Dear Colleagues:

Attached are three interesting articles provided by Philippe Martin, Pierre Collin and Emmanuelle Cortot-Boucher of the Conseil d'État in France. I am sure you will find these of interest and our appreciation is provided for the completion of same.

The 4th Assembly of the IATJ is fast approaching, to be held in Amsterdam on August 30 and 31, 2013. Certainly we invite your attendance. The program is quite substantive, with over twenty-nine very interesting speakers from around the world, on a wide variety of topics, so of which I am sure will be of interest in carrying out your judicial duties. We are developing for our web site some additional information which will be available to members and that is a summary of tax treaty litigation in each country on an annual basis. This is another reason why you should join the IATJ – in addition to the access to the IBFD database.

By way of additional news the IATJ participated in a Judges' Panel at the recent 6th Annual U.S./Latin American Tax Strategies Planning Session in Miami, U.S.A. On the panel were judges from Canada, Guatemala, Mexico and Brazil. The IATJ will be doing another panel at the same conference in 2014. In addition, the IATJ, through association with IFA, will be participating in a panel of judges in San Paolo, Brazil in late September/early October on the topic of internal law and its influence on interpretation in applying tax treaties. These are the type of activities that the IATJ Judges are actively participating in and again, we solicit your support and assistance by joining the IATJ.

We look forward to seeing you at the 4th Assembly in Amsterdam. There is still time to register. Registration particulars may be found on our website together with the program Agenda.Reservations can be made at Golden Tulip/Tulip Inn under booking number: 141569/IATJ, and at IBIS under block code: IBFD290813. Contact information is: Golden Tulip/Tulip Inn, Schipholweg 3, 2316 XB Leiden, Tel: +31 71 4083500, reservations@goldentulipleidencentre.nl and IBIS Leiden Centre, Stationsplein 240-242, 2312 AR Leiden, Tel: +31 71 516 00 00, H8087-RE@accor.com

The IATJ is continuing its efforts in being a voice for tax judges from around the world. If you have any ideas that you wish to bring to the forefront for discussion at the Board of Directors meeting or at the Annual Assembly, please do not hesitate to forward same to myself at your earliest convenience. I thank you for your continued participation and support of the IATJ and extend my very best wishes to you.

Kindest personal regards,
E.P. Rossiter, President

Place of effective management : the Paupardin case (Conseil d'Etat, 16 April 2012)

Philippe Martin

The Paupardin case, decided by the Conseil d'Etat on 16 April 2013, deals with the concept of « place of effective management » mentioned in Article 15(3) of the OECD model convention, regarding income from employment. There are few cases about Article 15(3), and the Paupardin case may also be interesting for the interpretation of the concept of « place of effective management » used in Article 4(3) of the OECD MC as a tie-breaker for the residence of companies.

Mr Paupardin was a French resident, receiving wages from employment as a captain on oil tankers operating in international traffic. These wages were paid by a New Zealand company called Maritime Resource Management Ltd (MRM). He did not report these wages for income tax purposes, either in France or in New Zealand. When taxed in France, he argued that France had no tax jurisdiction under Article 15(3) of the France-New Zealand DTC of 30 November 1979, which provides that "remuneration derived in respect of an employment exercised aboard a ship or aircraft operated in international traffic may be taxed in the state in which the place of effective management of the enterprise is situated". This is the same rule as in Article 15(3) of the OECD MC.

New Zealand tax authorities informed their French colleagues that the wages were paid by MRM on behalf of a company called Maritime Multi-Resource Management Ltd (MMRM), whose registered office was in Vanuatu and which was designated as the employer in Mr Paupardin's employment contracts. The NZ company (MRM) recruited seafarers as an agent for MMRM, although it was sometimes designated as "manager".

Mr Paupardin challenged the tax adjustment in the tax courts. He won at first instance, but lost before the administrative court of appeals. He brought the case before the Conseil d'Etat as a final appeal.

The first argument submitted by Mr Paupardin dealt with the methodology to be followed when applying Article 15(3). In order to locate the place of effective management in New Zealand, and thus to escape French income tax, he argued that the term "enterprise" used by Article 15(3) should be interpreted as designating an economic entity, not necessarily a legal person. He added that the search for the place of effective management should take into account the fact that seafarers may not be able to look beyond their practical relationship with the manning agent: in his case, he stressed that he dealt with employees of MRM in New Zealand and received his assignments and his wages from this NZ company.

The Conseil d'Etat held that Article 15 deals with the taxation of employees and therefore the enterprise mentioned in Paragraph (3) was the employer. As such, the lower court had made no mistake in looking for the employer and then for the place of effective management of this employer. After deciding that the employer was MMRM (it was never argued in the case that MMRM was fictitious and should be disregarded as an employer) the lower court could legally check whether the place of effective management of MMRM was in New Zealand.

The second argument submitted by Mr Paupardin dealt with the notion of "place of effective management". He argued that the main test should be the location of the operational management, where day-to-day operations are managed.

The Conseil d'Etat provided, for the first time, a definition of the "place of effective management": it is the place, "where the persons exercising the highest functions in the enterprise make the strategic decisions that determine the conduct of the business of this enterprise as a whole". This is a direct interpretation of the tax treaty, without any resort to domestic law under Article 3(3) of this treaty (equivalent to Article 3(2) of the OECD MC) or any express reference to the OECD commentaries on Article 4(3) regarding the place of effective management for residence purposes, including the French observation on this topic (Paragraph 26.3 of the commentaries on Article 4).

Finally, Mr Paupardin challenged the application of the law to the facts by the administrative court of appeals. He claimed that the lower court had unduly created a presumption of place of effective management just by looking at the registered office of MMRM located in Vanuatu. The Conseil d'Etat rejected this criticism. Mr Paupardin was claiming the benefit of the France-NZ DTC, Article 15(3), which meant that the place of effective management of his employer had to be located in New Zealand if he wanted to escape French income tax. Therefore the issue was to determine whether the place of effective management of MMRM was located in New Zealand. In practical terms, the court had to answer the following question: do the functions performed in New Zealand by MRM (the only facts put forward by Mr Paupardin) show that the strategic decisions regarding the management of MMRM were made in New Zealand? The fact that employees of MRM in New Zealand recruited crews, assigned them to shipping companies and paid them had no strategic significance for the management of MMRM as a whole: the NZ operations could be local operations, alongside similar operations

located in other countries. The Conseil d'Etat decided that the lower court had rightly denied the benefit of Article 15(3) of the France-NZ DTC.

The Paupardin decision leaves open the question of the application of Article 15(3) to manning agents recruiting crews and assigning them to shipping companies. This issue was never raised by the parties to the case and the courts did not solve it ex officio. In order to clarify that this issue had been seen by the court, but not addressed or solved, the Conseil d'Etat wrote in its decision that the benefit of Article 15(3) has been rightly denied, "if it is accepted that the activity of manning agent exercised by MMRM could fall within the scope of Article 15(3) of the tax treaty".

In his opinion on the Paupardin case, the *rapporteur public* Julien Boucher expressed the view that Article 15(3) is related to Article 8 regarding "shipping enterprise" and therefore requires that the enterprise operates ships. In his view, Article 15(3) applies only when the employer is a shipping company and not when the seafarer is employed by a manning agent.

If this is the correct interpretation, it means that Article 15(3) does not challenge the tax jurisdiction of the state of residence in the presence of manning agents acting as employers. This issue could be clarified at the international level.

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Taxation of the Digital Economy

Pierre Collin

The digital revolution has taken place. It has given rise to a digital economy that challenges our concept of value creation. The digital economy is actually based on conventional production of goods and services. But, increasingly, start-ups and global companies serving millions of users are changing the rules and bringing radical transformation to all sectors of the economy: through their intense reliance on digital technologies; through their innovative business models; though the abundant financing accessible to them, particularly venture capital; through the continuous improvement in the design of their interfaces and the experiences that they offer through their applications; through the special relationships that they forge with the users of these applications; and through the use that they make of the data derived from the users' activities. Through these companies, the digital economy has come to account for a growing share of the value added in the economies of the largest countries.

The digital economy has become an intimate part of millions of individuals' lives, but its value added is slipping through our grasp. Its organisation, the power of the network effect and the scale of the externalities induced by its business models confound the rules for measuring value added. Yet the number of terminals and connected devices is growing exponentially. The time spent using these devices is showing sustained growth. Entertainment, shopping and production are now taking place in a digital economy that is part of daily life, and even an intimate part of it, for billions of individuals, including

consumers, creators, payroll employees and self-employed workers. The digital economy is everywhere, but we are still unable to measure it properly. The fact is that a significant share of its value added has been shifted out of large countries to the accounts of companies set up in tax havens. This shift has a major economic and, more importantly, tax impact. Despite doing a lot of business in the most populous countries, the major digital economy companies pay virtually no tax in those countries. This means that the productivity gains achieved through the digital economy have not led to increased tax revenues for large countries. There is no historical precedent for this situation.

Therefore, a Task force was commissioned to draft a report on taxation of the digital economy by four ministers of the French Government.

The starting point of the reflection was that the common feature of all large digital economy corporations is the intense use of data obtained from the regular and systematic monitoring of their users' activities:
- Data, particularly personal data, constitute the key resource of the digital economy. These data enable the companies that collect them to measure and improve the performance of an application, to customise their services, to recommend products to their customers, to support innovation efforts that give rise to other applications and to make strategic decisions. The use of data may also be licensed to third parties under a software platform business model, for example. As a general rule, data constitute the leverage that large digital companies use to scale their business and attain high levels of profitability.
- Data collection reveals the "free labour" phenomenon. Everything leaves a trail in the digital economy. Regular and systematic monitoring of their online activity means that data on application users are collected without any monetary consideration. Users become virtual volunteer workers for the companies providing the services that they use. The data from the users' "free labour" are collected, stored and processed to be integrated into the production chain in real time, blurring the dividing line between production and consumption. Users are attracted by the quality of interfaces and network effects. The data that they provide makes them production auxiliaries and they create value that gives rise to profits on different sides of the business models.

Consequently, the digital economy has stepped outside the theory of the firm: it is possible to "work" the users of an application, in the same way as suppliers and employees were "worked" in the past. The fact that users receive no monetary consideration for their activity explains some of the dramatic productivity gains of the digital economy. The fact that the labour of users in one country contributes to the formation of profits declared in another countries raises an objection on a matter of principle: it is troubling that the companies concerned do not contribute tax revenues to the country where their users live and "work" for them for free. The activity of application users is made possible and even greatly enhanced by public expenditure, particularly expenditure on education, social security and the extension of networks to cover all of the country's territory. The development of the digital economy per se calls for an aggressive industrial policy, which requires additional public expenditure. The

major digital economy companies leveraging the activity of web users should contribute their share to this expenditure.

On the basis on this diagnosis, the task force formulated three sets of proposals.

1 – Regain the power to tax the profits earned in the country by digital economy companies:

- Corporate income tax is the most appropriate tool ultimately for seeking a contribution that is proportionate to the creation of value inside the country. Net income, or profit, is an aggregate that is specifically intended to measure the net wealth created by a company from its business. Therefore, tax law needs to be reformed so that corporate income tax is assessed on digital economy profits.
- A country cannot achieve this result on its own. Given the specific constraints of international taxation, it is essential to initiate negotiations in the European Community and at the OECD to amend the rules on the division of tax powers. This will call for a definition of a permanent establishment that is specific to the digital economy.
- This definition must be based on the central role played by the data and "free labour" provided by users, which are not yet taken into consideration for tax purposes, even though they are at the heart of value creation, easily attributed to a given country and common to all of the dominant business models of today's digital economy.
- The purpose of these negotiations is to identify a permanent establishment when a company does business in a country using data obtained by regular and systematic monitoring of web users in that country. The share of profit stemming from the use of these data would be subtracted from the transfers made as payment for intangible assets located offshore.

2 - In the meantime, create a tax on the use of data obtained through regular and systematic monitoring of users' activity in the country.

Collecting data obtained through regular and systematic monitoring of users is the only taxable event that ensures the neutrality of the tax with regard to business models, technologies and business location strategies. Linking tax to the collection and use of data is an approach that is both neutral and sustainable. It is a way of linking the digital economy to a country and it is a strategy, backed by economic and industrial arguments about the value of data, for building up political capital for the coming international negotiations on the division of the power to tax major digital economy corporations.

The task force's proposal does not consist of taxing data collection per se. Instead, the aim is to create a tax incentive for businesses to adopt practices with regard to collecting and using data obtained through regular and systematic monitoring of web users that are consistent with four public interest objectives:
- Enhancing the protection of individual freedom;
- Promoting innovation in the digital trust market;
- Fostering the emergence of new services for users;
- Generating productivity gains and growth.

The purpose is to apply a principle similar to the “polluter pays" principle that underlies environmental taxes to companies that engage in regular and systematic monitoring of their users’ activities. This does not mean that these companies are in any way exempt from the obligations governing fundamental rights relating to the protection of personal data. This “predator pays” principle means that the tax will apply to companies that formally comply with the laws in force and actually engage in a form of exclusive capture of the data collected, by creating de facto obstacles to the portability and personal reuse of the data by the users themselves.

3 - Create a tax environment that favours the emergence of new companies by reforming the tax treatment of R&D and market financing.

More specifically, by:
- Adapting the definition of R&D to the characteristics of the digital economy;
- Reforming and simplifying the main measures (research tax credit and young innovative business tax status);
- Providing incentives for the growth of market financing for the digital economy.

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The Société BNP Paribas *decision (12th June 2013) : a fiscal advantage granted by French legislation can be refused to a taxpayer on the basis of an international tax convention*

Emmanuelle Cortot-Boucher

According to French tax case law, an international tax convention can never serve as a basis to establish a tax. It is necessary that a provision of French domestic law should exist to constitute that basis. This very well established rule was solemnly reaffirmed by a decision rendered by the highest judgement formation of the Conseil d’Etat through a decision read on the 28th June 2002, known as the *Schneider* case (n° 232276).

In another decision, read on the 12th June 2013 and dealing with a litigation involving the French society *BNP Paribas* (n° 351702), the Conseil d’Etat was asked the following question : should the rule set out by the *Schneider* case be considered as meaning that an international tax convention cannot be invoked to refuse to a taxpayer an advantage that is guaranteed by domestic law on the ground that an international tax convention prevents this advantage from being conferred ?

The facts submitted to the Conseil d’Etat were the following ones. The French society *BNP Paribas*, owning 100% of the shares of a subsidiary established in Canada, had decided to enter provisions for impairment of those shares. The French society had deducted those provisions of its taxable profits, claiming that French domestic law allows in general the deduction of provisions for impairment of shares.

The French tax administration had denied the society the right to deduct those provisions by taking argument of the tax convention concluded by France and Canada on the 2nd May 1975. The French authorities claimed that, in the version applicable to the dispute, the article 13 of that convention stipulated that the gains resulting from the alienation of shares representing a substantial participation in the capital of a society established in one of the two contracting countries would be taxable in that country. Besides, the article 23 of the same convention said that the French part would eliminate the double imposition liable to hit the gains mentioned at article 13 by implementing the exoneration method.

The Conseil d'Etat decided that the French tax administration was right, through a reasoning based on three steps. Firstly, it affirmed that, according to French domestic law, a provision may only be deducted of taxable profits if the risk or the charge it aims at anticipating upon can be, in itself, deducted of taxable profits.

Secondly, the Conseil d'Etat judged that this rule prevents provisions from being deducted of taxable profits when the risk or the charge they aim at anticipating upon cannot be deducted of taxable profits, including in those cases where the impossibility to deduct such a risk or a charge results from an international tax convention.

Thirdly, the Conseil d'Etat said that, according to French national legislation, a loss in capital should be regarded as deductible of taxable profits only if, should that loss have been a gain, that gain would have been taxable under French domestic law.

Combined with one another, those three assertions led the Conseil d'Etat to judge, in the present dispute, that the convention concluded between France and Canada, mentioning that the gains resulting from the sale of the totality of the shares owned by the French society in the capital of its Canadian subsidiary would not be taxable in France, prevented that the loss resulting from the same sale, if any, could be deducted of the taxable profits of the same society. Since that loss could not, in itself, be deducted of taxable profits of the society, it was consequently impossible for that society to deduct any provision for impairment of those shares.

Among the three points mentioned above, only the second one directly deals with the articulation between French domestic law and international tax conventions. It clearly rules out the idea that there might exist a non-aggravation principle according to which international tax conventions could only improve the situation of taxpayers, but never degrade it in comparison to what national legislation provides.

To put it more precisely, the Conseil d'Etat asserts that the provisions of French domestic law that allow advantages to taxpayers should be ruled out when they are contrary to what an international tax convention stipulates. It is the consequence that, according to the French Constitution, international conventions take precedence over national legislation once they are published. Another way to express the position taken by the Conseil d'Etat in the present case is to say that it judged it necessary to take international tax conventions into account to appreciate the situation of taxpayers with regard to French domestic law.

By opting for this position, the Conseil d'Etat made it clear that, in its opinion, international tax conventions should be interpreted as aiming at establishing a balanced allocation of taxing powers between contracting States. On the contrary, they should not be read as intending only to define a number of situations where taxpayers, although they are taxable under the national legislation of one of the two contracting countries, will nonetheless escape taxation under that legislation.

The revenues international tax conventions mention should therefore be interpreted as categories of revenues, the taxation of which is attributed, under a number of conditions, to one of the two contracting countries. Therefore, when an international tax convention provides that a certain type of revenue is only taxable in one of the two contracting countries, it should be read as preventing not only that the revenues in question should be taxed under the law of that country, but also as hindering that the whole legislation of the same country related to that category of revenues should be applied to any taxpayer who would invoke its benefit.

11 July, 2013

IATJ 4th Assembly
August 30 and 31, 2013

International Bureau of Fiscal Documentation
H.J.E. Wenckebachweg 210
Amsterdam, The Netherlands

AGENDA

Thursday, August 29, 2013	Meeting of the Executive and Board Directors in Leiden
6:00 p.m. to 7:00 p.m.	Walk from the hotels to restaurant 'Het Koetshuis'
7:00 p.m. to 9:00 p.m.	Meeting and Dinner
Friday, August 30, 2013	*IBFD, H.J.E. Wenckebachweg 210, 1096 AS Amsterdam*
7.30 a.m.	Bus shuttle from hotels Leiden to IBFD Amsterdam
8:00 a.m. to 9:00 a.m.	**Registration**
9:00 a.m. to 9:05 a.m.	**Welcome by Wim Wijnen** (NL)
9:05 a.m. to 9:45 a.m.	**IATJ Business Meeting**
9:45 a.m. to 10:00 a.m.	Health Break
10:00 a.m. to 10:05 a.m.	**Welcome by Sam van der Feltz** (CEO IBFD)
10:05 a.m. to 12:30 p.m.	**Substantive Session on Tax Avoidance/ Evasion** **Chair:** Peter Panuthos (US) **Panel:** Jurgen Brandt GER), Malcolm Gammie (UK), Stef van Weeghel (NL), Frank Pizzitelli (CAN), Pierre Collin (FRA)
12:30 p.m. to 2:00 p.m.	Lunch on board boat IBFD to Court of Appeal A'dam

Court of Appeal, Palace of Justice, IJdok 20, Amsterdam

2.00 p.m. to 2.05 p.m.	**Welcome by Herman van der Meer** (President, Court of Appeal Amsterdam)

2:05 p.m. to 3:30 p.m.	**Substantive Session on Indirect Taxation: Subjective Elements in VAT** **Chair:** Friederike Grube (GER) **Panel:** Dagmara Dominik-Oginska (POL), Timothy Lyons (UK), Emmanuelle Cortot-Boucher (FRA)
3:30 p.m. to 3:45 p.m.	Health Break – coffee/tea
3:45 p.m. to 5:00 p.m.	**Substantive Session on Objective Law and Subjective Judges:** **Chair:** Eveline Faase (NL) **Presentation:** Geert Corstens (President Supreme Court (NL)) and Klaus-Dieter Drüen (GER) **Moderator:** Richard Happé (NL)
5:00 p.m. to 5:45 p.m.	**Conducted tour** with architect in the new building of the Court of Appeal
5:45 p.m. to 7:30 p.m.	**Cocktail Reception Court of Appeal**
7:30 p.m.	Bus shuttle from Palace of Justice to hotels Leiden

Saturday, August 31, 2013	*IBFD, H.J.E.Wenckebachweg 210, 1096 AS Amsterdam*
7:45 a.m.	Bus shuttle from hotels Leiden to IBFD Amsterdam
9:00 a.m. to 10:30 a.m.	**Substantive Session on Transfer Pricing:** **Chair:** Philippe Martin (FRA) **Panel:** Nadia Djebali (NL), Vineet Kothari (IND), Philippe Martin (FRA), Gerald Rip (CAN), Stefan Wilk (GER),
10:30 a.m. to 10:45 a.m.	Health Break
10:45 a.m. to 11:30 a.m.	**Substantive Session Transfer Pricing** (continued)
11:30 p.m. to 12:30 p.m.	**Substantive Session recent Case Law on Treaty Override:** **Chair:** Joao Bianco (BRA) and Manuel Hallivis Pelayo (MEX)

	Panel: Manuel Hallivis Pelayo (MEX), Peter Panuthos US), Anthony Gafoor (TT), Pramod Kumar (IND), Peter Darak (HUN), Jennifer Davies (AUST), Ulrich Schallmoser (GER), Alexandre Teixeira (BRA)
12:30 p.m. to 2:00 p.m.	Lunch – IBFD
2:00 p.m. to 3:30 p.m.	**Substantive Session recent Case Law on Treaty Overriding** (continued)
3:30 p.m. to 3:45 p.m.	Health Break – coffee/tea
3:45 p.m. to 5:15 p.m.	**Substantive Session on Conclusive Force of Declarations of Foreign Authorities:** **Chair:** Robert Jan Koopman (NL) **Panel:** Clement Endresen (NOR), Emilie Bokdam-Tognetti (FRA), Petri Sauko (FIN)
. 5:15 p.m. to 5:30 p.m.	**Substantive Session on Excise Duties in EU** **Presentation:** Harald Jatzke (GER)
5 :30 p.m. to 7:30 p.m.	**Boat tour** - Cocktail on board
7:30 p.m.	**Closing Dinner** - Okura hotel
	Guest Speaker: Peter Wattel (NL)

9:30 p.m. Bus shuttle from Okura hotel to hotels in Leiden

<u>Sunday, September 1, 2013</u>

Leiden

Business :
09.30-11.00: Meeting of the Executive and Board of Directors at International Tax Centre University of Leiden, Rapenburg 65

Excursion*
11.00-12.00: conducted tour by Prof. K. van Raad at ITC Leiden
12.00-13.30: boat trip through Leiden to Kager plassen**
13.30-15.00: lunch at Kaag Sociëteit **
15.00-16.30: boat trip through Kager lassen to Leiden **
16.30-18.00: walk through the historical city of Leiden
18.00-20.00: dinner at the old city gate Zijlpoort **

* with accompanying persons
** costs of boat trip, lunch and dinner approximately €75 p.p.

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