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Do we need a new definition of Permanent Establishment for digital operations in Double Tax Treaties?

by

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HARN60 Master Thesis

Master's Programme in European and International Tax Law

2019/2020

Spring semester 2020

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Submission date: 2020.05.31

Word count: 10 424

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Summary

This master thesis investigates the need for a new Permanent Establishment (PE) definition for digital purposes in Double Tax Treaties (DTTs).

In the core of the necessity to pursue the analysis of this, are the digital economic developments, and the challenges that they pose for international tax law, policymakers, countries, and businesses. More specifically, the physical presence of digitalized businesses, or the lack of it, in certain jurisdictions for tax purposes is of particular importance, because these create the difficulty for countries to retain their tax base.

Those challenges motivate the question if the current PE concept in DTTs is still efficient, a definition whose main purpose is to determine the allocation of taxing rights over the business income of other jurisdiction under the condition of a fixed place of business with economic activity. Furthermore, the business, that is deemed to have a PE, should participate in the other jurisdiction's economic life.

In relation to that, this thesis outlines, analysis and discusses the recent changes made in legislation, OECD MC and UN Model, as well as the provided Multilateral Instrument for applying those. The works and recommendations from OECD BEPS Actions 1, 7 are followed, and other related official OECD documents providing with the proposal for a new approaches to counteract the digital challenges.

Furthermore, the aim of the master thesis is to attempt to evaluate the efficiency and capabilities of the given amendments and potential propositions for solutions to the arising problems. One problem addressed is whether the proposals for Virtual PE would be sufficient, and whether there is a need to implement a new definition in DTTs for digital purposes.

Abbreviation list

ALP	Arm's Length Principle
AOA	Authorised OECD Approach
BEPS	Base Erosion and Profit Shifting
BEPS Action 7	Additional Guidance on the Attribution of Profits to Permanent Establishments
DTT	Double Tax Treaties
ISP	Internet Service Provider
MLI	Multilateral Instrument
OECD	Organisation for Economic Co-operation and Development
OECD MC	OECD MC Income Tax Convention on Income and Capital
PE	Permanent Establishment
TFEU	Treaty on the Functioning of the European Union
UN Model	United Nations Model Double Taxation Convention 2017
VCLT	Vienna Convention on the Law of Treaties

1. Introduction

1.1 Background

The developing digital economy, and the general globalization trend, are imposing challenges to international tax law, and how businesses income is taxed.[1]

Nowadays, a great deal of businesses have digital solutions incorporated in their business model, which is also what defines the understanding of "digital economy". It becomes difficult to separate the two terms "economy" and "digital economy", because digital economy is in great proportions the economy.[2]

The need for a physical presence to conduct business has changed. E-commerce is heavily applied in selling products and services internationally. In some cases, this allows the circumvention of the physical requirements for Permanent Establishment (PE) for tax purposes.[3] As a result, many jurisdictions have suffered economic loss.

The factors above, have initiated the need of public discussion in order to define the need and to identify possible solutions.[4] In the author's opinion, the factors also pose the question if there is a need for a new PE definition for digital purposes, a Virtual PE, where the need for a physical place of business is not going to be necessary requirement to constitute a PE.

There are currently no specifically designed rules to be applied in the existing treaties, cross-border businesses might suffer overtaxation as a result of countries levying taxes in the country where the value creation is identified and in the country of residence without the obligation of relief in either.[5]

The need for countries to bridge the gap between adequately defined legislation caused by digital economy developments, causing the suffering of base erosion, and tax revenue losses. This creates the apparent need to

[1] Kofler Georg, Mayr Gunter and Schlager Christoph, *"Taxation of the Digital Economy: A Pragmatic Approach to Short-Term Measures"*, European Taxation, IBFD, 2018, p.123.
[2] Larking Barry, *"A Review of Comments on the Tax Challenges of the Digital Economy"*, Bulletin for International Taxation, 2018 (Volume 72), 26 March 2018, p.2.
[3] Larking Barry, *"A Review of Comments on the Tax Challenges of the Digital Economy"*, Bulletin for International Taxation, 2018 (Volume 72), 26 March 2018, p.2.
[4] OECD (2018), *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project*, OECD Publishing, Paris.
[5] Brauner Yariv, Pistone Pasquale,*"Some Comments on the Attribution of Profits to the Digital Permanent Establishment"*, 72 Bull. Intl. Tax n. 4a/Special Issue, 2018, Bulletin for International Taxation IBFD, p.1.

investigate the potential solution by introducing the concept of Virtual PE in Double Tax Treaties (DTT).[6]

The needs described above, together with other related issues, that are to be discussed in this thesis, are the precedent for analysing the need of redefining the definition of PE for digital operation purposes.

1.2 Aim

The aim of this project is to investigate if there is a need of implementing a new definition of Virtual Permanent Establishment in Double Tax Treaties for digital purposes.

1.3 Method and material

In the aim of solving the issue at stake there will be the use of primary and secondary law materials. Case law will be introduced to support analysis and considerations. For the purpose of reflecting the latest legislation available, the 2017 OECD MC will be used. Apart from some historical background and more principal rules, that need to be explained, the aim is to use current articles reflecting the latest developments on the matter.

The legal method that has been chosen is the legal dogmatic method, as it analyses the law as it stands, and possible future law proposals. Through this method, it is meant to take on an internal perspective in the analytical process of interpreting law.[7]

1.4 Delimitation

This master thesis project focus is on the PE concept for digital purpose and therefore will be limited to that extent. There will be a discussion on the current rules of the concept and the suggestions made on the need of a Digital PE concept for digital purposes. Double Tax Treaties (DTTs) are included since the aim of the project is to answer the question if there is a need of a Virtual PE in DTTs. Specific country's DTTs will not be discussed, because the goal of the thesis has a holistic approach towards the concept of PE in all DTTs. The EU law will not be included since DDTs are under UN Model and OECD MC.

[6] Brauner Yariv, Pistone Pasquale, *"Some Comments on the Attribution of Profits to the Digital Permanent Establishment"*, 72 Bull. Intl. Tax n. 4a/Special Issue, 2018, Bulletin for International Taxation IBFD, p.1.

[7] Douma Sjoerd, *"Legal Research in International and EU Tax Law"*, 2014 Edition, Wolters Kluwer Business, p. 17-18.

Related topics, such as how is defined source and resident tax under digital market conditions will not be discussed, as well as, the Ottawa Taxation Framework Principles, due to striving to stay on topic and the page limit constrains of this master thesis.

1.5 Outline

In order to create a structured answer to the research question through analyzing relevant topics, the outline of this master thesis will be as follows.

The thesis will start with an introduction of the definition of a Permanent Establishment (PE), where it comes from, and how the term came into use for taxing purposes. Introducing what Double Tax Treaties (DTT) are, in order to create an understanding of the core competences that DTT has in general and in relation to PE. (Chapter 2)

After that, a discussion on the differences between UN Model and OECD MC will be provided with the purpose to illustrate what are the difficulties that countries encounter when drafting their DTTs. Further, recent changes made in legislation on the topic will be presented shortly. Finally, it is discussed what constitutes the existence of PE, under what conditions, and how is defined.(Chapter 3)

Chapter 4, introduces the digital market definition, the issues related to the digital market contemplating the concept of PE. It follows a discussion on the value creation and attribution of profits, where there are incorporated the changes made in OECD Action 7, regarding preventions of avoidance of the PE in a result of the digital economy challenges. Thereafter, the proposal of new definition from OECD for a “Virtual PE” will be presented with the different approaches.

Afterward, an analysis of the new definition and proposed solutions will be given, and on their sustainability to resolve the identified problems that they are aimed at.

The final part, (Chapter 5), of the thesis, will present a conclusion of the performed research work.

2. Permanent Establishment (PE) and Double Tax Treaties (DTTs)

In line with the research question of analysing the need of a new concept of Permanent Establishment (PE) for digital purposes, it is important to shortly introduce the background of the concept. Furthermore, the goal is to identify some of the problems related to the original concept that are still current and relatable. Furthermore, a presentation of DTTs will be provided.

2.1 The definition of Permanent Establishment (PE), short history and introduction

The Permanent Establishment (PE) concept has been in place for many years. The existence of the term dates back to the 19th century, where it was used in Germany.[8]At first, the term was not used in a tax law context, but later on it was implemented in tax law terms of use. It was used as a term in the Prussian tax law for the first time in 1885. In that period of time other countries also began to use it as a term into their tax law legislations, such as Austria and Holland.[9] The shaping of the PE definition has been influenced by the German law, providing the categorisation of a PE:

"place of management, branch, factory, purchase, selling offices, office, any place where business can be carried on by the entrepreneur or by his confidential clerk or other permanent representative"[10]

The term was implemented as a definition for the first time by the German Double Taxation Act of 1909, which was similar to the one presented in the Organisation for Economic Co-operation and Development (OECD).[11]

The facts above establish the importance of the concept and the roots of constructing the definition. From an early stage though, problems were

[8] Jones John F. Avery, De Broe Luc, Ellis Maarten J. and others, *"The Origins of Concepts and Expressions Used in the OECD MC and their Adoption by States"*, Bulletin-Tax Treaty Monitor, IBFD, *2006*, p. 233.

[9] Jones John F. Avery, De Broe Luc, Ellis Maarten J. and others, *"The Origins of Concepts and Expressions Used in the OECD MC and their Adoption by States"*, Bulletin-Tax Treaty Monitor, IBFD, *2006*, p. 233, (footnote 156).

[10] Jones John F. Avery, De Broe Luc, Ellis Maarten J. and others, *"The Origins of Concepts and Expressions Used in the OECD MC and their Adoption by States"*, Bulletin-Tax Treaty Monitor, IBFD, *2006*, p. 234.

[11] Jones John F. Avery, De Broe Luc, Ellis Maarten J. and others, *"The Origins of Concepts and Expressions Used in the OECD MC and their Adoption by States"*, Bulletin-Tax Treaty Monitor, IBFD, *2006*, p. 233-234; Skaar, A.A., *"Permanent Establishment: Erosion of a Tax Treaty Principle"*, Deventer, Netherlands: Kluwer Law and Taxation, 1991, p.72-75.

identified such as having permanent establishment in both states, as resident and non-resident, which highlighted the need to differentiate between the terms permanent establishment and enterprise (as in Swiss law).[12]Other problems encountered were the inclusion of taxation of auxiliary activities (indirectly contributing to the earnings), related to a certain business. The problem was that some countries did include it and some did not into their taxing rights.[13]

Another critical point is the difference between countries with different legal systems, civil law and common law countries. A setting example is the "agent" permanent establishment provision (Article 5(5) and 5(6) in the OECD MC)[14], interpretation problem. In countries with civil law basis, the "agent" is interpreted differently as to the given authority to enforce legally binding contracts for another party (the principal) directly or indirectly, resulting in the binding effect for the principal. In short, if the "agent" is given a direct authority to conduct contacts on behalf of the principle, it is legally binding. Whereas in the other case of indirect authority, the "agent" role is merely as an intermediary thus not legally binding for the principal of the conducted contracts. In common law countries, the conducted contracts by the "agent", ultimately are binding for the principal enterprise unless otherwise stated in the contract. This is due to the broad contracting terms, where common law, in contrast to civil law, does not oblige contracting parties to disclose an eventual third party (the principal enterprise) that is represented ("agent").[15]

The presented problems and some consequences of these will be discussed further on in the thesis. They are relevant in respect of the considerations of a new definition of Permanent Establishment concept to be introduced in Double Tax Treaties (DTTs). Therefore, the next chapter contains the introduction to DTTs and the PE definition.

[12] Jones John F. Avery, De Broe Luc, Ellis Maarten J. and others, *"The Origins of Concepts and Expressions Used in the OECD MC and their Adoption by States"*, Bulletin-Tax Treaty Monitor, IBFD, *2006*, p. 234.
[13] Jones John F. Avery, De Broe Luc, Ellis Maarten J. and others, *"The Origins of Concepts and Expressions Used in the OECD MC and their Adoption by States"*, *Bulletin- Tax Treaty Monitor*, *IBFD*, *2006*, p. 234-236.
[14] OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.32.
[15] Jones John F. Avery, Lüdicke Jürgen, *"The Origins of Article 5(5) and 5(6) of the OECD MC"*, World Tax Journal, 2014, p.204-206 ; Jones John F. Avery, Baker Philip QC, Daxkobler Katharina and others, *"Dependent Agents as Permanent Establishments"*, Michael Lang ed., Linde, 2014, p. 161-162.

2.2 PE in DTTs

The term of PE was introduced for the first time in tax treaties in the concluded tax treaty between Austro-Hungarian Empire and Prussia of 1899; then other countries followed to include it in their tax treaties. The rules on PE were that the income earned should be taxed in the, source country. The definition, and categorising elements were not much different than today. As for permanent establishment to be constituted, it was necessary a fixed place of business carrying out the business activities for a foreign enterprise. It also included the agent and purchasing elements.[16]

The foundation of Double Tax Treaties is the works of the League of Nations (1920s), that later on become what is known today as the United Nations (UN). Following in its steps, the OECD took the lead in creating the guidelines for tax treaties. OECD MC and their commentaries have marked the basis for implementing the rules in tax treaties. Countries that are not OECD members also follow the OECD MC to draft their tax treaties.[17]

2.3 Double Tax Treaties definition

2.3.1 DTTs: legal basis, scope, interaction with domestic law

The scope of the Vienna Convention on the Law of Treaties (VCLT) constitutes the general frame of rules in tax treaties such as interpretation, obligation, and introduction. Article 2 describes the nature of tax treaties; Article 26 and 31 state the binding nature between contracting parties, and that it should be executed and interpreted in a good faith according to its context.[18]

DTTs are mainly bilateral agreements between countries determining their taxing rights distribution. The right to invoke the benefits of a tax treaty imposes direct effect on taxpayers. When drafting its DTT, contracting countries are following the OECD MC Treaty or UN Model Treaty in their

[16] Kobetsky Michael, *"International taxation of permanent establishments : principles and policy"*, Cambridge tax law series, 2011, .p.110-111.
[17] Kobetsky Michael, *"International taxation of permanent establishments : principles and policy"*, Cambridge tax law series, 2011, p.152.
[18] Arnold Brian J., *"International Tax Primer"*, 3rd. Edition, Kluwer International B.V, 2016, p. 136-137; Vienna Convention on the Law of Treaties Signed at Vienna, 23 May 1969.

negotiation process. The OECD MC is most often used for developed countries, and the UN Model for developing countries.[19]

DTTs are qualified as *leges speciales (*special legislation)[20], according to Klaus Vogel, due to its application in cross-border situation, as opposed to domestic general tax law. Furthermore, according to the rule of *"lex specialis derogat legi generali",* meaning that the special legislation overrides the general law, thus DTTs override domestic tax law, unless otherwise stated in domestic constitutional law. In general, the introduction of a new domestic legislation will not influence treaties that are already in place.[21] Double Tax Treaties have the stipulation of adding a clause stating that the thereby treaty shall apply to any future additional or similar provisions in domestic laws that the tax treaty already is in force for.[22]

This rule as all others has its exception; unless the newly drafted domestic general law is stipulating the change of provisions in *lege speciales* as well. Other problems that can occur are if the domestic legislation does not implement tax treaties in their legislation automatically once they are signed.[23] In addition to that, when introducing new taxes, the interpretation, if the new legislation is similar or in addition to the existing one, could cause problems.[24]

The reciprocity principle is a central factor in the function of the DTT. The purpose of the principle is for the regulations to apply equally, reciprocally when imposed on the either resident of the contracting state. DTTs cannot find application until they are to some degree incorporated in Domestic law. [25]

2.3.2 What are DTTs purposes and application

The purpose of Double Tax Treaties is to some extent, to foster fairness in cross-border taxation in the sense that they can be a remedy for double taxation, tax evasion or avoidance and elimination of tax discrimination regulated by the OECD MC.[26] In addition to that, in result of the OECD G/20

[19] Finnerty Chris J., Merks Paulus, Petriccione Mario, Russo Raffaele, *"Fundamentals of International Tax Planning"*, IBFD, 2007, p.11-15.
[20] Vogel Klaus, *"Tax Treaties and Domestic Law"*, IBFD Publications BV., 2006, p.3.
[21] Vogel Klaus, *"Tax Treaties and Domestic Law"*, IBFD Publications BV., 2006, p.4.
[22] Finnerty Chris J., Merks Paulus, Petriccione Mario, Russo Raffaele, *"Fundamentals of International Tax Planning"*, IBFD, 2007, p.11.
[23] Vogel Klaus, *"Tax Treaties and Domestic Law"*, IBFD Publications BV., 2006, p.3.
[24] Finnerty Chris J., Merks Paulus, Petriccione Mario, Russo Raffaele, *"Fundamentals of International Tax Planning"*, IBFD, 2007, p.12.
[25] Arnold Brian J.,*"International Tax Primer"*, 3rd. Edition, Kluwer International B.V, 2016, p. 137.
[26] Article 23A and 23B, Article 26, Articles 24, OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris.

BEPS, the OECD MC 2017, extends the purpose of DTTs to preventing non-taxation or lower taxation in result of tax avoidance or evasion. In that sense, pointing the attention to countries to mind each other's tax systems that might create the possibility of enabling non-taxation.[27]

The main purpose of a DTT historically, is the prevention of juridical and economic double taxation[28], and the treaties serve this purpose by allocation of taxing rights.[29]This is achieved, when one, or the other contracting state is given the exclusive right to tax an income. In this sense, the DTTs also limit the contacting states taxing rights to the limits of the given exclusive rights to tax.[30]

Tax discrimination can occur on the grounds of nationality or providing better tax treatment for non-resident or resident companies in the contracting states that a bilateral tax treaty is in place. The main goal is the prevention against differentiated tax treatment. Here, the principle of reciprocity is applied that all tax treaties are to obey. If it is to be defined whether discrimination is in place, the key aspect are the circumstances that the certain company may be under. No privilege should be constituted to either of the resident or source state taxing subject.[31] The principal of discrimination applies to PE in a full manner regarding where, and to whom the PE belongs to. There are examples in relation to the place of effective management that are relevant to the subject and displays the discrimination. These examples will however not be included in this research, due to their extensiveness and the page constrains on this thesis.[32]

Countries that need to be in conformity with the EU law in regard to discrimination, have to consider the Treaty on the Functioning of the European Union (TFEU) Article 110 prohibiting imposed internal taxes on products from other Member States (MS) that are higher than the one on a similar domestic product. The other provision on free establishment is Article 49.[33]

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[27] Garbarino Carlo, *"Taxation of Bilateral Investments: Tax Treaties after BEPS"*, Edward Elgar Publishing Limited, 2019, p.100.; *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.15 (16,1).

[28] Kobetsky Michael, *"International taxation of permanent establishments : principles and policy"*, 2011, p.107.

[29] Article 7, OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.33-34.

[30] Finnerty Chris J., Merks Paulus, Petriccione Mario, Russo Raffaele, *"Fundamentals of International Tax Planning"*, IBFD, 2007, p.14-15.

[31] OECD (2017), Commentary on Model Tax Convention on Income and on Capital: Condensed Version 2017, OECD Publishing, Paris, p. 407-411.

[32] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 411-413, para. 20.

[33] Consolidated Versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, Official Journal of the European Union, (2016/C 202/01).

European Union (EU) Member State (MS) Countries have the sovereignty to decide what to include in their DTTs, as there is no Community legislation as such to determine what should be included. Article 293 of the TFEU serves as the legal basis. The conclusion of DTTs within MS countries is the tool for combating double taxation.[34]

In order for a DTT to find application, the income tax of a resident of one of the contracting states should be in place, as per Article 1 of the OECD MC.[35] This however becomes disputable since in the commentaries of Article 1 of OECD MC 2017, the "citizen" is exchanged by "resident", "irrespective of nationality", which broadens the application of DTTs. That, however does not mean that the benefits of DTTs are granted right away, because they can be denied on the grounds of other provisions for the purpose of prevention against treaty abuse, such as Article 29.[36]

Furthermore, for a DTT to apply, there should be an income received by a resident company (Article 4), and by its "effective place of management", regulated by Article 4(1) of the OECD MC. Article 4(3) contains the tie-breaker rule that helps resolve the problem when the legal entity is resident for tax purposes in both contracting states. [37]

3. Discussion on differences, recent changes, and what constitutes a PE.

3.1 Discussion on differences of PE definitions in UN Model and OECD MC

As mentioned earlier, DTTs follow the definition of PE from the OECD MC in developed countries and the UN Model in developing countries. The definition of PE can be found in Article 5 in both Model Conventions. The UN Model and OECD MC Treaties are generally aligned in their provisions,

[34] Working document, *"EC Law and Tax Treaties"*, Brussels, 2005 Ref.: TAXUD E1/FR DOC (05) 2306, p. 6-7.
[35] Finnerty Chris J., Merks Paulus, Petriccione Mario, Russo Raffaele, *"Fundamentals of International Tax Planning"*, IBFD, 2007, p.15.
[36] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 55. ; Garbarino Carlo, *"Taxation of Bilateral Investments: Tax Treaties after BEPS"*, Edward Elgar Publishing Limited, 2019, p. 52-53.
[37] Finnerty Chris J., Merks Paulus, Petriccione Mario, Russo Raffaele, *"Fundamentals of International Tax Planning"*, IBFD, 2007, p.15 ; Article 4, Article 4(1), Article 4(3) ,OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.30.

since the UN Model follows the OECD MC.[38] The important difference in terms of PE is that the UN Model Treaty does not exercise the same range of tax restriction. The source country has wider taxing rights by lowered threshold categorizing a PE.[39] Generally, the UN Model follows strategy advocating "source country" taxing rights, rather than the "resident country" ones, as opposed to the OECD MC. This position has been met with conflicted opinions from developing countries, some favours it in their DTTs, other regard it as an issue.[40]

There are though, some specific differences that can create differentiated existence of PE and in the interpreting process. The provision regarding construction site (paragraph 3 (a)), will not be discussed as it is not relevant to the research.

Another quite notable difference is the service provision that is included in the UN Model and it is not in the OECD MC. More precisely, the provision concerns services provided by employees and/or personnel related to the enterprise in question. It also bound by a certain time period limit (183 days in any twelve-moth period). [41] The explanation for that could be that some provisions are intentionally more vague in the OECD MC, namely because it is the main source followed by countries. The aim is also circumventing conflicts between OECD member countries.[42]

The difference results that the commentaries of the OECD MC regarding "commercial coherence"[43] might be of a less importance for the UN Model.[44] Furthermore, an Article12 has been introduced to the UN Model 2017, regarding fees for technical services[45], that is not existent in the OECD MC. The new article and its meaning will be discussed later on in the following section 3.2.

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[38] Arnold Brian J., *"International Tax Primer"*, 3rd. Edition, Kluwer International B.V, 2016, p. 142.
[39] Arnold Brian J., *"International Tax Primer"*, 3rd. Edition, Kluwer International B.V, 2016, p. 141.
[40] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 3, p.6.
[41] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 143-144.
[42] Arnold Brian J., *"International Tax Primer"*, 3rd. Edition, Kluwer International B.V, 2016, p. 142.
[43] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 121, para. 24-25.
[44] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 148.
[45] United Nations Model Double Taxation Convention between Developed and Developing Countries, Article 12A, United Nations, New York, 2017, p. 23-24.

Another difference is the removal of the provision regarding "Independent personal services" from the OECD MC, whereas it is kept in the UN Model Convention. The inclusion in DDTs is optional for countries.[46]

The grounds for the removal are, according to OECD, that there are no significant changes in the PE definition in Articles 7 and determining the fixed base, as well as, the already existing time threshold in provisions regarding PE. It is also stated that it created confusion as to which situation fell under which of the provision, therefore, in future independent services and income derived from similar activities will be dealt with under Article 7.[47] In the point of view from countries though, there are differences in the PE and fixed base definition which creates opportunities for loss of taxing rights for the source country. Therefore, the UN Model have provided with guidance on alternatives and possible implication of choosing to delete it. The UN Model has preserved the provision with the presumption that if deleted, it creates more differences rather than simplification, and therefore the definitions of both provisions not being able to be comprised in one.[48]

The next difference to be discussed regards "preparatory and auxiliary activities". In the list of activities that do not constitute a PE; the "delivery" activity is not included in the UN Model, which creates clearly the difference that under the UN Model "delivery" will deem the existence of a PE whereas under OECD MC the might not be the case.[49]Even though the UN Model has followed and included the changes made to the provision in OECD MC 2017, it is still chosen to refrain from the inclusion of the "delivery" activity. The reasoning behind, is the existence of "warehouse" in the list, that should serve the purpose of identifying "delivery".[50] Furthermore, for developing countries, the list appears to be too wide ranged and difficult to comply with due to some countries administrative challenges. Therefore, there is an optional inclusion of the provision or only the activities relevant for the specific country and their capabilities according to the specific considerations. For example, some members have the concerns of improper use of the exceptions.[51]

[46] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 143.
[47] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 304.
[48] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 164.
[49] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 143-144.
[50] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 172.
[51] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 182-183.

The next discussion is related to the provision defining the existence of a PE, when a "dependent agent" is involved. The correlation between "dependent agent", "principle role" and "habitability" is closely related when determining if a PE exists or not. Other factors weighing in are the "routinely conclusion of contracts without material modification by the enterprise"[52] In relation to those characteristics, the UN Model acknowledge the existence of PE by "dependent agent" not necessarily only on the grounds of "habitually exercising the authority to conclude contracts in the name of the enterprise". In the case of the agent habitually maintaining a stock of goods or merchandise and execute regularly delivery of those on behalf of the enterprise, can constitute the existence of a PE.[53] This approach is more comprehensive than in the OECD MC. From the commentary is covered that where a person is soliciting and receiving orders, without formally finalizing them, to a warehouse, from where the goods are delivered, the provision applies.[54] In the view of the UN Member States, the more condensed approach taken by the OECD MC might give the opportunity for dependent agents to claim that they are independent, hence circumventing the requirements that apply to a dependent agent.[55]

Furthermore, regarding the wording of the provision: "that are routinely concluded without material modification by the enterprise", the UN Model has noted that even if there is a modification on contracts, depending on the activities of an agent, it still might be categorized as dependent agent for the purposes of PE. For example, if the activity still falls under being "habitual" and have a "principal role" and lead to concluding other contracts that are not modified by the enterprise.

Some countries have expressed concerns that if formulated that way the provision may raise grounds for enterprises to claim that the conditions have not been met and circumvent it. Thus, some countries preferring more comprehensive formulation and restrain from including it as it stands.[56]

The last, but not least difference that will be presented is the provision regarding insurance business, that is included in the UN Model and does not appear in the OECD MC.[57] The need of that clause is based on the fact that

[52] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p.194.
[53] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p.143 and 13.
[54] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.143, para. 89.
[55] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p.194.
[56] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p.194.
[57] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 195.

in this line of business, insurance agents often have not been delegated the authority to execute contracts. Thus, they do not meet the conditions for dependent agent, creating not taxed income form the conducted business. In result of that, many OECD Member countries do include such a provision into their DDTs.[58]

The reason why the OECD MC restrained from including such a clause, might be due to the specificity of each country's legal conditions, and the facts concerning the issue, which makes it not plausible to be included.[59]

The above discussed factors, make it difficult for countries to tackle distinguishing between dependent and independent agents. Some can be solved by including a more elaborated provisions approach, as some countries take the decision to do as seen from the above.[60]

In the author's opinion, it is essential for businesses involved in conducting cross-border business, to firstly refer to the the specific DTTs concerning the specific countries that are to do business together.

3.2 Recent Changes regarding PE, OECD MC, MLI and UN Model

The implementation of PE definition in DDTs is decisive for both, contracting states and businesses to determine whether the income tax of a non-resident enterprise, should be taxed in the other contacting state. In result of harmful practices adopted through time to circumvent tax and the definition of PE as it stands, OECD Action Report 7 (2015) on Preventing the Artificial Avoidance of Permanent Establishment Status, have been created. In result, a few changes on the OECD MC Article 5 have been introduced, more precisely to Articles 5(4),5(5) and 5(6) concerning the "agent"/"commissionaire" rule and the so-called fragmentation rule respectively.[61]

Those changes are directly influencing DDTs because OECD MC is used extensively in DDTs negotiation process, and the aim of the BEPS package is to be implemented, with the certain changes made, in domestic law, tax treaties, and legal practices. In relation to the implementation of the changes, a Multilateral Instrument (MLI) has been put in place in 2016, for

[58] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 195-196.
[59] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 196.
[60] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 196.
[61] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 116.

tax treaties to follow. The instructions on the changes to be implemented on PE can be found in Article 10 and Part Four Article 12,13,14 and 15 of the MLI.[62] According to the information provided from OECD, 94 countries have already signed the MLI and is in force since 1st of July 2018.[63]

The MLI will not function as amending protocol, but as addition to the existing DTTs, in accordance with BEPS measures. Furthermore, the implementation will be as a minimum standard in relation to the Final BEPS package. Considerations towards different countries and jurisdictions are provided, if a provision is already in line with the minimum standard, there is a possibility to refrain from implementation. There is also, the possibility to opt out of provision partially or entirely under specific circumstances. This is ensured by the method of "reservations" provided for each provision.[64]

Furthermore, as introduced in the previous chapter, a new Article 12A, has been introduced to the UN Model, that is concerning fees for technical services. It has been introduced in the UN Model 2017, published on 18 of May 2018.[65] The article is set out to address the present developments in the technical services area in cross-border situation, as they are prompted to be dealt with in many various ways in DTTs.[66] The fact that a company resident of one State can be grasping a reasonable share of other State economy without necessarily doing so through a PE, fixed place of business or even physical presence in the other State, does not makes it easier for countries and DTTs to cope with that issue.[67] Hopefully, this new approach can shed some clarity onto how to tax business income of technical services more effectively in general and for DTTs.

The new approach taken is contrary of what is usually done when distributing taxing rights between States, as provided from Article 7(1):[68]

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[62] OECD Multilateral Convention (MLI), *"Multilateral Convention to Implement Tax Treaty Released Measures to Prevent Base Erosion and Profit Shifting"*, 2017, IBFD, p. 10-15.

[63] Signatories and Parties to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, Status as of 30 April 2020.

[64] OECD *"Explanatory Statement to The Multilateral Convention to Implement Tax Treaty Realted Measures to Prevent Base Erosion and Profit Shifting"*, OECD publishing, 2016, p. 3-4, para. 13-14.

[65] Malan. T. Monique, Arnold Brian J., IBFD's Tax Treaty Unit, *"New Article 12A of the UN Model Regarding Fees for Technical Services: Ahead of Its Time or a Step Too Far?"*, Bulletin for International Taxation, IBFD, 2019, p. 58.

[66] Malan. T. Monique, Arnold Brian J., IBFD's Tax Treaty Unit, *"New Article 12A of the UN Model Regarding Fees for Technical Services: Ahead of Its Time or a Step Too Far?"*, Bulletin for International Taxation, IBFD, 2019, p. 58.

[67] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 318.

[68] Malan. T. Monique, Arnold Brian J., IBFD's Tax Treaty Unit, *"New Article 12A of the UN Model Regarding Fees for Technical Services: Ahead of Its Time or a Step Too Far?"*, Bulletin for International Taxation, IBFD, 2019, p. 58.

"Profits of an enterprise [of a resident] of one Contracting State shall not be taxed in the other State unless the enterprise carries on business in that other State through a permanent establishment situated therein"[69]

Whereas Article 12A, enables the source State to tax fees for certain technical services paid to a non-resident gross basis, providing the certain services. What is more, a specific threshold to meet has not been included, such as the existence of PE or a time period threshold, for the source State to be able to impose tax on business income.[70] What categorises as certain technical services, as provided in the UN Model, are payments for services within the technical, consultancy or managerial character. The rate of the fee is to be negotiated by Contracting States.[71]

On the grounds of diminishing base erosion, profit shifting due to anti-avoidance rules provided in DTTs and domestic law, low or non-taxation opportunities, the UN Committee of Experts sees the justification of including such provision granting expansion of taxing rights in regards to technical services as categorised above.[72] Even though, form the recommendations of OECD/G20 BEPS Action 1: Final report, the introduction of withholding tax on digital transaction was not expressed, where digital cross-border services fall under, or imposing a significant economic presence test, countries are able to take those factors under consideration and choose if they should include such provisions and other defence instruments countering BEPS in DTTs.[73] There are however some negative factors that can occur and countries should consider. Further discussion on those will be provided in chapter 4.5.

3.3 The PE concept, what constitutes a PE

The concept of PE is used to determine the right to tax of a contacting state income of an "enterprise" "resident" of the other contracting state under cross-border circumstances.[74] Generally, the PE definition is by Article 5 paragraph 1 and 2, the "status" of "fixed place of business" from where an

[69] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 33.
[70] Malan. T. Monique, Arnold Brian J., IBFD's Tax Treaty Unit, "*New Article 12A of the UN Model Regarding Fees for Technical Services: Ahead of Its Time or a Step Too Far?*", Bulletin for International Taxation, IBFD, 2019, p. 58.
[71] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 318.
[72] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 322.
[73] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 119.
[74] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 116.

enterprise is conducting its business, economic activity, "wholly or partly".[75] There are three main requirements to be met in order for a PE to be constituted:

- "place of business" to be in place, where any premises, facility or machinery and equipment.

- a degree of permanence should be constituted via "fixed" place of business at a specific place with specific degree of permanence.

- the business activity should be conducted from that fixed place. "Personnel" dependent in a way to the certain "enterprise" should be conducting the business activity in the State of fixed place of business.[76]

These requirements are used as a line of tests that should be passed in order for a PE to be deemed to exist. Namely, place of business, right to use, location test and duration test and lastly, the business connection test.[77]

Furthermore, the conducted activities through place of business must be of a "productive character" characterised by continuity and regularity. Regarding tangible property, a PE can be deemed to exist if through the fixed place of business those are leased to third parties and maintained by enterprise of a Contracting State in the other State. Examples of tangible property can be: facilities being industrial, commercial or scientific equipment, buildings. Intangible property can be patents, procedures and property of alike.[78] The situation for capital made through a fixed place of business is the same. When the intangible/tangible property or capital with no letting or leasing activity though, a PE will not be constituted.[79]

A Permanent Establishment can exist also in the case of enterprise conducting its business through automatic equipment, where the employees are responsible merely for the maintenance, controlling, operating and setting it up. In this case, what is important is whether there is other activity rather than just setting up, as described above. Therefore, if the certain machines, set up by the enterprise, are leased to another enterprise, PE cannot be deemed to exist.[80]

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[75] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 117.
[76] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 117.
[77] Garbarino Carlo, *"Taxation of Bilateral Investments: Tax Treaties after BEPS"*, Edward Elgar Publishing Limited, 2019, p. 11-12.
[78] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 151.
[79] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 151.
[80] OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 126, para. 41.

In line with the above and the economic developments, the OECD MC and the UN Model have included electronic commerce chapter in their commentaries, discussing if the more often use of computer equipment by electronic commerce operation can constitute a PE.[81]

As discussed above, automated equipment or tangible/intangible property can deem the existence of a PE. The issue with electronic commerce is that a website, that consist of software and electronic data, might not be accounted as a tangible asset on its own, because it cannot constitute a " place of business". What can constitute a "fixed place of business" though is the server where a website is stored, because there is a facility or actual physical location where it is stored and can be characterised as a equipment.[82] Therefore it can only constitute a PE if it passes the test of fixed place-a fixed location, continuity over a period of time in compliance with paragraph 1.[83]In relation to that, intricate Swedish case can be applied in support of the above mentioned factors that may or may not constitute a PE under these conditions.[84] Further on similar Danish case can be applied.[85]

Furthermore, a PE can be found to exist in the situation where there are no employees at the dedicated "fixed place of business", in the case of operating computer equipment. In that particular situation, having personnel is not vital for determining if the business is wholly or partially carried at the specific place, because there is no such a need for that particular type of business activity to be carried. That concerns specifically electronic commerce businesses as well as any other that can be conducted solely by automatic equipment.[86]

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[81] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 204; OECD (2017), Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 151-152.

[82] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.152. Para. 123.

[83] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.152. Para. 125.

[84] Supreme Administrative Court of Sweden, Case no. 4890-13; Kemmeren Eric, Smit Daniel and others, *"Tax Treaty Case Law around the Globe 2014"*, Series on International Tax Law, Michael Lang, Volume 89, IBFD Linde, p.23-27.

[85] *Bundgaard Jakob, Kjærsgaardp F. Louise, "Taxable Presence and Highly Digitalized Business Models", Commentary & Analysis, Tax Notes International, 2020,* p.986.

[86] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.152. Para.127.

4. Digital market, issues and recent amendments, SEP and discussion on PE.

4.1 What does the digital market comprise?

In general, the digital market comprises of all products and services that can be acquired by the customer through website and digitally instead of physically. In other words, any commercial activity conducted by electronic means.[87] In more detail, an example of online store sales products can be: "soft merchandise"-e-books, music, software and documents (direct e-commerce), ordering tangible products (indirect e-commerce). Financial or other services provided online, security transactions etc. Electronic fund transfers, electronic data interchange, subscriptions to internet service providers, as well as credit and debit card activities.[88]

Business models reflecting the digitalization through which companies are conducting their businesses can be: selling physical products through online platform, selling digitalized products and content through online platform, providing online marketplace for the sale of products and services and business providing online services and solutions.[89]

The digital market is mainly characterised by companies relying their businesses to intangible assets, collection of user and participation data and creating scale without mass.[90] Furthermore the digital market can be divided into two main types; single-sided market, where the seller targets one type of customers and sells directly to the customer; and multi-sided market which is characterized by differentiated target group of customers that are buying various products and services.[91] In reflection of the facts, it can be said that, the multi-sided business model is the main one used by companies

[87] Dr. Chetcuti Jean-Philippe, *"The Challenge of E-commerce to the Definition of a Permanent Establishment: The OECD's Response"*, Inter-Lawyer, 2002, p. 1-2.
[88] Singh Manoj Kumar, *"Taxing E-Commerce on the Basis of Permanent Establishment: Critical Evaluation"*, Intertax, Volume 42, Issue 5, Kluwer Law International BV, The Netherlands, 2014, p.326-327.
[89] Spinosa Lisa, Chand Vikram, *"A Long-Term Solution for Taxing Digitalized Business Models: Should the Permanent Establishment Definition Be Modified to Resolve the Issue or Should the Focus Be on a Shared Taxing Rights Mechanism?"*, Intertax, Volume 46, Issue 6 & 7, Kluwer Law International BV, The Netherlands, 2018, p. 477-478.
[90] Bundgaard Jakob, Kjærsgaardp F. Louise, *"Taxable Presence and Highly Digitalized Business Models"*, Commentary & Analysis, Tax Notes International, 2020,p. 979.
[91] Brodd Johan, *"Income taxation at the right place at the right time, An analysis of the need for a virtual permanent establishment"*, Lund University, 2018, p. 11; OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 28.

on the reliance of creating scale without mass. This is achieved by locating in different jurisdictions parts of the business production functions, acquiring potential customers internationally without limitations. The outcome being, that the company is involved in the economy of the country of business activity operations, without substantial or no physical presence.[92]

4. 2 What are the problems with the current definition of PE, and does it reflect the Digital economy?

The development of the concept has not changed as much as some may deem necessary, but the economy has and it is important in this line of thought to discuss in greater detail what are the current problems with the definition of PE.

The main problem is the physical presence requirement, as the PE definition relies on, which cannot be necessarily sufficed by the present way of conducting business in the digital era. Within the present business developments, it is possible for companies to have a significant economic presence without having a fixed place of business. The problem with dependant agent is similar.[93] An example is, a recent French case, where the dispute is with Google Adds, about online advertisement business, regarding dependent agent and the existence of PE. The Administrative Court ruled, that there is no *"independent agent"* nor fixed place of business.[94]

The core values of a business, those that are decisive for locating and constituting a PE have also shifted in the result of the digital market developments. For example, having personnel, creating value, advertising, customer support, and reaching potential customers. All these activities can be conducted from different jurisdictions and mainly online. The spreading throughout jurisdictions of core business activities creates difficulties for locating the place of business qualifying to be the place of business, PE. Furthermore, in the result of advanced software and server functionalities, decision-making processes, customer support, marketing, etc., can be conducted partially or fully without the involvement of personnel. It

[92] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p.24, para.33.
[93] OECD Public Discussion Draft *"BEPS Action 1: Address The Tax Challenges of The Digital Economy"*, 24 March 2014 -14 April 2014, p. 57, para.181.
[94] Administrative Court of Appeal, 25 Apr. 2019, Case No. 17PA03067; Michel Bob,*" The French Crusade to Tax the Online Advertisement Business: Reflections on the French Google Case and the Newly Introduced Digital Services Tax"*, European taxation, IBFD, 2019.

becomes far easier to reach larger customer base. [95] There is no doubt, that these digital advancements nourish the business and start-up sector, as it is easier to start a business, but also more complicated for tax policies to keep up, and countries tax authorities to retain their tax base. Becoming more difficult to locate the business activity and their business income, essentially, the very meaning of PE, granting the taxing rights to a State to tax a non-resident attributed profits to PE, is compromised. This is a vital provision in DTTs, and principal in international tax law.[96]

Another issue in relation to the above, is when a business is conducted in cross-border situation trough e-commerce will constitute a PE in the other countries jurisdictions where the customers are located. If this is the case, the problem of how to attribute the profits of the PE arises. Furthermore, another problem that possibly can occur as a result of spreading business activities through different jurisdictions, their qualification as a taxable PE factors is, how to ensure that the attributed income is taxed only once.[97]

In addition to the above, when a business values are ensured through the means of intangible assets and intellectual property, software and websites, can indicate the jurisdiction with the right to tax, under the condition that they are controlled and managed in that jurisdiction. On the other hand having such assets, enables epicentres to easily move those to different jurisdictions with potentially more favourable tax rates and conditions.[98]

Another of the basic requirements that can constitute the existence of a PE is put on test. The question if a business is carried wholly or partially, becomes difficult to answer since when a business has a server at its disposal it is not straight forward to answer that it can be categorised as a facility and performed business function.[99] Furthermore, the website that the company conduct its business through, can be stored on a server that is not at the company's disposal, but rendered to be stored by a contracting Internet Service Provider (ISP), which essentially does not qualify as place of business.[100] This situation creates opportunity for businesses to avoid

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[95] OECD Public Discussion Draft *"BEPS Action 1: Address The Tax Challenges of The Digital Economy"*, 24 March 2014 -14 April 2014, p. 56-57, para 178-179.
[96] Singh Manoj Kumar, "*Taxing E-Commerce on the Basis of Permanent Establishment: Critical Evaluation"*, Intertax, Volume 42, Issue 5, Kluwer Law International BV, The Netherlands, 2014, p. 327.
[97] Singh Manoj Kumar, *"Taxing E-Commerce on the Basis of Permanent Establishment: Critical Evaluation"*, Intertax, Volume 42, Issue 5, Kluwer Law International BV, The Netherlands, 2014, p. 328.
[98] Bundgaard Jakob, Kjærsgaardp F. Louise, *"Taxable Presence and Highly Digitalized Business Models"*, Commentary & Analysis, Tax Notes International, 2020, p. 979-980.
[99] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.152. Para.126.

to constitute a PE, by contracting the website to a ISP instead.[101] The ISP, will not be eligible to constitute a PE either, as an agent, since they will not cover the requirements of acting on their behalf, concluding contracts and also, the stored website on the server cannot be characterised as a "person" for that purposes.[102]

The specific problems that are addressed in OECD Action 7, are related to circumventing the current rules through commissioners or other similar arrangements (Article 5 (5) and (6)). The twelve-month threshold is being avoided by fragmenting the contacts for executing a certain project (5(3)). Furthermore, the list of preparatory and auxiliary activities (5 (4) and (3)), is also avoided.[103] An extended commentary on the topic will follow in the next chapter, although Article 5(3) will not be discussed as it concern a building site construction and is not of a main relevance for the research further on.

4. 3 Value creation and attribution of profits to PE

Historically, when characterising what PE is, often a "productive character" have been assigned to it. The meaning being, that a "well-run business organisation" each part of the company should contribute to the whole of the enterprise's productivity. With that said, this might not always be the case, it is of essence, that the PE has to have profits that can be attributable to it for the context of being taxed at the particular jurisdiction.[104] That however, becomes essentially difficult to be apprehended with the digital business models at hand. As presented above businesses are increasingly conducting their business through intangible assets and the cross-jurisdictional scale without mass, which are co-related with the value creation process for digital businesses. Other related processes are, data and user participation. There is however, a different point of view for the different countries on the

[100] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.152. Para.124.
[101] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 208.
[102] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.154. Para.131.
[103] *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 31-32; Spinosa Lisa, Chand Vikram, *"A Long-Term Solution for Taxing Digitalized Business Models: Should the Permanent Establishment Definition Be Modified to Resolve the Issue or Should the Focus Be on a Shared Taxing Rights Mechanism?"*, Intertax, Volume 46, Issue 6 & 7, Kluwer Law International BV, The Netherlands, 2018, p. 482.
[104] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 145, para. 3.

extent and contribution to the value creation process though those characteristics of digital businesses. In the centre of the different point of view is to what extent such exchange, between businesses and user interaction, can be monetized. These non-financial transactions, where there is no payment in place, pose difficulty for tax systems to grasp and handle.[105] The result of those differences is that countries cannot find common grounds on to what extent and how the international tax rules should change. Considering, that those characteristics are not present in all digital business models.[106] Some of the concerns expressed by countries are, that will be created a mismatch between, where the value is created, and where the profits are taxed, in result of the inability of tax systems to validate value creation through data and users participation and their profit allocation rules.[107] Other countries share the view, that the above mentioned value creation process does not necessarily qualify as such, especially if occurred in the user's jurisdiction. They should be merely treated as any other independent third party business source in the supply chain.[108]

Another important issue to be discussed is the attribution of profits. In relation to that, as earlier mentioned, OECD Action 7 Report has directed the recent changes and the problems at hand with artificial avoidance of PE through commissionaire arrangements and activity exemptions. Due to the changes in the economy, and the manner that digitalized business conduct their business, some activities that are regarded as *"preparatory or auxiliary"*, may now be considered main activities, and thus not being taxed accordingly.[109] The amendments in Article 5(4) from the OECD MLI 2017, present two options for countries to choose from to implement in their DTT, Article 13 (2) and (3) respectively. The first option is to condition the exception for those activities to their *"preparatory or auxiliary"* character. The second option is to ensure their application irrespectively of them being of *"preparatory or auxiliary"* nature. In both cases, the list provided in Article 5(4) (a)-(d), is to be sustained.[110]

[105] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 25, para. 36-39.
[106] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 171, para. 387.
[107] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 171, para.389.
[108] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 172, para.393.
[109] OECD (2018), *"Additional Guidance on the Attribution of Profits to Permanent Establishments"*, BEPS Action 7, p. 9.
[110] OECD *"Explanatory Statement to The Multilateral Convention to Implement Tax Treaty Realted Measures to Prevent Base Erosion and Profit Shifting"*, OECD publishing, 2016,

Furthermore, the *"fragmentation of activities"* is another way of taking advantage of the exceptions list of *"preparatory or auxiliary"* activities by companies. By actively spreading their core business activities throughout the market jurisdictions with the aim to qualify the activities as *"preparatory or auxiliary"*.[111] To counter that problem, the anti-fragmentation rule by Article 5 paragraph 4 (1) is to ensure to cover for activities performed by one company in several places and extending towards related enterprises spreading their activity in different, as well as, at the same place.[112] The provision applies both to where there is a constituted PE in the source country and when there is no existing one, under the condition that the activities are not considered to be *"preparatory or auxiliary"*. In both cases the company in question should constitute *"complementary functions that are part of a cohesive business operation"*[113] When countries adopt Article 13, the anti-fragmentation rule is automatically included, and may apply even though none of the options are chosen. In addition to this, States have the possibility, to take advantage of their reservations right, and some countries that have selected the second option, have refrained of applying the rule.[114] On that note, the author would like to observe, that such a trend might lead to fragmented and disharmonized application of rules, creating unclear areas of law. Even more so, when the anti-fragmentation rule has been created in addition to paragraph (4), preventing from wrongfully exempting a PE solely on *"preparatory or auxiliary"* activities. [115]

The other avoidance of PE, though commissionaire arrangements have been addressed, through amendments to Article 5(5) and (6). There are quite a few examples of that in case law, the *Zimmer* case being one[116],where

p.42-43, para. 171-173.

[111] OECD (2018), *"Additional Guidance on the Attribution of Profits to Permanent Establishments"*, BEPS Action 7, p. 9; Spinosa Lisa, Chand Vikram, *"A Long-Term Solution for Taxing Digitalized Business Models: Should the Permanent Establishment Definition Be Modified to Resolve the Issue or Should the Focus Be on a Shared Taxing Rights Mechanism?"*, Intertax, Volume 46, Issue 6 & 7, Kluwer Law International BV, The Netherlands, 2018, p. 482.

[112] OECD (2015), *"Preventing the Artificial Avoidance of Permanent Establishment Status"*, Action 7 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, p.39, para. 15.

[113] OECD (2018), *"Additional Guidance on the Attribution of Profits to Permanent Establishments"*, BEPS Action 7, p. 10, para. 8-9.

[114] Spinosa Lisa, Chand Vikram, *"A Long-Term Solution for Taxing Digitalized Business Models: Should the Permanent Establishment Definition Be Modified to Resolve the Issue or Should the Focus Be on a Shared Taxing Rights Mechanism?"*, Intertax, Volume 46, Issue 6 & 7, Kluwer Law International BV, The Netherlands, 2018, p. 483.

[115] OECD (2018), *"Additional Guidance on the Attribution of Profits to Permanent Establishments"*, BEPS Action 7, p. 10, para 7.

[116] Supreme Administrative Court, Société Zimmer Limited, 304715 and 308525 (31 March 2010); see Wittendorff Jens, *"Agency Permanent Establishments and the Zimmer Case"*, International Transfer Pricing Journal, IBFD, 2010.

commissionaire does not constitute a PE. The reason is that a commissionaire is characterized by person selling products in its own name in a State, on behalf of an enterprise in another State that owns the products. Thus, this type of arrangement does not qualify to constitute a PE. In practice, there are attributable earnings for tax purposes, but since the commissionaire is not the owner, he can be only taxed on his received commission.[117] Other circumventing practices include the conclusion of contracts, where their negotiating process is in one State, but it is finalized in another State, or when the person with authority to sign the contracts qualifies as *"dependent agent"*, thus falling under the exception provided by Article 5(6).[118] Therefore, the amendments focus on, not granting the exception to a person that acts *"exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related"*[119] In conclusion, the changes have sharpened the threshold to the existence of PE, but have not changed the characteristics of PE in regards to what usually is considered for a dependent agent. In regards to the attribution of profits, when a PE is found to exist, the same approach remains, as before the changes.[120]

In relation to the methods of attribution of profits, there are two, that are mostly used by DTTs. The Authorised OECD Approach (AOA), based on Article 7 of the OECD MC, and the Arm's Length Principle (ALP). Article 7(2) expresses the separate entity principal of a PE, that is most used by bilateral tax treaties and most efficient regarding to administration and compliance.[121] That principle is characterised by earnings attributable to PE on the basis of the arm's length principle. The Authorised approach contributes profits according to activities conducted by the PE, and their attributable assets, risks, as well as, the PE interaction with other divisions of the enterprise.[122] Furthermore, in order to determine those, functional and factual analysis is necessary. The transactions made with other divisions of the enterprise, head office, have to be done in compliance with the arm's

[117] ECD (2015), *"Preventing the Artificial Avoidance of Permanent Establishment Status"*, Action 7 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, p. 15, para.5.
[118] OECD (2015), *"Preventing the Artificial Avoidance of Permanent Establishment Status"*, Action 7 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, p. 15, para. 7.
[119] OECD (2018), *"Additional Guidance on the Attribution of Profits to Permanent Establishments"*, BEPS Action 7, p. 13, para. 29.
[120] OECD (2018), *"Additional Guidance on the Attribution of Profits to Permanent Establishments"*, BEPS Action 7, p. 13, para. 30.
[121] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 176, para. 12.
[122] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 177, para. 15.

length principle.[123] The committee of experts of the UN Model convention, however have decided not to follow that approach as it is in contradiction with their Article 7(3), that does not allow deduction for payments made from the PE to the head office of the enterprise.[124] Therefore, in the author's opinion, DTTs are faced with the choice of which approach to follow. As a result, this allows countries to adjust their choice according to the domestic law, allowing them to exercise their sovereignty rights. On the other hand this contributes to difficulties in respect of businesses that aim for cross-border trade, which can be argued is one of the main purposes of DTTs, to foster international trade (see 2.3.2). In the UN Model, at the end of Article 7, it is noted that the issue regarding attributable profits to PE for goods and merchandise bought by the PE for the enterprise, *"was not solved"*. This seems, in the author's opinion, to open up for even more differences, and it is left for the contracting states to be dealt with in their DTTs.

4. 4 Proposal for a new definition, a Virtual PE, SEP test

After the work presented by "BEPS Action 1 report (2015)", there were identified several international tax issues related to digitalisation, that were beyond the scope of BEPS works. Those issues relate to nexus, data, characterisations and allocation of taxing rights between countries of income generated form digitalized international business context.[125] In response, three possible solutions have been presented by the "OECD Interim Report (2018)";- the Significant Economic Presence test (SEP), withholding tax to be applied to only certain types of digitally conducted transactions, and equalization levy of tax countering unequal tax treatment between foreign and domestic businesses, after passing the SEP test. The solutions proposed by the "Action 1 report" were merely optional for countries to eventually introduce as complementary to their domestic laws, to counter BEPS, if they are in line with their existing DTT obligations.[126] The extended efforts, to come to a proposition for the solution of the above, resulted in releasing the "OECD Public Consultation Document, Addressing the Tax Challenges of the Digitalisation of the Economy"(2019), noting that

[123] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 178-179, para. 21-22.
[124] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 212.
[125] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 18-19, para. 18.
[126] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 18-19, para. 19-21.

in order to cope in a more efficient manner, the nexus and profit allocation should be dealt with together as they intrinsically related.[127] In relation to that, three options have been presented: *The "user participation" proposal, The " marketing intangibles" proposal, The "significant economic presence" proposal.*[128] *The "user participation"* approach is aimed to counter the value creation by digitalized businesses through users, collecting data and content, creating value generating profits for them, but not being taxed. By change in the profit allocation rules for digital purposes, jurisdictions will be able to capture the profits generated from users in that jurisdiction with no need of physical presence.[129] The allocation of taxing rights process is suggested to be based on non-routine profits (residual profit split method, earning after profits attributed by arm's length principle) attributed to the certain activities performed.[130]

The "*marketing intangibles"* proposal aims to a wider scope than restrictively towards digital businesses. In respect of digital businesses, it will be applicable towards sales and marketing activities in a certain jurisdiction, where the revenue is acquired and there is no feasible physical presence for tax purposes.[131] The approach will be applicable, also in situations where the digital business have some presence in the jurisdiction, where there are generated some profits, but they are deemed too little. The aim is to capture the tax nexus that it is not possible under the current rules. The proposal would also cover for consumer product businesses with similar activities, performed remotely or through "*limited risk distribution"*.[132] There are considered a few different approaches to the income allocation.[133]

The third approach presented is *"significant economic presence"*. The aim is to provide a solution to one of the central problems arising from the digital economy. The possibility for businesses to be considerably involved

[127] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 8, para 13.
[128] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019.
[129] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 9-10.
[130] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 10, para. 24.
[131] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 13-14, para. 40.
[132] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 14.
[133] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 15.

and present in the economy of a country where they do not represent having a physical presence. Furthermore, according to OECD, this makes the current rules obsolete for countering the issue at stake.[134] For a presence subject to tax to be in place, a non-resident enterprise must have economic presence based on certain criteria. The criteria, taken into considerations are, profits on a regular basis, interactions with purpose with the certain jurisdiction provided via digital technology and alike. More precisely, there are six outlined criteria that are to found a significant economic presence. It is important to mention, that the factors establishing the economic presence should be related to the profit generated through the activities. The measures are as follows; user base and related data input, volume of the gained digital content from the jurisdiction, locality in form of invoices and payments made in currency the local currency, website in the country's language, providing for additional support services(repair and maintenance) and basic ones (delivery of goods), and consistent sales and marketing conducted online or differently.[135]

Other theoretical suggestion based on the economical presence and in line with OECD Action 1 by Hongler and Pistone, which propose a four requirement approach to the existence of PE. The proposed thresholds are: - a time threshold, minimum revenue, digital services and user threshold. In addition to that, a suggestion to OECD Article 5(8) has been made. The existence of a PE should be constituted by an enterprise of one State, offers digital service, such as application, database, online marketplace, online storage or online advertising in another State. Those are further conditioned by a 1,000 users per month from the other State and a certain amount of revenue per year.[136]

4. 5 Will the recent changes and new definition of PE solve the problems

The recently added Article 12A of the UN Model has taken a forward approach in trying to cope with, very recently discussed problem, the implications of the digitally conducted businesses. Expanding the taxing rights of Contracting States towards being able to tax non-resident can

[134] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 16, para. 50.
[135] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 16, para. 51.
[136] Honlger Peter, Pistone Pasquale, *"Blueprints for a New PE Nexus to Tax Business Income in the Era of the Digital Economy"*, IBFD, 2015, p. 2-3.

eliminate improper tax advantage over the resident service provider, low or non-taxation.[137] Furthermore, it can be a solution to base erosion, as illustrated from the example bellow:

Company A fee paid → Company B, Company A deduct fee from Country A = reduced tax base for Country A

Company A fee paid → Company B, Country A impose tax on the payment made by Company A to Company B = preserving Country A tax base.

If the fees paid by a resident company of Country A, or non-resident having conducted its business/services through PE or fixed base in that state, country A will be able to tax them.[138]

It is noted in the UN Model, that there might be some negative impacts in the result of the fees paid on a gross basis, namely excessive or double taxation. There are some suggestions in relation to how to avoid those negative impacts. One way is through credit or exemption method, and the other is trough setting a maximum tax rate for the fee and through the negotiated gross amount of the fee.[139] Some members of the Committee have expressed disagreement with the taxing method on gross basis, as the double taxation relief methods might not be sufficient in that particular situation. The problem that they are referring to is the inability for the service provider to include expenses related to providing the service, which if it was to levy tax on a net basis, it would have been deductible.[140] It seems that, that there is no perfect solution and in some cases it becomes somewhat of a vicious circle, but in the author's opinion, it is one step ahead towards possibly a more efficient approach, for taxing digital services. One thing is clear, it will be necessary to pass time and to observe how it will function in practice, in order to come to a conclusion if it will solve the problems or it will solve ones and create others.

Regarding attribution of profits, as a general rule, as stated in the OECD Commentaries of Article 7, an enterprises profits should not be taxed until, the latter has established a PE and participating in the other States economic life.[141] As discussed previously, this can become problematic in terms of digital businesses, resulting from the phenomenon of cross-jurisdictional

[137] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 322.
[138] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 321-322.
[139] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 323, para. 15.
[140] United Nations Model Double Taxation Convention between Developed and Developing Countries, Commentary, United Nations, New York, 2017, p. 324-325, para. 20.
[141] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p.175, para.11.

scale without mass.[142] This issue has not been fully tackled until this moment, in author's opinion, because the Commentaries are the first source of interpreting law, when an issue arises, and not the eventually proposed solutions. Furthermore, in relation to the amendments made to Articles 5, it is stated that the changes made are not significant to attribution of profits rules, but there are additional guidance regarding the application of the rules as they are to the changes made.[143] It seems in the author's opinion that the aim is to adapt the present concept with a few additions, which might not necessarily lead to clarity of the provision and solution of the issues.

There is, however, a change to Article 5(4)(a), that usually a warehouse from where products are stored would not constitute a PE. From the commentaries of OECD MC, it is worthy to note that, in regards of a warehouse where the enterprise maintains it and sells the goods in that other state, PE can be constituted under certain conditions. The conditions being, that there are workers with their main tasks to store and deliver, the goods owned by the enterprise, and are sold online to that other state. These conditions, witness for the essentiality of the activities for the business, have involved employees actively working for those purposes, and therefore does not qualify for the exception.[144]

In regards to the approaches proposed by the "OECD Public Consultation Document, Addressing the Tax Challenges of the Digitalisation of the Economy"(2019). There are involved, changes to the profit allocation and nexus rules for the purpose of taxing digitalized business. In order to sustain fairness and equality in taxation towards businesses, the rules should apply to both digital and consumer businesses. With that said, there is a potential risk related to the end results of the application of both the "user participation" and "marketing intangibles" options. The latter rises concerns, of the potentially creation of double taxation and disputes.[145] For preventing these, there is a suggestion to impose changes to the provisions for eliminating double taxation in DTTs.[146] Furthermore, in order for countries to benefit from the proposals, it will be necessary to implement them in addition or by amending the PE definition and the correlated Articles (7 and

[142] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p.24, para.33.
[143] OECD (2018), Additional Guidance on the Attribution of Profits to Permanent Establishments, BEPS Action 7, p.7.
[144] Commentary on *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, p. 133, para. 62.
[145] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 14, para. 42 and p. 16, para.49.
[146] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 21, para. 80.

9) in their DTTs, as well as changes in their domestic law.[147] This presents some administrative burden ahead for countries and policymaking in the author's opinion.

Further on, in comparison with the suggested theoretical PE concept, it is argued that when creating a new nexus, providing minimum threshold is necessary in order to ensure fair taxation and avoid fragmentation of the taxable income.[148]

According to comments received by OECD on Action 1, on the SEP test, there were expressed concerns with the data use. It is argued that raw data has no value and the processing and analyzing it is what brings value. It is further stated that data collection is not new to the business model conducted beforehand. As mentioned above, it imposes difficulty in incorporating the profit allocation rules into new or extended version of PE. Furthermore, the constant changes might create uncertainty.[149] There is also the consideration to be taken into account, that, user value creation, is an activity not conducted by the taxpayer, as they are an external compound for value creation.[150] Furthermore, the withholding tax solution, have not been met with much enthusiasm. The reservations are related to difficulties for applying it in regards to compliance, potential negative results of gross taxation, and conflicts with EU trade. Similar problems are to arise with the equalization levy tax since it is also based on gross taxation. Another concern is that it might be out of scope for DTT, thus creating double taxation. It is suggested to be solved by only applying to non-taxable income or subject to low taxation. It is further noted that this could also be a solution to the digital withholding taxes, as otherwise, it could be an incentive for businesses to circumvent it by doing their business otherwise.[151]

The Multilateral Convention (2017) is set out to incorporate the measures from OECD BEPS Action 7, into existing DTTs. It also serves a purpose in the negotiation process of conducting bilateral tax treaty agreements. According to early projections from the OECD Interim Report 2018, the

[147] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019, p. 22, para. 82.
[148] Honlger Peter, Pistone Pasquale, *"Blueprints for a New PE Nexus to Tax Business Income in the Era of the Digital Economy"*, IBFD, 2015, p. 26.
[149] Larking Barry, *"A Review of Comments on the Tax Challenges of the Digital Economy"*, Bulletin for International Taxation, 2018 (Volume 72), 26 March 2018, p. 4.
[150] Schön Wolfgang, *"One Answer to Why and How to Tax the Digitalized Economy"*, Intertax, Volume 47, Issue 12, Kluwer Law International BV, 2019, p. 1013.
[151] Larking Barry, *"A Review of Comments on the Tax Challenges of the Digital Economy"*, Bulletin for International Taxation, 2018 (Volume 72), 26 March 2018, p. 4-5.

implementation rate of the recent changes is not very promising. For the PE dependent agent rule amendments, about 17% of the 1246 tax agreements that are under MLI, meaning about 206 bilateral tax agreements only have adopted the rule. For the activity exemption Article 5(4), there is slightly higher number of 22%, in total 277 tax agreements have adopted those. [152] Even though in comparison to the total of signatures of, as earlier estimated until this moment of 94 jurisdictions, over 1680 treaties to be modified, from all countries, no matter their development levels. After it came into force since 1st of July 2018[153], it can be noted that the changes were well received, with a moderate implementation rate. This however, cannot be of e decisive matter, because with time countries might lower their reservations towards the PE provision changes. A positive development in the economic, private sector should be noted, that several digital conglomerate MNEs, such as Facebook, Google, Amazon and E-bay, have begun restructuring their remote sales structures. In the author's opinion, the environment was created for changes to be made at least,.[154] Furthermore, for the implementation of the new PE definition the situation is promising in long term, since the OECD MC has always been in the centre of the negotiation process for DTTs.[155]

[152] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 94-95, para. 271-174.
[153] *"Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting"*, Multilateral Instrument - Information Brochure, OECD publishing, May2020, p.2.
[154] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 95, para. 273.
[155] OECD (2018), *"Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project"*, OECD Publishing, Paris, p. 95, para. 274.

5. Conclusion

Based on the conducted analysis and observations throughout the presented master thesis, the concept of the permanent establishment has been both subject of many discussions and a pivotal point for jurisdictions for the allocation of their taxing rights in coherence with digitalized businesses and how they interact together.

The concept still remains to rely on the physical presence in its definition of both the OECD MC and UN Model Article 5. In the author's opinion which is also confirmed by scholars, the fixed place requirement for constituting a PE cannot suffice with the developing digital economy. The amendments made, therefore, present more of a short term solution to the current problems faced currently by the international tax law.[156]

It is expected that the PE concept will evolve, a finding also based on the examined historical developments. It is important that the economic developments are reflected and the countries can rely on, in order to retain their tax base and taxing rights.

Countries can exercise their sovereignty right to decide what to include in their domestic law, but that has intrinsic connection with what will be in DTTs, and, thus, how these will be interpreted and applied. That can create disparities in the international cross-border business taxation. In relation to that as performed in this thesis analysis, there are apparent differences between the OECD MC and UN Model for DTTs to consider when drafting their provisions. Furthermore, the complications with the developments in the digital business have pushed the long awaited changes.

It is also evident, that the changes and proposals made still arise problems such as possible double taxation, fragmentation of taxable income, disputes and administrative burden, for countries that are to implement those. These are the very issues that international taxation law suffers most from, in general, and obviously when changes are to be made, it is no exception. As it is noted, from the analysis, countries have some level of reservations

[156] Honlger Peter, Pistone Pasquale,*"Blueprints for a New PE Nexus to Tax Business Income in the Era of the Digital Economy"*, IBFD, 2015, p. 14.

towards both implementing the MLI and the proposed approaches to counteract the digital economy issues.

In order to apply the new nexus requirement ensuring jurisdictions taxing rights related to the "user participation", "marketing intangibles" and SEP test, countries are presented with the option to amend the current provision or add to it. Because of the different approach on which the existing provision is built upon, the transaction between enterprises and their co-related entities and the new approach focusing on the total profit of numerous entities, a "stand alone" approach is available. In relation to that outcome, the author agrees with the OECD's view, that a new nexus with a specific threshold is necessary regarding the SEP test.[157]

It might be concluded, that the present amendments and proposals are on the right path to address the digital economy challenges, but as discovered in the analyses, it is too early to be able to assess the full impact and the implications it may bring. The current situation is that there are some solutions, even though not flawless for countries to implement in their domestic law and DTTs regarding the new Virtual PE definition.

It seems that a tendency is observed towards shift in taxing rights, where now after Article 12A of UN Model a Source State can tax in a form of a fee for technical services paid to a non-resident. An argument can be made, that it is a shift towards taxing rights where the value is created.

It is therefore interesting to extend the research towards what is the future of extended taxing rights under digitalized businesses and jurisdictions and the implications thereof.

[157] OECD/G20 Base Erosion and Profit Shifting Project, *"Addressing the Tax Challenges of the Digitalisation of the Economy"*, Public Consultation Document, OECD 2019,p. 22, para. 82.

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