CHAPTER 27

OVERVIEW OF MODEL TAX CONVENTIONS



LEARNING OUTCOMES

After studying this chapter, you would be able to:

- **appreciate** the need for Model Tax Convention;
- **appreciate** the key features of the OECD and UN Model Tax Conventions;
- **identify** the subject of the various articles of the OECD and UN Model Tax Conventions;
- **appreciate** the broad similarities and differences between the principles enshrined in certain articles of the OECD Model Tax Convention *vis-à-vis* the corresponding articles of the UN Model Tax Convention.

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27.1 INTRODUCTION

In order to enable various countries to enter into treaties, which are standardized to some extent, Organisation for Economic Co-operation and Development (OECD) and the United Nations (UN) have developed certain Model Tax Treaties. These treaties can be used by various countries as a starting point in their negotiations with other countries. While these Models are not legally binding, they have been extensively used by various countries as a reference point while entering into Tax Treaties. In some cases, they have been incorporated verbatim or with minor changes. However, in other cases, countries have made suitable changes in the draft model according to their economic environment and commercial and tax considerations.

The significant model conventions have been briefly discussed hereunder:

OECD Model - Work on model bilateral tax conventions began under the League of Nations in 1921, with the first model bilateral conventions adopted in 1928 and later Mexico (1943) and London (1946) Models. The OEEC Fiscal Committee began its work in 1956; after the OECD succeeded the OEEC in 1961, the OECD published its Draft Double Taxation Convention in 1963. A substantially revised Model followed in 1977 and has since been updated periodically. The latest update was approved by the OECD Council on 18 November 2025. The full version of the OECD Model Tax Convention 2025, incorporating these updates, was published by the OECD on 30 September 2026.

The OECD Model Convention (OECD MC), although historically developed in the OECD member-country context, is widely used by OECD Members and non-Members as a basis for negotiating, applying and interpreting bilateral tax treaties. Compared with the UN Model, it generally allocates relatively greater taxing rights to the Residence State.

UN Model – In 1968, the United Nations set up an Ad Hoc Group of Experts from various developed and developing countries to prepare a draft model convention between developed and developing countries. In 1980, this Group finalised the UN Model Convention (UN MC) in its present form. Since its first publication in 1980, the Model has been updated previously in 2001, 2011, 2017 and 2021. The latest updation was in the year 2025. *The 2025 update was adopted by the UN Committee of Experts on International Cooperation in Tax Matters at its thirtieth*

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session held in March 2025 and was published in September 2025. In that update, the words "between Developed and Developing Countries" have been deleted from the name of the Model, which is now titled simply the "United Nations Model Tax Convention".

The UN Model generally favours retention of greater so-called "source country" taxing rights under a tax treaty – the taxation rights of the host country of investment – as compared to those of the "residence country" of the investor. This has long been regarded as an issue of special significance to developing countries, although it is a position that some developed countries also seek in their bilateral treaties. To reflect this fact, the Committee decided in 2025 to delete "between developed and developing countries", which had previously been included in the name of the Model.

The United Nations MC seeks to be balanced in its approach. As a corollary to the principle of taxation at source, the Articles of the Convention are based on a recognition by the source country that -

(a) taxation of income from foreign capital should take into account expenses allocable to the earnings of the income so that such income is taxed on a net basis,

(b) taxation should not be so high as to discourage investment and

(c) it should take into account the appropriateness of the sharing of revenue with the country providing the capital.

In addition, the United Nations MC embodies the idea that it would be appropriate for the residence country to extend a measure of relief from double taxation through either a foreign tax credit or an exemption, as is also the case with the OECD Model Convention.

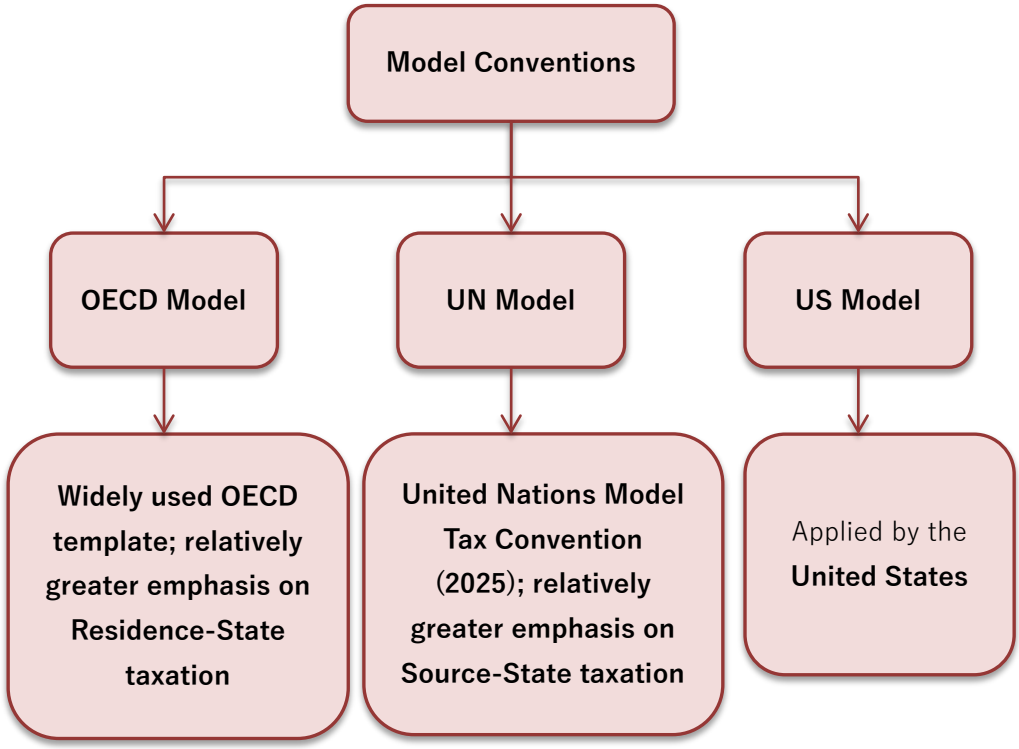
US Model – This Model Convention is used by the United States while entering into tax treaties with various countries. The US Model Convention was last revised in 2016.

These Models have a significant influence on international treaty practice and have important common provisions. The similarities between these Models highlight the areas of consistency. The areas of divergence indicate some critical

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differences in approach or emphasis which need special focus. These differences are mainly in relation to the taxing rights which would be available to a country under domestic law and the extent to which any country should forego, under a bilateral tax treaty, in order to avoid double taxation and encourage investment.

The above model conventions have been illustrated in the following diagram:



OECD Model contains VII chapters comprising of 32 articles and UN Model also contains VII chapters but comprising of 31 articles. List of articles of OECD MC and UN MC is given below:

Article	OECD Model, 2025	UN Model, 2025
	Chapter I: Scope of the Convention	
1	Persons covered	Persons covered
2	Taxes covered	Taxes covered
	Chapter II: Definitions	
3	General definitions	General definitions
4	Resident	Resident

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5	Permanent establishment	Permanent establishment
5A		Income from the exploration for, or exploitation of, natural resources
	Chapter III: Taxation of Income	
6	Income from immovable property	Income from immovable property
7	Business profits	Business profits
8	International shipping and air transport	International shipping and air transport (Alternatives A & B)
9	Associated enterprises	Associated enterprises
10	Dividends	Dividends
11	Interest	Interest
12	Royalties	Royalties
12A		***Fees for Technical Services [Deleted 2025]***
12AA		***Fees for services***
12B		Income from automated digital services
12C		***Insurance premiums***
13	Capital gains	Capital gains
14		***Independent personal services [Deleted 2025]***
15	Income from employment	Dependent personal services
16	Directors' fees	Directors' fees and remuneration of top-level managerial officials
17	Entertainers and sportspersons	Artistes and sportspersons
18	Pensions	Pensions and social security payments (Alternatives A & B)
19	Government service	Government service
20	Students	Students
21	Other income	Other income
	Chapter IV : Taxation of Capital	
22	Capital	Capital

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	Chapter V : Methods for the Elimination of Double Taxation	
23A	Exemption method	Exemption method
23B	Credit method	Credit method
	Chapter VI : Special Provisions	
24	Non-discrimination	Non-discrimination
25	Mutual agreement procedure	Mutual agreement procedure (Alternatives A & B)
26	Exchange of information	Exchange of information
27	Assistance in the collection of taxes	Assistance in the collection of taxes
28	Members of diplomatic missions and consular posts	Members of diplomatic missions and consular posts
29	Entitlement to benefits	Entitlement to benefits
30	Territorial extension	
	Chapter VII : Final Provisions	
31/30	Entry into force	Entry into force
32/31	Termination	Termination

Now, let us discuss the comparative analysis of some of the significant Articles in the Model Tax conventions.

27.2 COMPARATIVE ANALYSIS OF SOME OF THE SIGNIFICANT ARTICLES OF OECD AND UN MODEL CONVENTIONS

Title and Preamble to the Model Conventions

The title of the UN Model Convention reads as follows:

"Convention between (State A) and (State B) for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion"

There is a specific reference to "the prevention of tax avoidance and evasion" in the title to emphasize its significance in the Model Convention.

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The Preamble to the UN Model Convention reads as follows:

"(State A) and (State B),

Desiring to further develop their economic relationship and to enhance their cooperation in tax matters,

Intending to conclude a Convention for the elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax avoidance or evasion (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States)"

The Title and Preamble to the OECD Model Convention is almost identical to that of the UN Model Convention. The only minor difference is the reference to "tax evasion and avoidance" in the place of "tax avoidance and evasion" in the Title and Preamble.

The Preamble clearly indicates that the UN and OECD Model Conventions do not intend to create opportunities for non-taxation or reduced taxation through tax avoidance or evasion including through treaty shopping arrangements.

This language of the Preamble would help ensuring that the provisions of the Conventions are interpreted and applied to prevent abusive treaty shopping arrangements.

Significant Articles in the Model Conventions

Over the years, both Model Conventions have seen a lot of convergence and the language is identical in quite a few Articles. However, there are key differences in approach and language in some Articles which will be the focus of our discussion, in the section below.

The jurisdiction or country of residence of the taxpayer is referred to as the Residence State and the jurisdiction or country where the source of income is located is referred to as the Source State.

Article 1: Persons Covered

The OECD and UN Model Convention would apply to persons who are residents of one or both of the Contracting States.

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For the purposes of these Conventions, income derived by or through an entity or arrangement that is treated as wholly or partly fiscally transparent under the tax law of either Contracting State shall be considered to be income of a resident of a Contracting State. However, the same would be treated as income only to the extent that the income is treated, for purposes of taxation by that State, as the income of a resident of that State.



State A and State B have concluded a treaty identical to the Model Tax Convention. State A considers that an entity established in State B is a company, and taxes that entity on interest that it receives from a debtor resident in State A. Under the domestic law of State B, however, the entity is treated as a partnership, and the two members in that entity, who share equally all its income, are each taxed on half of the interest. One of the members is a resident of State B and the other one is a resident of a country with which States A and B do not have a treaty. The paragraph provides that in such case, half of the interest shall be considered, for the purposes of Article 11, to be income of a resident of State B.

***Note** – The above example forms part of the Commentary to the UN Model Tax Convention.*

With the exception of benefits granted under certain Articles of these conventions, these Conventions would not affect the taxation, by a Contracting State, of its resident.

The UN Model (2025) has introduced a new paragraph 3 in Article 1 containing a subject-to-tax rule (STTR). Under this paragraph, the Convention does not affect the taxation, by a Contracting State of income arising in that State and derived by a resident of the other Contracting State, where that income is subject to a low level of taxation in that other State.

Income is treated as subject to a low level of taxation in either of two situations. The first is where it is subject to a statutory rate at or below a percentage to be established through bilateral negotiations. The second is where it is subject to a higher statutory rate, but the beneficial owner is entitled to a special exemption, exclusion or reduction linked directly to the income or to the entity receiving it, with the result that the tax paid on that income is less than the amount which the negotiated rate would have produced. Sub-paragraph (c) leaves space for exclusions agreed bilaterally.

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This new paragraph 3 of Article 1 is intended to address cases of unintended double non-taxation. Under this paragraph, a source State is required to reduce its domestic tax on an item of income pursuant to the allocation rules of a bilateral tax treaty only if that income is subject to tax in the residence State (at a rate not less than a minimum rate to be agreed through bilateral negotiations). This "subject-to-tax rule" was added to the UN Model in order to address concerns expressed by developing countries that they were giving up taxing rights in cases where there is no double taxation because of the domestic rules in the other Contracting State.

The rationale is that a source State accepts restrictions on its taxing rights on the understanding that the income concerned is taxed in the residence State. Where it is not, the Commentary describes the rule as conferring a secondary taxing right on the source State rather than as reallocating taxing rights. This rule should not be confused with the subject-to-tax rule developed under the OECD/G20 Inclusive Framework, which operates differently, as a treaty-based top-up tax on defined categories of covered income at a specified nominal rate.

Consequent upon the insertion of paragraph 3, the saving clause is renumbered as Article 1(4) and the collective investment vehicle provision as Article 1(5).

Article 1 of UN Model Convention covers provision dealing with the application of the Convention to "Collective investment vehicles". Funds that are widely held, hold a diversified portfolio of securities and are subject to investor-protection regulation in the country in which they are established are referred to as "collective investment vehicles" (CIVs) like REITs.

These funds adopt different legal structures and may be set up, for instance, as companies, partnerships, trusts or contractual arrangements that create a joint ownership. It is to ensure that investing through a domestic CIV should result in a tax burden that is equal to the one that applies in the case of a direct investment, i.e. an investment where the CIV would not exist and where the investor in the CIV would have acquired directly its share of the assets held by the CIV.

Article 2: Taxes Covered

The OECD and UN Conventions would apply to taxes on income and on capital imposed on behalf of a Contracting State or of its political subdivisions or local authorities, irrespective of the manner in which they are levied.

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Taxes on income and on capital cover all taxes imposed on total income, on total capital, or on elements of income or of capital, including taxes on gains from the alienation of movable or immovable property, taxes on the total amounts of wages or salaries paid by enterprises, as well as taxes on capital appreciation.

The existing taxes to which the Conventions would apply in case of each Contracting State are specifically to be mentioned.

The Convention shall apply also to any identical or substantially similar taxes which are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of significant changes made to their tax law.

Article 4: Residence

A taxpayer has to demonstrate that he is a resident of one or both Contracting States to be able to gain access to a tax treaty and avail the benefits thereunder.

The concept of 'resident of a Contracting State' has various functions and assumes significance in the following three scenarios:

- In determining a convention's scope of application;
- In solving cases where double taxation arises as a consequence of double residence;
- In solving cases where double taxation arises as a consequence of taxation in the state of residence and also in the state of source of income.

As per paragraph 1 of the UN Model 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 that person's domicile, residence, place of incorporation, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof as well as a recognized pension fund of that State**.** 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.

Paragraph 1 of the OECD Model Convention is worded on similar lines. It does not include "place of incorporation" as a residence criterion in the Model text; however, since the 2017 update it expressly includes a recognized pension fund.

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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.

As per paragraph 3 of this Article, whereby reason of the provisions of paragraph 1, a person other than an individual is a resident of both Contracting States, the competent authorities of the Contracting States shall endeavour to determine by mutual agreement, the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention. They shall do so having regard to its place of effective management, the place where it is incorporated or otherwise constituted and any other relevant factors. In the absence of such mutual agreement, such person shall not be entitled to any relief or exemption from tax provided by this Convention except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States.

The situation of dual residence may arise where one Contracting State attaches importance to the place of incorporation and the other to the place of effective management. The current OECD and UN Models use a competent-authority mutual-agreement approach for a person other than an individual, having regard to factors such as place of effective management, place of incorporation or constitution, and other relevant factors. Resolution is by mutual agreement under Article 4(3), using the competent-authority/MAP machinery.

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The last sentence of paragraph 3 of this Article provides that in the absence of determination by the competent authorities, the dual resident person would not be entitled to any relief or exemption from tax provided by this Convention except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States. This will not, however, prevent the taxpayer from being considered a resident of each Contracting State for purposes other than granting treaty reliefs or exemptions to that person.

Article 5: Permanent Establishment

The concept of "Permanent Establishment" (PE), defined in Article 5, is central to Article 7: business profits falling within Article 7 are taxable in the Source State only where the enterprise carries on business there through a PE. Separate distributive Articles, including Articles 12, 12AA, 12B and 12C, may independently permit source taxation without a PE.

The broadly comparable domestic-law concept in India is "business connection". Its statutory location must be read under the Indian income-tax legislation applicable to the relevant tax year. The domestic-law business-connection test and the treaty PE test are distinct; where a treaty applies, the treaty PE threshold may restrict the Source State's taxing right over Article 7 business profits.

As the PE concept gives the Source State the right to tax, it is an important Article for developing countries. Hence, the UN Model Convention varies from the OECD Model Convention in the following respects:

- As per Article 5(3) of the OECD Model Convention, a building site or construction or installation project constitutes a PE if it lasts more than twelve months. The UN Model Convention is wider as it's article 5(3)(a) covers "assembly or installation project" or "supervisory" activities in connection therewith and requires the activity in question to continue for six months for constituting a PE.
- Article 5(3)(b) of the UN Model makes a specific reference to Service PE which is absent in the OECD Model. Article 5(3)(b) of the UN Model reads as follows –

  "The furnishing of services by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only if activities of that nature continue within a Contracting State for a period or periods

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aggregating more than 183 days in any twelve-month period commencing or ending in the fiscal year concerned."

The reference to "including consultancy services" in Article 5(3)(b) has been deleted in the UN Model Convention 2025, because a distinction between consultancy and other services is no longer relevant under the Convention as a result of the addition of Article 12AA to replace former Article 12A and Article 14.

In the absence of a Service PE reference in OECD Model, the presence has to be ascertained through general principles under Article 5(1).

- Article 5(1) states the "basic rule" for a PE and expresses the primary meaning of PE. The definition of PE in Article 5 does not use the qualifying words "unless the context otherwise requires". As such, the definition needs to be followed in all cases unless specifically excluded.

  Paraphrasing Article 5(1), a PE exists if the following conditions are satisfied cumulatively:

  - There is an "enterprise".
  - Such enterprise is carrying on a "business";
  - There is a "place of business";
  - Such place of business is at the disposal of the enterprise (may be owned/rented but must be one which the enterprise has the effective power to use);
  - The place of business is "fixed", that is, it must be established at a distinct place with a certain degree of permanence.

  The business of the enterprise is carried on wholly or partially through this fixed place of business.

  A PE does not exist unless all the aforesaid conditions are satisfied.

- As per Article 5(2), the term "permanent establishment" includes especially:

  (a) a place of management;

  (b) a branch;

  (c) an office;

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(d) a factory;

(e) a workshop, and

(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

- ***The 2025 update to the OECD Model Tax Convention Commentary on Article 5 has been updated to clarify the circumstances in which an individual's home or other relevant place may constitute a "place of business" of the enterprise. The changes reflect modern working arrangements and provide greater certainty on when working from a home or similar location may, or may not, result in a fixed place of business PE.***
- Agency PE under OECD and UN Models targets activities done by a dependent agent of the enterprise in the Source State. The definition of dependent agent PE includes instances when an agent habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts routinely concluded without material modification by the enterprise.

  In UN Model Convention, PE is constituted even if the person does not habitually conclude contracts nor plays the principal role leading to the conclusion of such contracts, but habitually maintains in that State, a stock of goods or merchandise from which that person regularly deliver goods or merchandise on behalf of that enterprise.
- ***The insurance PE provision formerly contained in Article 5(6) has been deleted from the Article, with source taxation of insurance premiums addressed through new Article 12C. The subsequent paragraphs of Article 5 have consequently been renumbered.***

Article 7: Business Profits

Business profits of an enterprise can only be taxed by the Residence State. Right of Source State to tax business profits of an enterprise only exists if a PE exists in its jurisdiction.

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As per the approach under the OECD Model Convention, once a PE is proven, the Source State can tax only such profits as are attributable to the PE. The UN Model Convention amplifies this attribution principle by a **limited** Force of Attraction rule (FOA).

The FOA rule implies that when a foreign enterprise sets up a PE in State of Source, it brings itself within the fiscal jurisdiction of that State (State of Source) to such a degree that profits that the enterprise derives from State of Source, whether through the PE or not, can be taxed by it (State of Source).

As per Article 7 of the UN Model Convention, if the enterprise carries on business in the other Contracting State through a PE, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to:

(a) that PE;

(b) sales in that other State of goods or merchandise of the same or similar kind as those sold through that PE; or

(c) other business activities carried on in that other State of the same or similar kind as those effected through that PE.

Article 11: Interest

Paragraph 1 of this Article provides the right to Residence State to tax interest. Paragraph 2, however, also confers right to the Source State to tax interest. Generally, the interest is taxed in the Source State at a given rate on gross basis. However, if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged cannot exceed a specified percentage of the gross amount of the interest. The OECD Model specifies the percentage as 10%, but the UN Model leaves this percentage to be established through bilateral negotiations.

It may be noted that the definition of interest in both the models viz. OECD and UN Model is similar in that it essentially means income from debt claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment are not regarded as interest for the purpose of this Article.

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Article 12: Royalties

This Article provides the right of Contracting States to tax income from royalty.

Key differences between the two Models are as follows:

- As per the OECD Model, royalties arising in the Source State and beneficially owned by a resident of the Residence State are taxable only in the Residence State. However, the UN Model provides that royalties may be taxed in the Residence State. Hence, the UN Model departs from the principle of exclusive right to tax provided to Residence State in the OECD Model. Thus, under the UN Model, the Source State may also tax royalties. However, if the beneficial owner is a resident of the Residence State, the tax charged by the Source State cannot exceed the specified percentage of the gross amount of royalties. This specified percentage is to be established through bilateral negotiations.
- The term "royalties" as per UN Model Convention means payments of any kind:

  (a) received as a consideration for the use of, or the right to use:

    (i) any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting;

    (ii) any patent, trademark, design or model, plan, or secret formula or process; or

    (iii) industrial, commercial or scientific equipment; or

  (b) received as a consideration for information concerning industrial, commercial or scientific experience; or

  (c) received as a consideration for the use of, or the right to use, any software, or paid as a consideration for the acquisition of any copy of software for the purposes of using it.

- ***In the UN Model (2025), the definition of "royalties" under Article 12 has been expanded by introducing sub-paragraph (c) in Article 12(3) to cover consideration for the use of, or the right to use, computer software, as well as consideration for acquiring a copy of computer software for the purpose of using it. The use of, or right to use,***

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copyright in the software is not required for such payments to fall within the definition of royalties.

- The definition of 'royalties' under the OECD Model does not include the following: (a) rentals for films or tapes used for radio or television broadcasting and (b) equipment rentals like rentals for industrial, commercial or scientific equipment. Moreover, the OECD Model does not have an express Article 12(3)(c) provision taxing ordinary acquisition/use of software merely because software is involved.

Article 12AA: Fees for Services

Until the 2025 update, the UN Model contained Article 12A on Fees for Technical Services (FTS). However, there is no specific reference to FTS in the OECD Model. Article 12A permitted both the Residence State and, subject to a maximum rate agreed through bilateral negotiations, the State in which the FTS arose to tax such fees on a gross basis. FTS was defined to include payments for managerial, technical or consultancy services, subject to specified exclusions.

India has had provisions relating to FTS in its domestic law since 1976, and several of its tax treaties contain specific FTS provisions.

In the 2025 UN Model, Article 12A and Article 14 (Independent Personal Services) have been deleted and replaced by new Article 12AA (Fees for Services). Article 12AA adopts a broader approach and covers payments for any service, rather than being restricted to managerial, technical or consultancy services.

Paragraph 3 defined the term "fees for services". It means any payment in consideration for any service.

As per Paragraph 1 to Article 12AA fees for services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. It implies that fees for services would be taxable in the resident State. However, Paragraph 2 permits the Source State to tax fees for services arising in that State on a gross basis, subject to a maximum rate to be established through bilateral negotiations. Paragraph 2 of Article 12AA is expressly subject to Articles 8, 12B, 12C, 15, 16, 17, 18 and 19.

Accordingly, income from international transport, automated digital services, insurance premiums, employment, directors' fees and remuneration of top-level

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managerial officials, artistes and sportspersons, pensions and social security payments, and government service continues to be governed by those Articles in priority to Article 12AA.

The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of fees for services, being a resident of a Contracting State, carries on business in the other Contracting State in which the fees for services arise through a permanent establishment situated in that other State, and the fees for services are effectively connected with: (a) such permanent establishment, or (b business activities referred in Article 7. In such cases the provisions of Article 7 shall apply.

Conversely, under Article 12AA(6), fees are deemed not to arise in a Contracting State where a resident payer bears them through a permanent establishment in the other Contracting State

Article 12AA is also subject to the specific provisions referred to in that Article, while it is not expressly made subject to Article 12 (Royalties); any overlap between a royalty and a service fee therefore needs to be resolved by determining the character of the payment.

Thus, the principal change in 2025 is the transition from taxation of specified managerial, technical and consultancy services under Article 12A to a broader rule covering services generally under Article 12AA, together with the removal of the exclusions contained in former Article 12A.

Article 12B: Income from Automated Digital Services

With the advent of modern means of telecommunications and the spread of digitalization, enterprises have the ability to effectively engage in substantial business activities in the market country (source jurisdiction) without a fixed place of business there, or to conclude contracts remotely through technological means with no involvement of individual employees or dependent agents.

Article 12B was added to the United Nations Model Tax Convention in its 2021 update to preserve the domestic law taxing rights for States from which payments for automated digital services are made. There is no article in the OECD Model corresponding to Article 12B.

Paragraph 1 of Article 12B provides that the income from automated digital services arising in a Contracting State, underlying payments for which made to a

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resident of other Contracting State, may be taxed in the Residence State. It does not, however, provide that the income from automated digital services is exclusively taxable in the Residence State.

Paragraph 2 establishes the right of the country in which income from automated digital services arises to tax in accordance with its domestic law. However, if the beneficial owner of the income is a resident of the Residence State, the tax charged by the Source State cannot exceed the specified percentage of the gross amount of payments underlying the income from automated digital services. This specified percentage is to be established through bilateral negotiations.

"Automated digital services" is defined in paragraph 5 to mean any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider.

An important indicator of the concept of automated services is whether there is ability to scale up and provide the same type of services to new users with minimal human involvement. Once the service offering an automated digital service business is developed (such as a music catalogue or a social media platform), then, the business can provide that service to one user, or many more, on an automated basis with the same basic business processes. On the other hand, a non-automated digital service business would see a proportionate increase in the costs per unit in connection with providing the services to new customers.

Paragraph 6 lists examples of services that may constitute automated digital services. However, the provision is not self-standing; the requirements of paragraph 5 must also be met. Paragraph 6 simply provides an indication that an activity may constitute an automated digital service; it does not provide that an activity listed therein necessarily is an automated digital service. The following services are expressly mentioned in paragraph 6:

(a) online advertising services;

(b) supply of user data;

(c) online search engines;

(d) online intermediation platform services;

(e) social media platforms;

(f) digital content services;

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(g) online gaming;

(h) cloud computing services; and

(i) standardized online teaching services.

The categories are not mutually exclusive; for example, a digital content service could be funded in whole or in part by online advertising.

Paragraph 7 provides that the provisions of Article 12B shall not apply if the payments underlying the income from automated digital services qualify as "royalties" or "insurance premiums" under Article 12 or Article 12C, as the case may be.

Article 12C: Insurance Premiums

Under Article 12C of the 2025 UN Model, insurance premiums arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State and may also be taxed in the State in which they arise, subject to a maximum rate on the gross amount of the premiums, to be established through bilateral negotiations. The treaty confers the taxing right on the Source State, while the manner of collection, including withholding, is governed by domestic law.

The term "insurance premiums" means amounts paid to an insurer pursuant to a contract (policy) in which the insurer indemnifies another person against losses from specific contingencies, perils or risks; the term includes amounts paid to secure reinsurance but does not include amounts paid to acquire or maintain an annuity contract or an insurance contract that includes a substantial investment component.

"Insurer" means a person or arrangement, the majority of the income of which consists of premiums and other amounts received in consideration for the issuance of insurance, reinsurance and annuity contracts and investment income related thereto.

Article 12C represents a significant change from the former Article 5(6), which dealt with insurance through a PE and expressly excluded reinsurance. The new provision permits gross-basis taxation of insurance and reinsurance premiums without requiring the existence of a PE. The change was made principally to avoid the difficulties of attributing profits to a deemed PE and to provide a simpler mechanism for source taxation.

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Where the beneficial owner carries on business in the Source State through a permanent establishment and the insurance premiums are effectively connected with that PE, Article 7 applies instead of Article 12C.

Article 13: Capital Gains

This is the most commonly used Article and it provides for the taxation of income arising from transfer of a capital asset, including transfer of shares. The right to tax income from capital gains may be exclusively with the Residence State or shared between the Residence and Source States.

The Article does not specify what is a capital gain and how is to be computed, this being left to the applicable domestic law. The Article contains rules for taxation of gains made from alienation of different assets such as immovable property, immovable property forming part of a PE, ships and aircrafts, etc.

In respect of gains from shares or comparable interests deriving more than 50 percent of their value, directly or indirectly, from immovable property, the OECD and UN Models contain broadly similar rules. The Source State may tax such gains where the relevant value threshold is satisfied at any time during the 365 days preceding the alienation.

UN Model Convention allows a State to tax gains from the alienation of rights granted under the law of that State as long as these rights allow the use of resources that are naturally present in that State and that are under the jurisdiction of that State. This would cover, for example, the alienation of rights such as fishing quotas granted by the State; the right to fell timber in a forest; the right to extract water; the right to explore part of a territory of the State for oil, gas or minerals; the right to install wind or tidal stream turbines in part of the territory of the State as well as the right to use all or part of the radiofrequency spectrum in the State, including for cell phone purposes.

This provision does not cover rights granted contractually between private parties even if these rights are protected under the law of the State. Thus, the alienation of exclusive right to use know how in a given State would not be covered by the provision as that right granted by the owner of the know-how is not granted under the law of the State.

Both UN and OECD Model convention gives exclusive right to Residence State in case of gains from the alienation of any property other than covered in the other paragraphs of this Article.

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Article 21: Other Income

This Article deals with taxation of items of income which are not specifically taxable under any other specific Article. Key differences are as under:

- OECD approach envisages that the exclusive right to tax is with the Residence State. UN Model contains an additional paragraph, Article 21(3), which provides that Source State may also tax other income.
- Article 21(2) of both OECD and UN Model provides that for income effectively connected with a PE maintained in a Contracting State by a resident of the other Contracting State, taxation is governed by the provisions of Article 7 (Business Profits).

Articles 23A & 23B : Elimination of Double Taxation

In many cases, the application of tax treaty may result into double taxation for taxpayers. In such a case, in order to provide relief to such taxpayers, Articles 23A and 23B which contains provisions relating to elimination of double taxation have to be applied. Articles 23A and 23B provide for the mechanism through which tax credit/exemption may be available in the Residence State for taxes deducted in the Source State.

The OECD and UN Model Conventions specify two approaches - Exemption method (Article 23A) and Credit method (Article 23B). Under the exemption method, tax exemption may be available in the Residence State. Under the credit method, tax credit may be available in the Residence State for taxes deducted in the Source State. These methods are not mutually exclusive and there may be cases where a treaty may adopt exemption method for certain types of income and credit method for other incomes.

The double taxation referred to here, is juridical double taxation, meaning the same income or capital is taxable in the hands of the same person by more than one State. It does not thus, encompass situations of economic double taxation, i.e. where two different persons are taxable in respect of the same income or capital. If two States wish to solve problems of economic double taxation, they must do so in bilateral negotiations.

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Article 25: Mutual Agreement Procedure

There may be a situation wherein a taxpayer may believe that the treatment accorded by either or both Contracting States is not in accordance with the provisions of the tax treaty. In such a case, there is a need for dispute resolution which is addressed by this Article. This Article requires competent authorities of both countries to endeavor to resolve the conflict by engaging in bilateral negotiations.

The UN Model Convention provides two alternatives - Alternative A and Alternative B, for the article on Mutual Agreement Procedure which were introduced in 2011. Under OECD Model the taxpayer may make a request to either Contracting State while UN Model (Alternative A) contemplates taxpayer going to Residence State or the country of his nationality. Alternative B of UN Model Article 25 contemplates reference to an arbitration process as part of the Mutual Agreement Procedure. The decision arrived at, through the process is binding unless a person directly affected does not accept it.

Key differences between the OECD Model Convention (Article 25) and UN Model Convention (Article 25B - Alternative B) are as follows:

- Article 25B(5) of the UN Model provides that an arbitration may be initiated if the competent authorities are unable to reach an agreement on a case within three years from the presentation of that case. However, Article 25(5) of the OECD Model provides a time limit of two years from the date when all the information required by the competent authorities in order to address the case need to be provided to both competent authorities.
- Article 25B(5) of the UN Model provides that arbitration must be requested by the competent authority of one of the Contracting States. Once such a request is made, the taxpayer will be notified. However, as per Article 25(5) of the OECD Model, arbitration must be requested in writing by the person who initiated the case.
- Article 25B(5) of the UN Model allows the competent authorities to depart from the arbitration decision if they agree to do so within six months after the decision has been communicated to them.
- The 2025 OECD Update introduces a new paragraph 6 to Article 25, dealing with the relationship between the tax Convention and Article XXII(3) of the

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General Agreement on Trade in Services (GATS). For purposes of GATS Article XXII(3), the Contracting States agree that a measure falls within the scope of the Convention only if it is a measure to which Article 24 (Non-Discrimination) applies. Any dispute between the Contracting States as to whether a measure falls within the scope of the Convention is to be resolved under the Mutual Agreement Procedure in Article 25(3) or through any other procedure agreed by both Contracting States, rather than through the GATS mechanism.

- *The 2025 UN Model introduces new provisions in Article 25 addressing the interaction between tax treaties and other international agreements. In relation to GATS Article XXII(3), the Contracting States agree that a dispute between them as to whether a measure falls within the scope of the tax Convention may be brought before the Council for Trade in Services only with the consent of both Contracting States. Any doubt regarding the interpretation of this provision is to be resolved through the Mutual Agreement Procedure or, failing agreement under that procedure, through any other procedure agreed by both Contracting States.*
- *The 2025 UN Model also provides that a taxation measure taken by a Contracting State in accordance with the Convention shall not be regarded as breaching any other treaty to which the Contracting States are parties. A dispute concerning whether a taxation measure is in accordance with the Convention or falls within its scope is to be settled only under the provisions of the Convention, without recourse to dispute-resolution mechanisms under another treaty. Other disputes concerning a taxation measure, including a dispute as to whether a measure constitutes a taxation measure, are also, unless the competent authorities agree otherwise, to be settled without recourse to dispute-resolution mechanisms under such other treaties as the Contracting States agree to cover.*

Article 26: Exchange of Information

In order to complete tax cases, a country may require certain information which may be available with the treaty partner. Article 26 provides for the information which may be exchanged and the manner in which such a request has to be made. The purpose of Article 26 is to facilitate effective exchange of information between Contracting States. From the perspective of many developing countries,

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Article 26 is particularly important not only for curtailing cross-border tax evasion and avoidance, but also to curtail the capital flight that is often accomplished through such evasion and avoidance.

The OECD and UN Model Conventions are similar with respect to this Article. A Contracting State cannot be expected to provide confidential financial information to another Contracting State unless it has confidence that the information will not be disclosed to unauthorized persons. A Contracting State can avoid the exchange of information obligations by showing that the information pertains to communication between an attorney and his client which is protected from disclosure under domestic law. However, lack of interest or use in such information cannot form the basis for a Contracting State to not co-operate with the exchange of information obligations.

The 2025 OECD Update clarifies in the Commentary on Article 26 that information exchanged under the Article may, subject to the applicable conditions, be used for tax matters concerning persons other than the person in respect of whom the information was initially exchanged.

Resources: The discussion on Model Tax Conventions in the above chapter is essentially based on the text and commentaries of the OECD Model Tax Convention, 2025 and UN Model Tax Convention, 2025 available at the websites https://www.oecd.org/content/dam/oecd/en/publications/reports/2026/06/model-tax-convention-on-income-and-on-capital-2025-full-version_4fd97b89/db32e18b-en.pdf and https://financing.desa.un.org/sites/default/files/2026-08/UN%20MODEL_2025_web.pdf, respectively.

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TEST YOUR KNOWLEDGE

Questions

1. *Explain briefly the significant difference between the UN and OECD Model Tax Convention.*
2. *When does it become necessary to apply the tie-breaker rule? Discuss the manner of application of the tie-breaker rule.*
3. *Explain the meaning of "interest" and "royalty" under the UN Model Convention.*
4. *What is the meaning of Automated Digital Services? Elucidate.*
5. *Explain the provisions relating to taxation of royalties under Article 12 of the OECD Model Convention and the UN Model Convention, highlighting the key differences between the two Models.*

Answers

1. The OECD Model is widely used by OECD Members and non-Members and generally places greater emphasis on Residence-State taxation, although it also provides for Source-State taxation in specified circumstances. The UN Model was developed with particular attention to the interests and treaty concerns of developing countries and generally gives greater weight to Source-State taxation. The change in the title of the UN Model in 2025 also reflects that the Model is not confined to treaties between developed and developing countries but is intended for use more broadly.

Thus, while the OECD Model generally gives relatively greater importance to the Residence State's taxing rights, the UN Model seeks to balance the Residence and Source States' taxing rights while generally providing greater taxing rights to the Source State than the OECD Model.

2. Every jurisdiction, in its domestic tax law, prescribes the mechanism to determine residential status of a person. If a person is considered to be resident of both the Contracting States, relief should be sought from Article 4 of the Tax Treaty. A series of tie-breaker rules are provided in Paragraph 2 Article 4 of Model Convention to determine single state of residence for an individual.

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The tie-breaker rule would be applied in the following manner:

(i) The first test is based on where the individual has a **permanent home**. Permanent home would mean a dwelling place available to him at all times continuously and not occasionally and includes place taken on rent for a prolonged period of time.

(ii) If that test is inconclusive for the reason that the individual has permanent home available to him in both Contracting States, he will be considered a resident of the Contracting State where his personal and economic relations are closer, in other words, the place where lies **his centre of vital interests**. Thus, preference is given to family and social relations, occupation, place of business, place of administration of his properties, political, cultural and other activities of the individual.

(iii) Paragraph (ii) establishes a secondary criterion for two quite distinct and different situations:

- The case where the individual has a permanent home available to him in both Contracting States and it is not possible to determine in which one he has his centre of vital interests;
- The case where the individual has a permanent home available to him in neither Contracting State.

In the aforesaid scenarios, preference is given to the Contracting State where the individual has an **habitual abode**.

(iv) If the individual has habitual abode in both Contracting States or in neither of them, he shall be treated as a resident of the Contracting State of which he is **a national**.

(v) If the individual is a national of both or neither of the Contracting States, the matter is left to be **considered by the competent authorities** of the respective Contracting States.

3. As per Article 11 of the UN Model Convention, "Interest" essentially means income from debt claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or

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debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment are not regarded as interest for the purpose of this Article.

- The term "royalties" as per Article 12 of UN Model Convention means payments of any kind:

  (a) received as a consideration for the use of, or the right to use:

  (i) any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting;

  (ii) any patent, trademark, design or model, plan, or secret formula or process; or

  (iii) industrial, commercial or scientific equipment; or

  (b) received as a consideration for information concerning industrial, commercial or scientific experience; or

  (c) received as a consideration for the use of, or the right to use, any software, or paid as a consideration for the acquisition of any copy of software for the purposes of using it.

4. As per Article 12B of UN Model Convention, "Automated digital services" means any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider.

The term "Automated digital services" includes specially:

(a) online advertising services;

(b) supply of user data;

(c) online search engines;

(d) online intermediation platform services;

(e) social media platforms;

(f) digital content services;

(g) online gaming;

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(h) cloud computing services; and

(i) standardized online teaching services.

5. Article 12 deals with the taxation of royalties and provides for the allocation of taxing rights between the Contracting States.

A key difference between the two Models relates to the taxing rights of the Source State. Under the OECD Model, royalties arising in the Source State and beneficially owned by a resident of the other Contracting State are taxable only in the Residence State. In contrast, under the UN Model, royalties may be taxed in both the Residence State and the Source State. However, where the beneficial owner is a resident of the other Contracting State, the tax imposed by the Source State cannot exceed a specified percentage of the gross amount of the royalties, with the rate to be established through bilateral negotiations.

Under the UN Model, "royalties" means payments of any kind received as consideration for the use of, or the right to use, copyright in literary, artistic or scientific works, including cinematograph films and films or tapes used for radio or television broadcasting; patents, trademarks, designs or models, plans, secret formulas or processes; or industrial, commercial or scientific equipment. It also includes payments for information concerning industrial, commercial or scientific experience.

The 2025 UN Model has further expanded the definition of royalties by introducing sub-paragraph (c) in Article 12(3) to cover consideration for the use of, or the right to use, computer software, as well as consideration for the acquisition of a copy of software for the purpose of using it. Importantly, the payment need not relate to the use of, or right to use, copyright in the software to fall within this provision.

In comparison, the OECD Model does not include rentals of films or tapes used for radio or television broadcasting or payments for the use of, or right to use, industrial, commercial or scientific equipment within the definition of royalties. Further, the OECD Model does not contain an express provision equivalent to Article 12(3)(c) of the 2025 UN Model covering software payments merely on the basis of the use of, or right to use, software or acquisition of a copy of software for use.

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