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TITLE

ISSUES ON THE DEFINITION OF A PERMANENT ESTABLISHMENT FOR ELECTRONIC COMMERCE TAXATION PURPOSES

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LIST OF ABBREVIATIONS

OECD	Organisation for Economic Co-Operation and Development
UN	The United Nations
OECD Model Convention	OECD Model Tax Convention on Income and on Capital
UN Model Convention	UN Model Double Taxation Convention between Developed and Developing Countries
PE	Permanent Establishment
TAG	Technical Advisory Group
CFA	Committee on Fiscal Affairs
ISP	Internet Service Provider
OSP	Online Service Provider
The Treasury Department	The United States Department of the Treasury

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INTRODUCTION

Today we live in a world where it is hardly possible to imagine the life without internet. Electronic commerce (e-commerce) has become an integral and vital part of today's economy. People around the world use e-commerce for downloading media, buying goods, trading securities, playing games, etc. The developments have brought us to a stage where all this can be done by using laptops, tablets or smartphones.

E-commerce comprises the electronic sale by online stores of downloadable "soft merchandise" such as music, e-books, e-newsletters, photos and video recordings, software and documents (direct e-commerce), the electronic ordering of tangible products (indirect e-commerce), online securities transactions, the provision of financial or other services, as well as the subscription to and use of an internet service provider (ISP) or an online service provider (OSP).[1]

E-commerce – a good and a bad thing at the same time. Despite having a lot of advantages and making life easier, e-commerce poses a major challenge to the world's economy and creates legal issues in the field of taxation.

At the times this issue came into light, it was deemed to be "the most consequential tax issue of the new millennium."[2] However, after the developments and solutions offered, it nowadays considerably seems to remain one of the most consequential tax issues. At the times when the international tax rules were developed, there was no e-commerce and accordingly, various issues related to it. At present, however, existing tax rules which cannot be successfully applied to e-commerce reality, need to be structured in a way to be applicable to e-commerce transactions, or maybe new rules have to be developed to address the problems e-commerce causes.

The e-commerce related tax issues include the determination of the country having the jurisdiction to tax the income, the classification of income from computer-generated transactions, the development of a unified approach for the determination of income

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[1] Dr Jean-Philippe Chetcuti, *The Challenge of E-commerce to the Definition of a Permanent Establishment: The OECD's response,* Inter-Lawyer Law Firms Directories (2002), http://www.inter-lawyer.com/lex-e-scripta/articles/e-commerce-pe.htm.

[2] *Id.*

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generated from e-commerce, particularly in classification of income to business profits or royalty and rent, the establishment of principles for tax administration and enforcement, as well as many other related issues.

The principle that a country has the right to tax business profits of a resident of another country only if that person has a permanent establishment (PE) in that country is one of the primary legal principles in international tax law and is a vital provision in international tax treaties.[3]

The term "permanent establishment" has been defined by The Organisation for Economic Co-operation and Development (OECD) as meaning *"a fixed place of business through which activities of an organization are wholly or partially carried out."* The term includes a place of management, a branch, an office, a factory, a workshop, and a mine, oil or gas well, quarry or other place of extraction of natural resources residing under a foreign jurisdiction.[4]

Though certain differences and difficulties in the determination of a PE can be somehow resolved by unified regulation and appropriate analysis, the complications that the principle of a PE faces in e-commerce taxation because of the lack of an identifiable physical location for websites or servers, seem to be quite hard to handle.

With the destabilisation of the traditional concept of PE, attention has quickly shifted onto the servers and websites for their possible qualification as a PE. Can a server, telecommunications device, computer terminal, or web page be considered a permanent establishment?[5] These and several other related issues are hot discussion topics amongst many tax and legal experts. Though the solutions are far to find, but the attempts to propose clarifications and approaches to address the issue are possible through relevant research and analysis.

E-commerce creates a number of issues, and not only for taxation purposes. The issue of the determination of a PE also has a lot of difficulties and discrepancies. These problems need to

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[3] Gauram Ramachandra Rao, *India: Concept of Permanent Establishment and Electronic Commerce,* Mondaq: Connecting knowledge and people, http://www.mondaq.com/india/x/20581/Ebusiness+New+Media/Concept+of+Permanent+Establishment+and+Electronic+Commerce (last updated Apr. 8, 2003).

[4] Model Tax Convention on Income and on Capital, OECD, 2014 [hereinafter OECD MTC].

[5] Chetcuti, *supra* note 1.

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be addressed and resolved to make the international legal and economic principles work properly.

A central tax issue in this field is the determination of the jurisdiction to tax the income from e-commerce based on the presence of a server in a country. Accordingly, the tax issue raised in this paper is the issue on the definition of a PE for e-commerce taxation purposes.

This paper is not designed to study the endless issues of both e-commerce and permanent establishment. The scope of research will then be limited to studying certain issues arising in the taxation of e-commerce on the basis of a PE, such as the international tax-avoidance behind the above mentioned problems, the difficulties in determining relevant taxation jurisdiction, and mainly the issues regarding considering servers as PEs for taxation purposes.

This paper provides a general overview on certain e-commerce and PE issues, analyses the best international practice in considering servers as PEs and discusses the possible implications and consequences of the issue in the Republic of Armenia. ***Chapter 1*** provides the determinations of e-commerce and permanent establishment to prepare relevant ground for the identification of the problem including the issues of both. The chapter gives information about existing threats that e-commerce poses for the economy as well as the differences of present approaches to the determination of a PE both according to the OECD Model Tax Convention on Income and on Capital (OECD Model Convention) and the UN Model Double Taxation Convention between Developed and Developing Countries (UN Model Convention). ***Chapter 2*** leads the reader to the main issue involving e-commerce within the scope of the determination of a PE. International best practice is taken into account, as well as possible solutions are considered and proposed to "the most consequential tax issue of the new millennium". And finally, ***Chapter 3*** addresses the same issues within the scope of possible implications in Armenian legislation, application in the new Tax Code of the Republic of Armenia, and reveals the question in Armenian reality. ***The Conclusion*** sums up the proposals and possible solutions to the problem of the determination of a PE for e-commerce taxation purposes, as well as provides a brief summary of the main findings of the paper.

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CHAPTER 1

DEFINITIONS OF ELECTRONIC COMMERCE AND PERMANENT ESTABLISHMENT AND THE ISSUES RELATED TO THEM

SUB-CHAPTER 1: ELECTRONIC COMMERCE

The beginnings of e-commerce can be traced to the 1960s, when businesses started using *Electronic Data Interchange (EDI)* to share business documents with other companies. In 1979, the American National Standards Institute developed *ASC X12* as a universal standard for businesses to share documents through electronic networks. After the number of individual users sharing electronic documents with each other grew in the 1980s, in the 1990s the rise of eBay and Amazon revolutionized the e-commerce industry. Consumers can now purchase endless amounts of items online, both from typical brick and mortar stores with e-commerce capabilities and one another.[6]

An e-commerce transaction is the sale or purchase of goods or services, conducted over computer networks by methods specifically designed for the purpose of receiving or placing of orders. The goods or services are ordered by those methods, but the payment and the ultimate delivery of the goods or services do not have to be conducted online. An e-commerce transaction can be between enterprises, households, individuals, governments, and other public or private organisations. Measuring e-commerce is difficult for a number of reasons including defining what constitutes e-commerce, the speed of its growth and evolution and the fact that in many cases firms conduct both e-commerce and traditional commerce simultaneously.[7]

The benefits of e-commerce seem to be endless: availability and easy access, wide availability of goods and services, speed of access, as well as international reach. However, certain

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[6] *Electronic commerce,* http://searchcio.techtarget.com/definition/e-commerce (last updated: June 2016).

[7] *Electronic commerce,* OECD Glossary of Statistical Terms, https://stats.oecd.org/glossary/detail.asp?ID=4721 (last updated Jan. 17, 2013).

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downsides are that the consumers are not able to see or touch a product prior to its purchase, certain time is required for the product to be shipped and reached to destination, etc.

One of the main prerequisites of good tax policy is deemed to be the proper application of the neutrality principle wherever possible. However, e-commerce poses a real threat in this aspect, as there are different approaches of taxing e-commerce which differ from the taxation of conventional commerce.

The United States Department of the Treasury (The Treasury Department) strongly advocates the neutrality principle, which *"requires that the tax system treat economically similar income equally, regardless of whether earned through electronic means or through more conventional channels of commerce."* The Treasury Department believes that the best way to achieve neutrality *"is through an approach which adopts and adapts existing principle in lieu of imposing new or additional taxes."* Though the Treasury Department's position is that the neutral tax policy, for economic reasons, should be implemented to the extent possible, however, there can be a doubt that pursuing the neutrality principle is possible in certain instances or that doing so will yield a positive outcome.[8]

Another problem emerged with the development of e-commerce is the distinction between royalties, business profits, and payments for electronic services. This distinction has become quite difficult to make.

Accordingly, problems arise in classification of income and in attempting to apply the tax rules to new electronic forms of business transactions. There are three primary types of income generated by e-commerce: (1) income from the electronic sale of goods; (2) rent (or royalty) income from the lease (or license) of certain electronic property; and (3) income from the provision of electronic services.[9]

(1) Income from the electronic sale of goods (tangible or intangible):

The distinction between tangible and intangible is mainly necessary because of its relevance in determining the source of income from certain cross-border transactions. For example, payments in consideration of a sale of an intangible that are contingent on the productivity,

[8] John K. Sweet, *Formulating International Tax Laws in the Age Of Electronic Commerce: The Possible Ascendancy of Residence-Based Taxation in an Era of Eroding Traditional Income Tax Principles,* 146 (6) U. Pa. L. Rev. 1949, 1952 (1998).

[9] *Id.* at 1960.

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use, or disposition of the intangible, receive source treatment as if they were royalties. Contingent payments received on the sale of tangible property, on the other hand, receive different source treatment. In case of e-commerce transactions, the sale of a "copyrighted article" under the proposed regulations is more easily analogized to the sale of tangible property. The principal value of a copy of a computer program ("a copyrighted article") to its purchaser is not the protection afforded by copyright law, but the right to use or sell the copy. In that respect, the computer program is similar to other property protected by copyrights, such as books or records. Since no one could reasonably characterize a book or a record as intangible property, there is no reason for a computer program, whether delivered to a customer on disk or by modem, to be so characterized. Thus, it is expected that the classification of copyrighted articles as tangible property is more accepted and somehow approved.[10]

(2) Income from the lease or license of certain electronic property:

The main approach towards the classification of rental and royalty income from property is that royalty income from intangible property is sourced based on where that property is used. An issue can arise whether the place of use is the residence of the payer of the royalties, or the location of the software's end user, or the place of installation of the software. The approach of determining the place of use by the residence of the payer of royalties has problems because of its simplicity and creates issues in case the places are different. The next approach of determining the place of use by the location of software installation arises the possibilities of abuse in cases of installing the software in a low-tax jurisdiction (a tax haven). Besides the application of place-of-installation rule would violate the neutrality principle. And the final way of determining the place of use by consumer location is also problematic as due to the anonymous nature of internet transactions, it is often difficult, or at times, impossible, to determine the consumer's location.[11]

Several studies have been undertaken in an attempt to develop guidelines to assist in distinguishing between the two types of payments. Indeed, where there is any uncertainty in the appropriate characterization of payments, perhaps not surprisingly, high-income countries tend to be biased in favour of characterizing the payments as business profits. For example, in a recent examination of the characterization of 28 e-commerce transactions, an OECD

[10] *Id.* at 1961-63.

[11] *Id.* at 1965-68.

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Working Group determined that only 3 of the transactions were royalties, while the rest of the transactions gave rise to business profits. In contrast, an Indian Ministry of Finance report concluded that in 14 of the 28 transaction examples provided, the transaction described gave rise to a royalty.[12] A report issued in 2001 by a Technical Advisory Group (TAG) established by the OECD suggested that most forms of e-commerce income should be characterized as business income. Only in the clearest of cases should the income be characterized as royalty income.[13]

(3) Income from the provision of electronic services:

Usually the place where the labour or services are performed determines the source of services income. In earlier times, the performance of services and the utilization of those services most likely took place in the same geographic location. However, this traditional source rule is threatened by the expanding nature of e-commerce. This can lead to a situation where the performance jurisdiction and the utilization jurisdiction have strong claims to tax the services provided, and accordingly this will result in double taxation. In addition to traditional types of services that have now taken electronic form, e-commerce has given rise to an entirely new breed of services sometimes referred to as "online information services." The most common types of these services made available by OSPs include internet access and electronic mail facilities, chat rooms and online shopping and web hosting services. Nonetheless, even though these common arrangements might not qualify as "pure" services, their "predominant characteristic ... is that of a service" in that they enable the customer to find and retrieve information. Accordingly, classifying these arrangements as services for tax purposes seems appropriate.[14]

Nevertheless, many problems other than the taxation issues arise in the field of e-commerce, which are endless and cannot be addressed in this paper, since it is bound to the issue of e-commerce taxation mainly on the basis of a PE.

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[12] Kim Brooks, *Tax Treaty Treatment of Royalty Payments from Low-Income Countries: A Comparison of Canada and Australia's Policies,* 5 (2) (Michigan Issue) eJournal of Tax Research 168, 188-89 (2007), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1078738.

[13] BRIAN J. ARNOLD & MICHAEL J. MCINTYRE, INTERNATIONAL TAX PRIMER 158 (2d ed. 2002).

[14] Sweet, *supra* note 8, at 1968-71.

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SUB-CHAPTER 2: PERMANENT ESTABLISHMENT

The concept of PE was first stated in the early model conventions of the League of Nations in 1928. League of Nations Draft Model Treaty provided that *"Income derived from any industrial, commercial or agricultural undertaking and from any other trades or professions shall be taxable in the State in which the permanent establishments are situated."*[15] It means that PE had been playing an important role in the same time as the tax treaty model was developed.[16]

The concept of PE which is used by OECD in current days was first introduced in the Draft prepared by the OECD Committee on Fiscal Affairs (CFA) in 1958 in their Draft Convention for the Avoidance of Double Taxation. However, although different in wording, that PE concept, in principal, was taken from the UN model in 1928.[17]

The "PE" concept has not changed significantly over the years. It is used by tax treaties for taxing business profits of non-residents in case the income is earned through a "PE" or actual fixed place of business in the jurisdiction.

Article 5 of both OECD and UN Model Conventions define permanent establishment:

> *"The term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.*
>
> *The term "permanent establishment" includes especially:*
>
> *a) a place of management;*
> *b) a branch;*
> *c) an office;*
> *d) a factory;*
> *e) a workshop, and*

[15] Draft Model Treaty, Report on Double Taxation and Tax Evasion, League of Nations, art. 5, Oct. 1928.

[16] Nufransa Wira Sakti, *Permanent Establishment for E-commerce in International Taxation,* 37 The journal of the study of modern society and culture 325, 326 (Dec. 2006).

[17] *Id.* at 333.

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f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources."[18] [19]

According to this rule, the source country may tax the profits arising from commercial activity carried out within its borders by a foreign entity through a substantial physical presence in the source country. To justify source taxation, such presence must reach the level of a "PE" by satisfying the following 3 prerequisites:

1. there must be a distinct place, such as premises, or in certain instances, machinery or equipment *("place-of-business test");*
2. it must be established with a certain degree of permanence *("permanence test");*
3. business must be carried on through the place, usually by personnel of the enterprise *("business-activities test").*[20]

Nevertheless, certain issues arise when applying the above mentioned tests due to the fact that there are different requirements for the distinct place, length of time and the personnel defined by different tax treaties. Though both the OECD and UN model treaties provide for the provisions on the PE but there are certain notable differences between them in terms of when a non-resident is deemed to be having a PE in the jurisdiction.

There are significant differences between the deemed PE rules in the two treaties, with the UN treaty deeming permanent establishments and hence allowing source country taxing rights, over a significantly broader range of business activities.[21] For example, there is a difference in the types of service provision in the source country to amount to a PE. Under the UN model, a non-resident enterprise that furnishes services of any kind in the source country for one or more periods aggregating more than six months within any twelve-month period is deemed to have a PE in the source country. Profits from the provision of services will be attributed to the deemed PE and thus can be taxed in the source country where the services are provided. In contrast, the OECD model treaty has no measure that allows a source country to

[18] OECD MTC, *supra* note 4.

[19] Model Double Taxation Convention between Developed and Developing Countries, UN, 2011.

[20] Chetcuti*, supra* note 1.

[21] Veronika Daurer & Richard Krever, *Choosing between the UN and OECD Tax Policy Models: An African Case Study,* EUI Working Paper RSCAS 2012/60, at 7.

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treat the long term provision of services as a deemed PE and thus bypass the rule denying source countries any right to tax business income unless the income is derived through a PE.[22]

One of the problematic questions is the issue of an equipment, for example, when the physical presence is established by an equipment placed in certain jurisdiction, without any human intervention. In such cases an issue may arise what can and what cannot be considered an equipment constituting a PE.

Besides, there are activities that both model treaties exclude from the definition of a PE. Those are business activities of a general, preparatory or auxiliary nature.[23] Meanwhile, certain activities can be carried out in a way as to comprise the above mentioned nature in order to avoid being deemed a PE for taxation purposes.

The particularities in the definitions of a PE according to OECD and UN model treaties are not the main issues with regard to the determination of PE concept, as it is not limited to only a fixed place of business. It may also include an agent that is legally separate from an enterprise but sufficiently connected and dependent upon the enterprise. Many other similar issues arise when exploring the difficulties of a PE. But, within the scope of research, in this paper, the main issue addressed, is the one involving the taxation of e-commerce on the basis of a PE.

[22] *Id.* at 9.

[23] *Infra* note 38.

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CHAPTER 2

THE ISSUE OF ELECTRONIC COMMERCE TAXATION ON THE BASIS OF A PERMANENT ESTABLISHMENT

SUB-CHAPTER 1: THE MAIN ISSUE INVOLVING ELECTRONIC COMMERCE WITHIN THE SCOPE OF THE DETERMINATION OF A PERMANENT ESTABLISHMENT

As the internet and Information Technology (IT) sphere grow the physical goods have been replaced by digitized goods, labor performed in specific place no longer necessarily requires a physical presence. At the same time, the service provider and customers do not need to be in one place to engage in electronic transactions.[24]

The OECD CFA, having the goal of reforming the international tax policies, has held several meetings concerning e-commerce tax related topics starting from 1997 in Finland, and later in Canada.[25] The Draft Commentary on Article 5 concerning the application of the current definition of a PE in the context of e-commerce, issued by Working Party No. 1 on Tax Conventions and Related Questions, was adopted by the CFA on 22 December 2000 which summarised some approaches with respect to above mentioned issues.[26] [27]

The overall conclusion of the specialists was that the traditional international tax law principles shall continue to be applied even in the e-commerce context. The OECD highlights the traditional principles such as the necessity to maintain neutral tax treatment in between

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[24] *Permanent Establishment under the OECD Model Tax Convention,* LawTeacher (Nov. 2013), https://www.lawteacher.net/free-law-essays/commercial-law/permanent-establishment-under-the-oecd-law-essays.php.

[25] Petrit Ademi, *PE Threshold for Business Profits in E-commerce Context – To what extent does the present Permanent Establishment Threshold influence the taxaxtion of Electronic Commerce cross-border transactions?,* Lund University Master Thesis HARN60, School of Economics and Management, Department of Business Law (June 2, 2014), at 18, http://lup.lub.lu.se/luur/download?func=downloadFile&recordOId=4452209&fileOId=4469753.

[26] Chetcuti*, supra* note 1.

[27] Clarification on the application of the permanent establishment definition in e-commerce: Changes to the Commentary on the Model Tax Convention on Article 5, OECD Committee on Fiscal Affairs, Dec. 22, 2000.

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e-commerce and traditional commerce, low administrative and compliance costs for the taxpayer and the authorities, reducing tax evasion and avoidance. A specific principle added to the traditional framework, is the necessity for a flexible approach towards the technological developments. Accordingly, several TAGs were created to come up with possible solutions.[28]

The amendments mainly referred to the physical presence as the key factor to determining the existence of a PE in the e-commerce. Thus, it was considered, that if there is no server (physical presence) in a fixed place of business - *situs test,* located at a certain point (geographically) - *locus test,* used for a certain period of time - *tempus test*, a PE is deemed to not exist. Moreover, the server should be owned or leased by the enterprise, the business itself must be wholly or partly carried on through the server and the activity must not be considered as auxiliary or preparatory for the business in order to give rise to a PE.[29]

The OECD Commentary questions if mere use in e-commerce operation of a computer equipment could constitute a PE and makes a clear distinction between tangible computer equipment (e.g. a server) and intangible software and data (e.g. a website) for the purposes of Article 5 of the OECD Model Convention. Yet, although a server as such cannot be a PE itself, the place where the computer is stored, together with the server, may constitute a place of business. If so, the issue arises in case of websites, whether the user's computer itself could be regarded as a "facility" as it is tangible and harbors the website itself. According to the Commentary, the existence of premises is not a precondition for the constitution of a PE. However, the comments apply where the enterprise operating the website and the ISP are located in countries that have a double tax treaty based on the OECD Convention as entirely different rules can apply if there is no treaty to rely upon.[30]

More accepted approach in this matter is that websites stored on a server should not constitute a PE. On the other hand, the server on which the website is stored and through which it is accessible is a piece of equipment having a physical location. Such a location may constitute a "fixed place of business" of the enterprise that operates that server as long as the server is fixed at a certain place for a sufficient period of time.[31]

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[28] Ademi, *supra* note 25, at 18.

[29] *Id.* at 18-19.

[30] S*upra* note 24.

[31] Chetcuti*, supra* note 1.

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In order to understand the mechanism of considering a server or a website as a PE, the difference between websites and servers needs to be clearly addressed.

A website is a collection of linked computer files located on the hard drive of a server that is connected directly to the Internet. Files that are displayed on the computer screen of the user are called pages. Each page of a website has a unique address, called a uniform resource locator (URL). The page of a website that users are expected to view first is called the home page.[32]

As for the ***web server***, it is a computer hosting one or more websites. "Hosting" means that all the web pages and their supporting files are available on that computer. The web server will send any web page from the website it is hosting to any user's browser, per user request. A web server can host multiple websites.[33]

Since e-commerce is done through the server, which forms an integral part of the hosting of material on the internet, the issue whether the use of such an equipment would satisfy the OECD conditions for being classified as a PE, requires a determination as to whether a server constitutes a place of business, the server can be said to be fixed and whether the activities of the website may be said to constitute the carrying out of business through such a fixed place of business or not.[34]

Some commentators have suggested that a website is a PE in the country where the server that hosts the website is located. The OECD argues, with considerable force, that this suggestion has little merit. What is located on the server is a collection of computer files. Although those files have a physical presence and do not constitute intangible property, they do not constitute an office or serve the function of an office. In any event, the tax revenue to be gained by

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[32] ARNOLD & MCINTYRE, *supra* note 13, at 151.

[33] *What is the difference between webpage, website, web server, and search engine?* https://developer.mozilla.org/en-US/docs/Learn/Common_questions/Pages_sites_servers_and_search_engines (last updated: Dec. 6, 2016).

[34] Augustus Fundo, *Major Problems Affecting International Taxation of E-commerce,* Lambert Academic Publishing (2011) http://www.academia.edu/4263520/MAJOR_PROBLEMS_AFFECTING_INTERNATIONAL_TAXATION_OF_E_COMMERCE.

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treating website files on a server as a PE is not likely to be significant, due to the ease with which the owner of the website could move the server to a remote location.[35]

From a policy perspective, a website should be treated as a PE only if it is used to perform the functions of a traditional office. Even if a website were treated as an office or fixed place of business, it would not constitute a PE in all cases. In general, a virtual office could constitute a PE only if it was used to make actual sales of goods or services on a more than casual basis. According to the Commentary, a PE requires a "physical presence" in a country, and a website is "intangible" and not physical.[36]

If an enterprise carries on business though a website and the server operated by another enterprise, it would not constitute a PE. In this case, the website is intangible and does not have a physical presence. On the other hand, if the same enterprise operates the server and carries on business through that server, it would constitute a PE.[37]

There were also certain approaches in the Commentary proposed to preparatory or auxiliary services. An indicative list of activities generally considered preparatory or auxiliary includes providing a communications link, advertising goods or services, relaying information through a mirror server, gathering market data or supplying information. These activities were deemed to not be attributable to the concept of PE. However, on the other hand, an online advertising agency's online adverts or the online research activities of an online market analyst are likely to constitute core activities and this can contribute to establishing a PE.[38]

In some cases, an enterprise might employ automated computer equipment that does not require human intervention for its normal operation. Some commentators have suggested that such automated equipment should not constitute a PE. The OECD Commentary takes the contrary position. It analogizes automated computer equipment to automated pumping equipment used in the oil or gas industry. It has long been settled that such pumping equipment should constitute a PE notwithstanding the lack of human intervention.[39]

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[35] ARNOLD & MCINTYRE, *supra* note 13, at 154.

[36] *Id.* at 154-55.

[37] Sakti, *supra* note 16, at. 339.

[38] *Chetcuti, supra* note 1.

[39] ARNOLD & MCINTYRE, *supra* note 13, at 156.

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In practice, many e-commerce businesses are done by using other machine equipment, server to be exact, either by leasing or renting some spaces of hard disk in the server. One server can have a lot of spaces that can be rented to others. In this case, that server is similar to the premises that consist of rooms, cubicle, floor or space which could be rented partially or wholly to others. And an issue may arise in determining the person involved. [40]

As regards the agent, the treaty rule, mirrored in the domestic laws of many countries, is that an agent does not create nexus for its principal if it is an independent agent acting in the ordinary course of its business. In most cases, an ISP would be an independent agent for tax purposes. The Commentary also takes the position that the hosting of a website typically would not cause the ISP to be a PE of its principal. This position does not appear to be controversial.[41]

In some cases, nevertheless, the business of an ISP might be so enmeshed in the business of its principal that it would be treated as a dependent agent and possibly a PE. Under tax treaties, based on the OECD model treaty, a dependent agent is a PE only if it has and habitually exercise the authority to conclude contracts on behalf of its principal. Tax treaties based on the UN model treaty treat a dependent agent as a PE if the agent has the power to conclude contracts or has a stock of goods out of which it fills orders for its principal. [42]

Moreover, servers are highly mobile and flexible in nature. Servers can transfer their programs almost instantaneously to a server in a different jurisdiction as necessary. E-businesses may own or lease a server located anywhere in the world and can conduct its business activities via this server in such a way as to ensure that their profits will either be taxed exclusively by the residence country or by some low tax jurisdiction. An e-commerce transaction can involve a number of servers strategically located in different countries for the purpose of making their business broader and the management of the business easier, as well as avoiding taxation requirements in some jurisdictions. The firm's website and its online store can be hosted on different servers or on one and the same server

[40] Sakti, *supra* note 16, at.337.

[41] ARNOLD & MCINTYRE, *supra* note 13, at 156.

[42] *Id.* at 156-57.

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situated anywhere in the world and accessible by online consumers from any part of the world.[43]

Due to the mobility of servers another very important issue of e-commerce emerges – the issue of personal data protection. Though, it is expected that the personal data of the customers are safely kept, the practice has shown that leaks of information even to other countries have also happened. It can be the case, for example, when the server operating the transactions is located in country A. It can keep the data of country B's resident, and further be moved to, for example, country C. The result can be leak of information of country B's resident to country C. Taking into account the fact that a customer enters into an electronic transaction with a trust that his or her personal data will be protected and not transferred to a third party in any case, this kind of situation can be against personal data protection rules, and can give rise to another legal issue. Thus, the protection of personal data can also be deemed one of the global problems of e-commerce.

The above mentioned ways to carry out business render the task of determining the location of a PE very difficult, if not impossible. The current PE rules can easily be circumvented either by carrying on only preparatory or auxiliary activities in the source state, or by using the server of a local ISP to carry on the core business activities of the foreign enterprise, or by positioning the server and establishing a PE in low or no tax jurisdictions.[44]

The approach to consider a server as a PE, though seems to give a kind of a solution to the problem of e-commerce taxation, but meets certain difficulties. As above mentioned, the servers can change their location and can be hard to be traced. The next issue is the issue of the length of time. The concept of PE requires 6 months operations in a fixed place of business, whilst in case of e-commerce, this can lead to tax avoidance by placing servers at different jurisdictions so they do not stay in the same jurisdiction for the above mentioned time to constitute a PE.

SUB-CHAPTER 2: INTERNATIONAL BEST PRACTICE

[43] Chetcuti, *supra* note 1.

[44] *Chetcuti, supra* note 1.

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Certain countries have taken different positions on considering servers having a taxable presence in a country. There are both critical approaches to this issue and confirming positions with a relevant practice already formed in the taxation of e-commerce on the basis of a PE.

Though the OECD Model Convention reflects one of the most influential multilateral tax treaty models, however not all of its members follow the amendments in the Commentaries on Article 5, concerning mainly to the physical presence, not all of them have deliberate reference to such issues, and as such most of them silently follow the OECD Model Convention actual interpretation. The countries are accordingly divided into three groups.[45]

1) OECD member countries that follow the amendments entirely: situs-locus-tempus test (server may constitute a PE, but a website not) - Australia, USA, UK, Italy, Estonia;
2) OECD member countries that do not follow the amendments entirely, only: "tempus test" and reframed situs-locus test (website may constitute a PE) - France, Spain (observation), Portugal (observation), Greece;
3) OECD member countries that silently follow the amendments: situs-locus-tempus test - Austria, Belgium, Denmark, Germany, Japan, Switzerland, Hungary, The Netherlands, and Sweden.[46]

This differentiation shows, that almost all OECD member countries, tend to consider servers as PEs, though, based on different grounds, one providing a stricter approach, and another considering broader framework for taxing e-commerce on the basis of a PE. The reason behind such policies can be hard to establish, but the uniformity can be considered to be the development of the economy in such countries. Taking into account the fact that OECD consists of developed countries, their approach to tax e-commerce can be justified for a reason, that they already have developed economy and international recognition for the e-commerce to take place in such countries, thus their main task in this matter can be the proper regulation of it. Thus, this can be the reason why capital exporting countries tend to give priority to residence based taxation not to restrict their power to tax the income derived from foreign investment, while capital importing countries give priority to the source based taxation.

In contrast to the countries, which are developing, and trying to create possibilities for the economy to grow in their countries, it seems that the OECD member countries have achieved

[45] Ademi, *supra* note 25, at 21.

[46] *Id.*

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certain degree of development of economy, thus, these countries may not mainly face the issue of taxation of e-commerce on the basis of a PE, and may not need to create certain tax benefits within the framework of e-commerce taxation.

Certain approaches and distinct examples of OECD member countries are provided below.

A large group of countries supports the position that a server by itself can create a PE.

For example, in 2007, Italy issued a ruling in which it expressed its position towards the servers.

> *In an example of a French company that offered video game subscriptions to Italian customers using servers located in Italy but whose configuration and operation were carried out in France,*

the tax authorities concluded that where all the stages of the business were carried out electronically via the servers, the servers would constitute a PE.[47]

In 2013, the Supreme Administrative Court of Sweden annulled a ruling by the Tax Board for Advance Rulings, which had determined that a server did create a PE.

> *At issue was a foreign company X that owned a server in rented premises that was made available to foreign company Y, its parent, for storing software. The server was automated with maintenance carried on outside Sweden. The Tax Board ruled that company X had a permanent establishment, but company Y did not have a permanent establishment, as its business with the server was auxiliary or preparatory...*[48]

In a relevant case involving Canada and US a different approach is distinguishable.

In 2013, the Canada Revenue Agency (CRA) issued a ruling regarding whether a data centre operated by a Canadian member of a multinational group created a PE for the US parent company under the income tax treaty between the United States and Canada. Under the facts of this ruling,

> *a Canadian affiliate of a US parent acquired assets to operate a data centre in Canada, which hosted the group's website that stored user data, advertised, and processed transactions. Employees of the Canadian company were*

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[47] Monica Gianni, *The OECD's Flawed and Dated Approach to Computer Servers Creating Permanent Establishments,* 17 Vand. J. Ent. & Tech. L. 1, 28-29 (2014).

[48] *Id.* at 29.

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responsible for the operation and maintenance of the data centre equipment while employees of the US parent company managed the data centre from outside of Canada and visited the data centre from time to time…[49]

The CRA determined that the US company did not have a PE in Canada. This ruling is the first time that a country has determined that management of applications and data of a server from outside of that country does not cause the parent to have a server at its disposal and, hence, a PE.[50]

Another approach – the concept of "virtual permanent establishment" has been adopted by several countries with a view to giving solutions to the issue of server PEs.

France has generally followed the position of the OECD regarding server PEs. France has, however, made clear that the presence of a server alone will be an auxiliary activity and, hence, not constitute a PE unless there are people involved. In certain circumstances, however, the French position is that a server alone, which completely and autonomously performs an enterprise's core function, could be a PE. France does not consider this position satisfactory and released a report in 2013 that proposes a virtual permanent establishment approach, wherein data uploaded by a consumer could by itself create a PE.[51]

Under pressure from France, the European Union organized a Working Group to devise a new taxation framework to address e-commerce. The European Union established a Commission High Level Expert Group on Taxation of the Digital Economy to pursue this study. This independent group was asked to examine key issues related to taxing the digital economy in the EU, and to present their ideas on the best approach to various challenges and opportunities in this field. The report was completed after five months of work by the Group, which consisted of six other experts from across Europe with different expertise relevant to this area.[52] [53]

President José Manuel Barroso said:

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[49] *Id.* at 28.

[50] *Id.*

[51] *Id,* at 30.

[52] Taxation of the Digital Economy: High-level Expert Group presents final report, European Commission Press Release, Brussels, May 28, 2014.

[53] Gianni, *supra* note 47*,* at 30.

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> "*With the crisis focusing attention on public finances, the issue of fair taxation has moved up the agenda, for both governments and citizens. A strong and fast-growing digital sector is good for our economy, but we must also think about how best to adapt our tax systems to the online world…*"[54]

Among the main conclusions of the report were:

- The digital economy does not require a separate tax regime. Current rules may need to be adapted to respond to the digitisation of our economy.
- Digitisation greatly facilitates cross border business. Removing barriers to the Single Market, including tax barriers, and creating a more favourable business environment through neutral, simplified and coordinated tax rules is therefore more important than ever. [55]

It can be seen that the Expert Group's position clarifies that no new rules need to be developed, but current ones to be applied in the digital economy thus somehow giving priority to the approach of considering servers as PEs.

France is not the only country raising a virtual permanent establishment approach.

In a 2012 case in Spain, the Spanish Central Economic-Administrative Court held that the Spanish subsidiary of the Dell Computer group constituted a PE for a Dell Irish sales company, Dell Products Ltd.

> *Dell Products Ltd. hosted a website outside of Spain, through which Spanish sales were effected, although it had no employees in Spain. Dell Products Ltd. had a Spanish subsidiary, whose employees translated the Web pages, reviewed content, and administered the Dell website.*

The court determined that, based on the E-Commerce Chapter, Dell Products Ltd. had a virtual PE in Spain.[56]

The Second Chamber of German Supreme Tax Court has ruled that the presence of personnel is not considered to be significant in establishing a PE. As long as any equipment used fulfilled the criteria of carrying on or operating a business in a jurisdiction, then it would be

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[54] *Supra* note 52.

[55] *Id.*

[56] Gianni, *supra* note 35, at 30-31.

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considered as having a PE in that jurisdiction. The court explained that in the case of fully automated equipment, a PE can exist even in the absence of a human presence.[57] [58] [59]

At the time most of the countries adopt policies on the grounds for considering servers as having taxable presence in a country, the United Kingdom, for example, has a critical approach not considering servers and websites to have enough presence to establish a fixed place of business, and therefore they do not create a PE.[60] [61] The United Kingdom has taken the express position that a server that conducts e-commerce through a website on the server cannot constitute a PE. This position holds regardless of whether the server is owned, rented, or otherwise at the disposal of the business.[62]

As for the United States, it regulates this matter on its local level, providing a strict rule that in order to be taxed in the US, an income should be derived from the physical presence in US.

According to the US law, for a non-US person performing business activities in the United States, US federal income tax is imposed at regular income tax rates on such person's business income only if the foreign person has income that is "effectively connected" with a "trade or business within the United States." The US concept of US trade or business, as the treaty concept of PE, requires a physical presence before a country can tax an enterprise's income. Although the United States has not taken any official position on whether a server can create a PE, it would, in general, be expected to follow the OECD position. Taking into account that the US position regarding whether a computer server can create a US trade or business or a PE is unclear, in the absence of any authorities on point, however, a foreign person locating a server in the United States would be at risk that the United States would exercise taxing jurisdiction based on the server's presence, whether or not a tax treaty applies.[63]

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[57] Anna Scally & Julie Burke, *2002 update to OECD Model Tax Convention,* Irish Tax Review, Jan. 2002, https://www.taxfind.ie/document/itr_2002_Jan_7-top_doc-547635912.

[58] Zaleha Othman & Hajah Mustafa Mohd Hanefah, *Taxation, E-commerce and Determination of Permanent Establishment,* 5 (2) Malaysian Accounting Review 1, 4-5 (2006).

[59] Sweet, *supra* note 8, at 1975-76.

[60] Othman & Hanefah, *supra* note 58, at 4.

[61] Peter R. Merrill, *International Taxation of E-commerce,* 71 (11) CPA Journal 30-38 (2001).

[62] Gianni, *supra* note 47, at 27.

[63] *Id.* at 23-27.

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Law as it stands in the international tax mosaic with the different standings from domestic laws, shows an increasing tension in regard to the two different approaches. While the debate in European doctrine is mainly focused on "how" to tax internet, in US the debate focuses on "whether" internet shall be taxed at all. This tension is arguably due to the fact that "United States is the largest net exporter of internet goods and services", leaving the rest, or most of the World as a net importer. [64]

Non-OECD members who have passively participated in working TAG groups like Russia or India follow the server rule, for the interpretation of the fixed establishment rule. However, India additionally has made observations in the late amendments to the Commentary, by stating that if a website is hosted in a server in a particular location it may give rise to a PE. There seems to be no exact indications so far related to Russian jurisdiction, as there is no particular case or legislation related to these issues.[65]

India, has the view that the application of present tax rules, the resident and source basis, cannot be applied to e-commerce transactions. The Indian authorities recognized that the present tax rules lead to loss of tax revenue. [66] In the debate of a PE issue, India has determined that a server alone can constitute a PE. A confidential settlement agreement under competent authority proceedings was reportedly reached in 2003 with a US multinational company that attributed profits to an Indian server permanent establishment. Subsequently, in 2012, the India Authority for Advance Rulings determined that the server of a foreign company created a PE. In that ruling,

> *a French company intended to enter into an agreement to provide information technology services to its Indian subsidiary, with all services to be provided from France through servers owned by the French company located in India.*[67] [68]

The tax authorities ruled that the French company had a PE, relying on the India-France income tax treaty, which included machinery or equipment within its definition of a PE.

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[64] Ademi, *supra* note 25, at 24.

[65] *Id.*

[66] Janet E. Moran & Jeffrey Kummer, *US and International Taxation of Internet: Part II*, 20 (5) Computer and Internet Lawyer 16 (2003).

[67] Othman & Hanefah, *supra* note 58, at 5.

[68] Gianni, *supra* note 47, at 29-30.

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Reference was made to the Commentary in the OECD model treaty, which states that a PE can exist through automatic equipment.[69]

Singapore and Hong Kong, have also officially stated that a server by itself cannot create a PE. Singapore takes the position that the mere presence of a server is not sufficient to constitute a PE. Instead, all of the business activities of a foreign person in Singapore must be considered together, including any server that would be regarded as a communication tool. Hong Kong similarly considers all of a foreign person's operations in Hong Kong, in addition to the presence of a server. The mere presence of a server, "even if an intelligent one – i.e. capable of concluding contracts, processing payments or delivering digital goods" – would not create a PE if there are no human activities.[70]

It can be inferred that Singapore and Hong Kong give priority to the existence of human intervention when deciding on the matter whether servers constitute PEs or not.

In Malaysia, a fast developing country in the region, a PE is defined as a fixed place of business through which the business of an enterprise is wholly or partly carried on or a dependent agent who has, and habitually exercises authority to conclude contracts in the name of a non-resident. Therefore, if a foreign company sets up a branch or has a place of management, an office, a factory, a workshop or a mine, an oil or gas well, a quarry or any other place of extraction of natural resources in Malaysia then that would be deemed a PE.[71]

The justifications for adopting certain approach lie behind each country's own tax policy. It is not absolute, that one approach can be justified for the worldwide issue of server PEs, but rather it can be concluded that each country tends to adopt a position which more contributes to the developments of its economy.

Several approaches have been proposed by many scholars, such as: virtual PE approach; establishment of a threshold of gross sale of certain amount in order to tax on a PE basis; establishment of international organisations or intermediary institutions for acting as a government in virtual world and regulating taxation issues in electronic world as well as registering taxpayers; the approach to tax e-commerce on the basis of a PE whenever an enterprise receives payment form the source country, etc. However, the practice and time have

[69] *Id.*

[70] *Id.* at 27-28.

[71] Othman & Hanefah, *supra* note 58, at 5.

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shown that neither of the approaches has proved to be effective in all matters, because they all face issues at certain matters. For example, it has been an issue over the time, how to determine the parties involved in electronic transactions, how to detect the cases of receiving payments from customers worldwide. Besides, in order to achieve these goals, countries need to assist each other and follow certain information exchange policies in order to be able to trace the transactions and ensure proper taxation in this field.

To sum up almost all the countries face the issues of e-commerce taxation. Though different countries have adopted different approaches regarding this issue, it can be assumed, that none has reached to a final solution in this matter, and different ways of taxing e-commerce on the basis of a PE do not seem to be sufficiently effective. To this end, there is no unified approach, and the positions taken by different countries have not been perfect so far. Though new approaches and proposals have been suggested with a view to reaching a resolution of the issues, debates and discussions continue to be raised by experts and relevant international institutions.

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CHAPTER 3

POSSIBLE IMPLICATIONS IN THE REPUBLIC OF ARMENIA

The issue of taxation of e-commerce on the basis of a permanent establishment can meet further difficulties in the Republic of Armenia due to the fact that there are mainly no regulations of the issue.

The Armenian legislation does not regulate e-commerce, and it remains one of the most complicated areas of the tax law. It has become a growing issue of the customs authorities of the Republic of Armenia within the framework of taxation of online transactions between Armenian residents and residents of the other countries.

Armenia nowadays faces the issue of taxing the electronic transactions, but, it has not yet faced the issue of taxing residents of other countries carrying out business through servers located in Armenia. However, this may be a growing issue in the nearest future.

Article 27 of the new Tax Code prescribes the definition of a PE according to the OECD and UN model treaties.[72] But the main issue here is that Armenia does not have a formed practice of taxing e-commerce in order to apply certain approach in relevant transactions between the countries that have already formulated positions towards the e-commerce taxation issues.

Armenia provides a regulation of a PE. However, in order to apply this rule in practice, relevant time is needed to form an experience in this field.

A situation can occur in future, if, for example, a French company carries out business in Armenia through servers, and an Armenian resident has servers located in France. Such an issue will be subject to regulation by the France-Armenia Tax Treaty.[73] The treaty provides for the definition of a PE, and according to the treaty, countries will tax the taxable presence of each other in another country, and the issues, such as the ones related to e-commerce taxation, will be left to regulation by domestic legislation. However, as the analysis has shown, France has a relevant practice in considering a server as a PE, whilst Armenia can face the issue of taxing the presence of a French resident's server located in the territory of the Republic of Armenia due to non-regulation of it and absence of practice. Taking into account that there are

[72] Tax Code of the Republic of Armenia, *adopted* on Nov. 4, 2016.

[73] Income Tax Treaty France Armenia for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, *in force* since May 1, 2001.

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notable differences in the approaches of taxing a "permanent establishment" of a non-resident, this situation can lead to a problem especially in the scope of e-commerce taxation where France has a developed approach in this matter, and Armenia does not have any regulation for the issue.

There has to be developed practice of taxing electronic transactions as traditional in order to apply the rules of a PE. On the other hand, to apply a certain country's relevant approach, there should be sound grounds, for example, justifications for the tax policy. It is evident, that Armenia is a developing country in this matter. Taking into consideration the new steps taken in this field, the degree of development of e-commerce in the Republic of Armenia, with a view to creating preferable conditions for the economy to grow, Armenia may even adopt an approach of not taxing e-commerce at all. As the analysis has shown, certain countries, the economy can, in many aspects, be similar to that of Armenia, tend to not consider servers as PEs. The reasons behind such policy can be the intent to create conditions for the growth of the economy by giving some kind of benefits for the electronic commerce. Thus, Armenia needs to take account of all the facts, advantages and disadvantages of treating servers as PEs for the taxation purposes in order to adopt a policy more considerable and beneficial for its own economy and legal system.

As far as explored, the Armenian tax system has many similarities to the one of Russia. Taking into account the similarities, and the fact, that there seems to be no specific and exact regulation of this issue in Russia as well, it can make the task difficult for Armenia to adopt an approach at least experienced by a country the tax system of which is quite similar to the one of Armenia. However, considering the analysis made with regard to different countries, for example the ones not developed very much economically, the approach of them not to consider servers as PEs cannot also seem to be a solution.

So far the Armenian tax system, in general, has not faced the issue of taxing e-commerce on the basis of a PE. The failure to regulate the issue, though may give an economy a chance to grow and develop further thus making the county a destination of worldwide electronic transactions, but on the other hand, may lead to the issue of non-taxation. If e-commerce remains unregulated or vague, the consequence can be, that by the time the Tax Code applies, countries may consider the territory of the Republic of Armenia a tax haven for business purposes. Therefore, the failure to provide for certain solutions now may lead to a problem in the future.

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Furthermore, if there is no regulation in the Tax Code at present, if it is amended later providing taxation regulations for e-commerce in the future, this approach can be unfair to the countries doing business through servers in Armenia, and can prevent them or discourage from continuing to do so further. Overall, it is better to provide for a somehow possible and fair solution by now, rather than waiting the issue to arise and become urgent to take measures aimed at the solutions of it later.

A sample approach could be a determination of a certain threshold and time-limit for the taxation to occur. At the same time, in order to encourage the development of economy as well, in case of Armenia the solution could be in a way of giving kind of tax benefits for the newly started businesses to develop, until reaching a specified threshold of the amount of income received through servers located in Armenia, and for a certain period of time, for example one year. However, a kind of reservation is needed in order for this rule to apply to the specific taxpayers in cases, where, for example, they move their servers from Armenia and then later start to do business in Armenia again. This kind of reservation is essential for preventing the cases of not falling within a specified time-limit and income-threshold and then just simply ending the business in Armenia thereafter.

One of the best and preferential approaches for Armenia, in my opinion, can be amending the legislation by adding relevant regulations for taxing e-commerce in order to make it fall under the taxation on the basis of a PE, meanwhile, those regulations should not be strict, but rather beneficial for the taxpayers, allowing the economy to grow and the electronic commerce to enhance in Armenia, but at the same time, not making Armenia a tax haven for different countries. This solution can ensure a proper taxation and tax privileges for the taxpayers for locating their servers in the territory of the Republic of Armenia, and at the same time can prevent from losing those taxpayers in case of amending the legislation and even if making those regulations stricter in the future. Armenia is a developing country, and recent years, notable progress has been achieved also in the field of IT industry. The creation of beneficial conditions for conducting business in Armenia thorough servers could promote this trend as well, and create opportunities for our country's economy to faster and easier engage in the worldwide economy and developments.

Concluding the research that I have done with regard to the issue presented, I consider it possible for our country to adopt a beneficial approach in addressing this worldwide issue, which could be in this case the regulation of e-commerce. I refrain from proposing specific provisions of regulations, as it is a task of not only lawyers, but economists and other relevant

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specialists as well, however, I suppose, that, at present, one of the best options could be regulating the issue not in a strict or neutral level, but to the extent providing for a ground for further regulation.

However, as a newly adopted legislation, the Tax Code needs to be applied and tested to make issues more obvious and foreseeable. At this moment, I consider it our responsibility to make it as effective within the scope of the regulation of tax issues as possible prior to entering into force and regulating the taxation in a new and updated way.

It is a need to have relevant provisions providing for the taxation of e-commerce, and it is a necessity to ensure possibilities for our country to develop economically and enter into the international level of commerce and taxation with an internationally developed and adopted practice.

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CONCLUSION

The issues of e-commerce and permanent establishment may be endless. By the time the economy develops, more sub-issues arise in this field. The e-commerce related issues such as determination of the country that has the jurisdiction to tax the income, classification of income to business profits or royalty and rent, establishing principles for tax administration and enforcement still do not seem to find proper solutions.

Though some of the issues in the field of e-commerce taxation have found certain solutions, many of them, however, still seem to be unsolved. The main findings and conclusions reached though research of the relevant materials, are as follows:

1. The electronic transactions need to be taxed in a similar way as conventional commerce in order to comply with the neutrality principle, however, this aim is not always followed and achieved;
2. The approach of considering income from the lease or license of certain electronic property more as business profits rather than royalties, has proved to be more effective, but has its positive and negative implications as well;
3. The e-commerce should be taxed on the basis of a PE, but with the proper regulation of the issue (based on the situs, locus and tempus tests);
4. Servers should be considered as a taxable presence in a country within the framework of a PE, but websites should not create a PE due to the fact that servers meet the qualifications for physical presence;
5. And finally, activities that are preparatory or auxiliary, should not be deemed as creating a PE.

The problem of e-commerce taxation on the basis of a PE has not so far reached a conclusion though relevant efforts have been made by countries and legislators to address the issue.

Various countries have adopted different approaches in their attempt to reach a solution of the e-commerce taxation issue, but the reasons behind it are deeper: the jurisdictions and taxation mechanisms of the countries, the resources available for the development of e-commerce in the relevant jurisdiction, the existing tax policy or the ways of establishing stricter tax policy in certain cases in order to stricter regulate or impose certain limitations in this field. Thus distinct reasons lie behind each country's position on the issue involved, and a universal

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approach may not seem to be applicable and effective. As a result, efforts by tax and legal experts to apply conventional international tax principles to the electronic world do not seem to be successful yet.

The solution can be deemed to be somehow achieved in that certain countries have adopted the approach of taxing a server as a physical presence in their country, but even that approach creates issues in terms of tax avoidance and especially time requirements for creating a taxable presence. I suppose that it is not possible and effective to have one uniform approach worldwide in taxing e-commerce on the basis of a PE. In contrast, the specific approach should better be based on the relevant practice and stage of economic development of each country.

As for the Republic of Armenia, it can be of urgent need to provide for a more accepted and appropriate approach in order to avoid the issue of non-regulation of one of the most difficult tax issues worldwide. It is better to think about the problem prior to its emergence and to adopt the relevant regulations before facing the unsolved issues.

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