Tax Justice Network submission to the

Call for contributions on the Draft Issue Note of Workstream 2 of the Intergovernmental Negotiating Committee on the UN Framework Convention on International Tax Cooperation

July 2025

TAX JUSTICE NETWORK

Table of contents

For the kind attention of:
Mr. Ramy Youssef, Chair of the Intergovernmental Negotiating Committee to draft a United Nations Framework Convention on International Tax Cooperation and two early protocols (INC)
Mrs. Liselott Kana, co-chair
Cc: Permanent Representatives and Observers to the UN in New York
Date: 11 July 2025

Abstract

The Tax Justice Network (TJN) welcomes the opportunity to provide input on the Draft Issue Note of Workstream II, as presented on 27 June 2025. As an independent, international organisation advocating for greater transparency, accountability, and fairness in tax systems, TJN supports the overall direction of the Workstream's approach to the work of the first Protocol. We align ourselves with the joint submission made by the Global Alliance for Tax Justice. This submission answers some of the key debates regarding the work of Workstream II. We propose that the protocol should tackle current problems, while paving the way for more fundamental change. We defend that the scope of services and taxes covered should be broad, to align with the mandate of the protocol, and in particular tackling challenges of a globalised economy. We defend the elements and the spirit of recent changes to the UN Model convention could be streamlined in the protocol as intermediate measures, while at the same time emphasising the need to move beyond bilateral tax treaties based on outdated nexus rules and a complex and unfair transfer pricing system. To do so, we defend the adoption focusing on real economic activity instead of value creation, and the adoption of a broad understanding of the concept of Significant Economic Presence.

Comments on the method of work

The Tax Justice Network welcomes the work of Workstream II and commends it for the breadth and synthetic nature of the Issues Note. We believe it adequately reflects the main discussions surrounding the cross-border taxation of services. We appreciate the committee's effort to keep the Note concise, as this allows a more focused engagement. We nonetheless wish to align with other submissions, such as those made by the Global Alliance for Tax Justice, that emphasise the need to ensure broader stakeholder participation in the discussions. This would enable us to be better prepared to engage with the process and to more effectively fulfil our role as stakeholders.

Specific remarks

We structured our comments around some of the most salient questions which appeared in the Note. The questions do not follow the same structure of the document, instead starting from broader commitments and goals to the specific technical details.

1. What should be the goal of the Protocol?

We agree with participants who noted that the main objective of the Protocol "should be to support domestic resource mobilization by providing for a fair allocation of taxing rights". We also agree that it is important for the Protocol to promote simplicity and administrability. Doing so, the Protocol would contribute to several principles listed in the Terms of Reference (ToRs 9(f)(g)(h)). The concern with making the Protocol "future-proof" is also aligned with the ToRs (9(e)).

We believe the best way to develop a system that delivers both simplicity and fairness is by replacing the current bilateral tax treaty network — based on outdated nexus rules and a complex and unfair transfer pricing system — with a multilateral approach that treats multinational companies as the unitary entities they are and allocates their profits based on their real economic activity.

We take note that some countries pointed out that challenges related to cross-border services taxation are not limited to the taxation of MNEs. While the overarching goal of the Protocol should be to pave the way for this new multilateral system, we also believe it should identify intermediate steps to address urgent current issues. In this regard, we consider that some of the measures developed by the UN Tax Committee could constitute useful transitional approaches.

This dual character — addressing immediate challenges while paving the way for deeper change — supports the adoption of a broad scope, highlights the importance of a well-resourced subsidiary body, and requires clear rules for amending and updating the Protocol to keep pace with the evolving nature of the issues it seeks to address.

2. What should be the scope of the Protocol?

The issues note indicates that there is an ongoing debate regarding the scope of the Protocol and asks whether it should cover only genuine digital services or also traditional services delivered through digital means of communication. In response, we want to emphasize that the Protocol should cover "cross-border services in an increasingly digitalized and ***globalized*** economy." The "globalized" aspect is just as relevant and risks being overlooked if the discussion narrows its focus solely to the digitalised economy (or, alternatively, to the digitalisation of the economy).

For developing countries in particular, discussions on the fair allocation of taxing rights of income from cross-border services delivered without physical presence both predates and *goes beyond* the digitalisation of the economy. **We urge the Committee to maintain a broad scope of services, encompassing all cross-border services**. A broad scope may also help the Committee avoid certain (unproductive) debates, such as defining what constitutes a digital service or what qualifies as the digital economy. The last decade of efforts demonstrates that ring-fencing or adjectivizing services often leads to unnecessary complexity. We understand this was one of the reasons the UN Tax Committee recently replaced the concept

of “technical services” in Article 12A with the concept of “fees for services”. The discussion on the digital economy or digitalised economy also proved an unfruitful avenue in multiple OECD discussions. It is also in line with the perception that challenges with service taxation may prove difficult even in activities that “involve a very close physical connection to the host State, such as the extractives industry and agriculture”. While certain services may have unique complexities that require specific rules, we suggest that the Committee adopts a broad approach, which could even be a backdrop option upon which more specific rules or guidance may later be developed.

3. Is the way services are currently taxed under the existing Model Conventions adequate?

We appreciate the synthetic description of the growing divergence in the taxation of services between the two treaty models, which highlights both the key shortcomings of the restrictive OECD model and the important efforts of the UN Model to secure taxation at source. We would like to express our appreciation for the important work of the UN Tax Committee in developing model rules aimed at guaranteeing the taxation of services at source, which we consider an important step toward addressing the current unfairness of the existing system[1].

As we have argued, however, we believe that countries should use the Protocol as an opportunity to transition from a bilateral approach to a multilateral system, and to start taxing MNEs as unitary entities. In addition, we note that model treaties continue to provide inadequate nexus rules. While the UN Model attempts to overcome this by prioritizing taxation on a gross basis and avoiding the need for a permanent establishment, we believe that deeper reform is necessary.

Our preference for a shift toward formulary apportionment does not preclude our recognition of the significant progress made by the UN Tax Committee. In particular, we welcome the broadening of scope in Article 12AA through the inclusion of the umbrella concept of “fees for services”, the adoption of fractional apportionment methodologies in Article 12B on Automated Digital Services, and the introduction of Article 8B concerning shipping services. Some of these elements could be incorporated as intermediate solutions. More importantly, the recognition of the role of fractional methods and the adoption of a broad scope seem to point into a correct direction, and the spirit of increasing the fairness in the allocation of taxing rights should be at the core of the current work on the Protocol.

[1] https://taxjustice.net/2025/07/09/how-the-un-model-tax-treaty-shapes-the-un-tax-convention-behind-the-scenes/

4. Should taxation of services take place on a gross or net basis?

As we understand, the divergence in the models is also a reflection of a divergence in the preferences of countries, some of which prefer gross basis taxation due to the simplicity and administrability, and others that advocate for net taxation.

Our preference is for a system that calculate the profits of MNEs as unitary entities and allocates the profits following a formula. However, we acknowledge that simplified solutions, such as withholding taxes, play an important role in revenue mobilisation and the allocation of a share of profits in source countries. We would suggest that, for developing countries, the Protocol would only be an adequate substitute to these methods if it delivered both in the ease of implementation and in a fairness in allocation. It is our view that unitary taxation with formulaic apportionment is the best path to deliver on these twin goals.

5. How should nexus be triggered? Is value creation useful to define nexus?

We are glad to see that there is a broad recognition that the existing nexus rules are not adequate for triggering taxing rights related to the provision of services in a context where physical presence is not needed. We understand that there seems to be a willingness to discuss nexus rules even among countries which favor a more restrictive view of service taxation.

We stress that part of this nexus discussion stems from an approach adopted by the OECD model, which sought to restrict source taxation of cross border services, only allowing taxation in the source state if the service provider has a permanent establishment. Both in a scenario in which the worlds moves towards a system of unitary taxation (which primarily solves the issue of the taxation of intra-group services but not services provided by the group to third parties) and in a scenario winch intermediates solutions are adopted for a sharing of taxing rights on services, it would be important to define the criteria that would trigger a taxable presence and formulas to allocate taxable profits.

Here, **we believe the term real economic activity should be a better proxy for than the vague notion of "value creation**". Value creation is a concept which can have both the pervasive effect of increasing inequalities among countries (emphasizing certain dimensions of the value chain in detriment to others), while at the same time being used to artificially allocate value creation (and therefore profit) in assets subject to lower taxation, such as intangibles. We would suggest including some language on real economic activity on the protocol and the main convention, and also some observable criteria to define this concept.

Regarding the trigger, the protocol provides an important opportunity to move beyond the notion of permanent establishment, and we welcome

that several countries proposed discussing the concept of Significant Economic Presence. We find it useful that the Committee framed the concept to incorporate not only a threshold of sale of services, but also elements such as marketing "or other indicia of deliberate targeting of the jurisdiction's market". We think this approach is adequate considering the different types of interactions which may constitute an economic presence in the current digitalised and globalised economy. The differentiation by economic size is also sensible and adequate to the different realities of UN member states.

6. What role should capacity building play in addressing the challenges related to the taxation of services?

We fully agree with countries that stressed that capacity building is not an adequate response for challenges of a transfer system which is extremely complex and based on misguided assumptions. We echo concerns that capacity building leads countries to direct a disproportionate amount of resources to a system which, by default, fails to allocate a fair share of taxing rights in countries where services are delivered, and users are located. We understand, in any case, that most developing countries would appreciate access to more information which would allow them to detect risks in the current regime. We would thus suggest that countries that emphasised capacity building might consider making the PCBCR reports of MNEs public and spontaneously sharing additional information that might assist their trading counterparts in developing country context.

7. How should digital taxes be classified?

The Note points to a discussion regarding the classification of certain taxes, and in particular digital services taxes, which some countries appear to want to see them considered as "indirect taxes". We welcome the fact that the Committee decided to focus on the nature of the taxes, instead of their label. We believe that this is a more adequate approach.

We further believe this discussion is artificial and stems from the very failure of current international tax rules to guarantee a fair allocation of taxing rights where services are delivered, and users are located. Countries with large treaty networks often need to rely on DSTs to secure some allocation of taxing rights in relation to services delivered in their jurisdiction, or due to their user participation, something which is otherwise hindered by the treaties they've signed. Thus, DSTs are intrinsically connected with the lack of effectiveness of existing rules and should not be kept out of the scope of the discussion.

8. Should there be a single or multiple rules for the taxation of services?

We understand that there is a discussion regarding whether there should be a single set of rules for all services, or if different rules should be adopted for each type of service. There is a long-lasting debate on this topic regarding the application of bilateral treaties. We suggest the Committee to prioritise simplicity, while also creating the necessary institutional elements to guarantee the adequate operation of the Protocol. This should include the creation of a Working Group or Subsidiary body to review and update the rules according to international developments. The Protocol should also clearly delineate the methods for adapting the rules for the taxation of cross-border services to new challenges.