

ELECTRONIC COMMERCE AND INTERNATIONAL TAXATION

Questions about applying tax law in cyberspace.

by

Edwin van der Bruggen¹

1. Introduction.

It is by now definitely cliché to say that our world has passed into the technology and information age. The so-called global information society poses, as we are often reminded by those trying to make a living from being a part of the process, a field of new opportunities and changes for everyone from the household to the multinational

enterprise. Internet and other information superhighways radically introduce new ways of communication, business, teaching and living, ranging from the way international currency transactions are cleared between financial institutions to the way you buy a book.

It is also changing the way we think about taxation.

¹ The author is a Bachelor of Laws (Antwerp, Belgium) and a Master in Tax Law (Brussels, Belgium). Previously a professor of "International Tax Law" at the IPO/Ufsia University and the Handelshogeschool University, Belgium, he is currently lecturing at the Faculty of Law of Assumption ABAC University.

Tax laws traditionally concentrate on concepts of physical business location, effective management and residence to decide which country should tax income arising from international business transactions, and which country may not. These concepts seem difficult to apply in the case of electronic commerce, where there are no offices required, nor a shop or even a warehouse in many cases. There is no way to determine where, if any, management is located nor does the user know what is the place of residence of his correspondent.

Does this mean that, because of the incompatibility of international tax law concepts, those engaged in electronic commerce can choose where and how much tax they are willing to contribute?

What will the economic effect be if companies selling products over the Internet can do so without taxation, while their traditionally organized competitor can not²?

Or does this mean that tax liability will usually only arise in the country of residence of the company exploiting the

electronic commerce, without a fair share for the country where the transaction has taken place? Given the fact that those companies are mainly situated in developed nations, would this not constitute yet another disadvantage for developing nations?

To put it in the words of Prof. Luc Hinnekens; "Is the technological revolution still a success if it would turn cyberspace into a virtual tax haven sheltering the dis-intermediated and portable profit margins of the world's virtual companies engaged in the sale of electronic products and services?"³

That the question is not an easy one to answer, let alone to implement in existing international tax rules, is illustrated by the "Internet Tax Freedom Act"⁴ which introduces a three-year moratorium on (among others) multiple taxes on electronic commerce.

This period, ending October 21, 2001, is deemed necessary to figure out how and where taxation of electronic transactions should be taxed.

In the following article the different questions will be introduced

² The objective of neutrality (defined as... "that the tax system treat economically similar income equally, regardless of whether earned through electronic means or through more conventional channels of commerce.") is the main consideration of the United States Department of the Treasury; "Selected tax policy implications of global electronic commerce", US Treasury, Office of Tax Policy, 1996.

³ Hinnekens, L., "Looking for an appropriate jurisdictional framework for source-state taxation of international electronic commerce in the twenty-first century", *Intertax*, 1998, 194.

⁴ Internet Tax Freedom Act (P.L. 105-277), included as titles XI and XII of the Omnibus Appropriations Act of 1998; Approved as H.R. 4328 by Congress on October 20, 1998. Signed as Public Law 105-277 on October 21, 1998.

that are relevant in the discussion on the relationship between international tax law and electronic commerce, by first describing the classic concepts of international tax and comparing them to the new possibilities after the communication revolution.

Then the possible need for a new framework is discussed as opposed to merely adapting current legislation. Though many tax-topics concerning e-commerce⁵ are merit of study, I will focus in this text on the crucial question of tax jurisdiction; which country will be entitled to levy taxes on the revenue generated by the e-businessman...

2. Classic concepts of international taxation.

Before examining how the international digital enterprise is affected by international taxation, it is useful to briefly note the concepts of residence, source and permanent establishment all though they are off course already very familiar for the tax-practitioner.

Countries can use two main attachment criteria in their tax legislation to submit income to taxation in their country;

⁵ For instance indirect taxation as value added tax and custom duties, determination of deductible expenses, determination of taxable moment.

-the subjective factor of residence: the income is taxable in the country if the beneficiary of the income is a resident of that country, regardless of from where the income was derived;

-the objective factor of source: the income is taxable in the country it was derived from that country, regardless of the place of residence of the beneficiary of the income.

It is obvious to the reader that almost every country⁶ applies both criteria at the same time. Residents are taxable in their country of residence on their worldwide income, while income derived from that country is taxable in that country as well, even if earned by a non-resident⁷.

⁶ A well known exception being the Hong Kong SAR that only taxes profits that arise or is derived from Hong Kong and certain other sources that are deemed by the Inland Revenue Ordinance ("IRO") to arise in Hong Kong (Section 14 IRO). Such income is taxable for residents and non-residents alike. The concept of residence is thus not used as a criterion to establish tax liability (FLUX, D., and SMITH, D., "Hong Kong Taxation. Law & Practice", Chinese University Press, 1998-99, Hong Kong, 10.) all though the IRO does use the term without defining it in provisions regarding assessment and transfer pricing (sections 15.1 and 20 of the IRO)

⁷ In the Kingdom of Thailand this fundamental rule is found in Sec. 66 of the Revenue Code: "All juristic companies or partnerships which are organized under the Thai law or which are organized under foreign law but carry on business in Thailand shall pay tax under the provisions of this division. The juristic companies or partnerships which are organized under foreign laws and carrying on business in

In international transactions a consequence from the combined application of the two criteria is that everybody will be subject to double taxation; one time in the country where the income was derived and one more time in the residence country of the beneficiary.

In order to curtail the negative consequences of that double taxation, countries have adopted measures in their domestic tax legislation to reduce or eliminate double taxation⁸. Also, more importantly, most countries have concluded international treaties for the prevention of double taxation.

These double taxation conventions (DTC) provide for a sharing of the tax-jurisdiction between the residence-country and the source-country. Business profits are only taxable in the country of residence of the enterprise and not in the source-country, unless the profit is attributed to a permanent establishment in the source-country⁹. In the latter case, the profit is taxable in the source-country where the permanent establishment is situated.

... Thailand shall pay tax on the net profits arising from or in consequence of the business carried on in Thailand..."

⁸ In the tax law of the Kingdom of Thailand an example can be found in Royal Decree No. 300, (Government Gazette Vol. 113, part 40a, 24 September, 1996) allowing a credit for corporate income tax in Thailand for taxes paid abroad by resident companies.

⁹ Article 7 OECD Model Convention on income and capital.

A "permanent establishment" is thus crucial to verifying the existence of a tax liability.

If there is no such thing, profit is only taxable there where the enterprise is resident. For companies that means where the effective management is situated¹⁰. It has been defined¹¹ as a fixed place of business through which the business of an enterprise is wholly or partly carried on. It includes specifically:

- A place of management
- A branch
- An office
- A factory
- A workshop and a mine, gas well etc.
- A building or construction site that lasts more than 12 months;

Certain cases are deemed not to be a permanent establishment such as a storage, a purchasing office, an office for collecting information or preparatory or auxiliary activities¹².

3. The communications revolution.

Electronic commerce is a feature of a much broader communications

¹⁰ Article 4 par. 3 OECD Model Convention on income and capital.

¹¹ Article 5 OECD Model Convention on income and capital.

¹² Article 5 par. 4 OECD Model Convention on income and capital

revolution that includes the convergence of previously separated communications and computation systems into an interoperable global network of networks¹³. It refers to telephone systems, cable and satellite communications and computer networks. The Internet is simply the most publicized part of the information superhighway with the "World Wide Web" as one of its fastest growing applications¹⁴

The Web documents from one company or individual ("Web-site") are accessible around the world. The information stored on these sites is stored on central computers ("Server").

Electronic commerce has been defined as "the ability to perform transactions involving the exchange of goods or services between two or more parties using electronic tools and techniques"¹⁵

A brief look into the goods and services offered illustrate the great variety of electronic commerce. Services include consulting, accountancy services, legal aid, health care automatisations, travel-agents, ... Computer software is acquired through the Internet, downloading it from the supplier's website. Books, CD's, pictures, movies, television, etc are

available both retail and wholesale. On-line research is quicker and more cost effective than publishing printed material or sending CD-Rom's to paying customers. In the business to business e-commerce examples are video-conferencing, clearing of financial transactions, virtual direct-mail, advertising, etc... Entertainment is provided with gambling and adult websites. Financial services such as stockbrokers and offshore banking are offered worldwide.

This list is by no means limitative. Every day an enterprise comes up with "the next big thing", expanding the products and services range of electronic commerce.

Technically, the products or services offered feature on a website of the supplying company. This website is located on a server that can be any computer wherever in the world. Payment is carried out through different possible ways. A third party can be involved, situated in whatever country.

4. Possible new frameworks for taxing electronic commerce?

Given the technical characteristics mentioned above, it should not come as a surprise that some doubts have risen around the application of the established concepts used in international tax law to appoint the taxing jurisdiction. Are new attachment

¹³ Department of Treasury, *ibid*.

¹⁴ Kessler, G., "Serving the Internet", LAN Magazine, Sept 1996, 43.

¹⁵ XIWT Cross Industry working team, Electronic commerce in the NII, 1995.

points needed to create an internationally just sharing of the taxation of income derived from electronic commerce?

A proposal for a completely new way of taxing electronic commerce is the so-called bit-tax, which is levied on the amount of bits transmitted over the Internet and received by its user. It received widespread attention recently when the United Nations Development Report called for the introduction of a one US dollar cent taxation on every 100 lengthy e-mails¹⁶.

The radical proposal has been criticized for burdening the new medium and discriminating Internet users compared to conventional traders. The effectiveness of a taxation connected to Internet Service Providers is debatable since the Providers can easily be moved across the world¹⁷.

More practical at face value is a taxation on payments for electronic purchase of goods and services. It takes the shape of a withholding tax on gross payments, so it is essentially a turnover tax. Since however nor Internet users, nor access providers can be identified with certainty, the burden of the turnover tax is geared to the banks involved in the payment. This approach

seems to enjoy the preference of the German Federal Ministry of Finance¹⁸.

There is a lot to say against such an approach. First and foremost, it introduces an intolerable discrimination between users who have the means to organize payments outside of the jurisdiction of the country levying the turnover tax on payments, and those who do not. Take the example of a German household buying a computer by e-commerce. If the family is sufficiently organized and, probably, wealthy, to pay through credit cards issued by a non-German bank, no taxation is due. The family next door without offshore accounts however, is subject to the taxation.

Also, the system has been described of leading to arbitrary taxation since the mere money transfer accommodated by the financial institution does not shed any light on the underlying transaction. Is there a sale, a service or any performance at all¹⁹? Perhaps it is a donation or a mere transfer between related parties.

The preference demonstrated for the turnover tax is furthermore less understandable given the wide

¹⁶ The Human Development Report, Oxford University Press, London, 1999.

¹⁷ Hinnekens, L., l.c., 193.

¹⁸ Dittmar, F., and Selling, H.J., "How to control internet transactions. A contribution from the point of view of German tax inspectors.", *Intertax*, Volume 26, Issue 3, 1998, 88.

¹⁹ Geurts, M., "How to tax electronic commerce transactions?", *Intertax*, Volume 26, Issue 10, 301.

interpretation the German authorities seem to attach to their permanent establishment principle²⁰

5. Adapting the existing tax law concepts to cyberspace.

Reviewing the published legal doctrine on the matter²¹, a slight preference is detected to hang on to the well-established concepts of international taxation that are already incorporated in most countries domestic and international legislation, although every body seems to agree that some extent of different interpretation or adaptation is necessary.

The OECD, a prominent player in the development of new international tax rules, is equally reluctant to jettison principles as residence and permanent establishment²²

The best indicator of things to come is however the first considerations by (tax-) legislators and authorities. There seems to be a consensus there that the principles that have governed international taxation since the invention of the steam-train, will not be overthrown by this latest technological development²³

But from accepting this as a principle to applying it in a business situation is quite a leap.

6. Applying international tax rules to electronic commerce.

In discussing the application of existing tax concepts to electronic commerce, let us use following examples.

6.1. First example: Internet based seller of books.

A company in country A maintains a website where it displays books for sale. Customers around the world can order on-line, submit their credit card

²⁰ See below.

²¹ Hinnekens, L., "Looking for an appropriate...", l.c., 193; Becker, H., "Taxation of electronic business in a globalizing world.", Intertax, 1998, 411.; Nutter, J.J., "State tax implications of providing internet services.", Journal of State Taxation, 1995, 68-75.; Morihiro, M., "Japanese taxation of electronic commerce.", Intertax, 1997, 127.; Vink, M., "Tax and legal complications of electronic commerce", Fiscale Actualiteiten, fed, Deventer, 60.; Harris, M.A., "Advising the cyberbusiness: Applying fundamental tax concepts to internet sales.", Taxes., 1996, 713.

²² "Dismantling the barriers to global electronic commerce", OECD, 18 November 1997; "Electronic commerce; Challenges to tax

authorities and taxpayers", OECD Committee on Fiscal Affairs, 1997.

²³ Department of the Treasury, l.c.,(US) ; "Taxation in a world without distance", Secretary of State of Finance, May 4th, 1998, (The Netherlands); "Globalization of Transnational Business", Inland Revenue, November 13th, 1996, (UK); "Tax and the Internet", Australian Tax Office, 1997 (Australia); Contra; Dittmar, F. and Selling, H.J., l.c., 88 (Germany).

details and get the purchased books delivered at home.

Where should tax be levied; at the country of the customer (A), there were the server or the Internet provider is situated (B) or at the residence of the company (C)?

Taxation in country A (where the buyer of the books is situated).

For country A to be entitled to tax the transaction, the website of the company displayed on the customer's monitor has to be regarded as a sufficient "attachment" to country A by that country's tax law. It seems that many countries would not explain their source rules in such a way.

It is indeed, as Powers²⁴ puts it "not different from a foreign seller offering products in the US by advertising in magazines, without having any office in the US". In Japan, the website "unlikely" constitutes a fixed place of business as required by Japanese tax law²⁵

Belgian tax law, though applying a slightly broader concept of (permanent) Belgian establishment would probably not regard this website as such²⁶. In The Netherlands, a government report

recommended that current source rules should be upheld²⁷. Also Hong Kong tax law would probably not qualify the electronic merchant to be carrying on business in Hong Kong, based on the fact that the mere import of goods is usually doing business *with* Hong Kong and not *in* Hong Kong²⁸.

In the case where a DTC should exist between the country of the company and the country of the customer, the provisions of that DTC will govern which country can subject the transaction to taxation. Article 7 of the Model Convention, regarding business profit allows only the country to tax where the company has its place of effective management unless the profit is realized through the intermediary of a permanent establishment in the other country. So, is the website in this case a permanent establishment? That is very uncertain, according to the OECD discussion paper²⁹. Indeed, a permanent establishment has to have a "fixed" character. "Thus in the normal way there has to be a link between the place of business and a specific geographical point³⁰." Even if the website should be deemed to be a "fixed place of

²⁴ Powers, J.P.P., l.c., 120.

²⁵ Murata, M., l.c., Intertax, 1998, 127.

²⁶ Malherbe, J., "Droit fiscal international", Larcier, Brussels, 1994, 315.

²⁷ "Taxation in a world without distance", State Secretary of Finance., May 4th, 1998.

²⁸ Famulak, D. and Sieker, S., "Taxation of Electronic Commerce: Asia-Pacific", Annual Asia Pacific Tax Conference, 1999.

²⁹ OECD, l.c., paragraph 96.

³⁰ OECD Committee on Fiscal Affairs, OECD Model Convention Commentary, Paris, 1998, Art 5, par 5. (hereinafter The Commentary)

business", it would probably qualify in this case as a "permanent establishment" with only a preparatory or auxiliary character³¹.

Taxation in country B (location of the server or ISP)³².

Can the country where the server with the bookselling website is located argue that this is a fixed place of business, sufficient to warrant tax liability in that country?

Countries as the US³³, Korea³⁴ and The Netherlands³⁵ answer this question negatively, while other countries such as Germany are more radical in accepting technical equipment as a permanent establishment in their domestic tax laws. Vending machines, even without staff attending to them, were retained as such³⁶. Even cables

have been allowed as permanent establishments³⁷.

A possible line of defense for country B would be to argue that the provider or server is acting as an "agent" to the company, thus qualifying as sufficient attachment to country B.

As an example one can consider the Canadian tax law that has an extended definition of "carrying on business in Canada" which provides that a non-resident who solicits orders or offers anything for sale in Canada through an agent or a servant, is deemed to carry on a business in Canada³⁸. Another illustration can be found in Hong Kong tax law³⁹, where it states that an agent who regularly fills orders on behalf of the principal, is to be regarded as a permanent establishment (confirmation of the order-form on the website). The case is particularly interesting since Hong Kong SAR did not conclude any DTC's.⁴⁰

³¹ The Commentary mentions "advertising" specifically as being an example of the exception cases included in art 5 par. 4.

³² We discuss here taxation directly linked with the transaction between sellers and customers. There have been taxes levied on telecommunication services provided by ISP's to all users.

³³ Powers, P.J., l.c., 123.

³⁴ Advertising, furnishing of information and other such activities do not qualify as a permanent establishment of a foreign enterprise. Art. 120 (4) Korean Income Tax Act.

³⁵ "Taxation in a world without distance", State Secretary of Finance, May 4th, 1998.

³⁶ Tipke-Kruse, AbgabeOrdnung, par. 12, lit. 1a.

³⁷ Steuergerecht Dusseldorf, EFG, 1992, 717.

³⁸ Section 253 of the Income Tax Act of Canada.

³⁹ Rule 5 (1) Inland Revenue Rules. However this rule does only concern itself with establishing the amount of assessable profits, and not with the question if a permanent establishment exists or not. Non the less the implication of the rule is that an agent is a prerequisite for liability under the Profits Tax.

⁴⁰ Unless one would regard the Memorandum between Hong Kong SAR and the mainland, which has many of the same provisions as the Model Convention, as a DTC.

Article 5 par. 6 of The Model Convention does however contain a specific provision for enterprises that conduct business by using independent agents in another country, stating that such activity does not constitute a permanent establishment if the agent is acting in its ordinary course of business. If there is therefore a DTC between countries A and B, rules such as Canadian section 253 ITA are doubt full to be applied.

Taxation in country C (residence of the bookselling e-company).

The only one left seems to offer the most effective tax solutions. By lack of any permanent establishment only the country where the enterprise exploiting the electronic bookshop is resident, has taxing possibilities.

This view is supported by the US Treasury department⁴¹ and by the OECD work on the subject⁴²

On the other hand there are some serious disadvantages to applying the residence principle without correction by permanent establishments.

- It would open the door for widespread tax avoidance resulting from establishing

enterprises in tax havens that maintain the digital business. Given the portable nature of the electronic commerce, such is not hard to accomplish.

- There is a serious developing countries issue as well. Residence taxation would definitely favor the western developed side of the globe and disfavor the third world⁴³. It is probably no coincidence that the increased influence for residence-based taxation finds support by the Treasury of the country with the world's highest concentration of Internet companies.
- It creates an unacceptable discrimination between international electronic sales and conventional sales.

6.2. Second example: Medical diagnosis through the Internet.

Suppose an engineering company (the customer is a resident of country A) is contracted to perform very specialized drilling and construction of an oil-platform in the coastal waters of country B. Internet company (located in country C) provides for portable medical diagnostic equipment that

⁴¹ "Selected tax policy implications of global electronic commerce", l.c.

⁴² "Curtailling of source jurisdiction rather than residence jurisdiction in this context makes sense...", OECD, 1997, l.c. par. 92.

⁴³ A computer costs the average Bangladeshi eight years of income, compared with less than one month wage for the average US citizen. Human Development Report, United Nations, l.c., 34.

monitors temperature, heartbeat, blood count etc.. of the crew performing the dangerous work. C's computers automatically diagnose and sound alert to real physicians if necessary.

Essentially the same questions are raised about where tax is due, with much the same answers as above, but for the country of the customer (A).

Can the services that have been rendered through the Internet create a tax liability in country A?

The answer to this question of course depends on the domestic tax-legislation of country C involved, but reviewing the international literature involved it seems that there is more room in this situation for (source-) taxation. For instance the U.S.⁴⁴ argues that sale of goods can easily become rendering services, with different source taxation rules. Hong Kong tax law is unlikely to be lenient in cases where services will be performed as online banking, stock trading, database searches and gambling⁴⁵. This position applies even more so if the server is located in the same country as the customer⁴⁶.

⁴⁴ Department of the Treasury, l.c., paragraph 7.

⁴⁵ Scholars refer to the Bartica Investment Ltd case, and the Hang Seng Bank case; Famulak, D. and Sieker, S., "Taxation of Electronic Commerce: Asia-Pacific", Annual Asia Pacific Tax Conference, 1999.

⁴⁶ Hinnekens, L., "Looking for an appropriate...", l.c., 195.

This view seems to find support at the level of the OECD. The Fiscal committee of the OECD included in the Model Convention Commentary the following:

"But a permanent establishment may nevertheless exist if the business of the enterprise is carried on mainly through *automatic equipment*, the activities of the personnel being restricted to setting up, operating, controlling and maintaining such equipment. Whether or not gaming and vending machines and the like set up by an enterprise of a State in the other State constitute a permanent establishment thus depends on whether or not the enterprise carries on a business activity besides the initial setting up of the machines. A *permanent establishment may exist*, however, if the enterprise which sets up the machines also operates and maintains them for its own account."⁴⁷

Also fully automated equipments that perform complete tasks in executing a whole or a part of the enterprise's business must be considered to be permanent establishments⁴⁸.

The existence, set up and maintenance of the diagnostic equipment, even without any employees

⁴⁷ Model Convention Commentary, OECD, Art. 5 par.10.

⁴⁸ VOGEL, K., Double taxation conventions, Kluwer International, 1997, 290 (on automatic pumpstations).

of the electronic merchant present to use it, might therefore already lead to acceptance of a permanent establishment.

Even without permanent establishment, taxation in the country of the customer might just as easily be achieved if the payment made is qualified as a royalty for the use of intellectual property. That can very quickly be the case for instance in Hong Kong, where "payments for the use or the right to use any copyright material"⁴⁹, include a very broad description, thus at least in theory applying to electronic delivery of software.

7. The OECD's struggle for answers.

Fully aware of the challenges made by the new ways of making Internet-money to the concepts of it's model DTC, Working Party No. 1 on tax conventions and related questions of the OECD released a proposal for clarification of the PE-concept for comments. Finally, a revised draft of the text was published, but it is characterized by its lack of providing any real solution to the PE-problem⁵⁰

⁴⁹ Section 15 (1)(b) IRO.

⁵⁰ "The application of the permanent establishment definition in the context of electronic commerce: Proposed clarification of the Commentary on Article 5 of the OECD Model Tax Convention", OECD, Paris, 2000. (hereinafter "Proposed Clarification")

The Proposed Clarification does clarify one issue beyond question, though; "the Working Party believes that the principles which underlie the OECD Model Tax Convention are capable of being applied to electronic commerce". The OECD sees no need for new rules, but just seeks clarification how to apply the old ones.

But that clarification does not present itself as the gospel truth, at least not for now. The Proposed Clarification is riddled with uncertainties. "It seems", "there could" and "it might" are keywords, and the Working Party had to postpone any decisions on final text to a later date "after further study". An upcoming congress of the International Fiscal Association in cooperation with the OECD in November 2000 (Bombay) might provide the forum for some more definitive answers.

However, one can already see where the OECD is going to end up with its opinion. Some salient points;

- Computer equipment may only constitute a PE if it meets the requirement of being fixed. In the case of a server, what is relevant is not the possibility of the server being moved around, but whether it is in fact so moved.
- An Internet website is a combination of software and electronic data that does not, in itself, involve any tangible

property. It therefore cannot constitute a “place of business”.

- A server on which the website is stored and used is a piece of equipment and may thus constitute a “fixed place of business” of the enterprise that operates it.
- A hosting arrangement between an ISP and an enterprise does not cause that enterprise to have a PE on the physical location of the server.

Besides questions concerning the PE-problem, the OECD has also formed a Technical Advisory Group to advise on the treaty characterization of payments related to e-commerce⁵¹. The main problem is whether to regard a certain revenue as a business profit (Art. 7 Model DTC), a royalty (Art. 12 Model DTC), or whether yet another treaty qualification will apply. With much more clarity than in the Proposed Clarification, this text provides a helpful guideline on how to tax payments for electronic order processing, downloading, licenses, updates and add-ons, application hosting, web site hosting etc.. under the treaty. In most cases, the preference seems to go out to taxation as business profits instead of royalties.

⁵¹ “Technical Advisory Group on Treaty Characterization of Electronic Commerce Payments”, *OECD*, Paris, 2000.

8. Conclusion.

The technological dimension of the globalization of commerce has posed new questions concerning the application of international tax rules. Scholars wonder if the trusted concepts of effective place of management, residence and permanent establishment need to be left alone, revised or thrown over board. Governments wonder how they can be certain of a (maximum) share of the digital profits that are expected to be realized⁵². Companies and users are wondering where they are supposed to pay tax, and how much.

And there are no certainties and but few probabilities to offer them.

Probable seems that in most cases, conventional commercial activities using the Internet as a new medium for advertising and ordering, for public relations and digital mailing, will be subject to taxation only in the country where the company is resident, and not where the server is located or where the customer looks at the website.

It also seems probable that where additional equipment or services are concerned, or there is any other business activity, the country of the

⁵² An excellent overview of the tax-legislative response by Asian governments on this subject can be found in BUTLER, M., CHEW, V., EPSTEIN, R., GAMBLE, I., DE RIDDER, P., ROOSE, E., RUSS, N., “The Taxation of Global E-Commerce”, *Asia Pacific Tax Bulletin*, 2000, 200-228.

customer or the equipment is more likely to apply source taxation, especially if the server is located there.

With the current uncertainty in applying existing rules to new technologies, governments might interpret them in the way that assures the highest share in the tax-cake that is to be shared internationally, as they often tend to do⁵³.

That this can lead to double taxation of the Internet is not an unreasonable concern. Even within the States of the U.S. that concern of double taxation has made a three-year moratorium on multiple taxes, necessary⁵⁴.

The observer can not help but notice that the OECD, the US and several other developed countries are all too happy to resort to the classic concepts of international taxation which guarantees in most cases tax jurisdiction in the country of residence of the e-company, and not in the source-country, much to the detriment of the treasuries

of developing countries. The risk that the whole taxation of e-commerce discussion will be concluded to the disadvantage of developing countries is very real, given the preliminary points of view of the OECD's Working Party.

But developing countries are not defenseless against such erosion of taxable base. After all, developing countries are not member-states of the OECD. Though DTC's between developed and developing countries are all originally inspired on the OECD Model DTC, the United Nations has created its own version of the OECD Model that is widely used as a basis for negotiation by developing countries. When applying such a DTC of a developing country one must refer to the UN's interpretation rather than that of the OECD (in case of conflicting interpretations)⁵⁵. Thus, an alternate point of view pronounced by the UN regarding taxation of e-commerce, more to the advantage of developing countries, would render the OECD's interpretation on the subject inapplicable. Perhaps something to keep in mind if you are the Minister of Finance of a developing country.

In the absence (at least for the time being) of firm OECD policy hopefully corrected by a United Nations initiative, the only certainty that can be offered is that as soon as (or perhaps if) the profits

⁵³ That authorities are very aware of the international "competition" for internet tax-dollars is illustrated by Singapore's introduction of the Approved Cyber Trader Scheme, including a reduction to 10% in corporate taxation for merchants in e-commerce; Budget Statement 1998, Ministry of Finance, 1998.

⁵⁴ Internet Tax Freedom Act (P.L. 105-277), included as titles XI and XII of the Omnibus Appropriations Act of 1998; Approved as H.R. 4328 by Congress on October 20, 1998. Signed as Public Law 105-277 on October 21, 1998.

⁵⁵ VOGEL, K., Double Taxation Conventions, Kluwer, Deventer, 1997, 45-46

start to come in, these questions will need to be answered with certainty.

Until that time however, the taxation of electronic commerce remains in the domain of virtual taxation.
