
The first DRT international conference had three main objectives. First, to discuss the international tax principles of developing countries, particularly the BRIC countries, comparing them with the OECD principles and guidelines. More discussions should be made about whether or not some convergence is feasible to reach a level playing field to enhance overall development. For instance the OECD work regarding international transparency followed by the G-20 and other countries has been successful to some extent and might be extended to other issues such as a desirable consensus on tax treaty interpretation, transfer pricing, and measures to tackle international tax avoidance.

The second objective of this conference was to bring more international approach to judicial authorities from developing countries where important issues have been discussed and are still pending. The analysis of international tax issues in some developing countries is still in its infancy and many issues such as CFC legislation, transfer pricing legislation, tax treaty interpretation, non-discrimination, are not settled yet. This international tax conference was also expected to enlighten and enrich those issues in developing countries as well as in developed countries that have been facing new economic realities and challenges.

The third objective of the conference was to discuss unilateral measures regarding protectionism, involving developed and developing countries. In a flat world facing the threat of a new global financial crisis or recession the importance of taxation may be higher particularly when countries may be tempted to unilateral discrimination against imports (goods and services). However, some tax incentives may be justifiable to promote the development of both wealth creation and distribution. Developed and developing countries may act together in pursuing a win-win situation.
Taking into consideration the above three objectives, the conference was divided into six main panels with the interaction of developed and developing countries views to find common solutions to similar problems, or a variety of solutions to different economic and social stages of each country.

The panels were then the following:


II. Transfer Pricing: (1) arm’s length principle versus worldwide unitary taxation (2) secondary and correlative adjustments and domestic legislation.

III. Tax Avoidance, Tax Evasion, Transparency and Exchange of Information.


V. Tax Incentives and Attraction of Investments.

VI. Tax Protectionism and Tax Discrimination: Relevance of Multilateral and Bilateral Trade and Investment Agreements.

The above topics were chosen by the steering committee because they may still represent the most important issues at stake in international taxation, where more fairness and consensus are needed. They cannot be isolated from each other, as they may interact with themselves, such as transfer pricing, tax avoidance and non-discrimination, and if they do not have a degree of common understanding and optimization, through for example their interpretation and application, the overall fairness and consistency in international taxation would be jeopardized. For instance, transfer pricing rules introducing fixed margin of profits, for the sake of simplification, but that mostly favour exports in detriment to imports, as it seems to be the case in Brazil, may be contrary to the non-discrimination principle under WTO agreements that underlie the prohibition of specific subsidies.
I. TAX JUDGES AND TAX TREATY INTERPRETATION: INFLUENCE OF INTERNAL LAW, INTERNATIONAL GUIDELINES AND INTERPRETATIONS IN OTHER COUNTRIES.

In the first panel on tax treaty interpretation, Manuel Hallivis clearly showed how the Vienna Convention on Law of Treaties is applied to double tax conventions as any other international treaty. Hallivis argued that a fundamental purpose of tax treaty interpretation is to reach “common interpretation”, which means that treaty provisions should be interpreted in the same way by both countries involved. Therefore, both contracting states should interpret the provision of a tax treaty in the most consistent way, in order to achieve a result that is acceptable for both parts.¹

A frequent proposal to facilitate the achievement of a common interpretation involves an increase in the status of the OECD Commentaries, which are often used by taxpayers, tax authorities and administrative and judicial courts for the interpretation of tax treaties patterned on the OECD MC.² This suggestion would help to pave the way for building the desirable consensus on tax treaty interpretation and for promoting a more international approach among judicial authorities from developing countries, as extensively debated in the DRT international conference.

Although adequate in general, this proposal currently faces some criticisms. First, the OECD’s approach of modifying the interpretation presented in the OECD Commentaries, without changing the wording of the articles of the OECD MC weakens their legal relevance before national courts,³ since the greater the gap between the OECD Commentaries and the actual wording of the tax treaty, the smaller the relevance of the former as an element for the interpretation of the latter.⁴⁻⁵ Second, an increase in the importance of the OECD Commentaries brings up the discussion about the procedure to interpret the OECD Commentaries themselves, which may also contain inaccuracies and ambiguities as any written text. The Vienna Convention applies only for the purposes of interpreting the provisions of an international treaty, not other extrinsic material relevant for that activity, such as the OECD Commentaries.⁶ Third, in various parts of their text, the OECD Commentaries offer few elements that actually help to solve the most intricate cases.

¹ On the straightforward application of the Vienna Convention, see in this book, Pelayo, Manuel Hallivis, “Using the Vienna Convention on the Laws of Treaties for interpreting tax treaties”
When it comes to developing countries, even more striking is the fact that non-member countries did not actively participate in the drafting of the OECD MC and its Commentaries, for which reason the attribution of greater legal relevance to the OECD Commentaries also raises a problem of lack of representativeness.  

It is true that the position of non-OECD countries is registered in the Commentaries to the OECD MC in a new section added in 1997. However, the fact is that most non-OECD countries, with the exception of India, just recorded their disagreements in relation to articles of the OECD MC itself, which would correspond to the reservations made by member countries. Consequently, even after 1997, it is still necessary to recognize that (i) the non-member countries did not participate in the discussions that led to the interpretation found in the OECD Commentaries, which prevented them to contribute to the debate and to forming the prevailing opinion within the OECD; and (ii) the absence of disagreements in relation to the OECD Commentaries by non-member countries may result from the belief that the interpretation proposed by the OECD is not binding to them, rather than from an acceptance of its content.

Finally, reservations represent the unilateral understanding of a single country in relation to the OECD MC itself, which do not necessarily reflect what was actually discussed and agreed upon by the two Contracting during a tax treaty negotiation. As each tax treaty is the result of a specific bilateral negotiations and the general views expressed in relation to the OECD MC may not coincide with the interests that countries may have when interpreting a particular tax treaty, there is no guarantee that the attribution of greater legal relevance to the OECD Commentaries will play an important role in solving divergences arising from tax treaty interpretation.

In order to illustrate the importance of a common interpretation, it can be noted that Brazilian and Mexican tax authorities had opposing views on tax interpretation of some specific Articles of the same Double Tax Convention to which they are party, such Articles 7 (business profits) and 21 (other income) regarding payment of services. Putting aside the controversy on the legal relevance of the OECD Commentaries, as there is no generally accepted view as to where the OECD Commentaries fit within the various categories of instruments referred to in Articles 31 and 32 of the Vienna Convention on the Law of Treaties, one may suggest that Brazil is not an OECD member and it is not obliged to follow the OECD commentaries, whereas Mexico is member of the OECD whose commentaries would be binding on tax authorities unless there is any specific reservation.

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8 Engelen, Frank, How ‘acquiescence’ and ‘estoppel’ can operate to the effect that the States parties to a tax treaty are legally bound to interpret the treaty in accordance with the Commentaries on the OECD Model Tax Convention, The Legal Status of the OECD Commentaries, Sjoerd Douma and Frank Engelen (Eds.), Amsterdam: IBFD, 2008, p. 69.
This shows that we are not yet close to a common interpretation that is one of the pillars of international agreements; however, as both countries are party to the Vienna Convention on Treaty Law, their national courts tend to have a similar approach to tax treaty interpretation and reach a reasonable common interpretation. The same can be said of other issues regarding income characterization, the notion of beneficial ownership, and other income. Pramod Kumar also gave due regard to the same principles and rules of interpretation of tax treaties, though India is not party to the Vienna Convention. This may show that India like the United States, which signed the Vienna Convention but not ratified yet, considers many of its provisions to constitute customary international law on the law of treaties. This may make easier for any other country to accept and apply the Convention, particularly its rules for interpretation and application of treaty law to Double Tax Conventions, and achieve the desirable common interpretation, which may not be just aspirational but really effective.

Focusing on some of the most common problems on tax treaty interpretation and application, Philippe Martin addresses the subsidiarity of tax treaties in relation to domestic law, which is a concept shaped by French case law that is closely related to what is known as “the restrictive effect of tax treaties”. The subsidiarity principle implies that treaty provisions do not give rise to tax liabilities, without sufficient legal grounds in the domestic law, as well as that domestic law provisions should serve only as a starting point for the qualification of an item of income in the distributive rules of a tax treaty. An interesting aspect of the subsidiarity principle pointed out by Martin consists in whether the application of a tax treaty may worsen the taxpayer situation. It has been argued before the Supreme Administrative Court in France (“Conseil d’Etat”) that, if tax treaties are designed to avoid double taxation and they cannot create tax obligations by themselves, the application of treaty provisions should never increase the tax burden of a taxpayer (“principle of non-aggravation”).

However, this concept is not interpreted uniformly by many countries, as the interaction between the tax treaty and the domestic law may increase the tax burden of a taxpayer. It may happen, for example, when, after the application of the tie-breaker provision, the losses of a dual resident company cannot be offset because only the profits but not the losses are attributable to a permanent establishment located in the country that lost the tie-breaker test (i.e. the country that is not the residence state). In the absence of a tax treaty and a tie-breaker test, profits and losses ascertained by the dual resident company could have been offset, thus reducing the overall tax burden.

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12 In the following year of the DRT Conference, in 2014 Brazilian tax authorities changed their view after a final decision was made by the Federal High Court in 2012 (Copesul case). The Federal High Court applied customary international law in interpreting the double tax convention and made some references to the OECD Commentaries. This change was very welcome by the international tax community and illustrates that a common interpretation is not only desirable but also possible. On the implications of the current official position in Brazil, see Ferreira, Vanessa Arruda, The New Brazilian Position on Service Income under Tax Treaties: If you Can’t Beat ‘em, Join ‘em, Intertax, Volume 43, issue 3, Kluwer, 2015, pp 255-62.


Still in relation to tax treaty interpretation, Błażej Kuźniacki analyzed the controversial debate on the compatibility of CFC rules with the tax treaties patterned on the OECD Model. Based on a comprehensive analysis of recent case law, Kuźniacki argued that even in the absence of safeguarding clauses in a tax treaty, national courts tend to confirm the compatibility of the CFC rules with tax treaties, based on following arguments: (i) the OECD Commentaries, after their amendment in 2003, state that treaty provisions do not prevent the application of CFC rules; (ii) CFC rules tax the income of domestic shareholders, not the income of the foreign company; and (iii) CFC rules aim to prevent tax avoidance, which is also one of the goals of tax treaties.

It is worth mentioning that, after the conclusion the article written by Kuźniacki, the Brazil’s Superior Court of Justice, in the judgment of the case National Treasury vs. Companhia Vale do Rio Doce (Special Appeal No. 1.325.709/RJ), held that article 7 of tax treaties signed by Brazil prevents the application of Brazilian CFC legislation. Thus, the Superior Court of Justice denied the application of Brazilian CFC rules to tax profits earned by controlled companies located in Belgium, Denmark and Luxembourg.

Although the Brazilian CFC rules depart from the international standard, encompassing all types of income (full inclusion CFC system), that decision shows that the discussion is still open, particularly because Brazil introduced new legislation supposedly to make clear that it is taxing the profits of the parent company in Brazil. Similar change was made in France after the Schneider case in order to avoid the discussion on the compatibility of French CFC rules with tax treaties. After this amendment, the parent company domiciled in France receives deemed dividends, rather than profits from the legal entity located abroad, which allegedly prevents the application of article 7 of tax treaties.

That decision rendered by the Brazil’s the Superior Court of Justice is very important for the future development of the matter under discussion, as article 7 of tax treaties based on the OECD Model Convention has an objective scope, rather than a subjective scope, protecting the profits attributable to an enterprise resident in other Contracting State. Thus, even if it is assumed that tax treaties do not limit the right of a contracting State to tax its own residents, it is certain that one State may not tax business profits earned by a company resident in the other Contracting State, irrespective of the taxpayer liable for the actual payment of the tax due. For this reason, future judicial decisions on the compatibility of CFC rules with the tax treaties may put the discussion back on track.

With regard to the protection of the interests of countries in general, a valid alternative to avoid future litigation would be the inclusion of safeguarding clauses in all existing tax treaties through the multilateral instrument to be prepared under Action 15 of the BEPS Project.

15 Paragraph 14 of the the OECD Commentaries on Article 7.
Another interesting feature of tax treaty interpretation is the legal status of international agreements according to Constitutional Law of each country. In this regard Brazil and France have a great similarity. As pointed out by José Carlos Francisco, Brazilian Constitution provides a special legal status for international treaties in general, varying from constitutional nature, such as international human rights instruments, to infra-constitutional but at a higher rank than regular legislation passed by the Parliament. Furthermore, Article 98 of the National Tax Code says that tax treaties prevail not only over previous legislation but also later tax legislation passed after the ratification of tax treaties. French Constitution provides a similar legal status for double tax conventions, which also prevails over later legislation, though the subsidiarity principle sometimes appears to override that prevalence.

Interesting issues may also be drawn from the legal status of human rights instruments and their interaction with tax treaties, such as the prevalence of the former over the latter provisions, and even the interpretation of tax treaty provisions, such as the non-discrimination that might be interpreted in the light of the non-discrimination as a human right. As such it may be argued that reasonable discrimination should be accepted under Art 24 (non-discrimination) of Double Tax Conventions, as it is the case where the treaty provision may not refer to fiscal residence as a circumstance to be taken into account in order to discriminate or not. Moreover, a reasonable justification must exist, such as the worldwide taxation for residents unlike the non-residents, and come into play to allow the discrimination against the latter.

19 See in this book, Francisco, José Carlos, ”Prevalence of International tax treaties in the Brazilian Law.”
20 See in this book, Martin, Philip, ”Subsidiarity of tax treaties in relation to domestic law.”
II. TRANSFER PRICING: (1) ARM’S LENGTH PRINCIPLE VERSUS WORLDWIDE UNITARY TAXATION (2) SECONDARY AND CORRELATIVE ADJUSTMENTS AND DOMESTIC LEGISLATION.

The second panel was about transfer pricing that showed a good comparison between developed and developing countries. It was argued that some differences are justified according to different economic stages or characteristics of each country as well as a diversity of views that look at the same problem from several angles may facilitate to spot the more appropriate method or rule.

Whereas transfer pricing evolution in developed countries maybe have reached a sophisticated and detailed level of regulation, it may still be failing under simplification, legal certainty, and fairness grounds. The recent proposals presented by the OECD under Actions 8, 9 and 10 of the BEPS project to ensure that transfer pricing outcomes are in line with value creation show that current transfer pricing rules may not have kept pace with changes in the global corporative business environment.

Focusing on the maintenance of the arm’s length principle as the international standard, the OECD is clearly trying to strengthen the functional analysis. However, it will probably be quite difficult to achieve significant results with the application of functional analysis to complex businesses, with the development of electronic commerce, internet and modern communications combined with the easy transference of intangibles assets, risks and functions. In addition, the approach adopted by the OECD under the BEPS Project may be too complex and costly to be applied consistently by developing countries. Thus, the contribution of some developing countries by adopting a more straightforward mechanism could be used by developed countries pursuing the objectives of counteracting manipulation of profits between related parties and at the same time bringing more certainty to taxpayers in tandem with a fair share of revenue for the countries concerned.

In this respect, the similarities and differences between the fixed margins of profits adopted by Brazil and the worldwide unitary taxation (formulary apportionment) show that the same objective of simplification and fairness may be reached by different approaches to transfer pricing.\(^\text{21}\)

\(^{21}\) See in this book, Valadao, Marcos Aurelio Pereira “Transfer pricing: arm’s length principle versus worldwide unitary taxation; correlative and secondary adjustments, and domestic legislation under Brazilian methodology.”
Marcos Aurelio Pereira Valadão argues that the Brazilian transfer pricing methodology is far simpler than the OCED transfer pricing guidelines, for which reason it can be very useful for other developing countries. However, the problem of simplified transfer pricing rules still relies on the high risk of double taxation. Brazilian transfer pricing rules are very effective to counteract base erosion and profit shifting strategies, but it can easily result in double taxation, as the other country will not make a correlative adjustment when the profit allocated to the company located in Brazil does not reflect the arm’s length principle. Thus, a high degree of international coordination is required to align transfer pricing outcomes among several tax jurisdictions. The formulary apportionment may avoid this double taxation issue, as long as the countries achieve an international consensus on a predetermined formula (the allocation keys commonly suggested in the formulary apportionment are assets, payroll and sales). However, the achievement of an international political consensus for a successful change towards the formulary apportionment is also an obstacle difficult to overcome.

Furthermore, as Carlo Gabarino pointed out the OECD guidelines on intangibles has been developing to avoid exploitations of formal legal ownership rather than the actual economic costs and risks bore by taxpayers in different countries. Questions about who creates value, and where, and how value is created and legally and economically allocated are not easy to answer. According to the OECD, all members of a multinational group must receive appropriate compensation for functions performed, assets used and risks assumed in connections with the development, enhancement, maintenance, protection and exploitation of intangibles. Therefore, it is necessary to determine, by means of a functional analysis, all relevant factors that may contribute to the creation of value or the generation of returns. The main criteria for the functional analysis are summarized in the table below:

22 See in this book, “Transfer pricing: arm’s length principle versus worldwide unitary taxation; correlative and secondary adjustments, and domestic legislation under Brazilian methodology.”
Carlo Gabarino presents some criticisms against the OECD’s approach, stating that it may lead to an overemphasis on the functions performed in connection to the generation of the intangibles, while the legal ownership of intangibles and the contractual assumption of risks appear to be excessively disregarded. He also mentions that the level of substance and control required by the OECD to attribute the intangible related return should be tested by reference to comparable transactions between third parties, rather than by a mere hypothesis about arm’s length behaviour. Finally, he argues that the approach adopted by the OECD failed to consider that functional and control analysis may change over time, while the entitlement to the intangible related return is defined at a given point in time. The result of this mismatch is that the intangible related return may not reflect the underlying causal dynamics that result from functional and control functions analysis.\(^\text{25}\)

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<th>Functions</th>
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<td>- design and control of research and marketing programs;</td>
<td>- intangibles used in research, development or marketing;</td>
<td>- risks related to development of intangible;</td>
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<td>- direction of and establishing priorities for fundamental researches,</td>
<td>- physical assets;</td>
<td>- risk that costly R&amp;D activity is unsuccessful;</td>
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<td>- control over strategic decisions regarding intangible development</td>
<td>- funding;</td>
<td>- risk of product obsolescence;</td>
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<td>- management and control of budgets;</td>
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<td>- product liability and similar risks.</td>
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<td>- defence and protection of intangibles rights;</td>
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<td>- quality control over functions performed by other enterprises that</td>
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<td>may have a material effect on the value of the intangible.</td>
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\(^{25}\) See in this book, “The OECD Intangibles Project and the concept of ‘Intangible Related Return’.”
There seems to be little doubt that the economic ownership test should prevail over the legal ownership, because within a multinational corporate group, the legal owner of an intangible may be chosen for purely administrative purposes, while the economic substance of the creation or enhancement of the intangible, along with all the associated financial and business risks, may rest with another company of the same corporate group. Thus, the core of the discussion relies on the criteria to be used in the economic ownership test and on how to carry out the test. In this regard, understand that the arm’s length is a range, and not an exact science, may help to overcome the criticism against the economic ownership test. The arm’s length range allows certain degree of flexibility into discovering the arm’s length price for transactions involving intangible assets, since it recognizes that there will be a certain amount of subjective judgement on the part of both taxpayers and tax authorities. As there is no single right answer, the consequence is that the tax authorities must accept the price used by the taxpayer in a concrete case, as long as it falls within the arm’s length range.

A much more fundamental question is whether a gradual shift from the arm’s length principle to an activity-based formulary apportionment, limited to the transfer pricing of intangible assets, represents a feasible model to solve the valuation problems of intangible assets. As mentioned above, a radical move towards a unitary taxation system seems unrealistic in the short or medium run, but an activity-based formulary approach, grounded on a customized formula, may contribute to achieve greater efficiency, effectiveness, simplicity and transparency for both taxpayers and tax authorities.

TP Ostwal posed the same issue of intangibles and value creation in analysing the operation of internet companies and the typical model of franchising companies, which pay royalties and other intangibles mostly from developing to developed countries. In sharp contrast with this discussion Brazil has opted out of transfer pricing traditional methods in respect of royalties that may also be a reasonable measure, for the sake of simplification and counteracting tax avoidance, by providing for a limited amount to be deductible of the tax base, irrespective of any arm’s length standard. This may be justified on simplification and fairness grounds, as it is applied across the board (to related and unrelated companies) and its result may be reasonable as it depends on the profits accrued each fiscal year. The higher the profit the higher the deduction, as the royalties allowance is a percentage of the annual profits. One may suggest that this rule is like a rule of thumb, which is not strictly accurate or reliable for every situation, in contrast with the complexities for determination of economic and legal ownership in each case. The more certainty and simplicity, there may be more unfairness in some situations, as it may be far from an appropriate fair market and commercial reality. Thus, a rule that brings certainty should be open to the more complex but also sometimes uncertain and utopian arm’s length principle in special cases.

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29 See in this book, “The internet: Achilles heel of the current international taxation regime?”
With regard to the taxation of electronic commerce, TP Ostwal does not agree with the proposals regarding the creation of a new tax applicable to internet companies (“bit tax”) or the introduction of a new PE definition for the digital economy, whereby a PE would be created each time internet user data is collected in a domestic market. Conversely, TP Ostwal believes that a response to the challenges posed by e-commerce already exists in the form of global formula apportionment.\(^\text{31}\)

On one hand, the separate-entity approach used to apply the arm’s length principle and the concept of permanent establishment are difficult to reconcile with e-commerce transactions. On the other hand, one may argue that the formulary apportionment is not very effective in addressing the challenges of the digital economy, because at least two allocation keys (assets and employees) are not directly connected with the place where the consumers are located (consumer market) and where the sales are carried out. Only the sales factor is designed to represent the demand side and the contribution of the market. However, in order to overcome this alleged deficiency, a valid alternative would be to modify the formula and attribute double weight to the sales factor, although it may create a stimulus to export transactions.\(^\text{32}\)

In any event, it is highly unlikely that an international consensus will be achieved on the adoption of a formulary apportionment in the short or medium term.

Turning to the arm’s length principle, Sandra Martinho Fernandes argues that thin capitalization rules should comply with the arm’s length principle, for the purposes of attributing free capital to a subsidiary or a permanent establishment. As the capital structure of subsidiaries and permanent establishments usually affects the profit attribution, mainly because the use of excessive debt financing may shift profits to the associated enterprise abroad, domestic thin capitalization rules or interest barriers rules must be used to avoid manipulations in the debt capital. In any case, in order to be compatible with articles 7 and 9 of tax treaties based on the OECD MC, Fernandes understands that domestic thin capitalization rules must comply with the arm’s length principle.\(^\text{33}\)

\(^\text{31}\) See in this book, “The internet: Achilles heel of the current international taxation regime?”
\(^\text{33}\) See in this book, Fernandes, Sandra Martinho, “Arm’s Length Principle and the issue of thin capitalization.”
This raises an interesting issue, as some countries adopt a fixed ratio approach to control the thin capitalization phenomenon. For example, Brazil has adopted a fixed ratio approach to limit the deduction of interest expenses in a situation of thin capitalization, which may not reflect the parameters required by the arm's length principle. Indeed, in concrete cases, the fixed ratio approach adopted by the Brazilian legislator may not reflect the financial conditions agreed by independent parties on the free market, thus departing from the arm's length standard. Thus, considering that Brazilian thin capitalization rules do not allow the taxpayer to prove that its debt capital reflects the market standards for that type of activity, it must be acknowledge that the use of fixed ratios for the attribution of free capital to a subsidiary or a permanent establishment in Brazil may be incompatible with the arm’s length principle and with the Authorized OECD Approach (“AOA”). The same discussion may arise in other countries that adopt a fixed ratio approach to control the thin capitalization.

Thus, the transfer pricing dilemma remains an issue in developed and developing countries, between some different approaches to the arm’s length principle, with a trend in developing countries for their own methods that sometimes favour more the source rule, and simplification, not always in line with the complexities of the OECD guidelines.34

34 China has apparently accepted the OECD guidelines, but it remain to be seen how they are in fact assessed and decided by tax courts.
III. TAX AVOIDANCE, TAX EVASION, TRANSPARENCY AND EXCHANGE OF INFORMATION.

In the third panel Pasquale Pistoni and Stef Van Weeghel raised some sensitive issues concerning tax avoidance, such as what really is abusive tax avoidance, its morality, the international fairness of tax systems, and the consumers and public reaction to aggressive tax avoidance as well as some aspects of the BEPS project of the OECD.

Pistoni argued about the concept of tax abuse, morality, and international tax fairness. In an international and comparative context tax avoidance may be viewed as any arrangement or transaction made by taxpayers whose sole or main purpose is to reduce their tax burden, what may be legitimate or not depending on the economic factual circumstances and the purpose of tax laws at stake. In this sense, tax avoidance may be abusive, wholly artificial, excessive or too aggressive, and thus illegitimate depending on the fulfilment of two requirements. Firstly, objective economic factors that may give or not business purpose or economic substance to the transaction must be ascertained; and secondly, it must be determined the specific purpose of the tax laws in play (the tax law that was supposedly circumvented and the tax law that should arguably be applied to the transactions). 35 The above two requirements of abuse are in line with the guiding principle set out by the OECD on abuse of a tax treaty that means the main purpose for entering into transactions is to obtain a more favourable tax position contrary to the object and purpose of the treaty provisions in play. 36

Not surprisingly, the UN Commentaries on the UN Model Convention follows the same line of thought. 37 Particularly on general anti-avoidance rules, the UN Commentaries seem to be fair to state, “These two elements will also often be found, explicitly or implicitly, in general anti-avoidance rules and doctrines developed in various countries.” 38 Thus, in the view of this general report, there may be already an international recognition and a legal framework to tackle tax abusive avoidance, according to a minimum common international standard. This standard may be inspired or underpinned by moral elements likewise the principle of good faith, but it must be as objective as possible, because other fundamental tax principles must be taken into account, such as the legality or lawfulness principles and its corollaries of legal certainty and legitimate expectations. Thus, the notion of tax abuse must be ascertained by objective economic factors in line with the commercial reality, the principle of good faith, and the objective and logic purpose of the tax legislation at stake.

35 Kevin Holmes points out that in most countries the essential issue of domestic and international tax avoidance “comes down to whether the legal form of an arrangement, which a taxpayer designs to minimize the amount of tax that it must pay, prevails over the underlying economic reality of the circumstances of the case” (International tax policy and double tax treaties - an introduction to principles and application, IBFD, 2007, p. 358. A general description on the role of general anti-avoidance rules or doctrines is also given by the OECD Report on BEPS of 12/02/2013, Chapter 4 (Key tax principles and opportunities for base erosion and profit shifting, p. 38) according to which they "limit or deny the availability of undue tax benefits, for example, in situations where transactions lack economic substance or a non-tax business purpose". Further, on tax avoidance definition, see also Tax avoidance and the Law - sham, fraud or mitigation?, Key Haven, 1997, Ed. Adrian Shipwright, and on an international distinction between tax avoidance and evasion, see Baker, Philip, "Tax Avoidance, Tax Mitigation and Tax Evasion", at www.taxbar.com/Articles, and "Improper Use of Tax Treaties, Tax Avoidance and Tax Evasion", Paper no 9-A, at www.un.org/esa/ffd/tax/2013TMTTAN/Paper9A.

36 Paragraphs 9.5. and 9.6 of the Commentary on Article 1 of the OECD Model Convention.

37 Paragraphs 22-26 of the Commentary on Article 1 of the UN Model Convention.

38 Paragraph 26 on Article 1 of the UN Convention Model.
Pistone also highlighted the issues of international fairness within the interaction of tax systems of developed and developing countries and their respective tax bases. A fair tax base is generally described, “as a matter of ‘horizontal equity’, while the specification of tax rates is characterized as a question of ‘vertical equity’.”

Both of these types of equity required by the ability to pay principle, according to which taxes should be limited to an affordable amount, taking into account traditional sources of revenue, such as income, consumption and wealth, in relation to the fair connecting factors to allocate them in different jurisdictions. Each of those sources, separately as well as taken together in the international arena, should form a fair tax base that should not be excessively allocated to residence taxation, which is based on the ability to pay principle, or source taxation, which is based on the benefit principle, both of which principles must be fairly balanced with each other. Whereas the benefit principle tends to favour source countries (generally developing countries), the ability to pay principle is more connected to residence countries (a principle usually more advocated by developed countries).

One of the conceptions about fairness requires not only equality, but also objective reasoning and due consideration or taken into account all other interests and principles at stake, and the interests and arguments of those concerned or other parties’ interests. Furthermore, among different jurisdictions there appears to be conflicting interests in applying some principles and rules regarding protectionism and non-discrimination, such as an international “trade neutral allocation of tax jurisdiction” that was analysed more specifically on the following panel.

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40 The ability to pay principle is a general principle of tax fairness that is appropriate for allocating public costs whose benefits are indeterminate and generally shared, reflecting a principle of political equality; whereas the benefit principle justifies the allocation of costs of publicly provided goods and services to their users only, such as highways, collection of waste and sewage (Duff, David, idem pp. 3-5).

41 See inter alia, Source versus Residence – Problems arising from the allocation of Tax Rights in Tax Treaty Law and Possible Alternatives, Lang, Michael, Pistone, Pasquale, Schuch, Josef and Staringer, Claus (Eds.), (Kluwer, 2008).

42 On different conceptions of fairness and fair taxation, see Rolim, João Dácio, Proportionality and Fair Taxation (Chapter I, section 3), Kluwer International, 2014.

Another interesting social and economic aspect was raised by Weeghel, who also pointed out the public perception about and reaction to aggressive tax avoidance in some countries, such as in the UK, where consumers have campaigned to boycott some multinationals for paying very low tax because of their tax avoidance schemes. As a result of that public perception, some companies became more concerned about their reputation in the UK, and searched a fair tax mark, like a fair trade label, which can be obtained by those who meet some compliance and non-abusive avoidance requirements. This would perhaps be a trend in the international scenario as long as consumers as taxpayers and other organizations be more aware of the implications of aggressive tax avoidance and of their economic and political power, particularly in developed countries. In contrast with this public perception in the UK, Paulo Rosemblatt showed in his paper why tax avoidance is not a main concern for developing countries, at least not yet, though tax authorities of most developing countries are firmly committed to combat tax avoidance and evasion in a joint task force with the OECD members.

As far as developing countries are concerned, Rosemblatt argues that general anti-avoidance rules should be accompanied by a tax reform, in order to strengthen administration and enhance officials’ integrity by increasing transparency, removing discretion and simplifying the law. To this end, Rosemblatt believes that a universal model of GAAR is currently unconceivable, so that each country should design a tailor-made rule, adapted to the particularities of its legal system.

Indeed, the introduction of a GAAR within the context of a broad tax reform seems to be a valid alternative to protect tax revenues, and at the same time to foster an enhanced relationship between the tax administration and the taxpayers. In this respect, the major challenge is to find a balance between the tax base protection and taxpayers’ rights, since it is particularly difficult to know where to draw a line between legitimate tax planning and tax avoidance. Other controversial issues for developing countries lay in choosing between different GAARs for direct and indirect taxes or a unified GAAR, and in combining specific anti-avoidance measures with a GAAR.

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45 In 2014 SSE, the UK’s broadest-based energy company was the first FTSE100 company to achieve the Fair Tax Mark. For every business type, the criteria are divided into two main categories that assess a business on, firstly, Transparency, and secondly, Tax rate, disclosure and avoidance (www.fairtaxmark.net).
46 See in this book, Tax avoidance in emerging countries: is a GAAR a suitable measure?
Even more striking is the interaction between domestic GAARs and tax treaties, given the fact that most developing countries believe that treaty-shopping opportunities represent an additional factor to attract foreign investments, as stated by the Supreme Court of India in the *Union of India v. Azadi Bachao Andolan* case.\(^\text{47}\) Apart from the discussion on the compatibility between anti-avoidance rules and tax treaties, the strict application of GAARs may contradict the tax treaty policy of fostering economic development adopted by many developing countries. With respect to the exchange of information between tax authorities to tackle tax avoidance and evasion, Cristián Billardi\(^\text{48}\) raised interesting issues regarding taxpayers’ rights, particularly the rights to be informed of a request for information, to participate in the process, and to challenge the legitimacy of the requirement and its use in tax assessment and penalties. It is generally accepted that the exchange of information may be challenged before domestic courts based on constitutional rights of the country of residence of taxpayers as individuals or companies. The basis for that challenge could be also international human rights instruments, such as the European Court of Human Rights or the Inter-American Court of Human Rights, if there is no remedy at domestic jurisdictions or if the domestic court rules against the taxpayer. In practice, the challenge is to reach a balance between the taxpayers’ rights and the effectiveness of exchange of information. On one hand, previous notification procedures allow tax evaders to appeal to national courts as a delay strategy, while relevant assets or unreported income are transferred to other jurisdictions.\(^\text{49}\) On the other hand, the right to be informed is important for the taxpayers to prepare the exercise of their right to defence, which can be particularly difficult when third parties provide the evidences of the case.\(^\text{50}\) Ideally, the exchange of information in tax matters should be combined with a procedure of best practices and with a minimum standard of taxpayer protection, both complying with the protection of human rights, constitutional guarantees and procedural rights.


\(^{48}\) See in this book, “Taxpayers’ protection and international fiscal cooperation.”


Another problem is to establish from what stage taxpayers would have the right to participate in the exchange of information process. Just two months after the seminar, on 22 October 2013, the European Court of Justice ruled that at the investigation stage (when information is requested and exchanged) taxpayers have no rights, whereas they are granted at the contentious stage (starting with the notification of the taxpayer of the tax adjustment). However, the Court stated that there was no prohibition for each Member State extend the taxpayers’ rights to the investigation stage. In our view, this decision should not influence courts of developing and developed countries, because of a number of reasons. First, it interpreted a European Directive that did not impose further obligations on Members States unless those expressly provided, and second, it left to the Members States regulate the issue under their national laws according to their fiscal sovereignty in tax matters. If national laws do not provide more protection to taxpayers against fishing tax expeditions, particularly when witnesses would be heard without previous notification to taxpayers and without their participation, this lack of protection could be challenged before their national courts and ultimately before International Courts of Human Rights, such as the ECHR and the IACHR. It is arguable that these courts may take the same view of the ECJ as they may adopt a common minimum standard of protection by granting protection only to the contentious stage and not to the investigation stage of the exchange of information.

Other relevant issue Billardi raised in the panel was more restricted to the Latin America under Article 5 of the Mutual Assistance Protocol on Criminal Law of 1996, which provides “... the requested State shall be able to refuse assistance when: ...c) requests refer to tax crimes.” This limitation seems to be outdated, mainly designed to avoid political persecution by stealth, common in some Latin America countries in the past, and not according to the present international standards to tackle tax evasion. Later exchange of information agreements may certainly take precedent over the 1996 Convention making them compatible with the rationale of international agreements and Article 5.c itself of that Convention. It would not make sense to use the exchange of information to combat tax avoidance, but not tax evasion that may represent more serious and grave offense to any legal system. Thus, the trend on transparency may also be to have a common approach among developing and developed countries.

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51 Case C-276/12, Sabou case, in which the ruling was the following:
“1. European Union law, as it results in particular from Council Directive 77/799/EEC of December 1977 concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation and taxation of insurance premiums, as amended by Council Directive 2006/98/EC of 20 November 2006, and the fundamental right to be heard, must be interpreted as not conferring on a taxpayer of a Member State either the right to be informed of a request for assistance from that Member State addressed to another Member State, in particular in order to verify the information provided by that taxpayer in his income tax return, or the right to take part in formulating the request addressed to the requested Member State, or the right to take part in examinations of witnesses organized by the requested Member State. 2. Directive 77/799, as amended by Directive 2006/98, does not govern the question of the circumstances in which the taxpayer may challenge the accuracy of the information conveyed by the requested Member State, and it does not impose any particular obligation with regard to the content of the information conveyed.”

52 The Sabou decision regarding the investigation stage was highly criticized by the Confederation Fiscale Europeenne, see “Opinion Statement ECJ-TF 2/2014 of the CFE on the case Sabou”, at www.cfe-eutax.org/node/3673.
IV. TAX TREATY POLICY: TAXATION OF SERVICES.

The fourth and fifth panels were, respectively, about tax treaty policy and domestic tax incentives, which may be interrelated themselves and to the previous panels in two ways. First, there appears to be a trend in developing countries that may go beyond a traditional oriented source taxation by favouring their exports in detriment to their imports, such as the treatment provided by transfer pricing rules, which deviates from the arm’s length standard.53 Secondly, domestic tax incentives may be also related to tax sparing clauses in double tax conventions as a policy of developing countries in order to grant the domestic incentives actually to foreign investors and not to the treasury of treaty partners, as pointed out by Aleksandra Bal.54

Interestingly, if developed countries are very reluctant to accept tax-sparing clauses, they begin to compete with each other by lowering tax corporate rates or introducing special tax regimes to attract more investments. The insistence in keeping tax sparing clauses may be in line with the source taxation policy, taking into consideration a huge variety garden of tax incentives available in developing countries (local and nationally), which in this particular follow other economic and social policies to promote growth and job creation. It is well known the OECD policy against tax sparing clauses for a number of reasons, such as the encouragement of capital repatriation to enjoy the tax benefit, instead of promoting the reinvestment of results in the country where the income was generated, the incentive to tax planning, tax avoidance and abusive practices in some cases, and the lack of real necessity of tax incentives for some developing countries, particularly those whose economic level is not considerably lower than OECD Members.55 Furthermore, it would be in apparent contradiction with some developed countries tax policy, particularly those that follow the capital export neutrality principle, by taxing the worldwide income. According to that principle, the investor should make a tax neutral decision about where to invest, either in the domestic or in the foreign market, as foreign and domestic profits would be taxed in the home country.

Therefore, the OECD countries share the view that tax-sparing provisions do not represent an effective way to promote foreign investments and to foster economic growth within developing countries, because investment decisions are supposedly based on political stability, market access, labor force, infrastructure and competitive costs, regardless of the existence of tax sparing provisions in tax treaties signed with developed countries.56

53 See above the second panel and commentaries about transfer pricing rules.
54 See in this book, “Tax incentives: Ill-advised tax policy or growth catalysts?”, section 4. In general tax sparing clauses are applicable to dividends, interests, and royalties, and Brazil, for instance, has them with 16 developed countries (Austria, Belgium, Canada, Czech Rep, Denmark, Finland, France, Hungary, Italy, Japan, Luxembourg, Netherlands, Norway, Slovak Rep, Spain, Sweden); and reciprocal tax sparing credit clauses with 4 countries in the 90s (Ecuador, India, Korea, and Philippines); and non-tax sparing with 9 countries.
However, the position adopted by the OECD is somehow contradicted by a study mentioned by Aleksandra Bal in her article in this book, which, after analysing the impact of tax sparing provisions on Japanese outbound foreign direct investment (FDI) between 1989 and 2000, concluded that Japanese FDI flows in tax sparing countries were almost three times bigger than in non-tax sparing countries, indicating that tax sparing provisions influence investors’ location choices.  

In order to find a balance between the interests of developed and developing countries, tax-sparing provisions can be restricted to certain categories of taxpayers, certain types of income, certain specified tax incentives and certain period of time (sunset clause). The amount of the tax sparing credit (deemed tax paid) may also be limited, and the contracting states may include a specific anti-abuse provision into the tax treaty to counteract the improper use of tax-sparing provisions.

Still in relation to tax treaty policy, but focused on taxation of services, Deeksha Sharma raised three key issues concerning India, which is followed by some developing countries and as a source of inspiration for others, and which may be a crystal-clear illustration of a deep and extensive opposition to the OECD principles. First, the PE services adopted by India, but not Brazil and China yet, second, the application of Article 14 of the Model to professional services (deleted from the OECD Model according to which services are taxed under Articles 5 and 7); and third, the broad definition of technical services under Article 12 of the Model regardless of from where the services are provided. In this case the only connecting factor to allow the source state taxation would be the location of the payer in its respective territory, which is the traditional source rule followed by developing countries based on the benefit principle as analysed before. Brazil is now following this path regarding Article 12 after having officially changed its policy in 2014 from a previous more oriented source rule under Article 21 (Other Income), under which there is no limit regarding the withhold tax rate. Concerning Article 14 Brazil has followed India and other developing countries as a matter of principle contrary to the OECD Model, and has agreed many Protocols with treaty partners including technical services and assistance under Article 12 (royalties). Furthermore, Brazil has been showing a more aggressive approach regarding taxation of royalties and technical services, because it imposes, in addition to the WHT of 15%, a social contribution of 10% over any remittance of these payments. Brazilian domestic legislation in this case circumvents Article 12 of tax treaties by providing that the taxpayer is the payer based in Brazil and not the payee based in any other treaty partner.

57 See in this book, “Tax incentives: Ill-advised tax policy or growth catalysts?”.  
59 See in this book, “India’s Tax Treaty Policy for Taxation of Services and the OECD Principles: How and why are the BRICs diverging from OECD’s scheme for allocation of rights to tax active income.”  
60 See also the first panel discussions and footnote 2 of this report.  
61 Only old five tax treaties signed by Brazil do not provide for a technical services taxation under Article 12.  
62 As the social contribution (CIDE) is not creditable in the country of residence of the payee, the payers have been challenging it in Brazilian domestic courts under the WTO agreements (GATT/GATS/TRIPS) for being discriminatory against payments to foreign providers, as any royalty or technical service paid to domestic providers is not subjected to the so-called social contribution.
The approaches adopted by India, China and Brazil may contribute to solve the new challenges of cross-border services, in which high value added services can be delivered over long distances, without the need for a physical presence. Indeed, in the current stage of economic development, many services can be provided at a distance, without a fixed place of business, because of new information and communication technologies, a trend that suggests that the use of the concepts of fixed place or permanent establishment as thresholds for source state taxation may be inappropriate for technical services. Conversely, one may argue that only human activities generate income, which means that the key intellectual element involved in a technical service provided at a long distance is found in the state where the activity is developed. For this reason, the allocation of tax jurisdiction concerning the income derived from technical services may require a substantial relationship between the activity and the state concerned, in line with the benefit principle and the economic allegiance. A merely occasional relationship may be insufficient for the allocation of taxing rights to the source state.

In essence, what is really behind the debate is the efficiency of the concept of permanent establishment for the allocation of tax jurisdiction between Contracting States. Although it is well established that an occasional presence is insufficient for the allocation of taxing rights to the source state, Action 1 of the BEPS project now attempts to address the tax challenges of the digital economy, in which one of the major issues involves multinational companies that manage to have a significant business presence in the economy of another country without any physical presence. The redefinition of the concept of permanent establishment, in order to reach business activities carried out without physical presence, may help to tackle tax planning structures commonly used by taxpayers, but it may also bring the risks of an unlimited force of attraction derived from the mere supply of services.

Within this controversial topic, the new technical services article to be included in the United Nation MC may play an important role, because it allows the source state to tax the remuneration derived from technical services on a gross basis, up to a certain percentage to be fixed during the tax treaty negotiation. As the levy of the income tax on services payments on a gross basis may lead to an effective taxation at rates higher than the residual taxation applied in the residence state, with a consequent limitation of the foreign tax credits, this new provision may encourage the non-resident taxpayer to use a permanent establishment for the provision of services in the source state, in order to avoid the taxation on a gross basis. Therefore, this new article may contribute to a fair allocation of taxing rights between developed and developing countries.

In any event, the new technical services article to be included in the UN MC also requires further refinements on the concept of technical services, which encompasses payments in consideration for any service of a managerial, technical or consultancy nature, unless the payment is the reimbursement of actual expenses incurred by the person providing the service. The main difficulties that arise consist in determining the boundaries among the concepts of technical services, independent personal services, business profits and royalties. The priority over Article 7 or Article 14 does not remove the lack of clarity in the technical service definition, which makes difficult to distinguish between technical services and other services. Moreover, this definition does not assist greatly in disaggregating the remuneration derived from mixed agreements into separate elements of payments for services or royalties, nor does provide any guidance on how to distinguish the principal element and the ancillary. As an alternative, the contracting State would include in the tax treaty a full description of technical services deemed to be included in this provision, as can be seen in Article 13 (4) of India and United Kingdom tax treaty (1993).

Furthermore, given the fact that the source of technical services is not always clearly defined, as it can refer to the state in which the services are performed, in which the contract is signed, in which the contract is executed, in which the payer is located, from which the payment is made, or which bears the expenses, the new technical services article could have expressly indicated how to identify the contracting state in which the payment for technical services arises.

Jacques Sasseville and Liselott Kana also raised the issues of taxation of technical services and the opposing views of developed and developing countries that may be reconciled in search for a fair share of the income generated by the increasing performance of services in a more globalized world. Among the issues that are at stake one may highlight the boundaries for a provision on permanent establishment service, the definition of technical services, taxation of gross or net income, and intra-group performance of services. In our view, the principles in play again would be the same as regarding source versus residence taxation, that is the benefit and the ability to pay principles coupled with the concern for double taxation and abusive tax avoidance. Whereas unlimited source taxation may cause undesirable or unjustifiable double taxation where the country of residence is a non-low tax jurisdiction, higher withhold tax could be imposed on services where the payee entered into abusive tax avoidance as agreed by international standards. Sometimes a base erosion principle is mentioned to justify the withhold tax on services performed by foreign providers, as the payment of services is deductible in the source country, but it would be wholly disproportionate not to have a reasonable limit at source taking into account the former other principles.

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66 In respect of this issue, see the work that has been done by the Committee of Experts on International Cooperation in Tax Matters (Secretariat Note, E/C.18/2013/CRP.17), analysing the UN Model to reach a common ground and consistency where an identical common policy is not possible.
67 See footnote 15. The foreign provider with no connection with the source country would have the benefit from its contractor that directly benefits from public services in the source country. Thus, the benefit in this sense is indirect, but it exists.
In this scenario, one may argue that, even if the two Contracting States establish a reduced tax rate, the gross taxation will often give rise to a tax burden that exceeds the profit margin of the non-resident taxpayer, in which case the foreign tax credit may be limited to the tax due in the state of residence on the same item of income. Moreover, as the gross taxation does not take into account the different cost structures of each taxpayer, it will often over-tax some revenues and under-tax others. However, it should be acknowledged that gross taxation is simpler for both taxpayers and tax authorities, as it provides certainty on the taxable income. It would be very difficult to set rules on the taxation of service payments on a net basis, given the fact that the source state does not have access to the relevant information on the costs incurred abroad. Many developing countries have limited administrative capacity and need a simple and efficient method to enforce tax on income derived by non-residents. Also, the gross taxation prevents the erosion of the tax base in the source state in cases where the costs borne by the non-resident to perform the service are mostly incurred abroad.

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V. TAX INCENTIVES AND ATTRACTION OF INVESTMENTS.

Another controversy related to the previous issues of transfer pricing and tax sparing clauses among developing and developed countries is the extension of tax incentives to attract investments as discussed in the fifth panel. First, it was raised the question over whether they are needed at all, as they are not considered as the most critical factor for investment decisions. As pointed out by Aleksandra Bal, other non-tax factors, such as macroeconomic policy, market structure, labour policy, infrastructure and a stable governance system, are important factors for investment decisions. Wei Cui also commented about it and gave the example of China where local incentives are spread around the country, although national incentives for FDI are no longer used since 2007. As China repealed the federal tax incentives, some of them can be reintroduced in accordance with WTO agreements, mainly the SCM agreement that only prohibits Members granting specific subsidies contingent on export performance or on local content, depending on the economic growth and competition from other developed and developing countries. India revoked some of its specific tax incentives, but continues with its export promotions tax schemes, for example, because it is allowed to do so on grounds of the per capita GDP exception. Brazil still grants federal tax incentives for FDI and some of them have been challenged before the WTO. In this regard, Caio Caetano Luna mentions that Brazil’s trading partners, especially the European Union, Canada and Japan, are questioning its trade policy and threatening to file claims in the WTO, on the basis that Brazil is increasingly using its indirect taxes as a form of subsidizing exports and overtaxing imports. However, under Article 8 of the SCM a agreement all non-specific tax subsidies are allowed, as well as some specific on grounds of some research activities, economically disadvantaged regions, and environmental considerations, but submitted to detailed terms and conditions, what gives some leeway for fair and reasonable tax incentives compatible with fair international trade.

71 See in this book, “Tax incentives: Ill-advised tax policy or growth catalysts?”
72 See in this book, “What Should We Talk about When Talking about Tax Incentives for FDI?”
73 See in this book, “World trade organization: BRICS and direct taxation”, by Peter Wilson, Peter, in which the author gave some evidence about the change of Chinese policy regarding tax incentives to FDI and state owned enterprises was due to accession to the WTO (sections 3.3.1.2 and 4.4).
74 See further on this, the next panel on the WTO.
75 See “World trade organization: BRICS…..”, footnote 33, section 4.4.1.
77 See in this book, Luna, Caio Caetano, “The Effectiveness of International Trade Agreements for Restricting Tax Protectionism in Brazil.”
Looking into the matter more closely, Aleksandra Bal argues that tax incentives should not be offered as a counterweight to investment disincentives inherent in the general tax and economic system. Thus, before introducing any tax measures, countries should investigate what caused the problem that is to be tackled, such as strict labor policy, undeveloped infrastructure or insufficient administrative capacities, and deal with the causes first. Only when those structural disadvantages are removed, countries may use tax incentives as an additional measure to attract economic activities. 78

It is certainly right to say that, when the tax incentives are intended to offset structural disadvantages that investors may face, the appropriate solution is to fix the problem and to build the necessary environment to attract foreign investments. However, practical experience shows that it is very difficult for a developing country to improve the legal and business environment within a reasonable timeframe. Thus, tax incentives may provide temporary relief until the fundamental reforms are carried out to build a more predictable and conducive business environment. 79

From a tax policy standpoint, the use of tax incentives to attract foreign investments may encourage the development of certain sector of the economy only through the amendment of the tax law, without the actual disbursement of budget funds as in the case of direct subsidies. However, tax incentives may lead to an inefficient reduction in tax revenues, because many taxpayers could have made the same investment in the absence of any tax reduction. This lead to a loss of tax revenues without any corresponding benefit to the developing country in which the investment is made (the host state). For this reason, countries should focus on special-purpose incentives, which can be targeted to particular desirable activities or to projects that would not have occurred without the tax incentive, in order to achieve regional development, employment creation, technology transfer etc. 80 The conclusion about the above issues may be that tax incentives are a worldwide reality and having been regulated by the EU on grounds of unjustifiable state aids that distort trade and fair competition, as well as by the World Trade Organization under the SMC agreement on subsidies. It may be better to regulate tax incentives rather than eliminate them, what may be more costly, but preferable in terms of conciliation of different public interests in play, such as pursuing economic growth, fiscal sovereignty, and a level playing field that avoids unfair competition and unfair economic and social conditions among developed and developing countries. This was also discussed in the next panel on the role of trade agreements in tax matters, particularly non-discrimination and non-protectionism.

VI. TAX PROTECTIONISM AND TAX DISCRIMINATION: RELEVANCE OF MULTILATERAL AND BILATERAL TRADE AND INVESTMENT AGREEMENTS.

This panel was chaired by Luiz Olavo Baptista, a former chairman and member (from 2001 to 2009) of the Appellate Body of the WTO, who referred to a number of cases in which tax matters were considered and ruled as direct or indirect discriminatory as well as arbitrary or unjustifiable or disguised but blatant protectionism. Besides some egregious cases regarding tax subsidies related to direct taxation, he mentioned some others such as the Bovine Hides case\(^81\) that dealt with indirect and unjustifiable discrimination regarding tax on gains (impuesto a la ganancias), a direct tax charged in a way that indirectly protected domestic goods.\(^82\) Thus, the importance and influence of the WTO agreements has been increasing and affecting tax rules and tax systems of its Members in a way that one could not easily have foreseen before, or as Jacques Sassaville pointed out an unintended result at the time of their ratifications.

The interdependency of the WTO agreements and double tax conventions is clear as Peter Wilson showed in his paper. One of the main objectives of the bilateral tax conventions is the same as the WTO agreements: liberalization of international trade and fair competition. Timothy Lions may be absolutely right to say that tax law is at the service of trade\(^83\), and not the other way around, what it may be more fair particularly where that both fields of law end up serving human rights.

Peter Wilson highlights the growing importance of direct taxation to the creation of a level playing field in world trade, not just for goods, but also for services and intellectual property. Based on the evolution of world trade and the interrelationship of the WTO and the OECD/UN objectives in freeing up world trade, Wilson states that an upward trend in the number of disputes with more obvious direct tax relevance may be expected in the future.\(^84\) Specifically with regard to trade and investment agreements, Timothy Lions argues that, except when contracting states decide to include a specific provision limiting their effects, the domestic tax laws of the countries concerned are also affected by their terms, such as the most favoured nation and the national treatment rule.\(^85\)

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82 This decision can be a landmark case related to direct taxation, as it was thought that direct taxation was not in the scope of the GATT. See further analysis on this case, particularly the necessity test and disguised restriction on trade applied by the Appellate Body. Proportionality and fair taxation (Chapter III, sections 3.2.b and 3.2.c). See footnote 17.
84 See in this book, Wilson, Peter, “World Trade Organisation: BRICS and Direct Taxation”.
In general, the potential impact of WTO rules on direct taxation may derive from different international trade rules, such as the non-discrimination, the most favoured nation obligation, the national treatment obligation, indirect and direct tax incentives that may qualify as subsidy, the dispute settlement mechanism, among others. However, the effects of the interaction between WTO rules and direct taxes rules are not always clear. On one hand, a subsidy element may be potentially found in every tax system that does not strictly apply CFC rules or transfer pricing rules. On the other hand, CFC rules and anti-avoidance measures that are applied only to specific or listed countries may be contrary to the non-discrimination provision and the most favoured nation obligation. These examples show that the potential impact of WTO rules on the area of direct taxation may raise several issues, whose effects should be considered more carefully. In the conference, the interesting pending case of Panama against Argentina was further discussed because may affect the right of Member States to set out a black list of countries for tax purposes, such as imposing higher taxes to remittances to those countries. On 12 December 2012, Panama requested consultations with Argentina with respect to certain measures imposed by Argentina that affect trade in goods and services. Panama alleged that various Argentine measures are applied exclusively in respect of certain countries listed in the Regulations to the Income/Profit Tax Law, Decree 1344/98, as amended by Decree 1037/00. Panama claimed that those measures are inconsistent with: Articles II:1, XI, XVI and footnote 8, and XVII of the GATS; and Articles I:1, III:2, III:4 and XI:1 of the GATT 1994.

In our view, Argentina may have a good reason for introducing those tax measures, but they have to pass the necessity test and not be an unjustifiable restriction on trade as assessed by the Appellate Body of the WTO. In other words, those tax measures must not go beyond what is necessary to achieve the legitimate objective of tackling tax avoidance and evasion. If there are other alternative less intrusive measures to trade, then those tax measures could be challenged. In this case, the objective is apparently legitimate and in the public interest of Argentina and many countries as well. How harsh the specific measures are and the existence or not of available less severe measures to achieve the same objective and level of protection to the Treasury and the chase of tax offenders might decide the case in favour of Panama. However, the possibility for instance of an Exchange of Information between Argentina and Panama that be compatible with the Inter American Human Rights Convention may be considered as a reasonable measure, which should be tried before any unilateral tax retaliation that could violate the international trade rules and principles as agreed within the WTO.

This case illustrates again how interacted international tax agreements may be with international trade agreements and to some extent to international human rights instruments. This interaction may require a degree of optimization and conciliation of apparent opposing interests and objectives, such as those also discussed in the previous panels: trade liberalization, economic and social growth, fiscal sovereignty, trade neutral allocation of tax jurisdiction, fair allocation of taxing rights between developing and developed countries, and due regard to the human rights of those concerned.

Bhawna Bakshi discusses the relationship between tax protectionism and tax discrimination. She argues that the non-discrimination principle in tax law should be interpreted based on the concept of competitive neutrality, which requires a uniform taxation in the source state and the adoption of the same method of double tax relief by all countries. Thus, from the perspective of the residence state, the competitive neutrality requires the adoption of either worldwide taxation with unlimited foreign tax credits or exemption of foreign-source income. The real political problem behind this proposal is how to achieve this full harmonization of tax systems, without ignoring the peculiarities of each country and other tax policy objectives. Countries will consider many other factors beyond neutrality, efficiency and competition in designing their tax system, such as fairness, equity, distributive justice, national welfare, among others, which turns Bakshi’s proposal very difficult to achieve in practice.87-88

Overall the speakers and attendees of the this international tax conference have discussed and learned from each other based on the exchange of experiences among judges, academics, and tax authorities from developing and developed countries. Experts dealing with international taxation in developing countries tend to act isolated from their colleagues in other countries. For instance, judges from developing countries do not know to some extent how and why the same articles of tax treaties are being interpreted by Courts from other countries. This scenario of greater convergence would bring more stability to the international tax environment and would enhance better conditions for economic activities and a fair share of social and economic growth. Furthermore, as shown in this report all main issues may be co-related, such as international trade, discrimination, tax avoidance and evasion, fiscal sovereignty, international human rights, and international fairness of tax systems, and cannot be solved separately, at least without due regard to the overall legitimate interests and principles at stake. The organizers and the participants believed that this event was an excellent opportunity to enhance and improve this challenging dialogue.