convention and decided that not only the salary fell within the wording of Article 17 but also a portion of the Dutch Company's profits that were attributable to the performance in Canada⁸, following the unlimited approach.

⁶ Molenaar, D and Grams, H; *Rent-A-Star: The Purpose of Article 17(2) of the OECD Model*; 2002

⁷ *Gordon Sumner, Roxanne Inc. v The Queen*, 7 December 1999, 2000 D.T.C. 1667, [2000] 2 C.T.C. 2359

⁸ *Gordon Sumner, Roxanne Inc. v The Queen*, 7 December 1999, 2000 D.T.C. 1667, [2000] 2 C.T.C. 2359

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The second case involved a Dutch company who loaned out a performer for concerts in Spain. The performer was paid a salary for the performance and the Dutch company received a payment as compensation for the contractual rights regarding the performer. The Dutch company argued that the compensation receipt was a royalty and as such taxed as such. The court (2001) however held that there was a direct link between the performance in Spain and the receipt, as such falling within the ambit of Article 17(2) and should be taxed according to these provisions. The court thus drastically reversed its 2000 decision where it interpreted the treaty as is, in that the Spain-Netherlands DTA does not contain a second paragraph to its Article 18 (which corresponds to Article 17 of the OECD model convention), as the treaty was concluded prior to the introduction of paragraph 2 in the OECD model convention. The 2001 decision went beyond the ordinary rules of interpretation as the contracting countries could not have intended a rule identical to paragraph 2 when they signed the treaty, however the appearance of a tax avoidance scheme could have justified the decision reversal⁹.

Both held that not only the salaries paid by non-resident companies to non-resident performers performing in Canada and Spain were taxable in the respective countries of performance, but also the profits of the non-resident companies attributable to these performances.

Contrary to the ‘unlimited approach’, the Supreme Administrative Court of Finland in 2001 decided in accordance with the ‘limited approach’. A Finnish promoter contracted a Dutch production company whose employees (performers) performed in Helsinki, and the employees had no share in any of the Dutch production company’s profits. The 1995 Finland-Netherlands DTA follows the OECD model convention and contains the full text of Article 17. Despite this, and the move in the commentary to the OECD model convention toward the ‘unlimited approach’; the court held that only the portion of the payment that related to the performance of the employees was subject to Article 17 of the Finland-Netherlands DTA, i.e. taxable in Finland, using the ‘limited approach’. The rest of the contract receipts were in turn subject to article

⁹ Vogel, Klaus; “Tax Treaty News”; 55 Bulletin for International Fiscal Documentation 8 (2001); at 319 (Taxation of payments to “star companies” in Spain)

7 of the treaty, as ‘Business Profits’, and thus taxable in the Netherlands¹⁰. This non-uniformity in findings proves the lack of the OECD model convention and commentary’s acceptance as customary international law.

The international taxation principles (customary international law) created by the decisions of these courts in interpreting the application of Article 17, especially paragraph 2, are that the ‘unlimited look-through approach’ should be adopted but only if the non-resident performer has an interest in the profits of the non-resident company receiving the performance income.

Article 17 also specifically states that it overrides the provisions of Articles 7 and 15. Thus the Article applies irrespective of the length of stay or whether there is a permanent establishment from which the performers operate, which is contrary in particular to Articles 7 and 15 of the model convention.

Article 7 applies to Business Profits and states that the profits of an enterprise of its resident country shall be taxable only in that country unless the enterprise carries on business in another country through a permanent establishment situated therein, and the profits attributable to the permanent establishment will be taxed in that other country. If Article 17 did not override Article 7, one can clearly see that most performers would avoid taxation in the country of performance, as not many performers operate through permanent establishments, let alone permanent establishments in non-resident countries.

Article 15 relates to income from employment/dependent personal services, and states that income from rendering employment services in a non-resident country will only be taxable in the resident country if:

- a) the recipient is present in the non-resident country for a period or periods not exceeding in the aggregate 183 days in any twelve month period commencing or ending in the fiscal year concerned, and

¹⁰ Rytöhonka, Risto; “Finland: Taxation of Non-Resident Artists’ Income”; 41 *European Tax* 9(2001); at 344.

- b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State, and
- c) the remuneration is not borne by a permanent establishment which the employer has in the other State.

Had Article 17 not stipulated that it applied notwithstanding Article 15, many performers would be able to avoid taxation in the country of performance as they would hardly ever perform in one country for a period long enough to satisfy the above criteria.

↳ Current Issues/Problems

↳ The Definitions

1. Sportsmen

At first glance the Article appears to be discriminatory against male sportspersons; however common practice is to interpret the Article as genderless, in line with the wording of the UN model convention which uses the word 'sportsperson'.

2. Residence

The concept of residence has various functions and is of importance in three instances regarding international tax:

- i. in determining a DTA's personal scope of application;
- ii. in solving cases where double taxation arises in consequence of double residence;
- iii. in solving cases where double taxation arises as a consequence of taxation in the country of residence and in the country of source.¹¹

Thus its definition is of key importance when it comes to assessing which country has the right to tax residents and non-residents alike. Paragraph 1 of Article 4 of both the OECD and UN model conventions define the term Resident as follows:

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 incorporation, place of

¹¹ OECD Model Commentary; July 2005

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*management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof. This term, however, 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.*¹²

Essentially this definition leaves the classification to the domestic laws of the contracting countries. The problem areas are not surrounding the definition thereof, but rather the situation when the domestic laws of both contracting countries see the performer as resident, i.e. dual-residency. Paragraph 2 tries to help in determining the performer's status as follows:

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 only 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 only 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 only 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 only 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.

The wording of the paragraph is clear in that it wants to cover all possible scenarios but still does leave a fair amount open to interpretation. In practice however the relevant domestic laws have interpretations from their courts with regards to these further interpretive issues.

¹² Article 4(1); OECD Model; July 2005 and UN Model; 1999

There is a third paragraph to Article 4 relating to non-natural persons, which in essence states that should there be any dual-residency conflict, one must look to the place of effective management of the entity. The only significance of this is if the performer is a non-natural person which is highly unlikely ever to occur. There is however the misinterpretation of the use of Article 17(2) in any DTA, where people incorrectly take the residency of the 'star company' and not the performer into account when deciding which DTA to apply. The correct DTA to use is the one signed between the country of performance and the country of the performer's residence.

3. Performer

As mentioned in the introduction to this paper no distinction will be made between an artiste/entertainer and sportsman/person. Based on the commentary to Article 17, the three are loosely defined as follows:

- Artiste/Entertainer – an entertainer, such as theatre, motion picture, radio or television artiste or musician.
- Sportsman/person – participates not only in traditional athletic/Olympic events but also golfers, jockeys, footballers, tennis players, cricketers and racing drivers.

These definitions are in no way exhaustive. More importantly is that the basic principle that an activity that is predominantly of an entertainment/performing nature will fall within the scope of Article 17. On the other hand, the definitions do not extend to visiting conference speakers or administrative and support staff¹³. As the three are dealt with collectively in this paper, any reference to a performer is within the scope of Article 17.

4. Source

The implementation of Article 17 is thus based on the source of the performer's income. Neither of the conventions, OECD nor UN, have definitions of 'source', so where does one find support for the definition of 'source'?

¹³ Commentary on Article 17; OECD Model Commentary July 2005.

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This leads to the guidance of Article 3 of both the OECD and UN conventions, which state that if a term is not defined one must look to the domestic tax legislation definitions of the contracting states. The problem is further exasperated by the fact that most, if not all, of the world's domestic tax legislations also don't have concrete definitions of the term. As such it is left to the domestic courts to decide on how to define the source of the performers' incomes. The first and possibly the most influential international cases regarding the taxation of non-resident performers' income and the rights of the source country to the taxation of non-resident performer's performance income is the Gerritse¹⁴ case of the European Court of Justice. Based on these articles, their respective commentaries, and the decisions of international and domestic courts, it is internationally accepted practice that non-resident performers are liable for income tax in the specific countries in which they perform, irrespective of whether they receive the income from the performance directly or indirectly.

A vital point to note with respect to the source of the performance income is the fact that the focus of Article 17 is where the performer actually performs, and not from whence the income is paid. This was highlighted recently when the House of Lords allowed an appeal by the UK Inspector of Taxes (IT) against a famous tennis player, Andre Agassi (Mr A). The IT was appealing against the non-taxability of the payment of endorsements by two non-UK resident companies into Mr A's non-UK resident company for the performance of Mr A himself in a UK tennis tournament. Mr A held that although he had performed in the UK, the payments were from a non-UK source as such the UK Inspector of Taxes had no jurisdiction over the income, i.e. claiming a territorial limitation. The court held the following:

The whole point of ss 555 to 558 was to subject foreign entertainers or sportsmen to a charge to tax on profits or gains obtained in connection with their commercial activities in the United Kingdom. Payments to foreign companies controlled by them were to be treated as payments to them. To read into the statutory provisions a limitation preventing the collection regime from applying where the payer was a foreign entity with no United Kingdom

¹⁴ Arnoud Gerritse v Finanzamt Neukolln-Nord, ECJ 12 June 2003, C-234/01.

*presence and thereby relieving the foreign entertainer/sportsman from the charge to tax could not possibly be justified on the basis of a presumed legislative intention. Accordingly, on the true construction of those sections a territorial limitation could not be implied and the statutory language should be given its natural meaning.*¹⁵

This natural meaning being that the source of the performance income is where the performer performed. As shown, although UK Tax Legislation has inserted a specific section to deal with the taxation of non-resident performers, it does not retract from the common international practice followed and upheld by other domestic courts.

5. Performance Income

Next, one has to know what income is subject to this tax. What is of vital importance however is the fact that only the performance income that relates to the non-residents performance in any country is taxable in that country. This creates two issues. First is what forms part of the taxable performance income and second is the practical difficulty of what proportion of the income relates to the performance in which country.

There are various forms of income a non-resident performer earns when they perform, varying in nature. According to Dick Molenaar¹⁶, there are 14 different types (list below) of income that relate either directly or indirectly to performances, and their variances in nature create a difficulty in classification and whether or not they fall within the scope of Article 17 or the relevant legislature relating to non-resident performers.

1. Performance and rehearsal fees
2. Reimbursement of/Payment for performance production expenses
3. Inducement payments, options, retainers and restrictive covenants
4. Cancellation fees and insurance cover
5. Advertising and commercial income
6. Sponsorship

¹⁵ Agassi v Robinson (Inspector of Taxes); House of Lords; [2006] UKHL 23; [2006] STC 1056

¹⁶ Taxation of International performing artistes; Molenaar, D; 2006

7. Endorsements
8. Subsidies
9. Royalties directly linked to the performance
10. Tour support
11. Publishing copyright
12. Neighbouring rights
13. Sales of merchandising
14. Pensions and other insurance benefits

As one can see, most of these forms of income are general payments for a performer's various performances around the world. It would be inefficient to make specific payments for each different performance on the payee's behalf, highlighting the difficulties in distinguishing what is taxable, and where. One explicit exception from this paper is royalty income not directly related to the performance, as this form of income is dealt with in a similar manner but a different set of tax principles are followed.

However for the purpose of this paper all forms of performance income will be dealt with collectively as the focus is not the type of income but rather the issues surrounding the taxation of the non-resident performer's performance income in South Africa.

☞ The Deductibility of Performance Expenses

When discussing what, where and how the non-resident performer's income is taxed, a question a performer should ask is whether it is their gross receipts or their net position after expenses that are taxed. This issue is very relevant in any form of business as who wants to operate at a loss, yet the issue seems to be ignored in the tax world regarding a performer's expenses. Most countries do not allow a deduction and the OECD model convention considers the determination of these expenses too difficult, in turn provides a neutral account of their non-deductibility. The only mention made is in Paragraph 10 of the 2005 Commentary to Article 17.

10. The Article says nothing about how the income in question is to be computed. It is for a Contracting State's domestic law to determine the extent of any deductions for expenses. Domestic laws differ in this area, and some

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*provide for taxation at source, at a low rate based on the gross amount paid to artistes and sportsmen. Such rules may also apply to income paid to groups or incorporated teams, troupes, etc.*¹⁷

This underestimation of the amount of the expenses (average between 64% and 75% of performance income¹⁸) a performer has to incur, coupled with the fact that most other forms of income are taxed after any allowances for expenses incurred in the production of such income, does not portray any form of equality for non-resident performers. Many countries have special rules to exclude smaller performance incomes from performance taxation. However they differ per country with no happy medium to create international tax practice, and to provide some form of relief, most countries do follow the practice of taxing the gross performance amount at a lower rate.

⊗ Elimination of Double Taxation and Non-Discrimination

The international customary tax law created is the taxation of gross performance income, irrespective of size, in the country of performance. At the same time the performers are also taxed on their worldwide income in their resident country, exposing them to double taxation. The next question is whether relief is provided, and if so, in what form? The crucial answer is dependent on either the DTA providing bilateral relief or the country of residence's tax rules providing unilateral relief.

Generally, relief is provided and currently two methods are applied, the tax exemption and the tax credit methods. The exemption method exempts the performance income already taxed from the performer's residence taxable income. Where the credit method subjects the performance income to tax in the performer's country of residence, it then allows a deduction from the domestic tax of the tax already paid in the country of performance. The exemption method allows the country of source the sole right to tax the performance income, whilst the credit method allows the country of residence a subsidiary tax right. The subsidiary right created under the credit method comes into operation if the country of source/performance has a lower tax rate

¹⁷ Commentary on Article 17; OECD Model Commentary July 2005.

¹⁸ Molenaar, D; Taxation of International Performing Artistes; at 224

than that of the country of residence, thus subjecting the performer to a tax rate equivalent to his resident country's rate.¹⁹

Which method is recommended for performers? Paragraph 12 of the Commentary to Article 17 recommends the use of the credit method, but does allow the contracting countries the freedom to choose any of the methods in order to ensure that the performance income does not escape taxation. The recommendation is logical so as to allow the country of residence the subsidiary right to tax especially when the performer performs in countries with low tax rates or tries to use tax havens to avoid tax. It also places the burden on the performer to present a tax certificate authenticating their claims of double taxation, also preventing non-disclosure in the country of performance as well. However some inequality does lie with the performers in that they could be subject to excessive tax when their country of residence doesn't allow a full tax credit, rather limiting the credit to the domestic tax that would've been payable, bearing the higher tax burden of the country of performance. This risk of over taxation deters the performers from performing in certain countries unless they are compensated for the excessive tax, creating market inefficiencies in the entertainment world, in turn hindering international economic development.

Although economically unfavourable, are there any international practice/customary law available to help rectify this dilemma? The best port of call would be the specific article of the DTA entered into between the contracting countries regarding non-discrimination. Article 24 of the OECD model convention has 5 paragraphs relating to various scenarios but the most applicable to this paper is paragraph 1, the general provision, and states:

1. Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This

¹⁹ Vogel, K; "Which method should the European Community adopt for the Avoidance of Double Taxation?"; 56 Bulletin for International Fiscal Documentation 1 (2002); at 4.

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*provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.*²⁰

The basic application of this article requires that no discrimination on the grounds of nationality is allowed, allowing both contracting countries diplomatic protection of their nationals. The key line in the paragraph is ‘*in the same circumstances, in particular with respect to residence*’²¹. International interpretation regarding withholding taxes on non-resident performers is only discriminatory if the non-resident is taxed at a higher rate than a resident performer who is assessed on income from a similar performance. The point this paper takes from Article 24 is the fact that the non-discrimination clause does not ensure fair or equitable tax treatment created by the differing tax rates between the contracting states, but merely protects the contracting states nationals

As a concluding comment on International Practice regarding the taxation of non-resident performers, although the OECD taxation model convention and commentaries do not form part of customary international law, they are still highly regarded as having a very persuasive nature with respects to clarifying international practice on this front. So any country looking to tax a non-resident performer does not have to rely on specific legislation being present their country’s tax legislation, they can use the jurisdictional link of source and the OECD model convention’s persuasive nature to tax the non-resident performer’s performance income. What they however do have to take into account is the possibility of discrimination, from a legal perspective in meeting the terms of any DTA’s entered into, as well as the economic consequences of any excessive taxation scenario.

²⁰ Article 24(1); OECD Model; July 2005.

²¹ Article 24(1); OECD Model; July 2005.

➤ Current Practice in South Africa

↳ Prior to the New Legislation: Practice, Issues and Problems

In South Africa all laws are subject to the provisions of the South African constitution, as section 2 of the South African Constitution²² (the Constitution) provides that it is the *supreme court of the land*, these laws being statute law, common law and international law. Under the heading international law, the Constitution deals with:

- International agreements (S 231);
- International Customary Law (S 232); and
- The application of International Law (S233).

From an income tax perspective S108(2) of the Income Tax Act²³ sets out the domestic procedures for the recognition of international tax treaties. S108(2) provides that once parliament has approved the international agreement per S231 of the Constitution and the arrangements of the treaties been notified in the government gazette, the provisions of the treaty will become part of the Income Tax Act. Accordingly a treaty will have the same effect as any other section contained in the South African Income Tax Act. However, what is of greater relevance and importance is whether the provisions of a treaty have privileged status under South African Law. The decisions of two South African cases, *Pan American*²⁴ and *South Atlantic*²⁵, make it clear that international agreements enjoy no privileged status under South African law. Even though the decisions are within a totally different context to South African Tax, they do create binding precedence in tax court cases as to the status of tax treaties in South African Tax law.

This clarifies that the provisions of both the treaty and domestic legislation are seen to hold equal weight, but still does not help clarify what the position is when it comes to conflicting provisions between domestic tax provisions and provisions created by any DTA. Prior to the implementation of the Constitution, an Australian tax case, *Lamesa*

²² Constitution of the Republic of South Africa, 1996 (Act No 108 of 1996)

²³ Income Tax Act No. 58 of 1962

²⁴ *Pan American World Airways Inc v SA Fire and Accident Insurance Co Ltd*, 1965 (3) SA 150 (A)

²⁵ *South Atlantic Inlands Development Corporation Ltd v Buchan*, 1971 (1) SA 234 (C)

*Holdings*²⁶, provided for the view that a DTA automatically overrides domestic tax law, this view was also held in the South African case ITC 1544²⁷ in 1992. Unfortunately neither of these decisions creates binding legal precedent; nonetheless they still carry persuasive influence.

However since the implementation of the Constitution the interpretive relevance of these cases is uncertain as to whether they still have any persuasive influence, leaving the issue to debate with the fact that there is also no specific domestic legislation which provides which provision takes precedence and S108(2) provides no assistance. Despite this, the majority argument is in favour of the provisions of the tax treaty having privileged status, as its object is to avoid juridical double taxation, thus any domestic legislation which has the effect of taxing the same income twice should be subordinate²⁸. The greatest support of this argument is found in the wording of S108(1):

‘...with a view to the prevention, mitigation or discontinuance of the levying, under the laws of the Republic and of such other country, of tax in the respect of the same income, profits or gains’²⁹

Even though the argument is strong, it does not create any binding precedence in South African Tax law. The procedure one has to follow then is a persuasive interpretive process starting with domestic rules, then look to international rules as far as they are relevant³⁰. During this interpretive process South African courts are constitutionally bound to follow an interpretation consistent with international law when interpreting domestic legislation³¹. This provides for an argument that the conflict should be resolved by following international interpretive rules; these rules providing for DTA’s precedence over domestic rules was reached in an Australian case³², in spite of these rules there is no binding precedence to follow them in South Africa.

²⁶ Lamesa Holdings BV, 1997 35 ATR 239, 97 ATC 4229

²⁷ ITC 1544, 54 SATC 456

²⁸ Olivier, L; Honiball, M; International Tax, A South African Perspective; 2005; at 31

²⁹ S108(1); Income Tax Act No. 58 of 1962.

³⁰ Olivier, L; Honiball, M; International Tax, A South African Perspective; 2005; at 33

³¹ S233 South African Constitution

³² Thiel v FCT (1990) 171 CLR 338

So there is no alternative to the persuasive interpretive process mentioned, however one tool that is imperative in this process is the OECD model convention and its commentaries. Internationally the OECD model convention and its commentaries are not used as binding interpretive tools for treaty provisions from an international perspective, as it does not form part of international customary law³³. From a South African perspective there is an argument that it should form part of South Africa's customary international law on the basis of its acceptance in South African case law (*opinion juris*) and general use as an interpretive aid (*usus*), in turn could be used as a binding interpretive tool in interpreting DTA's between South Africa and other countries. Yet again this is a strong argument, but not binding in South Africa. As such there is still no basis on which to interpret whether domestic laws override the provisions of a DTA or vice versa. Despite these interpretive issues there is one final port of call one can look to; it is the treaty itself to see if there is an Article that allows for mutual agreement between the contracting countries when such an issue arises. This mutual agreement is not through any form of court, merely a means of mediation to decipher which provision should take precedence, and thus no binding precedent is created from such agreements.

Looking to the specific tax at hand, the taxation of non-resident performers performing in South Africa, and applying the afore-mentioned rules of interpretation, the CSARS uses the following domestic and international principles to tax the non-resident performers.

The CSARS follows the same principles as international practice when it comes to jurisdictional links, whereby South African residents are taxed in South Africa on their worldwide income, and non-residents are taxed on their South African source income. As this paper is looking at the taxability of non-residents in South Africa, one has to ascertain whether there is a jurisdictional link between the non-residents' income and South Africa, i.e. the source of the performance incomes. As mentioned there is no international definition of source, so one has to first ascertain domestic interpretation of where the source of any non-resident's income is. The principle test used in South Africa is the *location* of the *originating cause* of the income. This test

³³ Olivier, L; Honiball, M; International Tax, A South African Perspective; 2005; at 28

was created by the decision of Watermeyer CJ in the Appellate case of CIR v Lever Brothers and Unilever Ltd, 1946:

*The source of income is not the quarter from which it comes but rather the originating cause of its receipt. The originating cause is the work which the taxpayer performs to earn the income, the quid pro quo given in return for which it is received.*³⁴

However the originating cause is not always clear cut and there could be multiple causes, so courts looked to the dominant cause and its location as the source of the income³⁵. Where it is not possible to determine the dominant cause, it would seem appropriate to apportion the source between countries; however South African courts are reluctant to apportion income. This reluctance is illustrated in the decisions of the *Transvaal Associated Hide*³⁶; *Black*³⁷; *Kirsch*³⁸ and *Shein*³⁹ cases. Despite the non-apportionment the principle test one applies is the location of the dominant originating cause.

Applying this principle to non-resident performers the source of their incomes in terms of South African Tax Law would be the location of the originating cause of the performance income, that being where they performed their acts/skills. The next interpretive tool, although not binding, is the OECD model and its commentaries. Even though South Africa is not a member of the OECD, the CSARS applies the guidelines set by OECD Taxation Model Convention when entering double tax agreements between South Africa and other countries. This *usus* allows for the use of Article 17 of the OECD model convention when interpreting the taxability of non-resident performers performing in South Africa. Article 17 reinforces the taxation of non-resident performers' incomes in the country of performance, i.e. South Africa.

³⁴ Watermeyer CJ; CIR v Lever Brothers and Unilever Ltd 1946 AD 441, 14 SATC 1

³⁵ Schreiner JA; CIR v Black 1957 (3) SA 536 (A), SATC 226

³⁶ Transvaal Associated hide and Skin Merchants v COT, Botswana 29 SATC97.

³⁷ CIR v Black 21 SATC 226.

³⁸ SIR v Kirsch 40 SATC 95

³⁹ COT v Shein 23 SATC 230

↳ New Legislation

Now one asks why the implementation of the new legislation, S47A to S47K? The answer to this question will illustrate the difficulties the CSARS faced(s) when trying to assess non-resident performers' incomes from their performances in South Africa. The primary difficulty the CSARS faced(s) was the inability to collect these tax revenues. The lack of effectiveness was due to numerous practical constraints; with the main contributor to these constraints being the short period of time for which most non-resident performers were physically present in the country. This failure by the CSARS to collect this tax revenue, in effect was, and still is, an erosion of its tax base in favour of the non-resident performers' country of residence. The performers' countries of residence would impose tax on the performers without the need to give credit for the tax that should have been paid in South Africa⁴⁰, as they did not declare their performance income in South Africa.

To exasperate the issue, international law provides that a country has no jurisdiction to impose its domestic laws within another country's jurisdictional borders, allowing non-resident performers safety from the CSARS as long as they are outside of South Africa's jurisdictional border. Coupled with this law is the international customary law that the 'revenue rule' applies in that one country will not assist in collecting tax revenues on another country's behalf⁴¹. This combination of international law and the avoidance issue is the major shortcoming that the new legislation wishes to remedy.

The solution the new legislation is enforcing is principally based on the fact that the bulk of the payments to non-resident performers are made by South African residents that organise the performances. Based on this statement S47D places the onus of the collection of the taxes on these payments primarily on the South African resident organisers paying the non-resident performer to perform in South Africa.

(1) Any resident who is liable to pay to a taxpayer any amount contemplated in section 47B(1) must deduct or withhold from that payment the amount of tax for which the taxpayer is liable under that section in respect of that amount.

⁴⁰ Explanatory Memorandum to the Revenue Laws Amendment Bill, 2005; at 35

⁴¹ Attorney-General of Canada v RJ Reynolds Tobacco Holdings Inc and Others; US Supreme Court of Appeals for Second Circuit; 12 October 2001; 268 F 3d 103.

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(2) A taxpayer from whom an amount has been deducted or withheld in terms of this section is deemed to have received the amount so deducted or withheld.⁴²

S47G(1) takes it one step further by holding any South African resident personally liable for the amount due to the CSARS, if they fail to withhold such tax, unless the performer themselves have paid the amount due to the CSARS (S47G(3)). Not only does the South African resident have to withhold the tax, but they also have to notify the CSARS of upcoming performances in terms of contracts entered into between the resident and any non-resident performer (S47K), as well as submit the non-resident performer's return (S47F(2)). At first blush the new legislation appears to remedy the previous problems encountered, but the administrative and financial burden the CSARS is transferring from itself to the South African resident organiser could be detrimental to the principle objective of the new legislation and of economic detriment.

The economic detriment could be a result of one of many possible scenarios. The most logical being that these additional burdens could out cost the viability to the South African resident organiser of bringing in the non-resident performer, in turn passing these lost profits on to non-South African resident organisers who will be able to attract the performers with the payments they want and still profit from the performances in South Africa. Another scenario is that the non-resident performer will have to live with receiving less money (net of the withholding tax), thus in turn may refuse to enter into contracts with South African residents and take their chance with non-South African resident organisers. Although no direct affect on tax revenues, the movement of these profits from South African resident organisers to non-resident organisers in itself depletes the South African tax base. One has to agree with the fact that the new legislation does in part remedy the collection problems when a South African resident organiser pays the non-resident performer, by transferring the burden, but what about the collection issues when a non-resident organiser pays the non-resident performer?

⁴² S47D, Income Tax Act No. 31 , 2005

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The non-resident performer is in no way liable to withhold any form of tax from payments to non-resident performers performing in South Africa. S47C places the general liability upon the non-resident to pay the tax due to the CSARS within 30 days of the receipt or accrual of payment for the performance in South Africa. This alludes to the question of how is this different to past practice, i.e. international practice with respects to the implementation of DTA entered into by South Africa and other contracting countries. Yet again one has to agree that the legislation broadens the tax base by encompassing all performers; irrespective of whether they are a resident of any country party to a DTA with South Africa. However it does not remedy the previous problems encountered with regards to collection of these tax revenues due to the CSARS. In both instances as the tax burden rests solely on either the South African resident or the non-resident performer themselves. By using non-resident organisers the non-resident performer can continue to take the chance of bypassing their liability to the CSARS, slipping under the radar by not declaring their performance income again, bringing the CSARS back to square one.

So at first glance one can easily see the probable ineffectiveness of the new legislation, leaving the CSARS in a position no better than his original dilemma. Strictly speaking, the non-resident performer is liable by South African law to the CSARS, but is it not a futile obligation given past practice? Were they not bound by international law originally if they were a resident of a country with whom South Africa had entered a DTA with, containing the equivalent of Article 17 of the OECD model convention? Where is the improvement? All that the new legislation has done is to include non-residents from a country with whom South Africa have not entered a DTA, admittedly broadening the tax base, but at the same time possibly, actually more than likely, losing the same, if not more, tax revenues as before.

As illustrated, the possible loss of tax revenues will almost be two-fold, the first in forcing non-resident performers to look to non-South African organisers, thus fly below the radar, secondly leaving the formally lucrative South African organisers to the vultures, consequently a loss of the tax revenues previously earned from them. The ever-globalising world, does not afford performers the room to tarnish their images by not paying their taxes, but the possibility is there, and as long as they know

that they can save more than an extra rand by hiding behind jurisdictional barriers and the 'revenue rule', they will.

So where does this leave the CSARS and what are the possible remedies to this scenario? The remedies always seem logical and simple, but it is the practical implementation that inevitably seems to be to the CSARS's detriment. This remedy brings us to the other purpose of DTA's, the prevention of fiscal evasion. Fiscal evasion refers to the above mentioned cases where non-resident performers fraudulently conceal their performance income and rely on the CSARS's inability to obtain information as well as impose domestic tax law abroad. This fiscal evasion is an international problem, so with the dramatic spread of international tax avoidance and evasion, countries have come to the realisation that co-operation is necessary. Thus the recent implementation of the Article 27 - Assistance in Collection of Taxes provided for in the 2003 amendment to the OECD model convention, allowing for fairly comprehensive mutual assistance by the contracting states. Clearly this flies in the face of the 'revenue rule', but does have a significant impact in assisting the country of performance to collect its taxes due to it, provided the article has subsequently been inserted in the DTA's entered between South Africa and the non-resident performers' countries of residence. Even though it provides comprehensive assistance there are two key inherent limitations to Article 27, the first is that the claim must be enforceable under the domestic law of the country requesting the assistance to collect the taxes and secondly that the taxpayer does not have a valid reason not to pay the taxes sought after.

The CSARS has created the domestic law to tax non-resident performers, so what the CSARS has to ensure before requesting assistance is that the non-resident performer has no reason not to pay the taxes due. The most evident valid reason would be where a South African resident organiser has withheld the taxes from the performer's fee, thus the organiser has assumed the non-resident performer's liability. However one tax principle that does operate in South Africa is the 'pay-now, argue-later' rule, which was upheld in the Metcash case⁴³. How this principle works is that if a non-resident performer is disputing his liability to the CSARS, it does not constitute a

⁴³ Metcash Trading Ltd v CSARS 63 SATC 13

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valid excuse which would prevent the CSARS from requesting assistance from the performer's country of performance, whom is party to a DTA with South Africa.

The implementation of Article 27 to the OECD model convention does assist the CSARS's position with respects to previous difficulties. However given its recent implementation it does not help with respect to DTA's entered into by South Africa prior to 2003, thus the absence of the relevant article allowing the request for assistance.

Another uncovered area is where the non-resident performers are resident in countries with which South Africa has not entered DTA's with. The most obvious remedy would be that the performers' countries of residence don't tax the performers so as to encourage them, through direct elimination of the possibility of double taxation, to pay the CSARS their taxes due. However this remedy goes against the fundamental tax principles of residence juridical taxation. In turn the performer is taxed twice on the same income with no course of relief.

➤ Conclusion: Shortfalls and Recommendations

Prior to the introduction of the new legislation, S47A – S47K, the CSARS followed international practice in the taxation of non-resident performers performing in South Africa, which was to tax these performers on the income received from their performances in the country of performance, i.e. South Africa. However due to practical difficulties, the taxation of these performance incomes was not as effective as it should have been, in turn eroding the CSARS's tax base.

The CSARS has definitely made positive strides forward in reducing the lost revenues lost in the past. The implementation of the new legislation passes part of the collection burden onto the South African taxpayers bringing the non-resident performer into South Africa. In essence the CSARS is regaining the right to reap some form of payment for the use of South Africa's resources.

However, the new legislation only in part remedies these practical problems encountered by the CSARS. The major shortfall highlighted arises from the situation when a non-resident performer is paid for his performance in South Africa by a non-resident. This scenario brings the CSARS back to square one, and in turn giving rise to detrimental economic possibilities.

The initial impression is that the possible loophole seems gaping. However recent developments in the OECD model convention of 2005 should help restrict the extent of the use of this shortfall. The implementation of the assistance (Article 27) and exchange of information (Article 26) articles into the model convention is definitely a helpful measure in allowing tax authorities to collect the taxes due to them from taxpayers hiding behind jurisdictional barriers. What the CSARS has to realise though, is that these new articles will only be effective once included in the DTA's entered into by South Africa and other contracting states. Since the articles were only introduced in the 2005 OECD model convention, most of South Africa's DTA's will not contain such articles; as such not help in restricting the shortfall.

The first recommendation is to implement more stringent checks on performances in South Africa. Although still practically difficult the lost revenues more than make up

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for the strenuous work involved. There are numerous possibilities on how they implement these checks, but the most favourable would be to follow the lead of other tax authorities. Thus the CSARS should employ a committee whose sole objective is the sourcing of non-resident performers' South African performance incomes, and then ensure the collection of the taxes due, similar to the HM Revenue and Customs' Foreign Entertainers Unit⁴⁴.

The second and more legislative based recommendation is for the CSARS to negotiate the addition of the new articles implemented by the OECD, either by the issue of a new DTA signed by the contracting states, or the issue of a signed Protocol to implement the specific amendments/additions to the DTA in force.

The new legislation is thus not totally ineffective, and given the movements in international practice concerning the taxation of non-resident performers, the CSARS should be able to collect the tax revenues lawfully due.

⁴⁴ <http://www.hmrc.gov.uk/feu/>