Because not always B comes after A: Critical Reflections on the new Article 12B of the UN Model Tax Convention on Automated Digital Services.

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Summary. **I. Introduction and scope of this contribution. II. A critical analysis of the restrictive interpretation of article 12 A of the UN Model Tax Convention: which services are of a technical managerial or consultancy nature? III. The introduction of article 12 B in the UN Model Tax Convention 2021: not only unnecessary but also disturbing.** III. 1. Article 12B undermines the institutional credibility of the Committee of Experts and of the UN Model Tax Convention. III. 2. Article 12B generates spillover effects on the interpretation of DTCs containing specific clauses for the taxation of services. III.3 Article 12B exacerbates the qualification problems already raised by the restrictive interpretation of Article 12A contained in the Commentaries to the UN Model Convention. III.4 Article 12B generates asymmetries in the tax treatment of Fees for Technical Services and Automated Digital Services. *III.4.1 Different tax rates limits on Fees for Technical Services and Automated Digital Services. III.4.2 Different treatment for B2C services under articles 12A and 12B. III.4.3 Different treatment for FTSs and ADSs paid for teaching activities. III.4.4 Gross taxation for FTSs and elegible net taxation for ADSs.*

I. Introduction and scope of this contribution.

Proposals to try to meet the challenges of the digital economy through a more or less extensive system of withholding taxes at source are a not great novelty[1]. However, in recent times, these proposals have gained new academic impetus in parallel with the work that, since 2013, and in line with the BEPS Plan, the Organisation for Economic Cooperation and Development (OECD) has been developing concerning taxation of the digitalized economy[2].

However, these proposals do not seem to have found their way into policymakers' work in international taxation, at least as far as the Organization for Economic Cooperation and Development (OECD) is concerned. Indeed, although the first report issued by the OECD under Action 1 of the BEPS Plan on the taxation of the digital economy showed a withholding tax on digital transactions as a possible option to tackle the broader direct tax challenges of the digital economy - together with the so-called new nexus based on the concept of significant economic

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[1] In this sense, the innovative proposal of Doernberg – a withholding tax by the State of residence of the service recipient on any payment to a non- resident service provider that erodes the tax base of the service recipient- was particularly noteworthy when it was not even possible to foresee the importance that the digital economy would acquire in the following years: Doernberg, Richard L. *Electronic Commerce and International Tax Sharing.* /In/ 16 Tax Notes International, Mar. 30, 1998, pp. 1013-1022.

[2] See: Báez Moreno, Andrés; Brauner, Yariv. *Withholding Taxes in the Service of BEPS Action 1: Address the Tax Challenges of the Digital Economy*. /In/ White Papers Series, IBFD, 2015. Báez Moreno, Andrés. Brauner, Yariv. *Tax Policy for the Digitalized Economy under Benjamin Franklin´s Rule for Decision Making.* /In/ Tax and the Digital Economy. Challenges and Proposals for Reform. (W. Haslehner *et al.* eds.). Aalphen and de Rijn: Wolters Kluwer, 2019, pp. 67-100. Báez Moreno, Andrés; Brauner, Yariv. *Taxing the Digital Economy post BEPS…Seriously.* /En/ Vol 58, Columbia Journal of Transnational Law, 2019, No. 1, pp. 121-188.

presence and the equalization levies[3]- the Interim Report, approved less than three years later, poured cold water on the hopes of those who saw withholding taxes as a feasible and straightforward alternative to face the colossal difficulties of taxing the digitalized economy. In fact, this new report rejected the withholding solution, labeling it unilateral and uncoordinated[4] and blaming it for major technical flaws[5]. The above explains why the reference to the withholding option has disappeared in the Inclusive Framework's subsequent work concerning the taxation of the digitized economy except perhaps as a mere accessory mechanism to some of the rules that make up the GloBE under Pillar 2 proposal.

Things are way different from the perspective of the evolution of the UN Model Tax Convention. Indeed, in 2017, Article 12 A was incorporated into the UN Model, which, in essence, attributes taxing rights to the source State regarding technical, managerial, and consultancy services (FTSs from now on) in the absence of a Permanent Establishment (PE from now on) and even in the absence of physical presence of the service provider in that state. Although the project to introduce this provision in the Model began without any link to the digital economy's taxation[6], its promoters soon perceived its importance in this area and recorded it accordingly in the Commentaries to Article 12A[7]. Beyond these mentions, it seems evident that a distribution rule attributing taxing rights on services to the source State in the absence of a PE represents a paradigm shift in the distribution of taxation powers concerning business profits; this shift might be particularly relevant in the digitalized economy that essentially revolves around the provision of digital services not requiring, by definition, the physical presence of the provider and, even less, the existence of a PE[8]. However, the brand new Article 12A committed *hara-kiri* when its Commentaries excluded from its scope services of a routine nature[9] and, therefore, most of the digital advertising and intermediation services that, as is well known, constitute the essential core of the digital economy. The logical consequence of this self-restraint has been that, when the UN Committee of Experts on International Cooperation in Tax Matters (the Committee from now on) finally became aware that a withholding tax on services could be a rational alternative to meet the challenges of taxing the digital economy, it has been forced to promote the introduction of a new distribution rule in the UN Model Tax Convention that would indeed cover those services that Article 12A left out.

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[3] OECD/G20. *Addressing the Tax Challenges of the Digital Economy ACTION 1: 2015 Final Report.* Paris: OECD Publishing, 2015, pp. 107-117.

[4] OECD/G20. *Tax Challenges Arising from Digitalisation –Interim Report 2018*. Paris: OECD Publishing, 2018, p. 135.

[5] However, apart from the complex operation of a withholding tax concerning business to consumer services, the fact is that the difficulties and dangers reported in the Interim Report are common to all so-called unilateral actions and are not exclusive to the withholding option (see OECD/G20. *Tax Challenges Arising from Digitalisation – Interim Report…op. cit.* pp. 178-190).

[6] The project was launched in 2009 and, therefore, long before the BEPS Plan included the taxation of the digital economy as one of its key concerns. For the initial historical development of this project see: Báez Moreno, Andrés. *The Taxation of Technical Services under the United Nations Model Double Taxation Convention: A Rushed – Yet Appropriate – Proposal for (Developing) Countries?*/In/ World Tax Journal, Issue 3, 2015, pp. 268-270.

[7] ComUN, art. 12 A, par. 2.

[8] On the growing importance of services in the digitized economy: Báez Moreno, Andrés. Brauner, Yariv. *Tax Policy for the Digitalized Economy…op. cit.* pp. 78-79. Báez Moreno, Andrés. *Cross Border Taxation of Services*. /In/Research Handbook on International Taxation (Y. Brauner ed.). Cheltenham: Edward Elgar Publishing, 2020, pp. 78-79.

[9] ComUN, art. 12 A, paras. 61-68; 83-98. The purported foundations of this restrictive approach will be critically analyzed in section II of this paper.

Indeed, during the 21st session of the Committee, held between October 20 and 29, 2020, members voted to include an article 12B on automated digital services (ADS from now on) in the 2021 Model Convention[10] in line with the proposal put forth by a drafting group coordinated by the Committee members Mr. Carlos Protto and Mr. Rajat Bansal (the proposal from now on)[11]. Apart from two important specific issues that we will refer to in detail below, the proposal essentially mirrors the basic structure of Article 12A with the only difference that its scope does not refer, like the latter, to technical, managerial, or consultancy services but automated digital services.

This paper does not intend to pronounce on the merits of a WTH on services as a solution to the enormous problems posed by the taxation of cross-border income generated within the digitalized economy, nor does it intend to expose its advantages and disadvantages concerning other alternatives already implemented or that may be implemented in the future as a result of the work developed in recent years by the OECD[12]. The intention of this new publication is much more modest: assuming that the UN Committee of Experts and the Model Convention it administers seem to have opted, unequivocally, for a withholding tax on services as a way to meet the challenges of taxing the digital economy it asks whether or not the new Article 12B covering ADSs is a good option in view, above all, of the existence, since 2017, of Article 12A dealing with FTSs. Following this *leitmotif* the rest of this article is organizes as follows: Section 2 explores whether or not the new Article 12B was necessary, on the assumption that only a restrictive and erroneous interpretation of Article 12A of the Model allows ADSs to be excluded from the scope of application of the latter. Section 3 analyzes some of the severe problems generated by introducing the new article 12B, focusing, above all, on its difficult coexistence with article 12A.

II. A critical analysis of the restrictive interpretation of article 12 A of the UN Model Tax Convention: which services are of a technical managerial or consultancy nature?

As we have already indicated, the introduction, in 2021, of a new article 12B in the UN Model Tax Convention attributing taxing rights to the source State on income arising from the provision of ADSs ended up becoming necessary, thanks to a restrictive interpretation of the scope of application of article 12A that had been incorporated into the Model in 2017. Indeed, although the Commentaries to Article 12A rightly saw the enormous potential of this rule to address the taxation of the digitized economy[13], those same Commentaries concluded that automated digital services, which constitute precisely the essential core of that digitized

[10] See Committee of Experts on International Cooperation in Tax Matters. *Committee of Experts on International Cooperation in Tax Matters Report on the twenty-first session (virtual session, 20–29 October 2020).* E/2021/45/Add.1-E/C.18/2020/4, pp. 18-21.

[11] Committee of Experts on International Cooperation in Tax Matters. *Tax consequences of the digitalized economy – issues of relevance for developing countries.* E/C.18/2020/CRP.41, pp. 9-28.

[12] This comparative work has already been carried out in previous publications as the OECD released its provisional conclusions on the most appropriate way to tax the digitalized economy: Báez Moreno, Andrés; Brauner, Yariv. *Withholding Taxes in the Service…op. cit.* Báez Moreno, Andrés. *A Note on Some Radical Alternatives to the Existing International Corporate Tax and Their Implications for the Digital(ized) Economy.* /In/ Intertax, Volume 46, Issue 6&7, 2018, pp. 560-564. Báez Moreno, Andrés. Brauner, Yariv. *Tax Policy for the Digitalized Economy…op. cit.* pp. 67-100. Báez Moreno, Andrés; Brauner, Yariv. *Taxing the Digital Economy post BEPS…Seriously...op. cit.* pp. 121-188.

[13]

economy, could not be qualified as technical, managerial or consultancy services. This restrictive interpretation was built upon two pillars: on the one hand, the idea that the term FTSs, contained in Article 12A, should be disassociated from the concepts of the domestic law of the Contracting States; on the other hand, on the basis that the fundamental concept underlying the definition of FTSs is that the services must involve the application by the service provider of specialized knowledge, skill or expertise on behalf of a client something that, by definition, would exclude services of a routine nature. These conceptual approaches are complemented in the Commentaries with the analysis of a series of examples according to which non-customized database access services[14], services corresponding to standard insurance contracts[15] and routine financial services[16] cannot be qualified as FTSs and, therefore, fall outside the scope of application of Article 12A of the Model. Although not expressly mentioned in the Commentary, it is easy to deduce that, according to this interpretation, most ADSs will also be excluded from Article 12A. In the opinion of this author, the theoretical foundations on which this restrictive interpretation is based are erroneous, as we will try to demonstrate in the following pages.

To achieve the restrictive interpretation of the concept of FTS, the Commentaries rule out any possible influence of the domestic law of the Contracting States when defining FTSs. To this end, the Commentaries rightly indicate that Article 12A does not refer to the Contracting States' domestic law[17]. More adventurously, the Commentaries also insist that Article 12A (3) contains a definition of FTSs[18] and that it would be inconsistent with that very definition for its terms to be determined in accordance with the domestic law of the country applying the treaty under article 3 (2) of the Model[19]. Utilizing this interpretative maneuver, the Comments undoubtedly seek to remove from the conventional concept of FTS the domestic regulations that include under the concept of technical services also services of a routine nature[20] and to avert the possibility that a Contracting State may, through a mere reform of its domestic law, extend its powers of taxation under Article 12 A[21]. It should, of course, be recognized that unlike other provisions of the UN Model -like for instance, Articles 4 (1) or 10 (3) of the UN Model-, Article 12A does not contain any implicit or explicit reference to the domestic law of the Contracting States at least as far as the concept of FTSs is concerned; however, to rule out any influence of national law on this basis would be a methodological error and, in the view off the author, a deliberate disregard of the mandate contained in Article 3(2) of the Model. Indeed, in the presence of a term not defined in the Convention, Article 3(2) requires recourse to that term's

[14] ComUN, art. 12 A, paras. 90-91.
[15] ComUN, art. 12 A, paras 92-93.
[16] ComUN, art. 12 A, paras. 94-96.
[17] ComUN, art. 12 A, par. 68.
[18] ComUN, art. 12 A, paras. 61; 62 and 68.
[19] ComUN, art. 12 A, 68 *in fine.*
[20] See regarding the concept of what constitutes "technical services" according to the domestic Law of several countries: Pickering, Ariane. *General Report.* /In/ IFA Cahiers – Volume 97A, Enterprise Services- , IFA, 2012, p. 33.
[21] Although this is merely suggested in the Commentaries themselves (ComUN, art. 12 A, par. 68), Professor Brian Arnold has made this purpose clear in some of his academic work: Arnold, Brian. *The New Article on Fees for Technical Services in the United Nations Model Convention.* /In/ Celebrating Twenty Years of the International Tax Program of the New York University School of Law (H. David Rosenbloom ed.). New York: New York University School of Law, 2016, p. 171.

meaning under the Law of the State applying the treaty, unless the context otherwise requires. In this context, although the very concept of "term not defined in the treaty" may sometimes be debatable, what seems quite clear is that neither the third paragraph of Article 12A of the Model nor any other of its paragraphs defines, even partially, the term *Fees for Technical Services*. The Commentaries indicate that "*Paragraph 3 defines "fees for technical services" as payments for managerial, technical or consultancy services*"[22]. However, if the dictionary defines definition as "*a formal statement of the meaning or significance of a word, phrase or idiom*" it seems complicated to conclude that Article 12A (3) defines FTSs; indeed, the provision merely restricts (qualifies in a grammatical sense) which services, among all the existing ones, are covered by that article. In this sense, Article 12A neither defines the noun "services"[23] nor the qualifying adjectives -technical, managerial, or consultancy- that delimit the services covered by the provision. The thesis that we hold here is, in fact, the same as that held by the Subcommittee on Services when, in 2012, it submitted a note to the Committee of Experts offering three possibilities for determining the type of services that should be covered by the new rule[24]. Among them was the possibility of referring to "technical, managerial or consultancy services" but leaving those terms undefined in the article as opposed to the other two options which, referring in the same way to the types of services mentioned, added an inclusive or exclusive definition of FTSs in the very article[25]. It is not easy to understand why what in 2012 was a mere undefined reference in the new Article, is presented in the Commentaries to Article 12A of 2017 as a definition which is additionally qualified as exhaustive[26]. In these circumstances, being clear that Article 12A does not define but merely lists different types of services covered, recourse to the law of the Contracting States or the construction of a conventional autonomous concept of FTSs will depend, as so often, on whether or not the context requires dispensing with domestic law.

The text of Article 3(2) of the OECD and UN Models is so obscure and the positions held by the doctrine and jurisprudence so opposed that the author prefers not to take sides, in a paper of this nature, on whether or not the context of the relevant DTC requires separation from an interpretation of the concept of FTS in line with the domestic law of the Contracting States; on the contrary, we will give our opinion on the possible interpretations of that concept based on the domestic law of the Contracting States and also on the possible construction of a conventional autonomous concept of *Fees for Technical Services*. Thus, two scenarios must be distinguished:

i) The national law of the State that applies the DTC is used to find the meaning of the concept of *Fees for Technical Services* since the convention does not define it, and its context does not require otherwise. This scenario will be rare; as rare as it is, in short, that domestic law defines or attributes a precise meaning to the concept of technical services. In fact, these definitions are rather exceptional in Comparative Law[27]. Indeed, if the law of the State applying the treaty does

[22] ComUN, art. 12 A, par. 62.
[23] As the Commentaries explicitly aknowledge: ComUN, art. 12 A, paras. 83-84.
[24] Committee of Experts on International Cooperation in Tax Matters, *Follow Up Note on Taxation of Fees for Technical Services and Comments on that Note.* E/C.18/2012/CRP.4, pp. 4-6.
[25] See E/C.18/2012/CRP.4, pp. 5-6.
[26] ComUN, art. 12 A, par. 61.
[27] Pickering, Ariane. *General Report...op. cit.* p. 33.

not provide a meaning for the term contained in the treaty there is no room for a resource to the domestic law of that State[28]. On the other hand, in the (probable) hypothesis, that taking advantage of the use of the *lex fori*, a Contracting State may, through a mere reform of its domestic law regarding FTSs, extend its powers of taxation under Article 12A, it has been argued that this would be one of those cases in which the context requires otherwise and, therefore, the construction of a conventional autonomous concept would be necessary[29]. However, possible recourse to domestic law should not be systematically discarded. Some of the countries that have recently been more belligerent in defending the introduction in their DTCs of provisions allowing the taxation of income from technical services at source in the absence of PE or the physical presence of the service provider have definitions[30] or, at least, precise meanings[31] of the concept of FTSs in their respective domestic laws. In this context, it is evident that the coincidence of the concept of technical service with that detached from the Commentaries to the UN Model Tax Convention - and therefore the exclusion from the scope of the rule of automated services - will depend on how the concept of FTS is interpreted in the law of the Contracting State concerned. The truth is that most of the countries that have a definition or sources in their domestic law that allow determining the meaning of the term FTSs seem to lean towards a broad understanding of the term referring to all those services that require specialized technical knowledge on the part of the service provider[32]. In fact, India seems to be the only country whose domestic concept of FTSs aligns with the restrictive interpretation in the Commentaries to the UN Model Convention described above, which has the effect of excluding automated services[33]. As we will have the opportunity to see later on - when we analyze the concept of FTSs at a conventional level - this restrictive interpretation

[28] Rust, Alexander. *Article 3. General Definitions.* /In/ Klaus Vogel on Double Taxation Conventions. Volume I. Fourth Edition. Aalphen and den Rijn: Wolters Kluwers, 2015, Art. 3 m.no. 111 and 126.

[29] Rust, Alexander. *Article 3. General Definitions…op. cit.* Art. 3 m.no. 124. This idea is also contained, in a way, in the Comments to the OECD and UN Model Convention when they state that "…*the wording of paragraph 2 provides a satisfactory balance between, on the one hand, the need to ensure the permanency of commitments entered into by States when signing a convention (since a State should not be allowed to make a convention partially inoperative by amending afterwards in its domestic law the scope of terms not defined in the Convention)* […]" (Comm. OECD, Art. 3, par. 13; Comm UN, Art.3 par. 14.

[30] For instance Brazilian Tax Authorities have defined "technical services" as *work, endeavor, or undertaking of which the execution depends on specialized technical knowledge by its provide* (see Rocha, Sergio André. *Brazil.* /In/ IFA Cahiers – Volume 97A, Enterprise Services- , IFA, 2012, p. 158). Although it is not possible to go into this question in more detail here, the date of the administrative pronouncement containing the definition - Normative Instruction no. 252/2002, in any case much later than most of the Brazilian DTCs that allow the taxation at the source of technical services - and the illegality that many Brazilian authors have attributed to this resolution (see for details Rocha, Sergio André. *Brazil...op. cit.* p. 158) could lead one to believe that we are dealing with one of those cases in which a Contracting State manipulates domestic law to obtain taxation rights that, in the absence of such manipulation, the DTC would not grant. As we have already indicated, there is some agreement that the context would require not resorting to domestic law in these circumstances.

[31] There is an agreement that Indian Law contains no statutory definition of the term "technical" in the domestic concept of FTSs, being the understanding of this term primarily driven by judicial precedents (see Bhattacharya, Saura; Sanghavi, Dhaval. *India.* /In/ IFA Cahiers – Volume 97A, Enterprise Services- , IFA, 2012, pp. 360-362. However, this should not be an obstacle to recourse to domestic law as a result of the application of Article 3(2) of the corresponding DTC if it is borne in mind that this provision does not require that domestic law contain a definition but only that it be possible to infer the meaning of the term from it, something that, of course, can be done using case law as a starting point (against this background: Rust, Alexander. *Article 3. General Definitions…op. cit.* Art. 3 m.no. 113.

[32] Although the statement made in the text perhaps required a detailed analysis of comparative law, that is the impression drawn from the reading of the General Report prepared by Pickering in connection with Issue 1 (Enterprise Services) of the 2012 IFA Congress (see Pickering, Ariane. *General Report...op. cit.* p. 33).

[33] As the Committee itself acknowledged years ago: See E/C.18/2012/CRP.4, p. 6.

lacks technical foundations; in any case, it is now sufficient to conclude that, even in a *lex fori* application scenario, the concept of FTSs will usually be interpreted in a broad sense, thus including automated digital services as well; from a pure fiscal policy point of view, it makes perfect sense that a concept formulated in domestic law in an extraordinarily comprehensive manner should not be subject to an unusually narrow interpretation, which, moreover, completely deprives it of utility in the context of the digital economy.

ii) The concept of "Fees for Technical Services" is interpreted autonomously at a treaty level based on the rules of interpretation set out in the Vienna Convention on the Law of Treaties (VCLT), because although the terms are not defined in the DTC itself, the context requires so. Although, as indicated above, the Commentaries on Article 12A do well - at least in many cases - to disregard the meaning attributed to the term FTSs by the domestic law of the Contracting States, it is more difficult to say that they have resorted to the criteria of interpretation of the VCLT for the proper interpretation of the concept. In this context, the problem is not so much that the Commentaries do not refer to the interpretation criteria in Articles 31 to 33 of the VCLT either explicitly or implicitly but that they do not apply them. This issue should be carefully analyzed.

The restrictive interpretation of the FTS concept advocated by the Commentaries seeks to be based on the terms of the treaty itself and, therefore, precisely on what must be the starting point for any interpretation of a treaty rule. Indeed, the Commentaries indicate that the fundamental concept underlying the definition of FTSs is that the services must involve the application by the service provider of specialized knowledge, skill or expertise on behalf of a client and all this allegedly based upon the ordinary meanings of the terms "managerial," "technical" and "consultancy"[34]. It is precisely the lack of this common element that makes it possible - still according to the Commentaries[35] - to exclude services of a routine nature and, therefore, automated services from the scope of application of Article 12A. If, following the peaceful interpretation of Article 31(1) of the VCLT and in general of any rule of domestic law that refers to the grammatical canon of interpretation, the determination of the ordinary meaning of a term can be drawn without problems from dictionaries[36] the starting point of the Commentaries does not seem wrong at first sight. Indeed, according to the dictionaries in use and also according to common sense, what is common to technical, managerial, or consultancy services and, I would dare say, to any services, especially in a cross-border context, is to require specialized knowledge, skill, or expertise in the service provider. Now, what is impossible to understand, from a purely grammatical point of view, is why a routine service and, by extension, also an automated service does not involve the application by the service provider of specialized knowledge, skill, or expertise on behalf of a client. If the treaty provision or its alleged ordinary meaning included a reference to *an immediate application of specialized knowledge, skill or expertise on behalf of a client* there would be (at least) a grammatical basis for the distinction between routine and customized services pretended by the Commentaries. In the absence of this grammatical nuance, a service provider applies specialized knowledge, skill, or expertise in a

[34] ComUN, art. 12 A, par. 62.
[35] ComUN, art. 12 A, par. 62 *in fine.*
[36] Dörr, Oliver. *Article 31. General Rule of Interpretation.* /In/ Vienna Convention on the Law of Treaties. A Commentary. Second Edition. (O. Dörr; K. Schmalenbach eds.). Berlin: Springer, 2018, p. 581.

mediate way - when creating the structures, algorithms, or platforms necessary for the provision of automated services[37] - or in an immediate way when providing any other type of services[38]. Thus, from a purely grammatical point of view, technical, managerial, or consultancy services are FTSs and are covered by Article 12A of the UN Model whether they are routine and automated or not[39].

In constructing their restrictive interpretation of the concept of FTS, the Commentaries appear to have paid no attention either to the context of the term *technical, managerial, or consultancy services*, which, again, Article 31(1) of the VCLT requires considering. The VCLT requires, first and foremost, consideration of the text of the treaty as a whole, before turning to other agreements and instruments mentioned in the concept of context referred to in the second paragraph of article 31 of the VCLT[40]. Although the text of the UN Model does not offer excessive contextual material to resolve the issue in dispute here, we should refer to other provisions in the Model whose wording and unanimous interpretation do not point precisely to the restrictive interpretation of the concept of FTSs intended by the Commentaries; in this regard, the following merits mention: i) Article 5(3)(b) of the UN Model Tax Convention has been regulating, since the creation of the Model in 1980, the so-called Services-PE deeming the existence of a PE when an enterprise furnishes services, *including consultancy services*, for some time within the other Contracting State. The reasons for adding this explicit reference to consultancy services, which by the way, does not appear in the alternative services PE provision of the OECD Model[41], have never been clear[42]. In any event, if, as the Commentaries claim, the fundamental concept underlying the definition of FTSs - given the ordinary meaning of the terms *technical*, *managerial*, and *consultancy*- is that the services must imply the application by the service provider of specialized knowledge, skill or expertise on behalf of a client and this allows routine and automated services to be excluded from the scope of Article 12A of the Model, it should also be concluded, for the sake of systematic consistency, that routine, and automated consultancy services are also excluded from the scope of Article 5(3)(b) of the Model. It is a fact that the Commentaries to the UN Model have never included such nuance concerning consulting services taxed in the Source State under Article 5(3)(b). Nor has

[37] As, on the other hand, the Commentaries themselves recognize implicitly when pointing out, in line with one of the examples they use - the one referred to a Company collecting organizing and maintaining databases - that: "*Although R Company used its knowledge, skill and expertise in creating the database, the services that R Company provides to S Company – access to the database- are routine services that do not involve the application of R Company´s knowledge, skill and expertise for the benfit of S Company*" (ComUN, art. 12 A, par. 90).

[38] As I previously stated in connection with draft article 12A and the proposed Commentary accompanying it: Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* pp. 300-301.

[39] This was precisely the position held by the Subcommittee on Services of the UN Committee not so many years ago when it stated: " *Alternatively, the terms might be given their ordinary meaning in accordance with Article 31(1) of the Vienna Convention on the Law of Treaties. The difficulty is that the ordinary meaning of "technical" is very broad and could encompass all services. For example, the relevant meaning of "technical" in the Shorter Oxford English Dictionary is "pertaining to, involving, or characteristic of a particular art, science, profession, or occupation or the applied arts and sciences generally."* (See E/C.18/2012/CRP.4, p. 5).

[40] Dörr, Oliver. *Article 31. General Rule of Interpretation…op. cit.* p. 582.

[41] ComOECD 2017, art. 5, par. 144.

[42] It has been suggested that the explicit reference to *consultancy services* seems to be made solely by way of example (Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* p. 298).

scholarship referred to such a restriction, assuming that the Services-PE covers any service[43]. ii) Unlike the OECD Model, the UN Model Tax Convention retains article 14, a specific distribution rule referring to independent personal services covering income derived by a resident of a Contracting State in respect of professional services or other activities of an independent character. If the adjective *professional* is defined as *relating to a job requiring skills learned through training or education*, one could expect that its scope of application would also be limited to the services involving the application by the service provider of specialized knowledge, skill, or expertise on behalf of a client and thus leave out services of a routine nature. Indeed, the fundamental concept underlying the definition of FTSs, according to the interpretation of the Commentaries, identified with the fact that the services must involve the application by the service provider of *specialized knowledge, skill or expertise* is very similar, if not identical, to the meaning usually attributed to the term professional, which requires, as we have seen above, that the job carried out *requires skills learned through training or education*. However, neither the Commentaries to the UN Model Tax Convention - before and after 2017 - nor the Commentaries to Article 14 of the OECD Model Tax Convention - when the Model still contained a specific provision referring to independent personal services - have ever excluded routine services from the scope of application of this rule. The only relevant exclusion that the Commentaries reflect refers to commercial and industrial activities[44] with very little to do with the issue at stake here.

In any case, beyond the grammatical and contextual arguments presented above, it is probably a purposive argument that most demonstrates the errors made by the Commentaries to the Model in proposing a restrictive interpretation of the concept of FTS. According to the Commentaries to the UN Model, three purposes appear to have been pursued in introducing Article 12A into the Model. On the one hand, to reduce the legal uncertainty concerning the taxation of services at source that had been posed by the always tricky delimitation between services and royalties and the divergent interpretation, in different jurisdictions, of the concept of "*information concerning industrial commercial or scientific experience*" contained in Article 12(3) of the UN Model[45]. Secondly, the Model Commentaries also refer to the limitation of *base erosion* as the basis for Article 12A, meaning the fact that income derived by non-residents might be deductible against the tax base of the source country whereas, in the absence of that provision, the source State might not offset that deduction with a tax on those fees[46]. Finally, the Commentaries also argue that the inability of source States to tax FTSs paid to non-resident service providers may entail, under certain circumstances, a tax advantage over domestic providers who are subject in any case to domestic tax at the ordinary rate applicable to business profits[47]. Of course, the consistency of many these purported purposes and even their usefulness in justifying a purposive interpretation of the terms contained in article 12A might be

[43] Arnold, Brian. *The Taxation of Income from Services under Tax Treaties: Cleaning up the Mess.* /In/ Bulletin for International Taxation, 2011, p. 63. Arnold, Brian J. *Article 5: Permanent Establishment*. /In/ Global Tax Treaty Commentaries, at 5.1.1.2.4. Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* p. 298.
[44] ComUN, art. 14, par. 10 (reproducing literally ComOECD 1997, art. 14, par. 1.
[45] ComUN, art. 12 A, paras. 4-6.
[46] ComUN, art. 12 A, paras. 7-10.
[47] ComUN, art. 12 A, par. 11.

questioned[48]; moreover, it is by no means less true that distributive rules in DTCs do not always support teleological interpretation, at least not with the clarity with which other (tax) rules do[49]. Be it as it may, and with all the difficulties that this conclusion entails, I believe it can be categorically stated that the exclusion of routine services from the scope of application of Article 12A of the UN Model Tax Convention is not consistent with any of the purposes attributed to this provision. Indeed, the exclusion of routine services not only prevents solving the problems of legal certainty that existed before its introduction in the Model but, instead, increases them since, on the one hand, most of the countries that already tax FTSs in their domestic law do not apply such exclusion[50] and, on the other hand, such an interpretation forces - and this is not an easy task - to distinguish between routine and non-routine services[51]. If the rationale upon which article 12A is based should be identified with the effect generated by base eroding payments with no corresponding source taxation, it does not seem to make any sense excluding certain payments (regarding, for instance, routine advertising services) that are undoubtedly deductible against the national tax base[52]. Finally, the exclusion of routine services from the scope of application of Article 12A does not seem consistent with the aim of avoiding privileged tax treatment for non-resident service providers; everything points in the opposite direction, since it was precisely the desire to ensure equal treatment of foreign and domestic suppliers that triggered the generalization of the so-called equalization taxes, which, without exception, are levied precisely on the provision of certain automated digital services (namely advertising and intermediation services)[53].

In short, any of the purposes attributed to Article 12A recommend that the FTSs covered by the article also include the automated digital services that constitute the essential core of the digitized economy. It should be borne in mind that the teleological criterion of interpretation is not just one of those available. Instead, interpretation is essentially oriented towards knowing the purpose of the rule and choosing the interpretative option that best suits it[54]. For this reason,

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[48] I myself have defended, albeit concerning other provisions in a DTC, that the aim, often attributed to many rules, of achieving legal certainty is of little help in their interpretation. Regarding for instance the concept of Permanent Establishment: Báez Moreno, Andrés. *Unnecessary and Yet Harmful: Some Critical Remarks to the OECD Note on the Impact of the COVID-19 Crisis on Tax Treaties*. /En/ 48 Intertax, Issues 8&9, 2020, p. 818.

[49] Zornoza, Juan José; Báez, Andrés. *The 2003 Revisions to the Commentary to the OECD Model on Tax Treaties and GAARs: A Mistaken Starting Point*. /In/ Tax Treaties: Building Bridges between Law and Economics (Michael Lang, Pasquale Pistone, Josef Schuch, Claus Staringer, Alfred Storck, Martin Zagler eds.). Amsterdam: IBFD, 2010, p. 157. Báez Moreno, Andrés. *GAARs and Treaties. From the Guiding principle to the Principal Purpose Test. What have we gained from BEPS Action 6?* /In/ 45, Intertax, Issue 6-7, 2017, p. 438.

[50] As previously stated most of the countries that have a definition or sources in their domestic law that allow determining the meaning of the term FTSs seem to lean towards a broad understanding of the term referring to all those services that require specialized technical knowledge on the part of the service provider.

[51] As we shall see in section 3 of this paper.

[52] In the same line with more references: Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* p. 301.

[53] OECD/G20. *Addressing the Tax Challenges...op. cit.* p. 115.

[54] This idea has become firmly established in German academic doctrine, which has dealt with interpretative issues more deeply than any other (see: Tipke, Klaus, *Über teleologische Auslegung, Lückenfeststellung und Lückenausfüllung*. /In/ Der Bundesfinanzhofund seine Rechtsprechung: Grandfragen-Grundlagen. Festschrift für Hugo von WALLIS zum 75. Geburtstag am 12. april 1985. Bonn: Stolfuss, 1985, p. 135. Tipke, Klaus. *Die Steuerrechtsordnung. Band 1. Wissenschajtsorganisatorische, systematische und grundrechtlich-rechtsstaatliche Grundlagen*. Köln: Dr. Otto Schmidt, 1993, pp. 1240-1241. This thesis has somehow permeated the jurisprudence referring to international treaties, which qualifies the object and purpose of a treaty as the most important part of its context (see Iran-United States Claims Tribunal *Federal Reserve Bank of New York v Bank Markazi* Case A 28

even if there were not - and there are in our case - sound logical and contextual arguments leading to a broad interpretation of the concept of FTSs, which in any case covers automated digital services, the purpose of article 12 A of the UN Model would undoubtedly advise such an interpretation.

In short, there is no sound legal or logical basis for a restrictive interpretation of Article 12A of the UN Model Convention; in particular, an interpretation that excludes automated services from the concept of FTSs makes no sense. For that reason, the introduction of a new article 12 B in the UN Model - which is based precisely on the idea that Article 12A does not cover automated services[55]- can, at best, be qualified as redundant and, therefore, unnecessary.

III. The introduction of article 12 B in the UN Model Tax Convention 2021: not only unnecessary but also disturbing.

The considerations we have made in the previous section should be sufficient to conclude that incorporating new article 12 B to the UN Model Tax Convention 2021 was a severe mistake. However, if the only problem underlying article 12 B is that it is unnecessary (in the context of a Convention that already has an article such as 12 A), the Committee of Experts could only be criticized for the time wasted in its discussion and the lack of normative technique involved in having a rule in a DTC that serves no purpose. However, the problems generated by Article 12 B are far more serious than those arising from its uselessness. Indeed, the new article is not only superfluous but, particularly, and this is the most serious, very disturbing both in itself and in relation to article 12A. What follows is an analysis of what we consider to be the most serious problems with Article 12B.

III. 1. Article 12B undermines the institutional credibility of the Committee of Experts and of the UN Model Tax Convention.

Neither the UN Committee of Experts nor any other organization in charge of designing the International Tax Regime can be required to know the future in advance. In this sense, in 2009, when the project of what would later become Article 12A of the UN Model Tax Convention was launched, it was not easy to foresee the business models of the digitalized economy and, even less, the importance that automated advertising and intermediation services would achieve in them[56]. However, the project was so protracted that, when Article 12A was finally incorporated into the UN Model Tax Convention in 2017, the crucial importance of these services for the digital economy was practically common knowledge[57]. In these circumstances,

(2000) 36 Iran-US Claims Tribunal Reports 5, para 58; quoted by Dörr, Oliver. *Article 31. General Rule of Interpretation…op. cit.* p. 587).

[55] Although, as we will see later, some passages of the proposal may be confusing in this regard: Committee of Experts on International Cooperation in Tax Matters. *Tax consequences...op. cit.* Annex 1, paras. 8 and 42.

[56] Although the OECD's work on the tax problems of the digitization of the economy had begun almost a decade earlier, it was very much focused on traditional e-commerce; see: OECD, Clarification on the Application of the Permanent Establishment Definition in E-Commerce: Changes to the Commentary on the Model Tax Convention on Article 5. Paris: OECD, 2000, 7 p. OECD, *Tax Treaty Characterisation Issues Arising From E-Commerce.* Paris: OECD, 2001, 35 p.

[57] Indeed, in 2017, it had been years since various academics warned of the importance of services for the taxation of the digital economy and the consequent need to connect the Model UN draft Article 12A with the OECD's work on the taxation of the digitized economy; see: Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* pp. 322-325 (and the references cited therein).

it seems inconceivable that what was very clear to a significant number of academics in 2017 (or even earlier) went unnoticed by the members of the UN Tax Committee who, only four years later, had to introduce a new article, Article 12 B, which does allow the Source State to tax exactly what article 12A is supposed not to cover: i.e. ADSs. In this context, there are only two scenarios in either of which the Tax Committee's institutional prestige does not fare very well: i) Either the UN Tax Committee members were unaware of the weaknesses of Article 12 A in dealing with the problems of taxing the digital economy, in which case the need to introduce Article 12 B very shortly thereafter is the exclusive result of the Committee's failure to anticipate[58]; ii) Or, alternatively, the Committee members (or some of them[59]) were fully aware of the extraordinary potential of Article 12A to address the challenges of taxing the digital economy but deliberately designed interpretative obstacles so that Article 12A could deploy full effects on the automated digital services that, in the end, constitute the essential core of the digitized economy. Although, as a purely external observer, I have no proof that this is what has happened (not to the contrary), there are indications in the Commentaries to Article 12A that point in precisely this direction. Apart from the restrictive interpretation of the concept of FTSs to which we have referred in detail in the previous section, mention should be made here of the alternative version of article 12A that the Commentaries present as an option for countries concerned about the scope of article 12A and the uncertainty associated with the definition of FTSs[60]. Indeed, the Commentaries to the Model provide an alternative provision to Article 12A that attributes taxing powers to the Source State concerning all services (*Fees for Services*) if they are provided in that State or if, wherever provided, they are paid by a resident of that State to a closely related enterprise or person[61]. In my opinion, this version is not intended to offer an alternative article to those who wish to negotiate a DTC containing a distributive rule referring to services with a scope different from Article 12A[62], but rather to support the idea - also present in the restrictive view of the concept of FTSs referred to above - that article 12A does not refer to all services but only to some types of services.

In any of the above scenarios, the Committee's and the Model's prestige are seriously compromised. Indeed, either the Committee was unable to advance what many had been predicting for some time or, worse, the majority of the Committee allowed itself to be convinced or simply tolerated an interpretation with minimal legal backing that has meant, in the end, a

[58] It is improbable that this was the case; not only because, as mentioned above, many academics had already been warning about this issue but, above all, because the Commentaries to Article 12A of the UN Model Convention themselves described, with absolute precision, the connection between cross-border services and the problems of taxation of the digital economy; see: ComUN, art. 12 A, par. 2.

[59] Who can be identified with what the Commentaries to the UN Model Convention often refer to as "*a significant minority of the members of the Committee*" and which, in my experience in Committee Meetings, coincides with Committee members originating from OECD Member States.

[60] ComUN, art. 12 A, paras. 26-31.

[61] ComUN, art. 12 A, par. 26.

[62] In fact, to date, and to the best of my knowledge (according to the IBFD DTC database), no treaties containing the aforementioned alternative provision have been ratified or negotiated. Typically, OECD Member States -which seem to be the natural addressees of this alternative provision- will either refuse to accept in the DTC any provision allowing services to be taxed by the Source State in the absence of PE or physical presence of provider (as anticipated by Arnold, Brian. *The New Article...op. cit.* p. 180) or, if they do accept it, follow the literal language of Article 12A of the 2017 UN Model or a very similar one; as indeed do all the Treaties signed since 2017 in which one of the Contracting States is a member of the OECD (see Treaties between Botswana – Luxembourg, Cambodia - Korea (Rep.), Latvia – Vietnam, Ghana – Norway, Chile – India, Brazil – Switzerland, Angola – Portugal, Bangladesh - Czech Republic, Botswana - Czech Republic and Pakistan – Switzerland).

massive loss of importance for Article 12A and its conversion into a practically useless instrument to meet the challenges of taxing the digital economy.

III. 2. Article 12B generates spillover effects on the interpretation of DTCs containing specific clauses for the taxation of services.

Article 12A of the UN Model Tax Convention was not an innovative creation. On the contrary, before introducing the provision in the Model in 2017, a good number of DTCs existed, which attributed taxation rights to the Source State concerning certain cross-border services[63] provided in the absence of PE or physical presence in the Source State[64]. Some authors have even suggested that one of the functions of article 12A would be to provide these autonomous treaty provisions for services with an interpretative guide that they lacked because they were negotiated outside any of the existing Models[65].

In these circumstances, many jurisdictions that more or less generally require the introduction in their network of DTCs of this type of provisions on services (e.g., Brazil, Malaysia, or Pakistan[66]) may have been disappointed in their expectations following the introduction of Article 12A in the UN Model given the restrictive reading of the concept of FTSs contained in the Commentaries to that article referred to in the previous section. Until the introduction, in 2021, of Article 12B in the UN Model Tax Convention, the exclusion of automated digital services from the scope of application of Article 12A was based exclusively on the restrictive interpretation of the concept of FTSs contained in the Commentaries to the Model Tax Convention to which we referred critically in the previous section. However, the new article 12B will provide the restrictive interpretation of the concept of technical, managerial, or constancy services with additional legal arguments. It is not just that the new Commentary to Article 12B reinforces the idea that Article 12A does not cover ADSs[67]; on the contrary, the

[63] As indicated by Wijnen, de Goede and Alessi refer to services as such most of them are addressed more specifically at technical services (Wijnen, Wim; de Goede; Alessi, Andres. *The Treatment of Services in Tax Treaties*. /In/ 66(1) Bulletin for International Taxation, 2012, p. 33).

[64] In an empirical work, developed by Miren Josebe Azcue, under the supervision of the author, it was verified that out of the 3250 bilateral DTCs existing as of May 1, 2021, 486 incorporated special clauses that, despite their non-homogeneous wording, allowed the Source State to tax income corresponding to services rendered without PE mediation or physical presence of the service provider in the Source State (Josebe Azcue, Miren. *Fiscalidad Internacional de los Servicios. Análisis del panorama jurídico global de los convenios para la eliminación de la doble imposición: especial atención al gravamen de los servicios digitales*, Madrid, 2021 (unpublished manuscript that I am handling by courtesy of the autor).

[65] García Prats, Alfredo. *Chapter 14: Impact of the Position of the BRICS on the UN Model Convention.* /In/ BRICS and the Emergence of International Tax Coordination (Y. Brauner & P. Pistone eds.) Amsterdam: IBFD 2015), at 14.4.1. Some members of the Committee also expressed this view in its X Meeting: E/2014/45-E/C.18/2014/6, par. 83. In previous work, I have questioned whether this interpretative function could justify the introduction of article 12A in the Model, which in no way implies that it will not fulfill such a function (see Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* p. 321).

[66] This might be evident in those jurisdictions - most of them, in fact, apart from India - that do not limit the concept of FTSs to customized (or non-routine) services in their domestic law.

[67] As, somewhat confusingly, the new Commentaries to Article 12B state by indicating: "*Until the addition of Article 12B, income from automated digital services, derived by an enterprise of a Contracting State (unless it also fell within scope of Articles 12 or 12A) was taxable exclusively by the State in which the enterprise was resident unless the enterprise carried on business through a permanent establishment in the other State (the source State) or provided professional or independent personal services through a fixed base in the source State and the income from automated digital services was effectively connected with such permanent establishment or fixed base*" (see E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 3).

restrictive interpretation of the concept of FTSs in article 12A now finds a solid contextual argument in the very existence of article 12B. Indeed, suppose a Contracting State intends to defend, as we have done in this paper, that ADSs can be understood as included in the concept of technical services in article 12A of the UN Model (or similar articles). In that case, the criticism of taxpayers or Contracting States intending to deny the granting of the corresponding credit under article 23 of the DTC will be very easy: if article 12A allows the Source State to tax automated digital services, why has article 12B been introduced in the Model?

This contextual argument and this is why we speak here of spillover effects, may affect even those DTCs that do not contain a clause similar to Article 12B; even if the text of the UN Model itself does not constitute one of the interpretative materials referred to in articles 31-32 of the VCLT[68] and even if recourse to parallel treaties poses serious problems in the interpretation of DTCs[69], it seems unquestionable that any court - and this is what counts in the final analysis - would tend to understand that it is complicated to interpret that the article of a DTC that refers to technical, managerial or consultancy services also covers ADSs when the UN Committee of Experts itself has considered necessary the introduction of a new provision - in this case, 12B - so that the latter can be taxed at source. The worst part of this interpretive contamination effect is that it will occur for DTCs that pre-date or post-date the introduction of Article 12A and even if a DTC containing the new Article 12B is never negotiated[70]. Indeed, the only scenario in which the interpretative argument we criticize would lose all its value would be one in which article 12B is eliminated from the Model, followed by the indication (in the Commentaries) that such elimination is due to its superfluous nature. This is not likely to happen in the short or medium term.

In short, Article 12B constitutes a definitive blow to any hopes that might have been placed in Article 12A to solve the problem of the international allocation of taxing rights in the digitalized economy. This path, which began in the Commentaries to Article 12A, now culminates in this new maneuver. It may be that everything stated here is nothing more than an ill-intentioned interpretation, but it is indeed surprising that, while the introduction of Article 12A in the Model took almost nine years of work and discussions within the UN Committee of Experts, Article 12B was approved after only 11 months of discussion[71] and without provoking the strong opposition from Committee members from OECD member states generated by the introduction of article 12 A.

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[68] Vogel, Klaus; Rust, Alexander. *Introduction.* /In/ *Klaus Vogel on Double Taxation Conventions.* (E. Reimer & A Rust (eds), 4th edn. Aalphen aan den Rijn: Kluwer, 2015, par. 100.

[69] Vogel, Klaus; Rust, Alexander. *Introduction...op. cit.* paras. 112-117.

[70] As some people are already predicting: Russo, Rafaelle. *60 Years Later: Wishes Coming True?* /In/ http://kluwertaxblog.com/2021/04/21/60-years-later-wishes-coming-true/ (accessed May 12th 2021). Sprague, Gary D.; Benett, Mary C.; Marques, Juliana. *Comments from Digital Economy Group (Baker McKenzie) on Proposed UN Article 12B of the UN Model Tax Convention*, 2021, p. 3 (available at https://www.un.org/development/desa/financing/document/comments-digital-economy-group-baker-mckenzie-proposed-un-article-12b-un-model-tax last accessed May 21st 2021).

[71] Even if it were understood that the final introduction of Article 12B is the culmination of a process that began with the early work of the Subcommittee on Tax Issues related to the Digitalization of the Economy presented at the 17th Session of the Committee held in October 2018 (see Committee of Experts on International Cooperation in Tax Matters. *Subcommittee on Tax Challenges related to the Digitalisation of the Economy*. E/C.18/2018/CRP.12) it is evident that the incorporation of the new article has been accomplished in record time.

III.3 Article 12B exacerbates the qualification problems already raised by the restrictive interpretation of Article 12A contained in the Commentaries to the UN Model Convention.

The typical mode of operation of DTCs determines the continuous need to make decisions on the correct characterization of the different items of income. Of course, introducing any new rule for the distribution of taxing rights in a treaty intensifies these problems. In this regard, the introduction in the 2017 UN Model Tax Convention of a new rule referring to FTSs raised the need to distinguish, from a conceptual and legal point of view, technical, managerial, or consultancy services from royalties in Article 12[72]. However, by far the biggest characterization problem posed at the time by the introduction of Article 12A was self-inflicted: the Commentaries to Article 12A, by excluding from the scope of FTSs all "services of a routine nature," forced to draw a line between the latter - covered in principle by Article 7 of the DTC and subject to the PE principle - and those other services which, due to their remarkable degree of customization, fell under the scope of application of Article 12A itself. As already mentioned, the Commentaries, instead of elaborating a conceptual distinction between routine/non-routine or customized/non-customized services[73], preferred to illustrate this difficult distinction by using three examples referring to the development of databases[74], the provision of insurance services[75] and financial services[76]. Obviously, and beyond the scant legal support for these distinctions, the fundamental problem lies in determining the degree of "customization" of a service that allows it to be considered a technical, managerial or consultancy service and, therefore, covered by Article 12A. To this already complicated scenario, the new Article 12B adds a layer of complexity by circumscribing its scope of application by reference to "automated digital services," which are defined as *any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider*[77]. This generic definition is complemented by a list exemplifying services that may constitute ADSs[78] and a negative conflict rule providing that the provisions of Article 12B shall not apply if the payments underlying the income from automated digital services qualify as “royalties” or “fees for technical services” under Article 12 or Article 12A as the case may be.

[72] A task that can be particularly complex in connection with payments received as a consideration for information concerning industrial, commercial or scientific experience (know-how) and to which the Commentaries to the Model have devoted considerable attention (see ComUN, art. 12, par. 12 and art. 12A, paras 97-103). However, this had been a problem of characterization, both for domestic law and DTC purposes, before the introduction of Article 12ª (see Pickering, Ariane. *General Report...op. cit.* pp. 26-29; 48-50).

[73] The Commentaries to Article 12A handle both pairs of concepts interchangeably, sometimes referring to services of a routine or non-routine nature (ComUN, art. 12 A, paras. 62; 90 and 95) and, in other cases, to customized or non-customized services (ComUN, art. 12 A, paras. 91 and 93). The terminological (and perhaps also conceptual) picture is complicated because, at times, and in line with the description of the examples mentioned above, the Commentaries refer to *services of a specialized nature* (ComUN, art. 12 A, par. 66), *specialized databases* (ComUN, art. 12 A, par. 91), *standard form insurance contracts* (ComUN, art. 12 A, par. 92) or *client's particular circumstances* (ComUN, art. 12 A, par.96).

[74] ComUN, art. 12 A, paras. 90-91.

[75] ComUN, art. 12 A, paras. 92-93.

[76] ComUN, art. 12 A, paras. 94-96.

[77] Article 12B(5).

[78] According to article 12B(6) The term “automated digital services” includes especially: Online advertising services; Supply of user data; Online search engines; Online intermediation platform services; Social media platforms; Digital content services; Online gaming; Cloud computing services; and Standardized online teaching services.

In a first very general and intuitive approach, the distinction between FTSs, covered by Article 12A, and ADSs, covered by the new Article 12B, seems straightforward: a service, to be considered a FTS, requires a significant degree of customization that, by definition, cannot be present in an ADS, which is precisely defined as one in which human intervention is minimal and, consequently, there is no customization or minimal customization whatsoever. Clear though it may seem at first, the concept of ADSs, and its distinction from FTSs, raises enormous problems that will undoubtedly result in ongoing disputes and discrepancies in characterization, which, as always, will lead to situations of double taxation and non-taxation. In this regard, the following should be taken into account:

i) As the Commentaries to the new Article 12B acknowledge - albeit attributing such a statement to a large minority of the members of the Committee - there is a concern (presumably only among those Members) that the term "income from automated digital services" is unclear[79]. The truth is that this concern seems to be well-founded because although the concept of *digital* service does not seem to pose many problems[80], the characterization of service as automated can involve enormous difficulties. Indeed, requiring "minimal human involvement from the service provider," which is what, according to Article 12B(5), characterizes an automated service, can be extremely difficult to implement in specific real-life scenarios. In addition, the Commentaries to the new Article 12B often do not help to specify what is to be understood by *minimal human intervention*, since in their description of the concept, they use equally vague expressions such as, for example, *very limited human response*[81], *significant customization*[82] or *limited interaction with instructors*[83]. In short, although perhaps not as intensely as in FTSs, the concept of ADSs raises the interpretative problem of what may be the threshold of human involvement that deprives a service of its automated status.

ii) Sometimes, the intuitive distinction between FTSs and ADSs referred to above does not seem to be entirely consistent with the rules contained in the new Article 12B or its Commentaries. In my opinion, the clearest of these contradictions is the one arising from new article 12B(7), providing that the provisions of Article 12B shall not apply if the payments underlying the income from automated digital services qualify as “fees for technical services.” Indeed, if ADSs are characterized by the existence of none or minimal human intervention or customization, it is impossible to understand how it can be possible that payments underlying the income from automated digital services also qualify as “fees for technical services.” If what characterizes FTSs is precisely their customization or non-routine character, one would tend to think that the concepts of "technical, managerial or consultancy services" and "automated digital services" are mutually exclusive; this is precisely the opposite of what paragraph 7 of the new Article 12B seems to suggest[84]. Other contradictions arise from the combined reading of the Commentaries to Articles 12A and 12B. In particular, the Commentaries to article 12B

[79] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 12.
[80] Article 12B(5) defines a service as digital if *provided on the Internet or another electronic network*.
[81] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 53.
[82] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 58.
[83] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 58.
[84] The commentaries to the new Article 12B do not resolve this contradiction by merely stating the preference of Articles 12 and 12A over Article 12B (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 63).

refer to a whole series of services that should be understood as not included in the concept of ADSs[85], among which "customized professional services" stand out. These services, among which the Commentaries include legal, accounting, architecture, engineering, medical professional or financial or other specialized expert consultancy services, seem to be understood as "customized by nature" since the Commentaries themselves, without making any reference to the degree of human intervention in their provision, understand that they require customization to each client, through the tailored exercise of professional judgment and bespoke interactions[86]. It is in this respect that new contradictions arise, as the Commentaries to Article 12A seem to suggest that some of these services - namely financial services - may be provided to customers on a routine basis, and therefore be excluded from the scope of FTSs[87], or tailored to the particular customer and his particular circumstances, with Article 12A applying to them in the latter case[88]. This lack of internal consistency in the Commentaries – which is the result, in my opinion, of the almost complete incorporation into the UN Model Tax Commentaries of the concept of ADSs developed within the Inclusive Framework on BEPS[89] - raises a crucial question that goes far beyond the specific discussion around financial services: Are professional[90] services automatically excluded from the concept of ADSs or, on the contrary, is it necessary to consider whether they involve the minimum human intervention that defines ADSs? The Commentaries to Article 12B seem to suggest the former by stating, without qualification, that these services (professional services) are not automated and require more than minimal human involvement on behalf of the professional individual or firm[91]; this statement seems to be confirmed in other more general passages of the Commentaries to Article 12B, such as when they indicate that, due to the nature of the automated digital services, it is unlikely that income from automated digital services would be dealt with in both Article 12B and Article 14[92]. This is also the conclusion suggested by the fact that the Commentaries to Article 12B, while closely following the conclusions of the IF Report on Pillar One on this issue, have not incorporated some paragraphs of the latter which offered a much more nuanced solution on the possible qualification of professional services as ADSs[93]. This dilemma, which

[85] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 59.
[86] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 60.
[87] ComUN, art. 12 A, par. 95.
[88] ComUN, art. 12 A, par. 96.
[89] Indeed, the concept of ADSs in paragraphs 5 and 6 of the new Article 12B and its interpretation in the Comments to that provision is the result of practically complete incorporation of the contents developed on that same concept in the Report of the IF on BEPS on the so-called Pillar 1 (Inclusive Framework on BEPS. *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint.* Paris: OECD, 2020, paras. 39-51).
[90] Although both the Commentaries to Article 12B and the IF Report on Pillar One refer to "customized" professional services, both seem to suggest, precisely, that professional services will always be customized by stating, with identical wording in both documents: "*Although such services may be delivered online (e.g. legal advice sent by email, an architect sending drawings ; or an accountant sending calculations in a spreadsheet), they require customization to each client, through the tailored exercise of professional judgment and bespoke interactions. These services are not automated and require more than minimal human involvement on behalf of the professional individual or firm*" (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 60; Inclusive Framework on BEPS. *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint...op. cit.* par. 47).
[91] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 60.
[92] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 20.
[93] Indeed, the IF Report on Pillar One states that where a professional service relies heavily on ADS, for example if a law firm relies on artificial intelligence software (AI) to conduct due diligence, or an architect's firm to draw plans, revenue from the provision of the professional service itself will remain out-of-scope of ADS, inasmuch as human involvement is required on behalf of the professional to use the AI and exercise professional judgment in

today may be of little importance given the -still remarkable- degree of human intervention in the provision of professional services, may become a serious interpretative problem in the short term; indeed, even though the total displacement of the professional as such may be inconceivable today, reality shows the growing automation of professional tasks[94] which, at least in theory, could lead to the total automation of certain professional services in the near future.

iii) Apart from the above, the Commentaries to Article 12B contain some obscure points that hinder the correct understanding of the concept of ADSs and their delimitation from other types of income covered by different distributive rules in tax treaties. We will now develop the three issues that we find most striking.

The Commentaries indicate that the handling by the user (service recipient) of specific parameters within an automated system to achieve a customized result does not deprive the services provided through that system of the status of ADSs[95]. This statement is logical and also entirely consistent with the concept of ADSs and FTSs, at least according to the starting points used in the Commentaries; indeed, according to them, routine or non-customized services and, for the same reason, automated services cannot be characterized as technical, managerial or consultancy services since they do not require the application of knowledge, skill or expertise by the service provider[96]. Therefore, it is logical that the exclusive result of the work performed by the customer does not affect the automated (or not) nature of the service provided. Concerning the above, the statement made by the same commentaries indicating that "cloud computing services may be 'assembled' or configured together for a particular customer whether by the service provider or by the customer on a self-serve basis"[97] is somewhat perplexing. Indeed, this statement, which is made in relation to cloud computing services but could be valid for any other allegedly automated services, raises the question of the role that the customization of the services by the service provider may play for the purposes of their qualification as ADSs. Unless the assembly or configuration of ADSs are considered routine services by nature[98], the above statements demolish the idea, at the very heart of the distinction between ADSs and FTSs, that it is precisely the customization by the service provider that makes it possible to distinguish one category of services from the other and, therefore, the application of Articles 12A and 12B.

order to provide the final service product to the client. However, and this is the relevant nuance, it is immediately indicated that where a user directly accesses an automated service online that may be equivalent to a professional service (e.g. if a user self-serves legal advice on a dedicated platform) then such service would qualify as ADS to the extent that it meets a category on the positive list or the elements of the general definition (Inclusive Framework on BEPS. *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint...op. cit.* par. 47 Box 2.22 *in fine*).

[94] Sampson, Scott E. *A Strategic Framework for Task Automation in Professional Services.* /In/ Journal of Service Research, 24(1), 2021, pp. 122-140.

[95] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 53.

[96] ComUN, art. 12 A, par. 62.

[97] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 58.

[98] Although the Commentaries do not define these concepts, they seem to imply precisely this idea when they state further on that some cloud computing services, however, involve a high degree of human involvement to customize the service to the needs of a particular client (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 58), thus suggesting that the assembly or configuration of ADSs does not exceed the threshold of minimal human intervention.

Following a regulatory technique not unfamiliar in the history of DTCs[99], the new Article 12B(6) establishes that the term ADSs includes, especially, a whole range of types of services. However, the Commentaries to Article 12B indicate that paragraph 6 of the Article is not self-standing; indeed, according to the Commentaries[100], while paragraph 6 notes that online advertising services, supply of user data, etc., are common types of automated digital services, when one is looking at the operations of a particular beneficial owner or multinational enterprise group, the requirements of paragraph 5 - i.e., be provided on the Internet or another electronic network and require minimal human involvement from the service provider- must also be met[101]. In this context, it could be concluded, as has been done on occasion by other authors referring to similar lists in the Model Conventions[102], that the new Article 12B(6) is essentially meaningless in that it does not add anything to the general concept of ADSs formulated in paragraph 5 of the same provision. However, the Commentaries to Article 12B seem to attribute to the list contained in paragraph 6 a legal value that would call into question this alleged irrelevance by stating that the listed services are common types of automated digital services and, above all, that the list provides an *indication* that an activity may constitute an automated digital service[103]. Of course, it is not clear what "indication" might mean in this context. However, it would not be unreasonable to think that, in the future, the legal operators in charge of applying this rule would tend to understand that, in principle, and in the absence of other indicators, the services listed in the above paragraph should be considered ADSs in a sort of "*in dubio pro automated principle*." This trend will be even more likely if we take into account that the Commentaries when analyzing in detail the listed services, refer to the possible customization and exclusion from the concept of ADSs of some of them - namely cloud computing[104] and online teaching services[105] - while for the rest of the listed services[106] no reference is made to such possible customization. The predilection of some legal operators, namely judges for this type of thumb rules - which facilitate a quick solution without entering into complicated interpretative disquisitions - increases the likelihood that many services provided online will end up being mechanically considered ADSs, without an analysis of the degree of human intervention in their provision.

[99] This is the case, for example, of Article 5(2) of the OECD and UN Model Tax Conventions or Article 14(2) of the UN Model Tax Convention. Article 2(2) of both the OECD and UN Model Tax Conventions follows a similar -yet not identical- technique.

[100] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 57.

[101] Herein lies a fundamental difference between the concept of ADSs in Article 12B of the UN Model Convention and that contained in the IF Report on Pillar One. Indeed, in the latter, the positive list of automated services is presented as constitutive (not purely declarative or exemplary) so that once it has been verified that a service is on the list, it is not necessary to verify that the service meets the relevant normative requirements to be considered an ADSs under the general description of this concept. This idea is repeated numerous times throughout the IF Report on Pillar One: Inclusive Framework on BEPS. *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint...op. cit.* paras. 39; 41; 42; 44.

[102] For instance in relation to article 5(2) of the OECD Model Tax Convention: Arnold, Brian J. *Article 5: Permanent Establishment*. /In/ Global Tax Treaty Commentaries, Global Topics IBFD (accessed 1 June 2021) at 2.2.1.1.4.

[103] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 57.

[104] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 58 *viii*.

[105] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 58 *ix*.

[106] *I.e.* online advertising services, supply of user data, online search engines, online intermediation platform services, social media platform, digital content services and online gaming.

ADSs services may be provided under complex contracts (mixed contracts and bundled packages) that include, in addition to the income corresponding to these services, other payments for the delivery of goods, payments for the use of information concerning industrial, commercial or scientific experience or the provision of services that do not qualify as ADSs. The qualification problems posed by these complex contracts are not new and the Commentaries to the OECD and UN Models have long offered solutions. In this regard, concerning franchising contracts, the Commentaries to the OECD Model Tax Convention state that the appropiate course to take is, in principle, to break down, on the basis of the information contained in the contract or by means of a reasonable apportionment, the whole amount of the stipulated consideration according to the various parts of what is being provided under the contract, and then to apply to each part of it so determined the taxation treatment proper thereto; however if one part of what is being provided constitutes by far the principal purpose of the contract and the other parts stipulated therein are only of an ancillary and largely unimportant character, the treatment applicable to the principal part should generally be applied to the whole amount of the consideration[107] (so-called ancillary principle[108]). The proposed treatment may lack a legal basis[109], and the concepts of ancillary and largely unimportant parts of a contract may be extraordinarily indeterminate[110]; however, the approach is logical and notably favors simplification in the always tricky tax treatment of these contracts; perhaps for that reason, this interpretation has been successful and has been used for the treatment of other mixed contracts even beyond the Commentaries to the OECD Model Tax Convention[111]. It is, therefore, very difficult to understand why the Commentaries to the new Article 12B seem to formulate a different or, at the very least, remarkably incoherent solution. One of the paragraphs of the new Commentaries adopts, emphatically, the primary solution referred to above concerning mixed contracts, stating that the appropriate course would be to break down the whole amount of the stipulated consideration according to various parts of what is being provided under the contract and then to apply to each part of it, as so determined, the taxation treatment proper to it[112]. Up to this point, the solution offered is identical to that contained in other passages of the Commentaries regarding mixed contracts; however, this paragraph makes no mention of possible different treatment in the event that some parts of the contract and their corresponding payments could turn out to be ancillary and largely unimportant, thus suggesting that when a mixed contract includes the provision of ADSs, it will be necessary, in any case, to provide a detailed breakdown of all the services included in the contract. However, this solution is very

[107] ComOECD, art. 12, par. 11.6.

[108] For nominal technicalities see: Beretta, Giorgio. *The Meaning and Scope of the Ancillary Principle Under Model Tax Conventions.* /In/ 46, Intertax, Issues 8&9, 2018, p. 642.

[109] On these problems in relation to article 12A of the UN Model: Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* pp. 292-293

[110] In this regard, see Beretta's excellent analysis of the different meanings of the term "ancillary" in the text of the OECD and UN Model Conventions and their respective Commentaries: Beretta, Giorgio. *The Meaning and Scope of the Ancillary Principle...op. cit.* pp. 639-653.

[111] Indeed, this solution has been incorporated *verbatim* in the Commentaries to the UN Model Tax Convention concerning mixed contracts including royalties and services (ComUN, art. 12, par. 12) and, more recently, for mixed contracts involving royalties and fees for technical services (ComUN, art. 12 A, par. 101. Although using different terminology, the IF Report on Pillar One has arrived at a very similar solution concerning dual category ADS or bundled packages: Inclusive Framework on BEPS. *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint...op. cit.* paras. 49-51.

[112] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 66 *in fine.*

problematic. Firstly, because it makes no sense for the ancillary principle to apply when a contract includes royalties or FTSs but not when it also includes ADSs; indeed, if a mixed contract were to include FTSs and ADSs, what part of the Commentaries should apply: paragraph 101 of the Commentaries to article 12A - which does refer to the ancillary principle - or paragraph 66 of the Commentaries to 12B - which do not contain such a reference? Perhaps, for this reason, other passages of the new Commentaries to Article 12B contain a different solution. Indeed, following the joint analysis of paragraphs 5 and 6 of the new article, the Commentaries repeat the preferential treatment to be given to mixed contracts including ADSs by indicating that each party to the contract should be treated accordingly under articles 12, 12A, or 12B[113]. However, immediately, the Commentaries qualify the previous statement indicating there are activities not clearly severable; accordingly, where a substantial part of the overall activity fulfills the criteria under paragraph 5 of Article 12B - i.e. those defining ADSs- and the remaining elements derive significant benefits from their connection to the elements having characteristics under paragraph 5, then the overall service may be regarded as covered under Article 12B; conversely where the elements fulfilling the criteria or matching the characteristics under paragraph 5 of Article 12B are merely ancillary and the rest of the service requires human involvement, the overall service shall not be considered as covered under Article 12B[114]. It could be argued that this nuance is nothing more than the ancillary principle expressed in other words and that, therefore, there is no contradiction with other parts of the UN Model Commentaries. However, apart from some minor differences, there is a notable divergence between the approach to complex contracts just described and the one traditionally held by the Commentaries to the Models. Until the incorporation of the paragraphs described in the Commentaries to the UN Tax Model, the application of the ancillary principle depended exclusively on whether some parts of the contract and their corresponding payments could be considered ancillary and largely unimportant. However, although this is not entirely clear from the Commentaries, it seems that these make the application of this principle conditional on the different benefits not being clearly severable[115]. In short, the new Commentaries seems to hesitate about the application or not of the ancillary principle to mixed contracts that may include ADSs. When they speak clearly in favor of its application, they do so by introducing nuances and conditions different from those that the Commentaries have traditionally handled to apply the principle.

The very complex interpretation of the concept of ADSs and their difficult distinction from that of FTSs will raise three fundamental problems. In DTCs that lack an article similar to 12B but

[113] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 61 *in fine.*
[114] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 62.
[115] Although not expressly stated, the possible application of the ancillary principle to mixed contracts including ADSs is headed in the new Commentaries with the following statement: There may be activities which are not clearly severable (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 62). The IF Report on Pillar One, from which the new Commentaries have taken (selectively) some of the contents referring to the treatment of mixed contracts, is much clearer in this regard by stating: "*The starting point being contemplated is whether there are multiple supplies that are identifiable and substantive in their own right (which could be evaluated, for example, by whether such supplies generate a separate revenue stream or are invoiced or priced separately for the customer, having regard to the need to avoid planning opportunities, such as arbitrary splitting of invoices), in which case each individual supply would be tested against the definitions. If the supplies are not separately identifiable and substantive in their own right, there could be an evaluation of the supply as a whole*" (Inclusive Framework on BEPS. *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint...op. cit.* par. 51).

allow the taxation of technical, managerial and consultancy services in the absence of PE, along the lines of article 12A of the UN Model Tax Convention, taxpayers will, in many cases, try to defend that the services provided, as ADSs, cannot be taxed at source under article 12A or similar. In DTCs containing both articles 12A and 12B, the asymmetries between them[116] will also lead to significant qualification conflicts between the taxpayer and the tax authorities. Finally, the treatment of mixed contracts will be more complex both in DTCs that include Article 12B and those containing only Article 12A.

III.4 Article 12B generates asymmetries in the tax treatment of Fees for Technical Services and Automated Digital Services.

The qualification problems described in the preceding paragraph will be all the more serious, the more significant the asymmetries between the treatment of FTSs under article 12A and ADSs under article 12B. Articles 12A and 12B are not structurally very different since, in essence, they are built on a very similar structure that replicates the basic architecture of Article 12 of the UN Model Tax Convention on royalties. This does not imply that there are no significant asymmetries between the two provisions.

Some these asymmetries will depend on how DTCs that decide to incorporate clauses similar to Article 12B are negotiated in the future. Other asymmetries already exist in the Model and, unless clauses are negotiated that deviate from it, they will be incorporated into the UN Model patterned DTCs. In any case, beyond the analysis of these asymmetries that we will deal with below, it should be noted that the disparate treatment of similar types of income - in this case, FTSs, and ADSs - not only entails all the problems associated with inconsistent rules but also induces arbitrage transactions or directly abusive operations aimed at (artificially) provoking the application of the most beneficial rule.

III.4.1 Different tax rates limits on Fees for Technical Services and Automated Digital Services.

Both Articles 12A and 12B of the UN Model Tax Convention have decided to leave the maximum tax rates to be established through bilateral negotiotions[117]. This allows[118], at least in theory, that the particular negotiation of each DTC could result in different maximum tax rates for FTSs and ADSs, which would subject the qualification of services to great tension, especially if we take into account the definitional problems referred to in the previous section. The likelihood that this asymmetry in tax rates will eventually occur depends on the negotiating positions of the Contracting States, and it is complicated to predict what may happen in the future. However, reference should be made to some differences in the Commentaries to Articles 12A and 12B that could, to some extent, encourage these asymmetries and the problems associated with them.

[116] To which we will refer immediately.
[117] Articles 12A(2) and 12B(2) of the UN Model Tax Convention 2021.
[118] In any case, this discrepancy could always exist since the Contracting States are not bound to the contents of the Model Conventions. However, it is also true that the contents of a Model Tax Convention are much more likely to end up being incorporated into a bilateral DTC.

First, the Commentaries to Article 12A of the Model, while suggesting the need to establish a relatively low maximum tax rate[119], do not suggest numerical references, not even in the form of a range. However, without any justification for this[120], the Commentaries to the new Article 12B do not limit themselves to recommending a modest tax rate for ADSs but explicitly refer to a rate of 3 or 4 percent[121]. This disparity may result in the future in a significant number of DTCs for which a different maximum source tax rate is foreseen concerning FTSs and ADSs, particularly in those DTCs that already have an article similar to 12A and decide, from now on, to add an article along the lines of article 12B.

Second, the Commentaries to Article 12A expressly indicate the potential benefits of applying the same rate of taxation to royalties and fees for technical services[122], particularly concerning mixed contracts[123]. This sage advice has not been incorporated into the Commentaries to the new Article 12B concerning mixed contracts that involve ADSs and royalties or FTSs as the case may be[124]. The reason for this omission is unknown to us[125] but it certainly cannot be that the Commentaries to Article 12B ignore the complexities of these contracts given the considerable attention paid to them in other paragraphs. Be it as it may, this omission may also increase, in the future, DTCs providing for different maximum tax rates for royalties, FTSs and ADSs.

III.4.2 Different treatment for B2C services under articles 12A and 12B.

One of the asymmetries enshrined in Articles 12A and 12B of the UN Model is the different treatment of payments made by individuals for services for their personal use. Indeed, while section 12A(3)(c) excludes such services from the concept of FTSs, Article 12B does not

[119] Pointing out the disadvantages of a high tax rate: ComUN, art. 12 A, par. 45.

[120] The reference figure may be given by the most common tax rate in the so-called Digital Services Taxes. Most of these unilateral taxes, at least in Europe (see Asen, Elke. *What European OECD Countries Are Doing about Digital Services Taxes.* /In/ https://taxfoundation.org/digital-tax-europe-2020/ (accessed June 3rd 2021)) likely levy certain digital services at a rate of 3 percent due to the direct influence of the abandoned EU Proposal for Directive on Digital Services Taxes, Article 8 of which established precisely that rate. However, this justification is not made explicit in the Commentaries, nor would it serve to justify the reference to an alternative 4 percent rate, nor, finally, seems to make much sense in a non-European proposal, such as that of the UN Committee of Experts; this is particularly true if one takes into account that this 3 percent tax rate is neither unanimous in the various European States nor is it the most common tax rate in the non-European States that have introduced DSTs in recent years (on these rates worldwide see: KPMG, *Taxation of the Digitalized Economy. Developments Summary*. KPMG, 2021 (available at https://tax.kpmg.us/content/dam/tax/en/pdfs/2020/digitalized-economy-taxation-developments-summary.pdf (accessed 3rd June 2021).

[121] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, paras. 4; 28.

[122] ComUN, art. 12 A, par. 45.

[123] ComUN, art. 12 A, paras. 99-100.

[124] The most apparent evidence of this deliberate omission is the discussion in the Commentaries to the new Article 12B of the factors to be taken into account in determining the precise level of taxation at source on payments in consideration of automated digital services. Among them, the new Commentaries do not refer to the potential benefit of applying the same rate of withholding tax to ADSs, on the one hand, and royalties or FTSs, on the other hand (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 29), something that, in turn, the Commentaries to Article 12A did do at the time (ComUN, art. 12 A, par. 45).

[125] This omission may be due to the intention of the Commentaries not to discourage the incorporation of Article 12B into existing DTCs that would already allow royalties or FTSs to be taxed at source at maximum rates higher than the 3 or 4 percent recommended by the same Commentaries for ADSs. Equalizing the taxation of all such income would mean either reducing the maximum rate for royalties and FTSs to 3 or 4 percent or setting significantly higher maximum rates for ADSs. It seems unlikely, in any case, that either of these scenarios would be acceptable to States wishing to renegotiate their DTCs to include the new Article 12B.

contain such an exclusion. At the time, the Commentaries to Article 12A of the Model provided both theoretical and operational rationales for this exclusion. In effect, payments made by individuals as a consideration for services for their personal use do not cause erosion of the tax base in the State of residence of the payer[126]; moreover, the imposition of withholding obligations on private consumers might prove difficult to enforce[127]. Although base erosion concerns seem to have almost completely disappeared in the Commentary's justification for Article 12B[128], the Commentaries continue to recognize the particular difficulties in imposing withholding tax obligations at source on such B2C payments[129]. However, the Commentaries to Article 12B have at no time justified why, given that there are difficulties identical to those described concerning Article 12A for taxing ADSs in a B2C context, this provision does not contain a similar exclusion; on the contrary, they merely acknowledge that these difficulties will require the implementation of additional collection measures and describe some of them[130]. Perhaps, for this reason, some members of the UN Committee[131] and comments on earlier versions of Article 12B have criticized the lack of justification for this asymmetry[132].

In the author´s opinion, the question here is not so much whether B2C services should be covered by the withholding tax mechanism under Article 12B[133], but whether there is any justification for the disparate treatment of such services under both Articles 12A (FTSs) and 12B (ADSs). Assuming that the Commentaries to Article 12B appear to have entirely abandoned the deductibility of amounts paid by the service provider as the ultimate basis for the attribution of taxing rights to the Source State[134], the asymmetry in the treatment of B2C services in Articles 12A and 12B of the Model could only be justified if the additional collection mechanisms required for the taxation of these services in the Source State are likely to work better for ADSs than they do for FTSs. Thus, the two additional collection mechanisms suggested by the Commentaries to Article 12B should be analyzed: i) The Commentaries to article 12B indicate that certain jurisdictions have the obligation to determine and pay the tax

[126] ComUN, art. 12 A, par. 72. It should not be lost sight of the fact that, rightly or wrongly, the Commentaries at the time justified the introduction of Article 12A in the Model UN as a measure to address the erosion of the tax base of developing countries (ComUN, art. 12 A, paras. 6-11).
[127] ComUN, art. 12 A, par. 72.
[128] The provision appears to be intended solely as a mechanism for the appropriate allocation of taxing rights. The most unambiguous indication of this change (or nuance) of rationale is the statement contained in paragraph 64 of the Commentary to Article 12B to the effect that: "*Even though such payments would not normally be deductible by those individuals for tax purposes, it cannot be disregarded that many multinational group enterprises that rely on digital business models derive a very significant portion of income from the provision of automated digital services generally to individual consumers*" (E/C.18/2021/CRP.17 Rev.1, Annex: (B) Draft Commentary on Article 12 B, par. 64.
[129] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 64 *in fine.*
[130] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, paras. 64-65.
[131] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 66.
[132]National Foreign Trade Council. *Comments on the draft of the U.N. Model Tax Treaty on the digitalization of the economy under Article 12B*, p. 5 (available at https://www.un.org/development/desa/financing/document/comments-us-national-foreign-trade-council-proposed-un-article-12b-un-model-tax-convention, last accessed June 17th 2021);
[133] On the problems of leaving B2C services outside of any withholding tax mechanism on cross-border services, we have already commented in previous works: Báez Moreno, Andrés. Brauner, Yariv. *Tax Policy for the Digitalized Economy…op. cit.* pp. 81-82; 88-89. Báez Moreno, Andrés; Brauner, Yariv. *Taxing the Digital Economy post BEPS...op. cit.* Pp. 131-132.
[134] If this basis is maintained, the differentiated treatment for ADSs and FTSs would lack logic since, being B2C services, they would never be deductible for the service recipient.

due by the non-resident provider, to the financial intermediary that individual consumers access to make the payments for the automated digital services involved[135]. Criticism of this alternative collection model has been constant, particularly among those who have analyzed it in the context of Article 12B. It has been argued that the financial intermediary collection model has been used in very few jurisdictions[136] because it involves the implementation of complicated technological and tax remittance mechanisms[137] and that, in the end, financial institutions encounter significant difficulties in identifying the transactions that should be subject to withholding[138]. Although it should be recognized that ADSs are more likely to be paid by automated electronic means and, therefore, with the necessary intervention of a financial intermediary, there is no evidence whatsoever that the problems associated with these collection models are any less severe regarding ADSs than they are concerning FTSs. In short, a collection model for B2C services that entirely or secondarily[139] relies on the imposition of information and withholding duties on the financial intermediaries involved in the transactions can only work if these services are paid through automated electronic means. However, if it is demonstrated that this system is not working correctly, it does not seem to make sense to subject only certain services -such as ADSs- to withholding tax on the basis that they are typically paid for by automated means. ii) The Commentaries to article 12B also suggest an alternative mechanism for collecting WHT corresponding to B2C ADSs, namely the obligation imposed by some jurisdictions on non-resident service providers to present a tax return where the tax obligation has been self-assessed and subject to examination by the tax administration (vendor collection model) [140]. This collection model, used by some regions and specific jurisdictions for the reporting and payment of VAT concerning digital services provided by non-resident suppliers, appears to have been well received by those who, so far, have pronounced on Article 12B[141]. This cautious optimism is surprising considering the harsh criticism that experts have levied against the vendor collection model concerning VAT tax compliance for cross-border B2C services. Indeed, the almost complete disconnect between substantive and enforcement jurisdiction[142] that afflicts these B2C services taxation models has meant that the registration

[135] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 65.

[136] National Foreign Trade Council. *Comments on the draft...op. cit.* p. 5. Sprague, Gary D.; Benett, Mary C.; Marques, Juliana. *Comments from Digital Economy Group...op. cit.* p. 8.

[137] National Foreign Trade Council. *Comments on the draft...op. cit.* p. 5. World Bank Group Staff. *Comments on Proposed UN Article 12B of the UN Model Tax Convention (Automated Digital Services)*, p. 2 (available at https://www.un.org/development/desa/financing/document/world-bank-group-staff-comments-proposed-un-article-12b-un-model-tax-convention-automated last accessed 17th June 2021).

[138] National Foreign Trade Council. *Comments on the draft...op. cit.* p. 5. World Bank Group Staff. *Comments on Proposed UN Article 12B...op. cit.* p. 2.

[139] As suggested in the Commentary to Article 12B, a financial intermediary collection model can be combined with a requirement to the non-resident service providers to present a tax return where the tax obligation has been self-assessed and subject to examination by the tax administration; in the latter case the obligation of the financial intermediary could be triggered only in cases the self-assessment is not submitted (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 65 *in fine*).

[140] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 65

[141] The World Bank Group Staff suggests using similar, or the same, online portals to those used for reporting and paying VAT on digitally provided services (World Bank Group Staff. *Comments on Proposed UN Article 12B...op. cit.* p. 2). Other papers that have been very critical of the financial intermediary collection model have not even commented on the advantages or disadvantages of this service provider collection model (National Foreign Trade Council. *Comments on the draft...op. cit.* p. 5. Sprague, Gary D.; Benett, Mary C.; Marques, Juliana. *Comments from Digital Economy Group...op. cit.* p. 8).

[142] According to the terminology brilliantly developed by Professor Hellerstein. A conceptual and bibliographical synthesis of this distinction can be consulted in Hellerstein, Walter; Owens, Jeffrey; Dimitropoulou, Christina.

(and therefore compliance effect) figures in the MOSS by non-EU services suppliers have been modest[143]. In any case, there is no reason to think that this system will work any better concerning ADS revenue collection than it might in relation to FTSs and, therefore, once again, the asymmetry between articles 12 and 12B of the Model is totally unfounded.

III.4.3 Different treatment for FTSs and ADSs paid for teaching activities.

Article 12A (3) b of the UN Model expressly excludes from its scope FTSs paid for teaching services in an educational institution or by an educational institution. Article 12B of the Model does not contain such an exclusion for ADSs, which is further confirmed by the inclusion of standardized online teaching services as ADSs in the sixth paragraph of the provision[144].

The Commentaries to Article 12A have not offered any explanation for this exclusion[145]. In any case, and whatever the tax policy rationale may be, it is not clear why it has not also served to exclude teaching services from the concept of ADSs and, therefore, from the scope of application of Article 12B. Once again, we are faced with an asymmetry that is difficult to explain. In any case, given the evidence that customized teaching services will in principle be more expensive than automated services, the asymmetry to which we refer could have regressive effects; in these circumstances, if one wishes to exclude some of these services from taxation at source, it would be more reasonable to exclude automated teaching services. Indeed, assuming the special rule is intended to prevent access to educational services from being hindered by the increased cost of providing it[146], it seems logical that this should be done precisely concerning those services in which the recipients may be more vulnerable to increased costs. Of course, the correctness of the above reasoning will depend on whether the additional tax cost generated by the withholding tax enabled by 12B concerning standardized online teaching services is finally borne by the consumers of such services. In any case, as some of the detractors of the new article 12B have pointed out, the complexity of the elective net taxation system implemented by the third paragraph of the article and its inability to achieve an effective

Digital Taxation Lessons From Wayfair and the U.S. States' Responses. /In/ Tax Notes International, April 15, 2019, p. 242 (fn 4).

[143] An analysis of these registration figures and the possible causes of the resounding failure of the MOSS system can be found in the successive works of Lamensch: Lamensch, Marie. *Are 'reverse charging' and the 'one-stop-scheme' efficient ways to collect VAT on digital supplies?* /In/ 1 World Journal of VAT/GST Law, issue 1, 2012, pp. 6-9. Lamensch, Marie. *Is There Any Future for the Vendor Colection Model in the 21st Century Economy?* /In/ 27, International Tax Monitor, 2016, p. 182. Lamensch, Marie. *Destination Based Taxation of Corporate Profits – Preliminary Findings Regarding Tax Collection in Cross-Border Situations.* /In/ Working Paper Series, Oxford University Center for Business Taxation, WP 17/16, 2017, pp. 13-14. Lamensch, Marie. *Chapter 9: Taxing Remote Digital Supplies.* /In/ Tax and the Digital Economy. Challenges and Proposals for Reform. (W. Haslehner *et al.* eds.). Aalphen and de Rijn: Wolters Kluwer, 2019, pp. 199-209.

[144] And its corresponding explanation in the Comments to Article 12B: E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, paras. 59 (*ix)*, 60 (*ii).*

[145] Professor Brian Arnold, who famously advised the Committee of Experts in the process of incorporating Article 12A into the Model, has argued, albeit rather bluntly, that this exclusion appears to be based on the idea that teaching activities carried out in the context of an educational institution are not commercial activities even if they constitute technical services (Arnold, Brian. *The New Article...op. cit.* p. 171).

[146] As, for example, the European Court of Justice has recognized in relation to the exemption for VAT purposes of services concerning school or university education services (Judgment of the Court (Fifth Chamber) 20 June 2002, *Commission vs. Federal Republic of Germany*, C-287/00, par. 47).

double taxation relief is likely to lead the providers of ADSs – in this particular case educational ADSs- to include gross-up clauses in their contracts[147].

III.4.4 Gross taxation for FTSs and elegible net taxation for ADSs.

Article 12A of the UN Model Tax Convention attributes the source State limited taxing rights on the gross amount of payments in consideration for FTSs. Paragraph 2 of the new article 12B contains an identical attribution concerning ADSs yet with a significant particularity: paragraph 3 offers an option for the taxpayer to be taxed on a (formulaic) net basis[148]. At this point, we do not intend to pronounce on the appropriateness of active income - in particular income from the provision of FTSs or ADSs - being taxed in the Source State on a net basis[149], nor to make a critical judgment on the many problematic aspects of the formula for calculating the net formulaic basis incorporated in Article 12B[150]. Our sole intention at this point is to determine, again, whether or not the asymmetries between the methods of taxation provided for in Articles 12A and 12B have a reasonable basis.

It is almost a truism to say that the existence of very different profit margins under various business models – and also under different taxpayers in the same business model- implies that taxation on a gross basis would lead to unequal results. For that reason, it seems unreasonable that any distributive rule in a DTC should completely ignore the method of taxation in the Source State, thus allowing taxation on a gross basis. Of course, this problem may be of lesser importance concerning items of income which, like dividends or employment income, in most cases do not entail significant expenses[151]. However, this does not seem to be the case for active income and, in particular, for income from the provision of services, regardless of their nature. Indeed, the problems of excessive taxation linked to gross taxation in the Source State – excessive taxation resulted from the insufficient correction of double taxation suffered by taxpayers with a low tax liability in the residence State or loss-making companies- and its economic effects (gross-up) that were once criticized regarding Article 12A[152] are the same as those on which the Commentaries to Article 12B now base the granting of an option for net taxation at source of ADSs[153]. In fact, if there were to be any difference between the two distribution rules with respect to the method of taxation, it would seem to make more sense to

[147] Tripathi, Ayush; Mehta, Shefali; Shah, Nishant; Joseph, Stella. *Taxation of Digitalized Economy: Analysing the United Nations Article 12B Solution*. /In/ The Dialogue and Economic Laws Practice, 2021, p. 1; 6. Sprague, Gary D.; Benett, Mary C.; Marques, Juliana. *Comments from Digital Economy Group...op. cit.* p. 9. This is something that a large minority of the members of the Committee to already warned about: E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 15.

[148] This formulaic net basis is identified with so-called "qualified profits" as defined in Article 12 B (3).

[149] On which I have already expressed my opinion in the past: Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* pp. 288-291.

[150] This formulaic method has been the most criticized aspect of the new Article 12B among those who have expressed their opinion on it so far: National Foreign Trade Council. *Comments on the draft...op. cit.* pp. 3-4- Sprague, Gary D.; Benett, Mary C.; Marques, Juliana. *Comments from Digital Economy Group...op. cit.* pp. 5-7. Tripathi, Ayush; Mehta, Shefali; Shah, Nishant; Joseph, Stella. *Taxation of Digitalized Economy...op. cit.* pp. 7-10.

[151] Arnold, Brian. *The New Article...op. cit.* p. 178, also referring to cases where administrative considerations make taxation on a net basis difficult.

[152] Báez Moreno, Andrés. *The Taxation of Technical Services...op. cit.* pp. 288-289 (and bibliography cited therein).

[153] E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 39.

facilitate net taxation for FTSs under article 12A. Although this is a conclusion that has been questioned very recently precisely because of the introduction of article 12B in the Model[154], there is a more or less generalized consensus that even though developing the technology required to provide ADSs can require substantial initial investment, once it has been created, providing subsequent ADSs requires limited marginal costs[155]. For this reason, it does not seem well-founded to deny a net income taxation scheme precisely for those services that, like the FTSs, would not be easily scalable in the absence of additional human involvement and, therefore, of high marginal costs[156].

In short, it seems reasonable to conclude that the new Article 12B adds unnecessary complexity to the Model UN Tax Convention and presents several unjustified asymmetries between the conventional treatment of FTSs and ADSs.

[154] Some detractors of Article 12B try to question whether the nature of the ADSs permits to provide the same type of services to new users with minimal human involvement and, therefore, minimal marginal costs. See: National Foreign Trade Council. *Comments on the draft...op. cit.* p. 3. Sprague, Gary D.; Benett, Mary C.; Marques, Juliana. *Comments from Digital Economy Group...op. cit.* p. 4.

[155] This scalability of automated services has been advocated by international organizations and academics alike: OECD/G20. *Addressing the Tax Challenges of the Digital Economy...op. cit.* p. 114. E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, paras. 54-60. Báez Moreno, Andrés. Brauner, Yariv. *Tax Policy for the Digitalized Economy…op. cit.* pp. 91-92. Cui, Wei. *The Digital Services Tax: A Conceptual Defense.* /In/ 73 Tax Law Review, 2019, pp. 103-105.

[156] Precisely concerning customized professional services, the Commentaries to Article 12B of the UN Model recognize that not being automated would require more than minimal human involvement on behalf of the professional individual or firm, thus making them more difficult to scale (E/C.18/2021/CRP.17 Rev.1, *Annex: (B) Draft Commentary on Article 12 B*, par. 60 (i).