



Iberoamerican Tax Moot Court 2019 Case Competition

I. Entities and Individuals

- A. Western Airline Inc. (WA), company duly incorporated under the laws of the Republic of Relojonia.
- B. Aviaper LLC., travel agency dully incorporated under the laws of the Republic of Baguette.
- C. Planning the future, private pension fund located in the Republic of Baguette.

II. Issues

- A. Western Airlines Inc. (here in after WA) is an international airline incorporated in the Republic of Relojonia. 100% of WA shares are fully owned by Planning the Future (herein after PTF) a private pension fund located in the Republic of Baguette.

WA carries out activities in several countries of the world, including Baguette, Llamaland and Relojonia. Normally, it provides international transportation, hence, it does not carry out domestic flights, except in two countries: Llamaland and Relojonia. In Llamaland, WA offers a national flight from the capital, Larco to Omblique, Llamaland's top tourist city. However, travelers willing to go to Omblique must buy the ticket from Baguette's capital: Sina. It is not possible to buy only the ticket Larco - Omblique or vice versa.

Similarly, WA provides transportation services from Sina to Terna, the capital of Relojonia, and from Terna to Telev, the economic and financial center of Relojonia. Nevertheless, it is not possible to buy the ticket from Terna to Telev or vice versa.

WA possesses a general operation center located in Telev, where the logistics of its international flights are managed. Currently, WA's staff is composed by 233 employees, whose tax residence is Baguette. 83 of WA's employees are a regular complement of the company's aircrafts.

Since its incorporation in 1990, WA has been entirely managed from Relojonia. However, as a result of its internationalization process, in 2011 it transferred its three main managerial bodies (CEO, board of directors and advisory council) to the Republic of Baguette.

WA's board of directors is composed by 5 members who are elected annually by the shareholders' assembly in its annual meeting. Likewise, WA bylaws set forth the existence of an advisory council, whose function is to provide concepts upon the board of directors' request on legal, financial, economic and accounting issues.

WA is a highly digitized company. All sales are made online or by phone and customer service is provided online or by means of a call center located in its operation center.

Its passengers' check-in is carried out digitally. Each passenger prints or downloads the boarding pass and registers their cabin luggage by using a machine located at each counter. Such machines are owned by the airports from which WA flights depart.

Following Llamaland's domestic legislation, WA's has a branch incorporated in said country. Nevertheless, its presence in Llamaland only includes the right to use 6 jetties for its airplanes, which are randomly assigned every week by the airport, as well as access to 10 counters, which are randomly made available by the respective airport 4 hours before each flight.

On March 25, 2014, Llamaland's tax authority requested WA to submit its tax income statement regarding income arising in Llamaland. However, WA replied to such a request by asserting that WA was not subject to taxation in Llamaland, for two reasons: (i) WA does not have a permanent establishment in Llamaland; (ii) WA has its place of effective management in Baguette and receives income derived from international transportation, which is not subject to tax in Llamaland, in accordance with the Double taxation convention in force between both nations. These arguments were accepted by Llamaland's tax Administration.

- B. WA provides its customers with on-board entertainment services, which enables passengers to access different films, videogames, documentaries, television, radio and music. Part of WA's profits arise from digital advertising because the company shows ads during its flights by means of the on-board entertainment system.

In respect of advertising services, WA has only one client called Aviaper, which is a travel agency who is resident in Llamaland for tax purposes. Payments made by Aviaper in favor of WA are not subject to withholding tax in Llamaland, since WA informed Aviaper that advertising services are an accessory service to international transportation, which Aviaper accepted.

- C. In February 2016, and upon recommendation of WA advisory body, the shareholders' meeting issued the "Five-Year Development Plan", which is the company's 2016-2021 action plan. Under this plan, WA transferred the operation of its area in charge of entertainment services to Relojonia. From that moment on, the

business consisting of the provision of on-board advertising services started to be entirely provided from Relojonia.

The plan also aims to transfer WA's entire operation to Relojonia, which is supposed to be achieved in January, 2021. WA chose Relojonia for several reasons: (i) Telev has the most prestigious engineering university in the continent, where WA could recruit the trained staff required to carry out its business; (ii) Telev's local government has an entire development plan to promote the consolidation of highly digitalized companies; (iii) Telev possesses a network of servers, known worldwide for their security and reliability; (iv) On April 1, 2016, Relojonia's National Parliament issued Law 4010, under which a tax benefit was created for those companies that provide services by means of technological platforms.

In accordance with Law 4010, the profits arising from technological activities are taxed at a special 3% income tax rate for a 10-year term. While the income tax's general rate in Relojonia is 25%.

Nevertheless, the implementation of the "Five-Year Development Plan" suffered and impasse because on February 15, 2018, while travelling from Larco to Ombligo, a Boeing 737 owned by ATO suffered a terrible accident causing more than 150 fatalities, including company's crew and customers. As a result of the accident and the national mourning generated in Llamaland, the board of directors, the CEO, Mr. Pictor Stark, and the advisory council decided to transfer its offices to Larco in order to face the crisis generated by the accident.

On April 2nd, 2018, ATO's board of directors, CEO and advisory council started to operate in Larco. Everything else remained unaltered. On October 15, 2018, WA's CEO, board of directors and advisory council decided to return its main operations to Sina, as the crisis unleashed by the accident had already been appeased; this decision was executed completely on November 15, 2018.

- D. On February 2nd, 2019 during its annual shareholder meeting, WA presented the following results: En 2018, for the sale of international tickets between Sina and Larco (which includes Ombligue) WA obtained profits equivalent to 35 million moons. The sales between Larco and Terna (which includes the route to Telev) represented 17 million Moons in profits. On the other hand, advertising sales meant 9 million Moons, 4 million on the Sina - Larco route (which includes the journey to Ombligo) and 5 million for the Sina - Terna route (which includes the journey to Telev).

Since 2017 WA is subject to taxation in Relojonia, where its income tax statement is filed. Such situation is due to a Mutual Agreement Procedure achieved between the tax administration of Relojonia and Baguette, according to which WA tax

residence is located in Relojonia. Therefore, following the MAP, WA global income is subject to taxation in Relojonia.

III. Legal and conventional framework

Double taxation conventions

- A. Between Baguette and Llamaland there is a Double Taxation Convention in force since 2014, which follows 2014 OECD Model Tax Convention. Article 10 of such convention reads as follows:

Article 10. Dividends

1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.

2. However, dividends paid by a company which is a resident of a Contracting State may also be taxed in that State according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed 10%.

The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of these limitations. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

3. The term “dividends” as used in this Article means income from shares, “jouissance” shares or “jouissance” rights, mining shares, founders’ shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident through a permanent establishment situated therein and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.

5. Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other State may not impose any tax on the dividends paid by the company, except insofar as such dividends are paid to a resident of that other State or insofar as the holding in respect of which the

dividends are paid is effectively connected with a permanent establishment situated in that other State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.

- B. Between Baguette and Relojonia there is a Double Taxation Convention in force since 2017, which follows 2017 OECD Model Tax Convention. Said Convention includes a protocol, which states:

VI. Ad. Article 10

Dividends paid by a company which is a resident of a Contracting State to a public or private pension fund resident of the other Contracting State may only be taxed in the first mentioned State.

- C. Between Llamaland and Relojonia there is a Double Taxation Convention in force since 2016, which follows 2014 UN Model Tax Convention. Article 12 of said Convention states:

1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed 15 per cent of the gross amount of the royalties. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation.

3. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment or for information concerning industrial, commercial or scientific experience. The term royalties also includes payments of any kind received as a consideration for technical services and digital services.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the royalties are paid is effectively connected with (a) such permanent establishment or

fixed base, or with (b) business activities referred to in (c) of paragraph 1 of Article 7. In such cases the provisions of Article 7 or Article 14, as the case may be, shall apply.

5. Royalties shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying the royalties, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the liability to pay the royalties was incurred, and such royalties are borne by such permanent establishment or fixed base, then such royalties shall be deemed to arise in the State in which the permanent establishment or fixed base is situated.

6. Where by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.

D. Baguette, Llamaland and Relojonia signed, ratified and deposited the Multilateral Instrument (MLI) and currently it is in force in all three countries. Nevertheless, all three countries submitted reservations with respect of the MLI and accepted, exclusively: (i) the minimum standard; and (ii) article 4 of the MLI. Baguette and Llamaland included as Covered Tax Agreements all their double taxation conventions in force. Relojonia included as as Covered Tax Agreements all its double taxation conventions in force, except for the double taxation with Llamaland.

Domestic legislation

A. Llamaland's Internal Revenue Code sets forth:

"Article 9. For tax purposes, a company shall be deemed resident in Llamaland if during the relevant fiscal period its place of effective management is located in Llamaland".

"Article 13. For income tax purposes the fiscal period starts on January 1st and ends on December 31st".

IV. Pleadings

In may, 2019 Llamaland's tax authority carried out an audit regarding the above-mentioned issues and claim the following:

- A. The Tax authority assessed that WA had its place of effective management in Llamaland during 2018. Therefore, WA is liable for taxation in Llamaland for its income obtained worldwide in 2018.
- B. The Tax Administration argues that WA should have withheld the dividends paid by WA in 2019 regarding profits that arose in 2018, in accordance with the double taxation convention in force between Llamaland and Baguette.
- C. The Tax Administration states that WA should have withheld the salaries paid to its employees in accordance with Llamaland's domestic legislation and following the provisions of the double taxation convention in force between Llamaland and Baguette.

V. Current procedure

The case is now pending before Llamaland's High Court. The Court in which you are filing the petition (and before which you will later plead orally) only assesses legal arguments. Assume that you are in a rule-of-law country, where rules as well as general principles of law may be invoked. Please note that the Court will not assess any procedural issue.