

## Tax Treaty Issues in Cyberspace: E-Commerce and the Permanent Establishment Concept

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This [Note] deals with tax treaty issues raised by electronic commerce and the challenge the internet poses to tax systems worldwide. The main dilemma for governments, apart from discerning where the transaction occurred, is to establish nexus or sufficient contact in a state to exercise its taxing jurisdiction. The international taxing system, through treaties, depends on the concept of a permanent establishment or a fixed place of business. The internet challenges the appropriateness of the concept since significant business may be achieved in a source country with little or no physical presence. Business on the “net” may be conducted on a remote basis.

Permanent establishment issues are related to the issue of income allocation since treaties generally prohibit taxation at the source of active business income unless attributable to a permanent establishment. Whether or not permanent establishment issues are significant depends on characterization of the relevant income. This determines whether they are business profits attributable to a PE or fall under passive income such as dividends, interest, and royalties. Whether fixed automated equipment such as a web server can constitute a permanent establishment should also be addressed.

The Philippine government and the Bureau of Internal Revenue have not addressed these issues adequately. However, the Philippine government, recognizing the need for mutually agreed upon allocation of taxing rights, has assumed a position of cooperation and coordination in a Joint Statement with the United States with the OECD principles and its Model Tax Convention Consensus is only the first step.

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<sup>1</sup> THE AUTHOR PROVIDED IN THE NOTE THE ABOVE CITED ABSTRACT.

In compliance to the pressing need for uniformity, this [T]hesis proposes to adopt and incorporate the U.S. Software Regulations for characterization of digitized and non-digitized income and develop guidelines for determining the circumstances under which a web server may constitute a PE. However, it will not address the issue whether changes should be made to the PE definition nor will this [T]hesis deal with sales, use, or VAT taxes.