That's Entertainment - Taxation of Entertainers and Athletes in New Zealand

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Entertainers are marked out for special treatment by tax authorities in almost all jurisdictions. The nature of their activities, their often high mobility coupled with the large sums that can be earned in short periods, make the general tax rules applying to individual personal services income inadequate. As a result, both in domestic and international law, specific provision has been made for this type of taxpayer. This article discusses the tax treatment of income earned by entertainers. It examines the tax treatment of non-resident entertainers in New Zealand and then compares it to the treatment afforded to such taxpayers under international law, focusing on Article 17 of the OECD Model Convention.

1 ENTERTAINERS' INCOME

Entertainers can potentially earn many different types of income. For example, an entertainer may receive payments for appearing or performing at an event. The fee for this appearance may be calculated either as a flat fee or according to ticket sales. The fee may also have reference to the broadcasting or recording rights to that event. In addition, either a sign-on fee or an inducement payment may have been made to secure the entertainer's presence.

At the event, paraphernalia bearing the entertainer's intellectual rights (eg likeness, image, trade mark, or copyrighted words) may be sold. These products may be sold either by the entertainer, a non-resident third person, or a local business, on payment to the entertainer for use of the rights (either as a flat fee or based on a share of sales/profits).

In addition, the entertainer may receive payments for endorsements either relating directly to the appearance in New Zealand or generally. Finally, the entertainer may receive payments based on their sales, popularity, or "air-time" in New Zealand and/or around the world.

To fully analyse the tax position of a non-resident entertainer it is necessary to apply a two-step test.

(1) Determine whether the income earned is subject to tax under domestic law (ie liable to tax in New Zealand under the Income Tax Act 1994 ("ITA 1994")). This involves two factors:

   (a) What is that nature of the income earned? and

   (b) Is that income sourced in New Zealand for the purposes of domestic law?

(2) If the income of the non-resident entertainer is subject to domestic tax, it is then necessary to consider the impact of the applicable tax treaty.

2 [(1998) Vol 4:1 NZJTLP 3, 4] NEW ZEALAND-SOURCED INCOME

The Income Tax Act 1994 applies to all income derived in New Zealand, whether by a New Zealand tax resident or otherwise. Thus, at least as a general concept, New Zealand provides for itself the right to tax all income having a source in this country.

New Zealand's right to tax income may later be superseded by the provisions of a tax treaty. However, as a starting point, all income derived from a New Zealand source is subject to New Zealand tax, including all income earned by non-resident entertainers. The source rules contained in ss OE 4 and OE 5 specify the classes of income that are deemed to have been derived from New Zealand. These types of income include most of those likely to be derived by non-resident entertainers and athletes, such

as:

- Income from personal services;
- Business income; and
- Royalties.

2.1 Personal services income

All salaries, wages, allowances, or emoluments earned in New Zealand are subject to tax under s CH 3, even if the employer is a non-resident. The wording of s OE 4 raises the question whether the income is “earned” in New Zealand or elsewhere. Many factors go into determining where income is earned, and it is a question of fact in each instance whether income from personal services was earned in this country. Factors to consider include:

- The place where the contract of service was entered into;
- The place where payment for those services was made; and
- The plce where the services are actually performed.

In many instances these factors will point to different conclusions and the over-all situation must be considered. In these cases the Courts may adopt a “practical reality” test whereby the income may be apportioned between different possible countries of source.

2.2 Business income

Income derived from any business wholly or partly carried on in New Zealand is attributed to a New Zealand source.

Where the business is carried on or the contract is performed partly in New Zealand and partly elsewhere, the income and expenditure of that business must be apportioned to identify the amount of net income that accurately reflects the income and expenses attributed to New Zealand.

2.3 Royalties

Income from royalties paid by a New Zealand resident is attributed to a New Zealand source.

2.4 Other income

Income derived from any contracts made or wholly or partly performed in New Zealand is attributed to a source in this country.

[(1998) Vol 4:1 NZJTLP 3, 5] A complete analysis of the rules of derivation are beyond the scope of this article. For the present purposes it can be presumed that all income is derived in New Zealand. Income not derived in New Zealand is not subject to tax in this country and therefore will not need to be allocated between New Zealand and another jurisdiction under the relevant treaty.

3 EXCLUSIONS FROM NEW ZEALAND INCOME TAX

Subpart CB of the ITA 1994 contains a number of exclusions for certain specified types of income. These types of income are exempt from tax in New Zealand. If such income is to be taxed at all, it will only be in another jurisdiction, such as the taxpayer’s country of residence. The following exemptions may have application to income earned by non-resident entertainers and athletes.

Section CB 2(1)(a) impacts on the taxation of non-resident entertainers and athletes. That section creates an exemption for income earned by non-residents from any activity or performance:

- Under a Government-sponsored cultural exchange;
- Of a foreign non-profit cultural organisation; or
- In a game or sport where the participants represent their national body administering that sport.

Under this exemption, entertainers and athletes who earn income from one of the stipulated sources will not be taxed on that income in New Zealand. This exemption is absolute and is not limited as to the length of time the participants spend in New Zealand or the source of the payment (whether from the New Zealand host or from a non-resident).

Section CB 2(1)(c) contains a further exemption for non-residents who provide personal services in New Zealand for a non-resident employer. Income earned by such persons will be exempt from tax in this country if:

- The non-resident is in New Zealand for fewer than 92 days;
- The income earned by the non-resident from the work undertaken here is taxable in the country of residence; and
- The services are performed on behalf of a non-resident.

Such an exemption would potentially apply to non-resident entertainers and athletes performing services through a loan-out company. However, this exemption is specifically foreclosed to that class of taxpayer. The proviso to s CB 2(1)(c) states:

> "this paragraph shall not apply to any amount derived by public entertainers (including, but without limiting the generality of the term 'public entertainers', theatre, motion picture, television and radio artists, singers, musicians, dancers, lecturers, circus performers, boxers, wrestlers, athletes, and other professional sportspersons)."

The combined effect of s CB 2 is to ensure that (subject to the narrow exemption in s CB 2(1)(a)) all income derived in New Zealand by non-resident entertainers and athletes is subject to tax in this country. Furthermore, the scope of the exemptions in subss (a) and (c) mirror the treatment of entertainers and athletes under the OECD Model Convention ("Model Convention").

4 COLLECTION OF TAX FROM ENTERTAINERS AND ATHLETES

The collection of tax from entertainers and athletes is dealt with under the Income Tax (Withholding Payments) Regulations 1979. These regulations prescribe a number of "speci **[(1998) Vol 4:1 NZJTLP 3, 6]** fied activities". Any person receiving income for engaging in these activities is deemed to be in receipt of a "source deduction payment". As such, the maker of the payment must withhold an amount of tax from the payment made.

The regulations apply to both resident and non-resident entertainers. The two categories are defined in the regulations as:

> "'Non-resident entertainer' means any person who is not deemed to be resident in New Zealand within the meaning of section [sic] Subpart OE of the Act and who, during the course of a visit to New Zealand, performs or participates in any specified activity, and includes any company or firm or other person in any case where the first-mentioned person is an employee or an officer of the company or a principal or employee of the firm or an employee of the other person, being a company, firm, or other person which provides the services of the first-mentioned person, during a visit to New Zealand of the first-mentioned person, in performing or participating in any specified activity:"'Resident entertainer' means a person who

> is deemed to be resident in New Zealand within the meaning of Subpart OE of the Act and who performs or participates in any specified activity."

Where non-resident entertainers perform personal services in New Zealand, the regulations deem them to be conducting a "specified activity". This term is defined as:

> "in relation to a non-resident entertainer or resident entertainer, means any activity or performance, including performances or appearances on or for radio, television, or a film, –
>
> "(a) In connection with any sporting event or competition of any nature, including motor racing, motorcar rallies, motor cycle racing, motor boat racing, and horse racing and trotting:
>
> "(b) In connection with lectures, speeches, or talks for any purpose, whether on a regular or casual basis:
>
> "(c) In connection with any performance by actors, entertainers, musicians, singers, dancers, comperes, or other artistes, whether regular or casual performers, and whether alone or with any other person or persons in choirs, choruses, bands, orchestras, ballets, or other entertainment groups, and whether for the purpose of education or culture or religion or entertainment or any other purpose."

The definition then excludes all activities that would fall within the exemption for income in s CB 2(1)(a) (see Section 3).

Importantly, the definition of "specified payment" under the regulations applies to any payment:

> "to that person, or to that person's agent or any other person acting on the person's behalf, being a payment paid in respect of or in relation to any services rendered or provided by the person in connection with that specified activity, whether that payment is paid as fees, remuneration, prize, or appearance money, or otherwise."

In this way any payment to any entertainer or athlete performing in New Zealand is liable for withholding tax whether the taxpayer:

- Is acting as an employee or an independent contractor; or
- Is providing the services personally or through an agent or "loan-out" company.

The scope of the specified activity relating to entertainers and athletes is similar to that provided under Article 17 of the Model Convention. The types of income caught as a specified payment ("fees, remuneration, prize, **[(1998) Vol 4:1 NZJTLP 3, 7]** or appearance money, or otherwise") are similar to those provided for in the Model Convention. Such payments are the expected consequence of performance as an entertainer and thus spring directly from that status. Payments to the taxpayer that do not arise directly from their entertainment or athletic activities (eg merchandising or royalties) would presumably fall outside the scope of the regulations. This approach mirrors that of Article 17 which applies only to income derived by the entertainers or athletes "from [their] personal services as such".

Another significant feature is that the regulations extend the definition of "non-resident entertainer" to encompass:

> "any company or firm or other person in any case where the first-mentioned person is an employee or an officer of the company or a principal or employee of the firm or an employee of the other person, being a company, firm, or other person which provides the services of the first-mentioned person, during a visit to New Zealand of the first-mentioned person, in performing or participating in any specified activity."

Likewise, the definition of "specified payment" includes payments made to "agents". The combination of these provisions ensures that entertainers cannot avoid the application of the regulations by providing services through an intermediary or loan-out company.

The regulations look to the services performed by the taxpayer not the method of contracting or payment used by the parties.

Extending the definition of non-resident entertainer to encompass intermediaries is an anti-avoidance measure to ensure the efficacy of the regulations. In this way the regulations mirror the treatment provided under the Model Convention.

5 DOUBLE TAX AGREEMENTS

All income derived by non-resident entertainers and athletes in New Zealand is subject to New Zealand tax. However, that liability may be relieved under a Double Tax Agreement entered into between New Zealand and the individual's country of residence.

The Model Convention contains a specific provision dealing with the taxation of income earned by entertainers and athletes. Article 17(1) of the Model Convention reads:

> "17 ARTISTES AND ATHLETES"17(1) Notwithstanding the provisions of Articles 14 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 an athlete, from his personal activities as such exercised in the other Contracting State, may be taxed in that other Contracting State."

Article 17(1), which was included in the Model Convention from its first publication in 1963, deals specifically with the taxation of income derived by entertainers and athletes. It forms an exception to the other Model Convention provisions dealing with independent or dependent personal services under Articles 14 and 15 respectively. To the extent that Article 17(2) applies to income earned by loan-out companies, it also provides an exception to the treatment of business profits under Article 7.

The effect of Article 17 has been summed up by one commentator as follows:

> " **[(1998) Vol 4:1 NZJTLP 3, 8]** Article 17 strikes with surprising vehemence against visiting entertainers and athletes, especially successful ones. The articles governing personal services, independent services, and business profits that would normally exempt short-term visitors from tax are made inapplicable to entertainers and athletes."

6 RATIONALE BEHIND ARTICLE 17

Under Article 17 entertainers and athletes are singled out and the income they earn is treated differently from that earned by other taxpayers. But what is the rationale behind this separate treatment?

The predominant support for Article 17 is based on the "benefits theory" which underlies a State's claim to tax income earned within its borders. In short, the theory states that taxes levied by a State are the price of all services provided by the State to that taxpayer. To a greater or lesser degree the theory is applied to various types of income under the Model Convention, indicating where countries themselves agree the benefits are provided and where the costs for those benefits should be paid.

The separate treatment of entertainers and athletes has been justified on the basis of the benefits theory. Non-resident entertainers and athletes are thought to enjoy a greater benefit than other taxpayers by virtue of the facilities they use while in the source country. These benefits include security measures, availability of venues, transportation, free press, and a market for their products or services. It is therefore expected that non-resident entertainers should contribute to the cost of providing those services from income derived in that country.

This rationale is vulnerable to criticism on a number of grounds. First, while a few high-profile entertainers and sports people enjoy enhanced benefits, most "jobbing" entertainers and athletes require or enjoy no greater benefits than other taxpayers providing personal services. Secondly, the benefits theory could equally be applied to other high-profile, highly paid taxpayers whose personal services do not fall within the scope of Article 17. Movie directors, choreographers, and coaches are but a few within the entertainment and athletic fields. Many other highly-paid taxpayers, such as those providing professional or consultancy services, also enjoy enhanced benefits but are not singled out for special treatment under the Model Convention.

As a result, the benefits theory alone cannot explain the universal acceptance by almost all countries of the need for Article 17.

An alternative explanation is offered by Professor D Sandler of the University of Western Ontario. Sandler points to both the high mobility of such taxpayers and the substantial incomes that can be earned in short periods of time. Sandler argues that Article 17 is merely a pragmatic recognition that the standard rules applying to personal services income do not adequately cover this type of taxpayer. In effect, Article 17 is a “tax grab” by countries seeking to impose tax on income earned within their borders. This desire for tax is, in turn, largely based on the reasonable assumption that, if not caught by the country of source, such income might escape tax altogether.

This pragmatism is based on the difficulty of enforcing tax against non-resident entertainers and athletes. In many instances these taxpayers have left the jurisdiction prior to any assessment being issued, and most have few economic ties with the countries in which they perform. Accordingly, recovery of tax on income derived in each separate jurisdiction is difficult, if not **[(1998) Vol 4:1 NZJTLP 3, 9]** impossible - unless each country was granted the right to tax that portion of the taxpayer’s income therefrom derived.

The pragmatic response of most countries to this enforcement problem is to impose withholding taxes on all income derived by entertainers within its borders. In some countries this withholding tax represents a final tax, while in others it is merely an estimation of tax owing which can be off-set against actual liability established on filing the appropriate return.

Accordingly, Article 17 has been incorporated into the Model Convention for efficiency reasons. It is the country of source which is best able to secure the payment of tax through the use of withholding tax coupled with sanctions on resident payers who fail to account for such tax. That country should therefore gain the benefit of collection. In this way, the Article provides international support for the collection of withholding tax by various jurisdictions.

7 SCOPE OF ARTICLE 17

Article 17 applies only to income earned by “artistes and athletes” from personal services in their capacity as such. Not surprisingly, the exact scope of the terms “artiste” and “athlete” is not settled. The Article lists a number of examples of entertainers who specifically fall within its scope but these cannot be taken as exhaustive of the definition. Strangely, no examples of “athletes” are given, although the exact scope of this term is far from certain.

The article does not expressly limit itself, but the commentary to the Model Convention states that it should apply only to performing entertainers. Thus only artistes and athletes who perform directly or indirectly before an audience come within the article. Behind-the-scenes artists (such as painters, sculptors, photographers, writers, and composers) are presumably outside its application. Individuals who provide managerial, technical, or supporting services (such as directors, choreographers, coaches, and make-up artists) are likewise excluded.

Traditionally the term “athlete” has been applied to sports people who perform in competitive games or sports. Thus, the provision covers not only participants in traditional athletic events but those engaged in all modern sports. The term therefore applies to “non-athletic” pursuits such as golf, motor racing, and equestrian events.

In 1992 the term “athlete” was replaced in the Model Convention by the term “sports man” so as to further extend the scope of the Article. The OECD commentary to Article 17 was amended at that time to encompass other activities “of an entertainment character, such as those deriving from billiards, snooker, chess and card tournaments”. Such performers would not fit within the generally accepted definition of “athletes” as that term continues to exist in treaties entered into before 1992. This indicates that such activities fall outside the scope of the previous wording of Article 17 - as still appears in most of New Zealand’s existing treaties.

The only international interpretation of the scope of Article 17 comes from the Italian Tax Authority. In 1981 the Authority issued a ruling to the effect that participants in the 1982 World Chess Championship held in Italy were considered to be athletes for the purposes of Article 17. The ruling stated that athletic activity should be interpreted widely so as to not only encompass its traditional meaning “but should also include any activity predominantly using physical or intellectual skills as a delight to onlookers or in the context of a competition or exhibition.”

[(1998) Vol 4:1 NZJTLP 3, 10] This wide (and somewhat self-serving) interpretation is open to question. The fact that the wording and commentary needed amending in 1992 so as to specifically include such non-athletic pursuits indicates that the Article as it then read had a narrower scope.

The narrow interpretation of entertainers and athletes under Article 17 seems somewhat arbitrary. Article 17’s focus on performance artists only leads to an illogical distinction between taxpayers who work on the same project according to the work they perform. Thus taxpayers who provide equally valuable work towards a performance (and are paid equally) will come within different articles of the Model Convention. For example, a director or coach is not caught under the Article while the actors or players are. This inconsistency was referred to by an Italian commentator, Dr Alfonso Trivoli, who stated:

> "As treaties derived from the Model [Convention] do not normally contain more detailed definitions, the result can only be widespread uncertainty as to the scope and application of Article 17, with the resulting confusion as to the tax obligations of the debtor and of the recipient of the income, in a field which is not administratively very sophisticated."

From the lack of academic discussion or decided case law on Article 17 around the world, this criticism appears to be well founded. In practice, the scope of Article 17 has been largely determined by the domestic law of each country.

8 INCOME WITHIN ARTICLE 17

Article 17 applies only to income earned by entertainers and athletes from their personal services "as such". This wording gives

Article 17 a narrow focus. Income earned by the individual in another capacity (ie other than as an entertainer or athlete) or not by way of performance is not included within the Article. I will examine each of these boundaries separately.

8.1 Income from personal services

There will often be instances where an entertainer receives income from personal services that do not directly relate to that person's professional field. Sponsorships and endorsements are but two examples. Where an athlete is paid to wear or use a particular product in the course of their sport, there is little difficulty in saying that the payment relates to the athlete's "personal services as such". However, payments to use or wear products that are not part of their sport do not relate to the athlete's activities as an athlete but to his or her general fame and would fall outside Article 17.

Likewise, inducement payments or signing bonuses paid to an entertainer or athlete may or may not relate to that person's performance, depending on the terms of the contract and the reasons for the payment. If the payment related directly to the performance, it would reasonably be caught within Article 17. However, if it was genuinely an inducement to enter the contract (as opposed to performing under it) such a fee would fall outside the Article.

While such distinctions are unnecessary under domestic law, identifying the actual services provided in return for the payment received is crucial to determining whether a particular payment falls within Article 17.

8.2 [(1998) Vol 4:1 NZJTLP 3, 11] Other income

In addition to income earned from personal services, an entertainer or athlete may earn many other types of income. These other types of income do not fall within the narrow scope of Article 17 which focuses only on income earned by the taxpayer from performances. For example, a fee or share of profits from the sale of paraphernalia bearing the individual's name, image, or trade mark cannot be said to be derived by that entertainer or athlete in their capacity as such - and therefore falls outside Article 17. Likewise, royalties and other forms of passive income earned by the entertainer or athlete do not come within the Article.

An interesting question arises from bonuses earned by entertainers or athletes from their performance over a whole tour, year, or season, rather than from one particular performance. While such payments are clearly income arising from personal services, they may not be said to have been derived from any single country. As payments of this nature will relate to performances in many countries, they cannot be said to have been derived by the taxpayer from personal services performed in any one country. In some instances an apportionment may be required to measure how much, if any, of the bonus can be attributed to performances in each State.

For example, annual ranking bonuses paid by the US-based Association of Tennis Professionals ("ATP") to competing professionals are not directly related to the tennis player's performance in any particular country but to their performance over the whole year in tournaments throughout the world. While the payment is actually made by the ATP (thereby presumably sourced in the US), it does not relate to personal services performed only in the US. Whether such payments can be apportioned between each country on the tour (and on what basis that apportionment should be made) has never been addressed.

8.3 Mixed income

A further difficulty arises where an entertainer or (less commonly) an athlete is paid a fee made up of many different components. The performer's contract may provide for a flat performance fee, a share of receipts, and a share of the television rights to any

performance. Such a contract is common in the film industry where actors are often paid a flat fee plus a share of the box office receipts on release of the film.

In this instance, the various types of income must be isolated out to determine whether each is earned by way of personal services - and therefore fall within Article 17.

9 LIMITATIONS ON ARTICLE 17

Article 17 contains a number of express limitations. The most general of these limitations is set out in Article 17(3):

> "17(3) Notwithstanding the provisions of paragraphs 1 and 2, income derived by entertainers or athletes who are residents of a Contracting State from the activities exercised in the other Contracting State under an arrangement of cultural exchange between the Governments of the Contracting States shall be exempt from tax in that other Contracting State."

Under Article 17(3) income from certain specified types of entertainment or athletic performances are excluded from 17(1), and thus are treated as either independent or dependent personal services under Articles 14 or 15 respectively.

The principle exception in Article 17(3) applies to income from events forming part of an official cultural exchange, charitable event, or government-funded programme. The reason behind this exception is that these types of events are non-profit in nature, and/or publicly **[(1998) Vol 4:1 NZJTLP 3, 12]** funded. As a result, it is recognised that the provisions of Article 17 should not apply so as to allow performers in such events to be taxed in the country where the event took place. To allow otherwise would effectively allow one State to tax income paid to performers by their own State of residence.

Under Article 17(3) income earned by such performers is either treated as dependent or independent personal services income, or as remuneration for services rendered to a government, depending on the identity of the party making the payment.

9.1 De Minimus exemptions

Article 17 is intended to tax in the country of derivation income earned by highly remunerated entertainers and athletes who would otherwise escape tax under the general treaty provisions. However, the Model Convention stipulates no income threshold. Thus, the Article applies to all income earned by entertainers and athletes in that capacity, regardless of the level of that income. Even small sums earned by "jobbing" actors or semi-professional sports people are caught under Article 17.

This general position is altered in the New Zealand-US Treaty. That treaty contains a de minimus exemption whereby Article 17 applies only to taxpayers with an income of greater than US$10,000 per year. This exemption effectively sets a base level of income below which Article 17 will not apply. Taxpayers earning less than that will be dealt with under the general rules of Articles 14 and 15.

10 USE OF LOAN-OUT COMPANIES

Many entertainers or performers utilise intermediaries or "loan-out companies" through which they provide their services. The use of such entities would avoid the provisions of Article 17(1). The income is earned by the intermediaries and not by the entertainer or athlete from their personal services - as required under the Article. Furthermore, under Article 7 tax on business profits is payable only in the intermediary's country of residence unless the intermediary has a permanent establishment in the country in which the income is derived.

Article 17(2) contains a specific prohibition against this all-too-easy means of skirting its effect:

> "17(2) Where income in respect of personal activities exercised by an entertainer or an athlete in his capacity as such accrues not to the entertainer or athlete himself but to another person, that income may, notwithstanding the provisions of Articles 7, 14 and 15, be taxed in the Contracting State in which the activities of the entertainer or athlete are exercised."

Article 17(2) stipulates that income paid "in respect of" personal services performed by an entertainer or athlete will be treated as

income of that person even if it is paid to an intermediary. To give effect to this extended meaning, Articles 7, 14, and 15 are expressly stated not to apply to such income. In effect, Article 17(2) is an anti-avoidance provision to ensure the integrity of Article 17(1) against perceived abuse.

Many countries have further supported the provisions of Article 17 by enacting domestic legislation to prevent the use of loan-out companies and other intermediaries. Such provisions work in a similar manner to Article 17(2) by deeming all income paid in respect of entertainment or athletic services to be paid to the taxpayer personally, regardless of the actual recipient of that income.

New Zealand has created just such a deeming provision by adopting a wide definition of "non-resident entertainer" in **[(1998) Vol 4:1 NZJTLP 3, 13]** the Income Tax (Withholding Payments) Regulations 1979. That definition encompasses any company, firm, or other person which provides the services of an entertainer. The effect of this provision is that payments to a loan-out company will be caught as if the payments were made to the entertainer personally. In this way, domestic law re-enforces the application of Article 17.

10.1 Limitation on article 17(2)

A number of treaties limit the effect of Article 17(2) only to instances where the entertainer or athlete providing the services has a financial interest in the loan-out company. This exception applies where (according to the terminology used by those treaties) the entertainer or athlete is entitled to share in the "profit" of the intermediary. The rationale behind the exclusion is that many entertainers and athletes are genuine employees of another entity. Members of a sports team or theatre troupe who receive only salary or wages are but two examples. It was felt that such taxpayers should not come within the provisions of Article 17 but should instead be dealt with under the general rules for personal services in Articles 14 and 15.

In most cases the exact nature of the profit-sharing required to fall within this exemption is not spelt out, thus creating uncertainty. However, the US-New Zealand Treaty applies a wide definition that encompasses:

> "deferred remuneration, bonuses, fees, dividends, partnership distributions or other distributions."

The effect of this wide definition of "profit" is to ensure that almost all entertainers working through intermediaries are caught within Article 17(2), thus greatly narrowing the exclusion.

11 "TRIANGLE" CONTRACTS

The use of intermediaries to loan-out an entertainer's or athlete's services raises another issue - that of so-called "triangle" contracts. Under this kind of arrangement, a resident of country "A" contracts with the intermediary (resident of country "B") for the supply of personal services by the entertainer (resident of country "C").

Applying Article 17(2), any payment to the intermediary would be taxed by the country of source as if it was paid directly to the entertainer personally. However, which treaty must the parties look to when determining whether the income is liable for tax in the country of source?

The Model Convention provides no assistance with resolving tax issues from triangular arrangements. Tax treaties are bilateral agreements between States. Article 1 (Personal Scope) stipulates that the Model Convention applies only:

> "to persons who are resident of one or both of the Contracting States."

As a result, no single treaty can resolve tax disputes involving residents of three or more States. Such would require either an amendment to the treaties concerned or the extension of the mutual agreement procedure. In practice, most States appear unwilling to address this issue.

11.1 Example

An entertainer is resident of the US. He performs services as an entertainer in New Zealand through a loan-out company resident in

Australia.

11.1.1 [(1998) Vol 4:1 NZJTLP 3, 14] New Zealand-US Treaty

The New Zealand-US Treaty would not apply to income paid to the loan-out company for the entertainer's services. While he is a resident of the US (one of the Contracting States), the income from his personal services as an entertainer does not accrue to him but to another person (the loan-out company). As that loan-out company is a resident of neither contracting State, the provisions of the New Zealand-US Treaty cannot apply.

Article 17(1) applies only where income is derived by an entertainer. Where a loan-out company is interposed no income is, in fact, derived by the entertainer - so there is no income to which Article 17(1) can apply. Likewise, Article 17(2) has no application as it (and the entire Treaty) cannot apply to income derived by the loan-out company, a resident of neither Contracting State.

Income paid to a loan-out company in these circumstances will therefore be subject to tax in the country of source under general principles. Such income may therefore be subject to double taxation (ie both in the source country and the intermediary's country of residence) unless it is dealt with under a separate treaty between these countries.

Provided there is no contrary provision in either New Zealand domestic law or in the New Zealand-Australia Treaty, New Zealand will retain the right to tax the income sourced within its borders. Either way, the country of source may tax the income derived by the non-resident entertainer.

This is the result reached in New Zealand where the Income Tax (Withholding Payments) Regulations 1979 tax income derived by an intermediary from the personal services of an entertainer unless relieved under a relevant treaty. If the intermediary is not a resident of any country with which New Zealand has a treaty, income earned by it will be subject to New Zealand law by virtue of s OE 4.

The right of the source country to tax this income is supported by a number of commentators:

> "Consequently, it appears to matter little where the performer resides since this will either be in a State that has signed a convention with State S (where the activity is performed), under the terms of which State S has the right to tax [per Article 17(1)] or else in a State which has no convention with State S, whose right to tax therefore cannot be limited."

11.1.2 New Zealand-Australia Treaty

The entertainer is a resident of neither Contracting State. Nevertheless it is the New Zealand-Australia Treaty that will determine the taxability of income earned by the loan-out company from the services of that entertainer.

The wide wording of Article 17(2) dictates that income paid to a loan-out company for the services of an entertainer continue to be taxable in the country of source. This provision over-rides the application of Article 7 that would normally apply to the earnings of a non-resident company.

Article 17(2) applies where "income in respect of the personal activities of an entertainer …" is paid to a loan out company. While contained within Article 17, and immediately following Article 17(1), it is questionable whether "an entertainer" in Article 17(2) need be the same entertainer as stipulated in Article 17(1).

Both on its face and by reference to the commentary, nothing in Article 17(2) requires the entertainer, from whose services the income is derived by the loan-out company, to be resident of either State. If payment is made to a loan-out company resident in either State, Article 17(2) **[(1998) Vol 4:1 NZJTLP 3, 15]** will apply. In such a case, the income will be taxed in the country of source "notwithstanding the provisions of Articles 7, 14 and 15".

12 SPECIAL TREATY PROVISIONS FOR ENTERTAINERS AND ATHLETES

In addition to the inclusion of Article 17, a number of Double Tax Agreements entered into by New Zealand contain special provisions for the treatment of income earned by entertainers and athletes.

12.1 Australia

The Australian Treaty contains a specific provision (cl 18(3), the so-called "Warriors clause") dealing with the taxation of players, managers, trainers, and support staff of teams who regularly compete in a rugby league competition conducted in both countries. This provision treats income earned by such taxpayers under the general provisions of Article 15.

Clause 18(3) is worded narrowly, applying only to taxpayers "regularly playing in a league competition organised and conducted solely in both Contracting States". This wording indicates that players engaged in triangular tournaments (such as the World Super League Challenge, involving teams from Australia, New Zealand, and Great Britain) would not come within the scope of the exclusion as the competition takes place across each country, not solely in Australia or New Zealand.

12.2 Canada, China, France, India, Indonesia, Korea, Malaysia, Norway

Treaties with these countries incorporate a separate provision whereby entertainers or athletes performing in the other State under State-sponsorship or as part of a cultural exchange are exempted from Article 17. Income from these activities is dealt with under Articles 14 and 15.

12.3 USA

There is a de minimus exemption in the US-New Zealand Treaty whereby Article 17 applies only where the taxpayer's income as an entertainer or athlete exceeds US$10,000. Also, where the income accrues to a loan-out company, Article 17(2) applies only if the taxpayer has an interest in the "profit" earned by that company's profits (see discussion at Section 9.1 above).

12.4 Japan

Article 17 is not included in the Japan-New Zealand Treaty. The income of entertainers and athletes is therefore dealt with under the general provisions of Articles 14 and 15.

13 COMPARISON WITH OTHER ARTICLES

The opening words of Article 17 specifically override the provisions of Articles 14 and 15 of the Model Convention. As such, income earned by entertainers and athletes from personal services that would otherwise be dealt with under those Articles (independent and dependent personal services) are brought within Article 17. But due to the narrow focus of Article 17, many types of income earned by entertainers or athletes will fall outside the scope of the Article. These types of income must be dealt with under a number of other Articles. The other relevant provisions include:

- Article 7, business profits;
- Article 12, royalties; and
- Articles 14 and 15, dependent and independent personal services.

13.1 [(1998) Vol 4:1 NZJTLP 3, 16] Article 7

Article 7 applies to business profits earned by an enterprise which has a permanent establishment in the country in which that income is derived. Effectively, the Model Convention gives a country the right to tax the business profits of an enterprise only if that enterprise has a permanent establishment within its borders. The Article then dictates how much of that profit can be attributed to the permanent establishment and therefore how much of that profit should be subject to tax in which country.

It will be rare that an entertainer or athlete has a permanent establishment in the country in which the business profit was derived. Due to the itinerant nature of the industries and the short time such taxpayers spend in any place, it is unlikely that profits from the taxpayer's non-personal services activities will be caught under Article 7. Therefore, such profits are taxable only in the taxpayer's country of residence, if at all.

Article 17 does not override Article 7 - except to the extent it applies to income earned by loan-out companies. Thus all income that

fits within the scope of business profits will be dealt with under Article 7, even where the income was derived by a business from entertainment or athletic pursuits. In practice, there is little conflict between the two Articles.

13.2 Article 12

Article 12 applies to royalties and dictates that royalties are taxable only in the country of residence of the holder of that intellectual property. As royalties are by nature passive income (ie not from personal services) there is no conflict between Articles 12 and 17, each dealing with different types of income. However, the opposing effects of each provision means that the different types of income will be treated differently under the Model Convention. Personal services income will be taxed in the country of source. Income from the sale of paraphernalia or from box office returns or air-time will be taxable in the country in which that taxpayer resides, if at all.

13.3 Articles 14 and 15

Articles 14 and 15 apply to income earned from personal services either independently or as an employee. These articles are expressly subject to Article 17(1). Income earned from personal services of the kind described in Article 17 are treated only under that provision. However, the narrow scope of Article 17 allows for the possibility that personal services income earned by the taxpayer from non-entertainment or athletic activities will fall outside Article 17. Such income will be dealt with under the general provisions of Articles 14 and 15.

Under Article 14 independent personal service income is taxable only in the country of residence of the taxpayer unless that person has a permanent establishment in the country in which the services are performed. Under Article 15 income from dependent personal services are likewise taxed only in the taxpayer's country of residence, provided:

- The taxpayer is present in the other country for less than 182 days in the year concerned;
- The remuneration is paid by the taxpayer's non-resident employer; and
- The remuneration is not met by any permanent establishment of the employer in the other country.

As with Article 7, the itinerant nature of entertainers' and athletes' activities means that few will have a permanent establishment in the countries in which they derive income. Nor, if employees, will their stay in a country generally exceed 182 days.

[(1998) Vol 4:1 NZJTLP 3, 17] As a result, the income earned by entertainers and athletes from non-performance services (eg unrelated product endorsements) will usually not be taxable in the country in which that income is derived. Instead it will only be taxable in their country of residence, if at all.

14 CONCLUSION

The itinerant nature of entertainers and athletes justifies their separate treatment under both domestic and international law. The right of source countries to tax all income derived by these taxpayers within their borders makes logistical sense in the face of taxpayers with no country of residence and loan-out companies based in tax havens. However, the scope of the specific provisions aimed at entertainers often produces illogical and unjustifiable distinctions between both different taxpayers who provide services to the same event, and the different types of income derived by the same individuals.

FOOTNOTES

1 The term "entertainer" also encompasses athletes, as discussed at Section 7.

2 Section AA 2 ITA 1994.

3 Section BH 1 ITA 1994.

4 Section BB 3 ITA 1994.

5
These types of income are taxed respectively under ss CH 3, CD 3, and CD 2 ITA 1994.

6 Section OE 4(1)(c) ITA 1994.

7
Case E46(1982) 5 NZTC 59,277, also reported as *Case 34*(1982) 5 TRNZ 301.

8
CT (NSW) v Cam & Sons Ltd(1936) 4 ATD 32, *FCT v French*(1957) 98 CLR 398.

9 *FCT v Mitchum*(1965) 113 CLR 401.

10 Section OE 4(1)(a) ITA 1994.

11 Section FC 2 ITA 1994.

12 Section OE 4(1)(r) ITA 1994.

13 Section OE 4(1)(u).

14 See Subpart NC of the ITA 1994.

15 Section BH 1 ITA 1994.

16 Article 14 (independent personal services) and Article 15 (dependent personal services) apply according to either the taxpayer's length of stay or the existence of a permanent presence in the source country. See comparison at Section 12 below.

17 *Income Tax Treaties*, p 714.

18 *The Taxation of International Entertainers and Athletes - All the World's a Stage*, The Hague, Kluwer, 1995.

19 Including New Zealand.

20 Note No 12/062, November 1981.

21 *Taxation of Non-resident Entertainers*, Cannes, IFA, 1995, p 71.

22 See, for example, the wide definition of "non-resident entertainer" adopted by New Zealand under the Income Tax (Withholding Payments) Regulations 1979.

23 New Zealand, like most countries, imposes tax on all income from personal services regardless of the nature of those services.

24 See Section 2 above.

25 Articles 14 or 15 respectively.

26 Article 19.

27 Refer to full definition at Section 4.

28 Particularly those entered into by the US.

29 See *Issues in International Taxation No 4, Model Tax Convention: Four Related Studies*, "Triangular Cases", p 39.

30 See *Issues in International Taxation No 2, Taxation of Entertainers, Artistes and Sportsmen*, Paris 1987, p 59.

31 Emphasis added.

32 Emphasis added.

33
This extends the exemption period of 92 days under domestic law in s CB 2(1)(c).