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White Paper on International Taxation of Entertainers

Background information

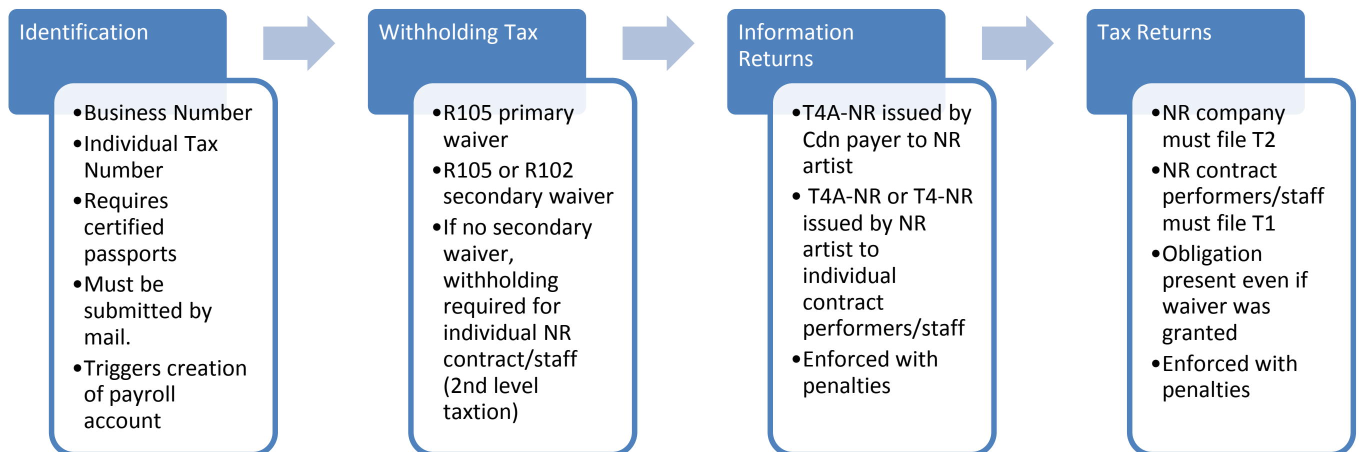
Major performing arts organizations in Canada regularly contract for the services of non-resident artists and companies, in addition to engaging a large number of artists residing in Canada. However, artists are subject to differentiated treatment in tax treaties and, as a result, the burden of compliance with non-resident taxation is regularly causing administrative and financial hardship to both Canadian engagers and to non-resident artists and companies (and vice-versa, when Canadian artists tour abroad). It is estimated that the cost of compliance could be up to 10 times greater than the potential tax revenues for the Canada Revenue Agency.

This white paper was developed out of recommendations first issued by the Performing Arts Tax Working Group in 2015. It focuses exclusively on observations and recommendations at the treaty level. The Performing Arts Tax Working Group has been and is still seeking streamlining at the administrative level with the Canada Revenue Agency.

Overview of Non-Resident Taxation in Canada

Every time a Canadian performing arts organization contracts a non-resident artist, intricate international taxation laws (Part XIII of the *Income Tax Act*) and regulations (R105, R102) apply. This regime is very complex and was decried in 2008 by the *Advisory Panel on Canada's System of International Taxation*[i], as well as by various associations such as the Tax Executive Institute and Chartered Professional Accountants Canada during Pre-Budget Consultations and in other forums.

The non-resident taxation process involves four steps:



Note: In June 2018, the Canada Revenue Agency introduced a simplified income tax process for non-resident artists. This policy only applies to self-employed entertainers (which only represent a very small portion of non-resident tours to Canada) and is consequently not reflected in this overview.

Observations and recommendations for a more flexible and fair treatment of entertainers in tax treaties

Article 17 of the OECD Model Tax Convention was introduced and in the 1960s and integrated in the OECD model in 1977 to create an exceptional rule for performing artistes (and sportspersons). The main reason for this special treatment is that top artists and athletes are very mobile, and they can easily move their residency to a tax haven in order to avoid taxation.

Paragraph 1 of Article 17 states that entertainers and sportspersons need to pay income tax in the country of performance, regardless of the general rules for companies, self-employed persons or employees. Paragraph 2 of Article 17 states that, when income accrues not to the entertainer, but to another person (such as a not-for-profit dance company or a so-called "star corporation), that income may be taxed in the country of performance. As a result of Article 17, non-resident entertainers cannot benefit from general exemptions under the business profit exemption (Article 7). Non-resident entertaining corporations are also subject to two level of taxation: first-level taxation on fees paid by the Canadian engager to the non-resident corporation, and second-level taxation on fees or salaries paid by the non-resident corporation to individual performers.

The original Article 17 was a "one-size-fits-all" and a number of issues have arisen over the years. As a result, OECD-member countries have agreed to introduce several options for the restriction of the scope of Article 17. The 2017 OECD Model Tax Convention includes several such options, including the following which we deem worthy of inclusion in Canada's tax treaties:

- ***De minimis* rule**
  Paragraphs 10.1 to 10.4 of the Commentary on Article 17 recognize that it would be inappropriate to apply Article 17 to a non-resident artist who would not be taxable in the performance state or who, during a given taxation year, derives only low amounts of income in that state. In order to exclude such low-risks situations, the paragraphs propose a minimum amount 15,000 IMF Special Drawing Rights (the equivalent of CAN$27,000 of US$20,000 at December 2016 conversion rates), under which artists fees are exempt from tax in the performance state. The existing $15,000 exclusion in the Canada-United States Convention is an example of a *de minimis* rule. However, the practice of "grossing up" revenues (see below) when assessing whether a non-resident qualifies for a *de minimis* exclusion isn't desirable, because it adds a significant layer of complexity to the preparation and the assessment of a waiver application. Notwithstanding this reservation, we believe a *de minimis* exclusion of an amount consistent with the Canada-United States Convention should be systematically negotiated in all of Canada's tax treaties.

- **Income from employment**
  Although the vast majority of touring artists are receiving wages as self-employed

workers, there are certain touring theatre and ballet companies that do have artists on payroll. In those instance, the artists are often support performers, they are fairly but not generously compensated for their work, and they do not participate directly or indirectly in the profits from the tour. In short, those employed performing artists are not the kind of high earning artists and sportspeople that were meant to be captured by Article 17. In order to limit the application of paragraph 1 of Article 17 to business activities, and to avoid the complexities associated with attributing a portion of salaries to services provided in another state, we recommend that Canada systematically adopt the alternative wording suggested in paragraph 2 of the Commentary on Article 17.

- **Income accruing to another person**
  Paragraph 2 of Article 17 allows for the taxation of income accruing to another person than the entertainer. While this makes a lot of sense in the case of star corporations, it creates an unfair treatment when this other person is a not-for-profit, tax-exempt corporation such as theatre, dance and opera companies. Since 1997, Canada, Switzerland and the United States have introduced a reservation on Article 17 to limit the scope of paragraph 2 to star corporations (see paragraph 16 of the Commentary). The Performing Arts Tax Working Group is highly supportive of this approach. However, currently, the language of the Canada-United States Convention is not specific enough to clearly exclude non-profit performing arts companies from the scope of paragraph 2. The Performing Arts Tax Working Group recommends that Canada reopens discussions with the United States, Switzerland and other potential allies to specifically exempt not-for-profit performing arts corporations from Paragraph 2 of article 17.

- **Public funds**
  Paragraphs 14 of the Commentary provides an option to exclude from Article 17 events supported from public funds. Canada's tax treaties with France and the United Kingdom include an exemption along these lines. While the option in paragraph 14 may grant an exclusion to non-profit corporations receiving public funds, the option has not yet been extended so as to specifically include not-for-profit organizations. We however consider that not-for-profit corporations should benefit from this exclusion since:
    - Not-for-profit corporations are tax-exempt under the *Income Tax Act*;
    - Canadian not-for-profit companies who tour abroad are generally supported by public funding through one or several components of the Creative Export Strategy; and,
    - Foreign not-for-profit companies are unlikely to tour Canada on a regular basis or for long durations.

- **Deduction of expenses**
  Paragraph 10 of the Commentary refers to the determination of taxable income. It proposes the deduction of expenses from gross income and taxation of net income

under the normal rules of each country. Currently, the guidelines for the administration for Regulation 105 Withholding do the exact opposite. Waiver applicants are asked to report expenses reimbursable expenses or expenses paid on their behalf by the payer. These expenses are then "grossed up" on top of the artist fee to determine the eligibility to a waiver. This provision in the Regulation 105 guidelines is imposed by the Canada-United States Convention, and it should be brought up with U.S. authorities when the convention comes up for renewal.

The ideal tax treaty should thus:

A. Include a *de minimis* exclusion for artists earning only limited income;
B. Exclude income from employment; and,
C. Exclude not-for-profit performing arts corporations.

Such a tax treaty would enable more non-resident art corporations to benefit from streamlining initiatives such as the Simplified Regulation 105 recently introduced by the Canada Revenue Agency or the Non-Resident Employer Certification program. At present, too few non-resident tours can benefit from either of these initiatives. We estimate at no more than 10-15% the proportion of tours benefitting from the Simplified Regulation 105 and there are to our knowledge no performing arts corporation that has ever benefitted from the Non-Resident Employer Certification program.

An effective, efficient and smart non-resident taxation regime is needed to adequately support rather than hinder the federal government's Creative Export Strategy. We need a regime that will allow Canada to effectively collect due income tax on highly profitable tours of foreign artists in our country, while protecting government-funded Canadian organizations from unfair taxation when they tour the world. And we need a regime that no longer places such undue administrative burden on both the non-resident artists and the Canadian payers.

Over the coming years, trade agreements such as the Comprehensive Economic and Trade Agreement may create opportunities Canada to reopen several bilateral treaties. We urge the government of Canada to take advantage of these renegotiations to integrate exclusions on Article 17 into Canada's tax treaties.

In addition, Canada's cultural diplomacy efforts, as part of the Creative Export Strategy, provide a unique opportunity to reform Article 17 of our tax treaties, and to considerably reduce the impediment of international taxation on cultural exchanges. Although tax treaties can't easily be reopened, we recommend that the government take advantage of cultural diplomacy initiatives, such as the Canada-China Joint Committee on Culture, to negotiate bilateral suspensions of Article 17, in favour of more flexible administrative policies such as are recommended by the Performing Arts Tax Working Group.

About the Performing Arts Tax Working Group

The Performing Arts Tax Working Group is a collective of twenty performing arts organizations and associations representing more than 1,000 Canadian stakeholders. It was formed in 2014 to examine ways to achieve greater efficiency and better risk management in the administration of taxation of non-resident entertainers. CAPACOA was designated by Working Group members to be the facilitator for the group. The Working Group is comprised of the following organizations:

Arts Commons
BAM! Baird Artists Management
Canadian Dance Assembly
Canadian Independent Music Association
Cusson Management
Danse Danse
East Coast Music Association
Eponymous
evenko
Festival international de Jazz de Montréal
Festival Transamériques
Festivals and Major Events Canada
Indie Montréal
Kokoro Dance / Vancouver International Dance Festival
Les Grands Ballets Canadiens de Montréal
Lula Music and Arts Centre
Montréal, arts interculturels
Music Canada Live
National Arts Centre
North American Performing Arts Managers and Agents
Pop Montréal
Regroupement des événements majeurs internationaux
Small World Music Society
The CanDance Network
TOHU et Montréal Complètement Cirque
CAPACOA

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On behalf of the Performing Arts Tax Working Group

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[i] "Canada's rules for international taxation are some of the most complex provisions of the Income Tax Act. Complying with these rules imposes a significant burden not only on Canadian businesses investing abroad and foreign investors doing business in Canada, but also on the CRA, which is responsible for administering the entire Act, including Canada's international tax rules. Given the nature of cross-border transactions and the sophistication of modern businesses, some complexity is inevitable. Even still, every effort should be made to minimize the compliance burden imposed on taxpayers in the international arena."
Enhancing Canada's International Tax Advantage: A Consultation Paper Issued by the Advisory Panel on Canada's System of International Taxation, April 2008.