THE INTERNET AND TAXATION IN CENTRAL ASIA

by

William V. Vetter, J.D., LL.M.

INTRODUCTION

A reference to "Central Asia" might evoke a mind-picture that is totally blank, or a montage of seas of grass, arid deserts, snow-capped mountains, long lines of two-humped camels carrying silk, cities of legend – like Samarkand and Bukhara – Alexander the Great and Transoxania, and other exotic things. For most of recorded history, that part of Asia between China and the Middle East, and north of the Indian subcontinent, and south of Russia has been known of in the European world, but not known. During some periods it was important because of the spice and silk trade from the East. While Europe was in its "Dark Ages", centers Islamic learning and culture flourished in its oasis cities. For most of the Twentieth Century, it was shrouded within the former Soviet Union. The demise of the Soviet Union has fostered new contacts with Central Asia, in no small part because of its wealth of natural resources.

The growth of the so-called "Global Information Infrastructure" (GII) has reached into previously remote corners of the world. Wherever there is an adequate communications infrastructure, one can access the GII - or at least that part commonly called "the Internet." The former Soviet Union did bequeath a sufficient communications base so that one can now access the Internet from the Central Asian republics that emerged with the Soviet Union's demise – Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan. The proportion of the population with access to the Internet in these republics may be small compared to the United States or Europe, but those with access are among the political, economic, and/or social elite, and they have been quick to take advantage of the benefits of instant worldwide communications.

The combination of international communications and oil has, in about 10 years, brought Central Asia and Central Asians from near total isolation to near center stage.[1] As independent republics, the Central Asian republics need income and they have adopted pages from other countries' books and instituted taxation.[2]

As they do with any person, event, or thing, political governments try to exercise their authority over the Internet and persons interacting through it. Because the Internet uses the existing communication system, most regulatory efforts are attempts to apply rules developed to regulate earlier communications media. In large part (particularly with respect to taxes) there are few laws drafted with Internet in mind; pre-Internet laws are the only ones available. In significant ways, that method of dealing with Internet-related issues is ineffective due to characteristics of the Internet, particularly its disrespect for political boundaries.

Though elected politicians may vigorously deny it, taxation is a subject near and dear to every government official and bureaucrat. With a few exceptions, taxation is the means through which governments confiscate desired financial resources. Tax revenues are used to pay bureaucrats' and elected officials' salaries, build government buildings and monuments, fund government programs and, ultimately, make government's continued existence possible. This extraction of wealth, quite naturally, tends to irritate those who create the wealth that is extracted, *i.e.* taxpayers. Governments (and particularly elected officials) constantly seek new methods to extract the maximum amount of wealth with the minimum amount of taxpayer irritation. As any basic text on taxation states, any thing or event can be used as a basis for taxation. Therefore it is not surprising that the Internet has drawn the attention of persons seeking additional tax revenue. But the Internet's characteristics make it difficult to apply "normal" tax rules and methods.

This paper discusses only taxes that may become due as a result of an event facilitated in some way by Internet communications.[3] In most situations, those will be transactions involving goods or services where the parties use the Internet to communicate about, or to perform all or part of, the transaction. The Internet involvement varies substantially, *e.g.*, it may be used only to transmit the parties' negotiations or agreements; or the "goods" may be fully delivered, or the services entirely performed, on the Internet; or only payment may be made electronically. The terms "Internet transaction" and "Internet-mediated transaction" are used here as including all of those situations, though some may not fall within the common definition of "transaction" and others may employ Internet communications only superficially.

This discussion reviews tax rules in Kazakhstan, the Kyrghyz Republic, and Uzbekistan,[4] and the application of those rules to Internet transactions, with particular attention to whether those raise any unique or insurmountable problems. Part I provides a brief overview of the Internet and Internet-related activities and provides some analogies that may be useful. Part II describes relevant tax rules. Part III discusses the application of those tax rules to Internet transactions.

---

*Assistant Professor of Business Law & Taxation

PART I — THE INTERNET: REALITY AND VIRTUAL REALITY

Many Internet-related discussions, including ones dealing with taxes, are based on assumptions about the Internet's characteristics. Those assumptions are rarely stated and, when exposed, often owe more to popular science fiction than to current reality. It is beyond the scope of this article (and its author's competence) to provide a technical description of the Internet's components or operation. However, a realistic, minimal, layperson-level description is necessary.[5]

It is relatively commonly known that the Internet evolved from a project of a U.S. Defense Department research group to inter-connect their computers.[6] One desired system characteristic was survivability, *i.e.* in the event of disaster (natural or man-made), the loss of part or parts of the system would not disable the entire system. At least in retrospect, it is obvious that a highly decentralized system was the most logical means of achieving that goal. Thus, the system that evolved, and the Internet, does not have a central control point, or even a limited number of major control points. Instead, it is a "system of systems" through which a communication from one point to any other point may take many different routes. A single communication is divided into a number of small portions ("packets") and each may take a different path from origin to destination. A packet traversing the Internet goes through a number of switching points and, at each point, can be passed on toward its destination by a number of routes. If a particular route is unavailable or overloaded, another route is automatically chosen. A route unavailable one moment may be available the next. Since the Internet operates at near-light speed, the fact that different parts of a message take very different routes is of little concern. This is really the heart and genius of the system; it not only satisfies the survivability requirement, it accommodates rapid expansion.

There are a number of potential analogies to the Internet network. One that should be fairly familiar is a city street grid. Assume that there is a small town that has a total of 40 two-way streets, 20 that run north and south, and 20 that run east and west. The outermost streets form a closed square. This creates 400 intersections, most with four potential entrance and exit routes. Now assume that there is a traveler at the far north-east corner of the street grid who wishes to travel to the far south-west corner. There are no restrictions on which streets the hypothetical traveler can take. At each intersection, the traveler can choose to go straight through, turn right, turn left, or reverse direction. Even in such a small grid, there are thousands of potential routes.

The Internet system is similar to the hypothetical street grid, except that there are tens, or hundreds, of thousands of streets and intersections, a message packet may have many more than four potential exit routes from any intersection, and near-light-speed travel makes distance an insignificant factor.[7] The potential number of routes for any Internet message packet between any two computers is effectively infinite.

Any two or more persons with access to Internet can communicate with each other essentially instantaneously. The communication may be data (documents, accounting figures), text (e-mail and "chat rooms"), visual (graphics), vocal (similar to standard telephone), or vocal and visual ("tele-conferencing"). As transmission and computer capacities increase, it is probable that tele-conferencing will soon emulate in-person communication, now without touch or smell — but a patent was recently issued for reproducing smells electronically.

All of these communications are mediated by computers — at least one at each end of the communication.[8] Thus the direct communication is actually between computers. Computers can and do exchange meaningful information without the direct, contemporaneous participation of a human. This point is important because a significant proportion of Internet communications are between a person at her or his computer and a distant computer.[9] For those "unattended" computers, the physical location to which communications are transmitted are irrelevant and need not be recorded.[10] The extent to which the distant computer "interacts" (exchanges information with the distant human) varies substantially.

As anyone familiar with commercial activities might surmise, the Internet's potential for producing economic gain was soon recognized and exploited.[11] Low-cost transmission of information is "natural" for the Internet and "email" remains one of the most-used Internet functions. The development of Internet "websites"[12] exponentially expanded the commercial potential of the electronic communication system. Persons selling digital information (computer programs, digitalized text, graphics, audio, video) can market, sell, and deliver their products to multiple purchasers, 24 hours per day, 365 (or 366) days per year, without employing any sales or delivery staff. The computer does it all, with appropriate programming, of course. Instead of the traditional sales employees, a website owner employs computer programming and maintenance personnel. Commercial use of the Internet has contributed substantially to its growth, and even more substantially to Internet-related legal controversies. Professor Lawrence Lessig makes a convincing argument that the commercialization of the internet is changing, or has already changed, the ability of governments to monitor and regulate Internet transactions and persons using the Internet.[13]

Much of the discussion about the Internet, especially the political kind, is really not about the Internet, but about a hypothetical realm referred to as "cyberspace".[14] "Cyberspace" is a term coined and popular in science fiction novels. It identifies a realm in which electronic communications take place — a realm with no physical existence and therefore no physical boundaries. That Cyberspace is perceptually separate from the physical reality in which human bodies exist and in which there are physical (and therefore jurisdictional) boundaries.[15] There has been significant discussion on how, and indeed if, traditional physical-reality governments can control or influence Cyberspace-related events.

However, Cyberspace – as so envisioned – does not exist on the Internet. In science fiction literature, a corporeal person has sensory stimuli solely from Cyberspace, *i.e.* he or she subjectively enters a totally different reality (*i.e.* a "virtual reality") where electronic data is directly perceived though all that person's senses (sight, touch, taste, feel, sound, etc.). That person

perceptually "moves" from one Cyberspace location to another, at light speed. The Cyberspace traveler's perceived surroundings change just as a physical-reality person's perceived surroundings change when moving from one physical location to another. Talking about Internet-interactions as taking place in "Cyberspace" implicitly adds those far-from-realized characteristics to today's Internet. Therefore, the discussions often ignore the physical reality that does and must exist to create and maintain the Internet and in which even future Cyberspace voyagers will still physically exist.[16]

Regardless of how it may be perceived by a participant, today's Internet is not, and in the foreseeable future will not be, detached from physical reality. An Internet transaction involves communication between computers that physically exist at some identifiable geographic location. The persons involved in that transaction also physically exist at some identifiable location. An electronic transmission from one computer to another is merely that, a transmission. Communication does not result until the transmission or its result is computer-converted to human-sensible form. There should be little doubt that the governments of real-space locations where the computers and/or participants exist have the ability to govern real-world actions, even if those real-world actions are Internet-related.

However, despite the general misapplication, Cyberspace is not a totally unreasonable or un-usable analogy. Geographic location is not inherently relevant to Internet communications — even communications between physical computers located in the same political jurisdiction may be routed across political boundaries. Communications between jurisdictions may avoid boundaries completely via satellite. The physical-world location of any particular Internet-connected computer is frequently not known to, or of any concern to, an Internet user.[17] To the extent that traditional geographic boundaries are irrelevant to Internet-related transactions, traditional legal concepts such as jurisdiction and venue may also appear irrelevant, or at least ill-suited to the task.

PART II — THE REPUBLICS' TAXES

In most instances, the tax laws of the three republics[18] discussed here are quite similar, and are generally consistent with other countries' tax regimes.

Taxpayers

As in any tax system, the most basic provisions relate to who must pay taxes. For income taxes, the republics' definitional provisions indicate that all persons, physical and legal, resident and non-resident, are taxpayers if they receive taxable income, as that is defined in their respective laws.[19] Those laws define "resident" as (1) a physical person who is physically present in the republic for 183 days (or more) during a 12-month period, or (2) a legal entity which was created under the republic's law or that has its effective place of management in the republic.[20] Non-residents are of two kinds, (1) those physical persons and legal entities that have a "permanent establishment" in the republic, and (2) those that only have taxable income sourced in the republic. A "permanent establishment" is defined broadly, and includes:[21]

- A permanent place of entrepreneurial activities of the taxpayer, including activities carried out through agents,[22]
- A construction, assembly, or installation site, including supervision of such sites,
- An installation or construction site, including vessels, used for natural resources exploration, including supervision of such sites, and
- Rendering services, including consulting services.[23]

Income Tax

The taxable income of a non-resident taxpayer (physical person or legal entity) with a permanent establishment includes the republic-sourced income related to that establishment, less establishment-related deductions.[24] If the non-resident taxpayer has unrelated republic-sourced income, the taxpayer is treated as a non-resident without a permanent establishment with respect to the unrelated income.[25] In addition to the "regular" tax a permanent establishment of a legal entity (but not of a physical person) must pay an additional tax . Kazakhstan requires payment of an additional tax equal to 15% of net after-tax income, payable with the regular income tax.[26] The additional Kyrghyz and Uzbekistan tax is 10% and limited to profits transmitted out of the republic.[27]

The taxable income of non-resident taxpayers (including income unrelated to permanent establishments) is limited to income from in-republic sources.[28] Article 5, paragraph 13 of the Kazakhstan Tax Law defines "income from Kazakhstani sources for foreign legal entities and physical persons" as including:

- Income from labor or employment in Kazakhstan[29]
- Income from the manufacture of goods, work performed, or services rendered in Kazakstan,[30]
- Dividend income from, and income from sales of an ownership interest in, a resident legal entity[31]
- Interest income from a Kazakhstani resident[32],
- Interest income from a legal entity with a permanent establishment or assets in Kazakhstan, provided the interest relates to that establishment or those assets,[33]
- Royalty income from the sale, exercise, or transfer of the right to use rights or property in Kazakhstan,[34]
- Income from immoveable property [generally real property] in Kazakhstan, including income from the sale of an interest in such property,[35]
- Income from selling property in Kazakhstan to a resident,[36]

- Pension income paid by a Kazakhstan resident,[37]
- Premium income from insurance agreements in Kazakhstan,[38]
- Income from telecommunications or transportation services between Kazakhstan and another country,[39]
- Income from entrepreneurial activities:
  - received by a permanent establishment in Kazakhstan
  - arising from the sale of goods when, at the time the contract is made, the goods are in Kazakhstan
  - arising from business activities that are the same as, or similar to, activities carried out through a permanent establishment in Kazakhstan, and
  - arising from any type of operation or services when the payment is deducted [for income tax purposes] by a Kazakhstan resident or a permanent establishment in Kazakhstan,[40]
- Any other income that "arises on the basis of activities in" Kazakhstan.[41]

Resident taxpayers, including "tax residents" under the 183-day rule, may be able to offset income taxes paid to foreign countries, not to exceed the republic's tax on the foreign-taxed income.[42]

Income of non-residents, not related to a permanent establishment, are subject to withholding by the payor, based on the gross amount paid, with no deductions:

	Kaz.[43]	Kyr.[44]	Uz.[45]
Dividends, Interest	15%	15%	15%
Insurance Premium Income	5%	5%	10%
International Telecommunications and Transportation Services	5%	5%	6%
Royalties; Services (managerial, consulting); Lease Income; *Other Income*	20%	30%	20%
Labor Income	5% - 30%	30%	20%

The withholding requirement applies without regard to where or how payment is made. A specific exception from the withholding requirement is made for payments to non-residents by Kazakhstan residents for goods imported into Kazakhstan "under foreign trade contracts."[46]

When payments to non-residents require withholding at the source, the payor is responsible for paying the withheld amount to the tax authorities.[47] In Kazakhstan, if payment is made by withdrawing funds from a bank, the withheld amount is to be paid simultaneously with the withdrawal of funds.[48] In all other cases, the withheld amount must be submitted to tax authorities within five banking days following the end of the month in which the payment is made.[49] Withholders are also required to annually submit a summary of amounts paid, amounts withheld, and identifying the payees.[50] While payments to non-residents' permanent establishments do not normally require withholding, under Kazakhstan rules if the payments are made to an account outside Kazakstan, withholding is required unless the payor obtains a "reference document" from the tax authorities and notifies those authorities of the payment.[51] Kazakstan also requires withholding from payments made to taxpayers with permanent establishments if the payment does not relate to the activities of that establishment.[52] The withholding requirements apply regardless of where or how payment is made or the pre-payment location of the funds used.

Value-Added Tax

Value-added taxes ("VAT") are imposed on transactions involving transfers of goods, work or services within each republic, and to all similar imports.[53] A non-resident with an in-republic permanent establishment is treated as a resident for VAT purposes.[54] However, if any other non-resident sells goods and services in a republic, the resident purchaser must pay the related VAT to the government.[55] When goods or services are imported, the VAT applies to import value, including processing and similar charges, but not including taxes.[56] Goods imported by physical persons are VAT exempt to the extent they are exempt from import duties.[57] There are a number of VAT exemptions, some of which might apply to goods imported in Internet transactions.[58] It is possible to interpret Kazakhstan's VAT provision (and its income-source provisions) as excluding transactions involving intellectual property transfers to an end-user. That is based on the Tax Law's general definitions. The Tax Law states that Kazakhstan-source income for non-residents includes "royalty" income from the use or sale of, or the transfer of the right to use, "rights or assets" in Kazakhstan.[59]

The VAT is generally equal to 20% of the sales price,[60] though it is possible that Kazakhstan's may be reduced to 16%.[61]

VAT paid earlier in the production-distribution process is deductible from the tax payable with respect to a later transaction, provided adequate documentation is available.[62] If taxable items are imported from a country that also has a VAT, similar deductions may be available, but the deductions or calculation methods may be varied by a specific treaty.[63] VAT on imported items is payable at the time and place customs duties are payable.[64] Otherwise, payment is made quarterly, monthly, or twice-monthly, depending on the taxpayer's average amount paid.[65]

For VAT-taxable transactions in Kazakhstan by non-residents, there is a payment procedure similar to "withholding at source" for income tax purposes. Kazakhstan residents, and non-residents with Kazakhstan permanent establishments, who purchase from non-residents are required to pay the VAT that would be paid by a resident seller.[66] The VAT so paid "shall be carried out at the expense of the funds transferred to unregistered non-residents".[67] However, this procedure does not apply when the payment relates to goods imported by a Kazakhstan resident under a foreign trade contract.[68]

Enforcement Techniques

Of course, taxes that cannot be enforced produce little revenue. Tax laws must provide methods and means for discovering which persons and entities should pay tax and how much. Payor withholding ("payment at source") is a popular and generally effective means of both identifying taxpayers and collecting the appropriate amounts. Spending other persons' money is much easier than spending one's own. The three republics require third party withholding in a number of situations.[69] Persons and entities that fail to properly withhold and submit are liable for the amounts that should have been withheld, plus interest and penalties,[70] which is a very strong incentive to comply. Not all taxes can be withheld by a payor, particularly taxes that allow deductions and offsets, such as net income taxes. Therefore, additional methods are required.

The most obvious way of determining true tax liability is examining persons' and entities' activities, normally called an "audit." The republics specifically provide for audits of actual and potential taxpayers.[71] Two specifically limit the frequency and length of audits, typically to one per year per taxpayer, to be accomplished in no more than 30 days.[72] So that auditing is possible, taxpayers are required to create and retain accounting records and documentation.[73] Tax officials have the right to receive and review all information concerning the taxpayer's economic activities, to examine the taxpayer's business premises without prior notice, to retain documents for copying, review accounting procedures, and to require the taxpayer to visit the tax department's offices with requested documentation and records.[74] The Kazakhstan Tax Law expressly authorizes tax authorities to adjust a taxpayer's "prices" with respect to transactions between related parties, barter transactions, when there is a significant variation in the taxpayer's prices within an accounting period, and when payments for imported goods or services substantially exceed market prices.[75] Kazakhstan authorities can also adjust the declared income of physical persons based on their consumption and expenditures.[76]

Third parties (not limited to those required to withhold and remit) can play a significant role in the tax compliance process. Except in Uzbekistan, banks have an independent obligation under the tax laws to execute clients' orders to pay taxes on a "priority and unconditional" basis.[77] On demand from tax officials, banks have affirmative obligations to review clients' accounts, provide information concerning those accounts, and to comply with tax officials' orders to freeze funds or pay clients' funds to the government, or both.[78] Other institutions that may have custody of taxpayers' funds have similar obligations.[79] Tax officials can also require that third parties provide information and documentation with respect to economic activities of a taxpayer under audit.[80]

After the tax liability is established, tax officials have a number of means for collecting from reluctant taxpayers, including obtaining a judgment and seizing the taxpayer's property (in his or others' possession) pursuant to court order, and seizing the taxpayer's assets that are in the import or export process.[81] The details of those procedures are not important for this discussion, except for the fact that none of those procedures allow the tax authorities to seize assets that are not within, or under the control of persons within, the republic's physical boundaries.[82]

PART III — DISCUSSION

Internet transactions can ignore political borders and therefore pose a challenge to tax collectors. However, for the most part, the use of electronic communications will affect only a very small part of tax collections. Companies and entrepreneurs will buy and sell properties and services, and own property, and secure gross (if not net) income, and will pay taxes on all those things. Similarly, individuals will work and receive wage and salary income, and will pay tax on that income. This means that the development of Internet will not prevent governments from receiving tax revenues at nearly the same, or maybe even greater, levels.[83] But that does not mean there will be no problems. Changes in society and business always present problems for tax authorities. Some of the problems that have arisen, or that can be anticipated, are discussed in the following pages.

Transaction-Size Related Problems:

One potential problem is the size or value of individual international transactions. Historically, only larger businesses engaged in international transactions, which involved large volumes or very valuable items. Current tax laws and enforcement methods reflect that pattern. The cost of customs inspections and clearance is a small percentage of the value of a shipload of oil, or a train car of full of toys, or even an individual automobile. Thus the cost of collecting related taxes was usually much less than

the amounts collected. Large businesses also have the resources to ensure compliance with a multitude of differing tax laws. However, Internet makes it possible for individuals and small businesses to engage in international transactions involving small, relatively inexpensive items. The resources available to these smaller operations are not abundant; a small increase in costs can turn a successful small business into a bankrupt small business. Costs and risks associated with doing international business can present a significant barrier to smaller businesses that might otherwise take advantage of the larger market available through the Internet. In context, "small" things like withholding rules for income or consumption taxes can be significant trade barriers.[84]

A modest website created by a small retail business in Bukhara, Uzbekistan, or Cody, Wyoming, can attract purchasers from all over the world. Those retailers can take advantage of another relatively recent business (international small parcel delivery services) and ship individual items to many countries with ease. A government's customs clearance costs for such deliveries may well exceed the value of the goods being delivered. Some republics, including Kazakhstan, has a relatively generous *de minimis* customs exemption for delivered parcels, US$200 and seven kilograms.[85] That may prove too low when the number of small shipments increases. An European Union proposal suggests that annual sales of less than 100,000 Euro was a reasonable *de minimis* for VAT registration purposes.[86]

Low customs exemption limits have a tendency to inhibit the entry of small enterprises into the global marketplace. Those enterprises are not in a position to be informed about the intricacies of customs procedures and costs in hundreds of jurisdictions around the world. One example should suffice: The small Wyoming retailer sells C.O.D. a piece of hand-made Native American jewelry for US$400 to an individual resident of Pavlodar, Kazakhstan. The shipping costs are added to the bill and the package given to a parcel delivery service. When it comes time to pay, the Pavlodar purchaser is legally required to deduct 20% for VAT and pay the retailer the balance.[87] It is highly unlikely that the Wyoming retailer would be aware of Kazakhstan's VAT requirements and build that into its selling price. As a result, the sale produces a much smaller profit, and if not a loss.[88] It would take only a few similar experiences before the retailer stopped making such sales to foreign, or any other, purchasers. However, the more common Internet transaction pattern is that the Wyoming business requires full payment by credit card before the item will be shipped, and the seller's website program will accept nothing less. If that procedure is used, the buyer must still pay the 20% VAT – on top of the already paid purchase price – when the item gets to Kazakhstan, which may be an unpleasant surprise. No matter which method is used, international sales are discouraged.[89]

This "small shipment" problem is easily solved. Raising the minimum duty-free, tax-free import limit to something equivalent to US$1,000 or $2,000, or even 100,000 Euros, may produce a net revenue gain. The higher exemption would remove trade barriers, stimulate the participation of small businesses, and eliminate the cost of personnel and facilities necessary to process thousands of small shipments.

Kazakhstan's withholding exemption for "foreign trade contracts" is curious, at least in this context. If it exempts all commercial-volume purchases, essentially all large transactions are exempt.[90] These are the ones with the lowest cost-to-return rate. If the "product" of a contract is delivered electronically, it does not go through customs processing so withholding is probably required.[91] Thus the combined *de minimis* and "trade contract" exemptions leave only medium-value consumer purchases that do not physically transit customs checkpoints subject to withholding. These have the highest cost-to-return rate and are the ones most difficult for tax authorities to detect.

Jurisdictional Problems:

Double Taxation

Jurisdiction to tax is a more challenging problem. It is commonly recognized that a country has jurisdiction over all persons (physical and legal), events, and things within its political boundaries, and over all persons (physical and legal) who are its nationals, without regard to their physical location. This jurisdictional pattern provides independent bases for imposing taxes: physical location and political affiliation.

Affiliation with a taxing jurisdiction creates the potential for double taxation of income whenever a taxpayer is involved in a trans-border event. It is customary to use the term "resident" to identify persons who are nationals and therefore taxed on their worldwide income. That use is not irrational. However, many of these countries also claim jurisdiction to tax their nationals on worldwide income, even if those nationals may be taxed as "residents" under another nation's tax laws.[92] These persons are subject to double taxation, not just on income earned in the "residence" country, but on their worldwide income. Similarly, legal entities can be can be associated with a taxing jurisdiction by either being created there or by having its general management offices there. Thus, a corporation created in one jurisdiction with its principal offices in another may be taxable on its worldwide income in both.[93]

However, this is a general problem, not one created by Internet transactions. Using Internet as a means of doing business increases the number of taxpayers potentially subject to multiple taxation, and will challenge some existing common standards. However, existing statutory and treaty provisions should serve as well with respect to Internet-related income as they do with other types of income. The more difficult problems are in the area of source-of-income rules and what constitutes "presence" in a taxing jurisdiction.

"Presence" in a Taxing Jurisdiction

As indicated earlier, in the republics' laws there are two types of taxable non-residents: (1) those with a local "permanent establishment"; and (2) those who only have republic-sourced income. The two categories, however, raise multi-layered and inter-related problems because taxpayers in the two categories receive differing treatment. Taxpayers with no permanent establishment are taxed on their republic-sourced income (without deductions) and the tax is paid via third-party withholding. In contrast, taxpayers with a permanent establishment are taxed in the same manner as residents, except that taxable income is limited to republic-sourced income and allowable deductions are limited to the expenditures related to that income. This treatment is not unique to Central Asia, therefore tax officials around the world are addressing these problems. Any local treatment that is inconsistent with any generally adopted standard (if and when created) will probably not be enthusiastically supported by foreign governments.

The new question raised by Internet-related business concern the nature and extent of "ecommerce" needed to justify treating it, or its owner, as a tax resident. That question can be narrowed down to what level of local involvement is sufficient to create an electronic "permanent establishment.[94] The level of relationship between the Internet business activities can range from merely being accessible from a given jurisdiction to locating the operational computers and programming in that jurisdiction.

What is sufficient to create a "permanent establishment" in the Internet context poses interesting questions. An Internet website can be "visited" by any person with access to Internet and an appropriate program. The geographic location of the computer containing the website's data (commonly called a "server") is irrelevant, as is the website's owner's location or nationality, which may be different.[95] As indicated earlier, there is usually no way for the Internet user to know where the computer "hosting" the website is located or where the website owner is located. The website could transmit that information, but there is often no reason to do so, and it is not difficult to have a mailing address in a jurisdiction separate from the website owner's. More importantly, rather than the Internet user "going" to the website's geographic location, the website transmits data to the user's computer, which uses its own program to interpret the data and present the results to the user. What the user observes may be no different from what he or she might observe using only programs on his or her local computer.

If a republic resident accesses a website from his domestic office, does that create a domestic presence for the website? An Internet website is functionally equivalent to a domestic physical site in many respects. If the desired product is digital, it makes no difference if the website is just down the street or on the other side of the world. If a tangible product is desired the only difference is delivery time, which also may not be substantially different. It may be more effective and efficient to conduct business through an Internet website than to physically go to a supplier just down the street. However, when the only contact is access from a jurisdiction, the website owner has nothing (tangible or intangible0 in that jurisdiction. There is only a copy of some data from the website program, and that exists only so long as it is held in the local person's commuter. Obviously there is nothing "established" or "permanent" in that circumstance.

Kazakhstan's definition of "permanent establishment" is (like most) based on how business is done in the physical world. Construction, assembly, and installation sites, mines, natural resources exploration sites, offices, factories and shops all necessarily have physical locations.[96] However, "rendering services," which can also lead to a permanent establishment, often does not require a local physical presence. Consultation services need not be delivered in person and are frequently delivered by mail or courier in written form, which can just as easily be done electronically via Internet. This possibility is not lost on persons intent on paying the least possible taxes. Persons and entities providing services and digital products can move their delivery sites or entire operation to jurisdictions with lower tax rates and encouraging legal rules. Those persons need not leave their home country. Of course, there are other persons willing to advise and assist in these moves and at least one of their promotional claims is tax avoidance.[97]

Kaz. Inst. No. 33 - Entities elaborates somewhat on what is required to create a "permanent establishment" by rendering services. Its paragraph 31 states: "Permanent rendering of various types of services . . . on the basis of a contract or any other conditions, the source of payment wherefor is Kazakhstan. . . " leads to a permanent establishment. In contrast, rendering services "on an irregular basis," does not. The implication is that some sort of continuing arrangement is necessary, but neither a continuous physical location nor a specific long-term contract is required.[98] There is also no requirement that the services be rendered to a particular or singular client or that the provider be physically present when services are delivered. The most logical conclusion is that a "permanent establishment" can come into being as a result of services rendered over some time span or by a long-term physical presence. The rules do not exclude a long-term relationship conducted electronically.

The possibility that a Kazakhstan "permanent establishment" might be created by rendering services under a continuing arrangement,[99] without a local physical presence, is supported by the "source of income" rules. Kazakhstan source income includes "income received from any type of . . . services when . . . [the payment] is recognized as a deduction . . . [by] a permanent establishment located in Kazakhstan, and (or) resident of . . . Kazakhstan."[100] The same paragraph includes any "other income" not previously listed that results from "activities in Kazakhstan".[101] From the various subparagraphs, it is clear that the *Instruction*'s writers included a local physical presence requirement when that was intended. Based on the "permanent establishment" description and the source rules, it is not unreasonable to conclude that Kazakhstan takes the position that a taxpayer can create a permanent establishment by rendering continuing services whenever the receiving party is a Kazakhstan resident or permanent establishment which deducts the payments for its own income tax purposes.[102] If services rendered are the use of a website, or data available there, any website accessible via Internet might be a permanent establishment.

Such an interpretation of "permanent establishment" would be inconsistent with developing international interpretation. The OECD takes the consensus position that a website program, in itself, cannot create a permanent establishment because the program has no physical existence.[103] If a website program's "presence" on a domestic server computer does not create a local permanent establishment, it is illogical to conclude that local access to a distant website can create a local permanent establishment.

Web Server as a Permanent Establishment

Even if the mere accessability of a website is insufficient to create a permanent establishment, there is an additional possibility, *i.e.* the server computer on which a website is electronically stored. When someone "visits" a site, she or he is interacting with the programs and data saved in the server-computer's memory. The programs in the server may interact in Cyberspace but the server itself has a real-world physical location. The long-term existence of a server in Kazakhstan would clearly satisfy the "permanent establishment" requirement *for the server's owner*. One computer can contain many websites. Thus, payments by website owners to the server's owner would be Kazakhstan source income, regardless of the website owners' various residence(s) or the place(s) of payment.[104]

Of course, Central Asia is not the only place where the relationship between Internet websites and the definition of "permanent establishment" is a problem. Various working groups of the Organization for Economic Co-operation and Development's Committee on Fiscal Affairs are currently considered many tax-related issues raised by electronic commerce. The OECD Fiscal Affairs Committee has adopted revised Commentary relating to the "permanent establishment" term in its Model Tax Convention, Art. 5.[105] That Commentary recognizes that the long-term physical existence of a server-computer can create a permanent establishment if the owner or lessee, even if there is no related human intervention.[106]

That a server-computer is a permanent establishment does not resolve the status of website programs on that computer. The OECD comments expressly take the position that the mere existence of a website's computer software on a server-computer within a country does not constitute a "permanent establishment" of the website owner in that country.[107] The website program, according to this comment, does not involve any tangible property and therefore is not "a location" that can satisfy the "place of business" requirement[108]

Does a website on a "resident" or "permanent establishment" computer take on the character of the host computer? In one sense, if a computer program can be said to have a physical location, that must be in a computer where the program is saved.[109] The problem here is one of fungibility and practicality. A copy of a website program can be placed on any friendly server in the world. If a government deems it economically desirable to have servers located within its jurisdiction, it may not be wise policy to take the position that a website's presence on the server is the website owner's location for tax purposes. Then even an otherwise-resident website owner could avoid taxes by moving its program to a server in a country with a different policy, which probably will not be difficult to find — something like an "offshore" computer bank, or "cyberhaven".

The OECD Commentary takes the position that a "permanent establishment" of the server's owner does not constitute a "permanent establishment" of any hosted websites unless the server-owner is acting as the website-owner's agent for website-based commerce.[110] This appears consistent with Kazakhstan's position that an independent agent's presence does not create a permanent establishment for taxpayers whom that agent represents.[111] If an independent agent's local, active efforts do not create a permanent establishment, the less-active, less-physical presence of a website on an independent operator's computer also should not create a permanent establishment.

The issue of what is a sufficient connection between a website and a physical location to allow taxation is being argued in the United States with much vigor and little logic. That argument centers on state sales and use taxes, but the issues also affect other taxes. There is no easy solution and any workable solution can only result from international agreement.[112] A unilateral decision by any country to regulate or tax website owners based on their programs' storage in a domestic server will undoubtedly result in a substantial portion of such programs being moved to another location. Therefore, the server-operators will have no clients or income, resulting in a net loss in tax revenue rather than a gain. If the majority of countries adopt a consistent policy, the migration of website programs will probably be substantially lower.[113]

Purely as a matter of administrative convenience (or administrative reality), the determination that a non-resident has a domestic permanent establishment should not be based on either the fact that its website can be accessed from a domestic location or that its website program is stored in a domestic computer. Any attempt to enforce such a conclusion would undoubtedly cost much more than any revenues that may be realized. The most (and maybe only) logical "legal" location of a website is the location of its owner. Regardless of where the computer program may temporarily be recorded, the owner will be less transient and much easier to locate. And, the records relating to the website's operation (and any related income) will be in the owner's control, not moving around with the program data.

On this particular issue, the subject republics' tax rules can currently be interpreted as being consistent with developing international norms. However, there can be serious temptation to interpret tax rules in the manner that imposes tax obligations on nonresidents, since, legally, they have little say in government. Realistically, though, nonresidents can have a significant influence on local government policies and revenue by severing all economic ties or by less transparent means.

Source of Website-Related Income

Resolving the problem of whether (and where) a website is a "permanent establishment" does not resolve all the problems.

For income tax purposes, every income item must also be "sourced" to a particular geographic location. Residents, non-residents, and non-residents with permanent establishments, must answer the question: "Is this particular income from a [*fill in jurisdiction's name*] source?"

The majority of activities and events that the republics' laws and rules identify as producing domestic-source income involve events that physically occur or items that physically exist within the republic, *e.g.* income from labor, income from immoveable property, interest and dividend payments from domestic persons, and the like.[114] There are some source rules where Internet transactions present questions, including those relating to: (1) income from services rendered; (2) income from selling goods or other property; (3) royalty income from the use of property or property rights; (4) non-residents' receipts with regard to which a domestic taxpayer has claimed an income tax deduction; and (5) income that arises from "local" activities. Depending on how source rules are applied, rendering services electronically or transferring electronic data, or the payment for those things by a domestic taxpayer, might result in a tax liability even if the seller/provider has never been in the republic and never directed any activity toward the republic.[115]

A person using a proprietary data base usually pays for that use. If a person in Astana, via Internet, uses an database stored on a computer in Singapore and pays US $100 for that use, has the database owner "rendered services in Kazakhstan"? Does (or should) the answer to that question depend on whether the Astana user can or does deduct the cost as a business expense for Kazakhstan income tax purposes?

Common source-of-income rules were developed before the advent of computerized global electronic communication. For the most part, those rules connect the "source" of any particular income with physical actions. Mineral extraction, manufacturing, sales of tangible items, physical and mental labor, and so on, still occur in an objectively identifiable physical location. However, items that once were sold embedded in tangible objects (*e.g.* audio recordings) can now be transferred without a related physical object. Via Internet, a person in one country can purchase a video recording from a person in another country, and have it delivered from a computer in a third country to a computer in a fourth country, all in a matter of seconds or minutes and without leaving any trace of the transaction.[116] Even if there is no effort to conceal this transaction, existing source rules do not identify the sale income's source. Rational arguments can be made to place the source in any of the four locations.

Similarly, professional services that once were performed using objects like physical books, accounting documents, and technical drawings, can now be performed using only computer memory and processing and electronic transmission. Even more locations might be involved in rendering services than in the video sale example. A professional might use a number of databases in various locations, some just to obtain data, others for more complicated operations. She might also use a remote computer to manipulate data at a higher rate, such as to create rotate-able, "zoom-able" three-dimensional drawings of a building being designed. Here, also, rational arguments could be made to source all or some of the services income where any of the person(s) are located and where any of the computer(s) are located.

With respect to source rules, the arguments, and the results, are very similar to those concerning "permanent establishment." While theory may support locating the income source in different places, common sense and administrative reality suggest that the location where a physical person takes services actions is the most appropriate place to source the income. The most appropriate analogy to Internet-supplied services is a person traveling to another jurisdiction for consultation. A manager of a local factory might go to Taiwan for training related to a new fabricating machine. The Taiwan company charges for, and the domestic company pays for, the training. Under currently accepted rules, the Taiwan company would have Taiwan-source income. If, instead of physically traveling to Taiwan, the manager sits at a computer in his local office and receives the same training via Internet, what and where the Taiwan company performs the training activities does not change. There is no strong argument for placing the source of the Taiwan company's income at the location where the manager is sitting.[117]

Concerning this issue, these republics' income tax source rules will normally cause no conflicts with world norms. But Kazakhstan's definition of "income from entrepreneurial activities" of nonresidents includes income received as a result of any operations or services when the payor deducts the payment for Kazakhstan income tax purposes.[118] Thus, any amount taken by one taxpayer as a business expense deduction must be reported by some other taxpayer as taxable income. It is not difficult to see how a literal application of that definition could cause problems. If a Kazakhstan business reaches out to a foreign supplier, then enters into a contract at, and takes delivery at, the supplier's location, the supplier is subject to Kazakhstan income tax on the contract's proceeds. With a little imagination, one can see how, via Internet, many nonresidents who never purposefully directed any activity toward Kazakhstan may be legally obligated to pay Kazakhstan income tax. Of course, the possibility of Kazakhstan ever collection those taxes from the nonresident may be small. Instead, payment could be extracted from the resident business through the income tax withholding requirements, thereby discouraging international transaction.

Internet and Consumption Taxes

Income taxes are not the only taxes that may be triggered by Internet-mediated events. VAT obligations are imposed on almost every transfer of goods or services. Where, geographically, a transfer occurs establishes which government has jurisdiction to collect the related VAT.[119] When transfer-related events spread over time and space, more than one place and time could be defined to be where the transfer occurred. Thus a transfer between parties in different countries could create VAT liability in both countries, depending on their respective definitions of when and where a transfer legally occurs.

The republics' VAT rules only allow two possible places for a potentially VAT-taxable event to take place: (1) if the transfer takes place within the taxing jurisdiction's political boundaries, the taxable event is the transfer, or (2) if the transfer takes place outside the taxing jurisdiction, the taxable event is moved to a place within the jurisdiction, *i.e.* where the transferred item first enters the customs process. For the sale of tangible goods, an Internet transaction is no different than any other transaction. The provision of VAT-taxable services also present no problem if the person performing the services is within the jurisdiction; standard rules are adequate.

However, when the VAT-taxable event is accomplished by electronic transmission, applying physical-world rules becomes difficult. When data or information is delivered via the Internet, where is "delivery" made? Under the republics' rules for physical goods, the taxable event (legal delivery) takes place where the transferor turns the item over to the carrier. In an electronic transfer, the corresponding act is a person entering a command that sends data from the data-holding computer into the communications system. But the acting person may be a buyer in one jurisdiction activating a computer in a different jurisdiction. The original data-owner takes part in this type of transaction only by previously programming its computer to act on commands from remote locations. Thus, a tangible-goods analogy works only so long is reference is made to the physical location of the transferred item at the time transmission starts, not to any act on the part of the owner of the item.[120]

As is the international norm, the language of the republics' rules were drafted with physical goods in mind, therefore some analogy to transactions involving physical goods must be made. If both the sending and receiving locations are within a single republic, the analogy to physical-world deliveries works. If the original information is in a computer in another jurisdiction, the republics' VAT rules assume there will be a border crossing as part of the delivery. In this situation, trying to apply rules by analogy creates problems because the "goods" do not enter the jurisdiction through any customs point-of-entry. If goods come into a republic, not through an established point of entry, there is a violation of import laws generally called smuggling.[121] To avoid that conclusion with respect to electronic deliveries via Internet, one might argue that information, as such, is not capable of being smuggled or entered through customs channels since it is incorporeal. Before the age of computers and digitalized information, that was probably true and it remains true in many instances. But something generally entered through customs, some item on or in which the information was recorded. Customs duties (and VAT) are based on the transporting physical item's sale price, which may or may not include the contained information's value. If the information happened to be only in a physical person's memory, it was not subject to customs clearance.

Products that were previously transferable only by physical means, which could be smuggled or declared, are now transferable electronically. In the United States there has been a great deal of discussion about this problem, with particular attention to computer programs. The result is that at "canned" or standard programs are treated as taxable goods (they are also sold in boxes from stores) but custom or customized programs are considered services.[122] That distinction might work well enough for sales tax purposes, but is really not relevant to VAT because VAT must be paid for sales of both goods and services. In addition, internationally, the tendency is to assign the VAT-taxable event to the jurisdiction of consumption, *i.e.*, if the seller is in France and the buyer in Germany, Germany's VAT tax would apply.[123]

Assuming that receiving electronic information via Internet is not smuggling, in these republics a buyer has two possibilities, to treat the transaction as one with a resident or as one with a non-resident (and it is possible that the buyer may not know with certainty which is correct). If the seller is treated as a resident or a non-resident with a permanent establishment, the buyer has no VAT obligations. If the seller is treated as a non-resident without a local permanent establishment, the buyer has the obligation to withhold the amount of the seller's VAT obligation, deducting that from the amount paid to the seller. The withheld amount must be submitted to the tax authorities. With most Internet transactions, it is not realistic to expect that the buyer would be able to obtain the desired item or information and unilaterally reduce the amount paid. The remote computer will not likely be programed to transmit any information for the established selling price less VAT withholding.[124] The purchaser is, therefore, required to make prior payment (credit card or otherwise) in the full amount. Thus, what first appeared to be a US $100 purchase is, in fact, a US $120 (or US $130) purchase (plus any income taxes that might also have to be withheld).[125] While the purchaser might avoid income tax withholding obligations by not taking a deduction for the expense, that would not excuse the purchaser from VAT withholding. Regardless of the domestic taxpayer's decision, it will pay (or should pay) at least US $120 for the US $100 purchase.[126] That might be considered a trade barrier that is inconsistent with WTO or other international obligations.

Realistically, tax authorities are unlikely to discover these transactions, partly because they do not come through established customs points. A purchase, or series of purchases, may be discovered in an audit, but only if the auditor was interested in VAT or import violations. The principal result is that VAT will be collected in those instances where the transaction is uncovered in an audit or when the purchaser voluntarily pays VAT (which is not an unrealistic possibility for large transactions). The secondary result is further disrespect for tax laws and tax administrators. If the average taxpayer can "get away" with not paying a tax, she or he will not pay, and will feel superior to the tax collector. And, of course, one successful avoidance encourages others.

The VAT of other countries raise similar problems; and apparently no consensus has been reached. A group of United States companies asked the European Commission to "redesign" the EU tax system so that European companies are not disadvantaged when foreign sellers make direct-to-consumer sales via Internet and do not pay an EU VAT.[127] The U.K.'s Inland Revenue has also recognized the problems with VAT collections posed by e-commerce, and has place that problem relatively high

on its working agenda..[128]

The most practical solution to this problem is to exclude such transactions from all tax withholding requirements. That would be relatively easy, at least in Kazakhstan. The Kazakhstan Tax Law excludes from the withholding requirements residents' payment to non-residents that relate to a "foreign trade contract".[129] By interpreting that term to include a contract that the non-resident performed solely via electronic transmission, the resident would be able to engage in Internet transactions without confronting trade barriers or additional taxes.[130]

The administrative problems posed by attempts to enforce VAT withholding requirements are daunting. If all payments were made through a bank subject to the buyer's republic's control, extracting VAT may be possible. However, there is no way to guarantee that the republics' residents use only one bank's credit card or e-cash card. Even if that were possible, it would not be long before Internet vendors refuse to accept that bank's cards. The result would be that persons who could evade the regulations would, and persons unable or unwilling to violate the rules would be barred from using one of the more popular Internet features. For the tax authorities, the result would be substantial costs which produce a decrease in tax revenue.

SUMMATION

Most of these republics' tax revenues will not be affected by Internet transactions. At least for these republics and the present time, the types of transactions that present problems may be best left alone. For administrative reasons, the most rational decision is to not impose VAT or income tax withholding and payment requirements on Internet transactions involving only electronic transmissions into the taxing jurisdiction. That may leave untaxed some theoretical domestic-source income and domestic VAT-taxable transactions, which is not a pleasant conclusion for any government tax authority. But at least for the present, that may be the only rational and economically feasible course. If a non-resident has a domestic permanent establishment (based on something more than the existence of a website program), sales and services from that establishment can be realistically taxed, even if they result from Internet transactions. Any attempt to impose income and VAT taxes on other non-residents as a result of Internet transactions will be a losing proposition, more likely to result in lower revenues. When and if an international consensus appears concerning these issues, the republics' rules can be changed to accommodate that consensus. Until that time, mere practicality suggests that tax collectors will be much more productive spending their time elsewhere.

Footnotes

---

[1]Within the U.S.S.R., Central Asia was not unknown, but an important part of the overall plan – atomic testing grounds, the Cosmodrome, cotton, abundant natural resources, melons and early crops from desert oases – all played a part in the Soviet scheme. But very few outside the Soviet Union had any information about contemporary events in Central Asia, which was also part of the Soviet plan.

[2]The author's Russian is very limited, therefore this is based on a translations and some differences in meaning or emphasis find their way into even the best translations. Also there may be relevant materials not available in English, but, with the exception of a few terse letters addressing specific taxpayers' questions, the author's inquiries have not revealed them.

The author used English-language translations by QSE, Ltd., 91 Gogol St., Almaty, Kazakhstan (3272-33-60-36), which is deemed reliable. If any errors crept into the English, it is due the to author's misunderstanding, not the translation. All of those translations are based on the official publication of laws in the republics.

NOTE ON NUMBERING FORMAT: The numbering formats used in the various cited sources are not consistent with each other (and sometimes within a single source). The "Bluebook" also does not provide a specific citation format for the relevant countries. The format here used is analogous to that provided for other countries. What would normally be called a "section" in U.S. statutes is normally called an "article" in the Codes here cited. If the source has distinct parts (often designated "sections") with subpart numbers starting with "1", both the part and subpart numbers are given. Numbered or lettered subparagraphs are identified by the article/paragraph number and subparagraph numbers, separated by a period (*e.g.* article 5, subparagraph 3 = art. 5.3). A similar arrangement is used for numbered or lettered sub-subparts. If there are unnumbered paragraphs or parts, a number is brackets is used (*e.g.* art. 234.7[5]).

[3]Many taxes, such as Kazakhstan's excise tax on manufacturing or importing specific types of goods (*e.g.* alcoholic beverages), taxes on subsurface users, the land tax, and tax on motor vehicles, will not be affected by some incidental use of Internet.

[4]These are the economically more important of the five Central Asian republics. Tajikistan continues to be involved in both internal political uncertainty and spillover from Afghanistan. Turkmenistan is relatively large but is mostly desert and has a small population; its petrochemical resources may increase its importance. Its government appears very stable.

[5]This description of the Internet is a layperson's understanding from a number of sources, including court decisions, law review articles, books, and general articles. Persons desiring a technical description will have to search elsewhere. For general descriptions and history, *see* JANET ABBATE, INVENTING THE INTERNET (1999); CHRISTOS J.P. MOSCHOVITIS, ET AL, HISTORY OF THE

INTERNET: A CHRONOLOGY, 1843 TO PRESENT (1999).

[6]The project was necessary to make it possible for computers connected with the system to communicate with each other, without regard to the make, model or operating system of any particular computer. As different companies developed computers, their basic programing and operational aspects differed, so interaction between computers was limited or not possible. Since the military and educational establishments used a wide variety of computers, a common "protocol" or language had to be developed to make the system operational. The most well-known version is known as TCP/IP. However, the Internet came into popular use after the development of "hypertext mark-up language", or "html". The development of html, together with some visionary ideas about the system's potential, lead to the "browser" programs that made the "world wide web" not only feasible, but popular. As the Internet has become more widely used, newer and more sophisticated software has been, and will continue to be, developed. The Internet's popularity and new programing are mutually reinforcing. As the Internet becomes easier to use, and thus more used, the incentive to provide more advanced programs is increased, which triggers even greater popularity. The developing programming may increase governments' ability to regulate Internet-mediated transactions and events. *See, generally,* LAWRENCE LESSIG, CODE AND OTHER LAWS OF CYBERSPACE (2000).

[7]Since light can travel around the globe a number of times in a second, the difference in travel time between an electronic signal traveling 15,000 miles and one traveling 15 miles would probably not be perceptible by unaided human senses. This assumes that there are no transmission delays. That assumption may not be realistic, due to the speeds at which various switching and re-transmission components can handle messages and the ever-increasing number of users.

[8]There are computers at each message switching and transmission point, but their function is independent of message content and the parties' physical location.

[9]For example, a person doing legal research contacts a computer containing legal data, such as statutes or court decisions, "searches" that computer's data for the desired information, and retains a copy of selected information on his or her personal computer (commonly called "downloading"). There are, no doubt, persons controlling or attending the distant computer, but none of them are required to participate in the legal researcher's activities.

[10]Some Internet-related transactions require that the information-recipient identify her or his physical location. For example, the sale of a physical item requires a physical address for delivery. However, that is not an inherent requirement of the communication itself, but is necessary for other purposes. For the sale of digitalized information (such as a computer program), the physical location of the buyer is irrelevant; the digital information is delivered electronically and the buyer pays via a credit card whose issuer need not be, and probably is not, in the same geographic jurisdiction as the buyer or seller.

[11]Even before the Internet, international computer networks were transmitting important commercial information, such as electronic funds transfers, letters of credit. *See, generally,* MOSCHOVITIS, ET AL, *supra* note ?.

[12]A "website" is a computer program that can be accessed by other persons via the Internet's World Wide Web. The website program/information is stored on a computer connected with the Internet (a "server") and is usually available 24 hours per day. The site can consist of any number of interconnected "pages". By "clicking" on a website's hyperlink, the person accessing the site is connected with the page or location indicated, which may be another part of the same site or another site entirely. The degree to which the website "interacts" with the accessing person varies substantially — some merely provide text information, others provide product information, accept orders, and arrange payment and shipment of a tangible item or transmission of a digital item.

[13]*Supra* note 6.

[14]*See* ABBATE, *supra* note ?; Howard B. Stravitz, *Personal Jurisdiction in Cyberspace: Something More is Required on the Electronic Stream of Commerce*, 49 S.C.L. REV. 925 (1998); William S. Byassee, *Jurisdiction of Cyberspace: Applying Real World Precedent to the Virtual Community*, 30 WAKE FOREST L. REV. 197 (1995).

[15]*See* WILLIAM GIBSON, NEUROMANCER at 5 (Ace paperback ed. 1984): "[The hero]... jacked into a custom cyberspace deck that projected his disembodied consciousness into the consensual hallucination that was the matrix." And "quoted" from a "kids' show":

> 'Cyberspace. A consensual hallucination experienced daily by billions of legitimate operators, in every nation, by children being taught mathematical concepts... A graphic representation of data abstracted from the banks of every computer in the human system. Unthinkable complexity. Lines of light ranged in the nonspace of the mind, clusters and constellations of data. Like city lights, receding....' *Id*. at 51.

Gibson's NEUROMANCER is generally credited as the origin of the term "cyberspace". For a "more advanced" version, *see* ALEXANDER BESHER, RIM (Harper Paperbacks ed. 1996), in which the "virtual" world intermingles with the "real" world and both become surreal.

[16]Some science fiction novels are based on the proposition that a human personality (soul?) can be converted to digital information and exist independently, whether the human physical body continues to exist or not. A variation with similar results is the creation of a self-aware computer ("artificial intelligence" or "AI") that exists solely in computer memory and processors. See, *e.g.* GREG EGAN, DIASPORA (1998), which features both, with physical-reality humans becoming extinct. So far as the author is aware, no one has yet succeeded in transferring a human personality to digital information or in creating a self-aware computer.

[17]Technical Internet addresses are a series of numbers and periods, without any obvious geographic reference. Those addresses are commonly counterparts of "domain names", which are "normal" letters and periods, and which may be familiar names. A person wishing to "visit" a particular computer via the Internet enters the appropriate domain name, not the technical address. Domain names may or may not give some indication of the nature or location of the website owner/operator. Many domain names end in ".com" [commercial], ".gov" [government], ".org" [non-governmental organization], or ".edu" [educational organization]. Many non-U.S. domain names include a two-letter abbreviation of the domain's physical (political) location, *e.g.*, ".vz" [Venezuela], ".cn" [China], ".ru" [Russia], "kz." [Kazakhstan]. However, despite the potential for some identification of the site's location or character, the Internet user is frequently indifferent to that identification. Most commercial websites end in ".com", which gives no location information.

[18]**Kazakhstan**: Law of the Republic of Kazakhstan Concerning Taxe s and Other Obligatory Payments to the Budget, *as amended through* Law No. 42 of 29th March 2000 of the Republic of Kazakhstan «Concerning the Introduction of Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan Concerning Issues of Banking Secrecy» (herein "Kaz. Tax Law ").

Previously the basic Kazakhstan tax rules were found in "Edict No. 2235 of 24th April 1995 of the President of Kazakhstan Having the Force of a Law." Significant revisions were made (including changing the title) by Law No. 440 of 16th of July 1999 of the Republic of Kazakhstan "Concerning the Introduction of Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan Concerning Issues of Taxation." Those revisions, and all others enacted through 2000, have been incorporated into the cited text.

The Ministry of State Revenues has been said to be working on a major re-write of the tax rules. However, unless the Ministry's efforts produce a result that is years ahead of similar efforts around the world (and the author hopes it does), most of the problems discussed here will remain.

Kyrghyz Republic: Law of 26th June 1996 of The Kyrghyz Republic, The Tax Code, as amended (herein "Kyrg. Tax Code"). The Kyrghyz Republic is popularly known as Kyrgyzstan but "The Kyrghyz Republic" appears to be its official name.

Uzbekistan: Law No. 386-I of 24th April 1997 of the Republic of Uzbekistan, Effective as of the 1st January 1998, The Tax Code of The Republic of Uzbekistan, as amended (herein "Uzb. Tax Code").

[19]Kaz. Tax Law, *supra* note 18, art. 6; Kyrg. Tax Code, *supra* note 18, arts. 72, 91; Uzb. Tax Code, *supra* note 18, arts. 13, 44. The Kyrghyz Tax Code distinguishes "income tax" (payable by physical persons) and "profits tax" (payable by legal entities). The distinction is not significant for this discussion.

[20]Kaz. Tax Law, *supra* note 18, art. 5.36; Kyrg. Tax Code, *supra* note 18, arts. 9.26, 9.39; Uzb. Tax Code, *supra* note 18, arts. 14, 45. The Kyrghyz Tax Code requires that the 183 days be "continuous" (Art. 9.26); the others only count the number of days present during 12-month periods.

[21]Kaz. Tax Law, *supra* note 18, art. 5.31. Additional detail on what constitutes a permanent establishment is given in paras. 27 -31, Instructions No. 33 of June 28, 1995 of the Main Tax Inspectorate of the Ministry of Finance of the Republic of Kazakhstan, "Concerning the Procedure for Assessment and Payment to the Budget of Income Tax from Legal Entities, *as amended through* Order No. 301 of 5th April 2000 of the Minister of State Revenues of the Republic of Kazakhstan, "Concerning the Approval of Amendments to the Instructions No. 33 of the Main Tax Inspectorate of the Ministry of Finance of the Republic of Kazakhstan «Concerning the Procedure for the Assessment and Payment to the Budget of Income Tax from Legal Entities»." (hereafter "Kaz. Inst. No. 33 - Entities"). Through interim reorganizations and changes of name, the collection of taxes has been reassigned from the Ministry of Finance to the Ministry of State Revenues. *See also* Kyrg. Tax Code, *supra* note 18, art. 9.39. The Uzbekistan Tax Code does not elaborate on the "permanent establishment" term. *See* Uzb. Tax Code, *supra* note 18, art. 33.

[22]Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 29, states that an agent "with an independent status" does not result in a physical establishment of the principal, with "independence" meaning both legal and economic independence. Apparently the word "agent" in Kaz. Tax Law, *supra* note 18, art. 5.31 is intended to include only employees and corporate subsidiaries. However, a corporate subsidiary formed under Kazakhstan law is considered an independent taxpayer and, therefore, it does not establish a Kazakhstan physical establishment for the holding corporation. *Id.*

[23]Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 31, explains that "[p]ermanent rendering . . . of services . . . on the basis of a contract or any other conditions" creates a permanent establishment. While less than absolutely clear, that indicates more than

infrequent or short-term services are required. A subparagraph states that the services, to create a permanent establishment, must be rendered in Kazakhstan. Based on those explanations, it would appear that when services work is principally done outside Kazakhstan and only the results delivered to Kazakhstan, no permanent establishment is created. From either the Tax Code or the *Instructions*, it is not possible to draw any reasoned conclusion concerning whether, or the point at which, providing long-term trans-border services gives rise to a permanent establishment.

The Kazakhstan Tax Law defines "long term contract" as one for performance over a period longer than one year. Kaz. Tax Law, *supra* note 18, art. 5.11. However, the *Instructions*, taken as a whole, make it quite clear that there is no minimum time necessary to create a permanent establishment. They also support the inference that the drafters had some sort of physical presence in mind.

[24]Kaz. Tax Law, *supra* note 18, art. 35; Kyrg. Tax Code, *supra* note 18, art. 93; Uzb. Tax Code, *supra* note 18, arts. 33, 45. *See also* Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 26; Instruction No. 40 of the Main Tax Inspectorate of the Ministry of Finance of the Republic of Kazakhstan "Concerning the Procedure for the Assessment and Payment of Income Tax from Physical Persons" *as amended through* Order 929 of 4th August 1999 of the Minister of State Revenues of the Republic of Kazakhstan "Concerning the Introduction of Amendments and Additions to Instructions No. 40 «Concerning the Procedure for the Assessment and Payment of Income Tax from Physical Persons»," para. 56 (hereafter "Kaz. Inst. No. 40 - Physical Persons").

If the permanent establishment's accounting records adequately separate the non-resident's out-of-republic source income, those are the only records, income, or expenses considered. However, all related transactions must be included in that accounting, including those actually taking place outside the jurisdiction. The republics thus use the "separate accounting" regime employed in many countries. The Kazakhstan *Instructions* include additional means for determining taxable income if the taxpayer's accounting is inadequate. The taxpayer and the relevant tax authority are allowed to agree to apportionment based on sales income, expenses, *or* number of employees (singly, not in combination). Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 4. If those methods prove impossible, taxable income can be determined based on receipts from sales, or on expenditures, assuming "25 percent profitability". *Id*. para. 5. Kyrghyz rules reach the same result, but indirectly. A permanent establishment's aggregate income is its Kyrghyz-source income. Kyrg. Tax Code, *supra* note 18, art. 93. Only costs "associated with earning [aggregate] income" are allowable deductions. Kyrg. Tax Code, *supra* note 18, art. 94.

[25]Kaz. Tax Law, *supra* note 18, arts. 35, 36; Kyrg. Tax Code, *supra* note 18, art. 109; Uzb. Tax Code, *supra* note 18, art. 30.

[26]Kaz. Tax Law, *supra* note 18, art. 37. Additions to paid-in capital are also deductible before calculating the additional tax. *Id*.

[27]Kyrg. Tax Code, *supra* note 18, art. 110 ("exported income"); Uzb. Tax Code, *supra* note 18, art. 35 (income "transmitted abroad").

[28]Kaz. Tax Law, *supra* note 18, art. 9.2; Kyrg. Tax Code, *supra* note 18, arts. 74, 93; Uzb. Tax Code, *supra* note 18, arts. 14, 45.

[29]Kaz. Tax Law, *supra* note 18, art. 5.13(a). *See also* Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 38. Kaz. Inst. No. 33 - Entities, para. 38, contains the source list similar to Kaz. Tax Law, *supra* note 18, art. 5.13. However, the *Instructions* concerning "physical persons" does not, perhaps raising some questions with respect to differing treatment for physical persons and entities. *See* Kaz. Inst. No. 40 - Physical Persons, *supra* note 24, paras. 53 - 57.

[30]Kaz. Tax Law, *supra* note 18, art. 5.13(b)

[31]*Id*., art. 5.13(d).

[32]*Id*., art. 5.13(e).

[33]*Id*.

[34]*Id*., art. 5.13(f).

"Royalty" is defined, for general purposes, in Kaz. Tax Law, *supra* note 18, art. 5.37 as:

> a) the right to use the subsurface in the course of extracting useful minerals and processing technogenic formations;
> b) the use or the right to use copyright, software, patents, drawings or models, trademarks, or any other similar types of rights; use or right to use industrial, commercial or scientific research equipment; use of know-how; use or right to use films, video films, audio records or any other recording facilities [media?]; rendering of technical assistance in this connection.

[35]*Id*., art. 5.13(g).

[36]*Id*., art. 5.13(h).

[37]*Id*., art. 5.13(i).

[38]*Id*., art. 5.13(j).

[39] *Id*., art. 5.13(k).

[40] *Id*., art. 5.13(c). Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 38[1], explains that the general "income from sale of goods" provision applies whenever the goods are within Kazakstan at the time the contract is made, regardless of the parties' physical locations or residences.

[41] Kaz. Tax Law, *supra* note 18, art. 5.13(*l*).

[42] *Id*., art. 38. Both the Kyrghyz Tax Code (Kyrg. Tax Code, *supra* note 18, art. 44.1) and the Uzbekistan Tax Code (Uzb. Tax Code, *supra* note 18, art. 15) appear to limit the foreign tax credit to taxes paid to countries with which the Republic has a "double tax avoidance" treaty. Kazakhstan has no similar limitation.

[43] Kaz. Tax Law, *supra* note 18, arts. 33, 36. *See also* Kaz. Inst. No. 33 - Entities, *supra* note 21, paras. 36, 47; Kaz. Inst. No. 40 - Physical Persons, *supra* note 24, paras. 44, 47. The Tax Code indicates that if a taxpayer does not withhold the required amount, the tax is levied on that taxpayer. Kaz. Tax Law, *supra* note 18, art. 54.5 (VAT), art. 163-4 (income tax). However, Ministry *Instructions* impose a 50% fine for failure to withhold (income tax) or pay the VAT due from a non-resident seller. *See* Section XXIX, para. 5 (VAT), and 6 (income tax) of Instructions No. 43 of 1st July 1995 of The Main Tax Inspectorate of the Ministry of Finance of the Republic of Kazakhstan. "Concerning Administrative Provisions Concerning Taxes and Other Obligatory Payments to the Budget", *as amended through* Order No. 929 of 4th August 1999 of the Minister of State Revenues of the Republic of Kazakhstan, Registered with the Ministry of Justice, No. 889, 13th September 1999, "Concerning Introduction of Amendments and Additions to Instructions No. 43 «Concerning Administrative Provisions for Taxes and Other Obligatory Payments to the Budget»." (hereafter "Kaz. Inst. No. 43 - Admin.").

[44] Kyrg. Tax Code, *supra* note 18, art. 109. *See also* "Instructions Concerning the Procedure for the Assessment and Payment to the Budget of Tax on Profits From Legal Entities (Issued on the Basis of the Tax Code)", approved by Decree No. 291 of 29th June 1996 of the Government of the Kyrghyz Republic, para. 26.

[45] Uzb. Tax Code, *supra* note 18, art. 30, 57.

[46] Kaz. Tax Law, *supra* note 18, art. 36.1. *See also* Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 36; Kaz. Inst. No. 40 - Physical Persons, *supra* note 24, para. 57. What is covered by "foreign trade contracts" is not obvious. Kaz. Tax Law, *supra* note 18, art. 73.2 (regarding VAT withholding) might be read to include only contracts with respect to which the goods have gone through normal customs processing. The other places where that term is used (Tax Law and Instructions) do not really support such a reading of the basic law.

[47] Kaz. Tax Law, *supra* note 18, art. 50.3; Kyrg. Tax Code, *supra* note 18, art. 50.2; Uzb. Tax Code, *supra* note 18, arts. 42, 63.

[48] Kaz. Tax Law, *supra* note 18, art. 50.4.1. *See also* Kaz. Inst. No. 43 - Admin., *supra* note 43, sec. XVI.

[49] *Id*.; Kyrg. Tax Code, *supra* note 18, art. 50.3 (10 days); Uzb. Tax Code, *supra* note 18, arts. 42, 63.

[50] Kaz. Tax Law, *supra* note 18, art. 50.4.3. A similar summary is to be given to the persons and entities to whom such payments have been made, if those persons request it. *Id*. *See also* Uzb. Tax Code, *supra* note 18, arts. 42, 63.

[51] *Kaz. Inst. No. 33 - Entities*, *supra* note 21, para 32. Though the mechanics of this process is unclear in translation, it is obviously intended to provide documentation of the permanent establishment's receipt of income that does not pass through Kazakhstan bank accounts (which are subject to audit by tax authorities). *See also* Kaz. Inst. No. 43 - Administration, *supra* note 43, paras. XI, XXVI. A similar documentation is required if payments (to residents or non-residents) are made by someone other than the entity receiving the paid-for consideration, though withholding is not required. *Id.*

[52] Kaz. Inst. No. 33 - Entities, *supra* note 21, paras. 36, 37.

[53] Kaz. Tax Law, *supra* note 18, art. 53.1; Kyrg. Tax Code, *supra* note 18, arts. 116, 117; Uzb. Tax Code, *supra* note 18, art. 67. *See generally* Instructions No. 37, Approved by Order No. 159 of the Minister of Finance of the Republic of Kazakstan, June 26, 1995, "Concerning the Procedure for the Assessment and Payment of Value-Added Tax," *as amended through* Order No. 929 of 4th August 1999 of the Minister of State Revenues of the Republic of Kazakhstan, Ministry of Justice Registration No. 963, 6 November 1999, "Concerning the Introduction of Amendments and Additions to the Instructions No. 37 of the 26th of June 1995 of the Main State Tax Inspectorate of the Ministry of Finance of the Republic of Kazakhstan «Concerning the Procedure for the Assessment and Payment of Value-Added Tax»." (hereafter "Kaz. Inst. No. 37 - VAT").

Various provisions are also made for the payment of VAT when a VAT payor diverts taxable items from the distribution stream for its own use or for the use of employees or owners. *See, generally*, Kaz. Tax Law, *supra* note 18, art. 56.

Under Kyrghyz rules the place of the taxable sale is the delivery location, but if delivery is made via transportation, the

sale location is where the goods are delivered to the carrier (Kyrg. Tax Code, *supra* note 18, art. 135) but if the goods are imported, VAT is applied where the goods first cross the border, regardless of the delivery method.

[54]*See* Kaz. Inst. No. 37 - VAT, *supra* note 53, paras. 9, 9-2.

[55]Kaz. Tax Law, *supra* note 18, art. 55.4. *See also* Kaz. Inst. No. 37 - VAT, *supra* note 53, para. 9-2.

[56]Kaz. Tax Law, *supra* note 18, art. 70.4 *See also* Kaz. Inst. No. 37 - VAT, *supra* note 53, para. 29.

[57]Kaz. Tax Law, *supra* note 18, art. 70.2; Uzb. Tax Code, *supra* note 18, art. 71.11 The Customs Committee's "Explanations Concerning Decree No. 1712 of 31st December 1996 of the Government of the Republic of Kazakhstan, «Concerning the Procedure for Conveyance of Goods by Physical Persons Through the Customs Boundary of the Republic of Kazakhstan, Including Transport Vehicles»" at paragraph 4.1 states that persons traveling into Kazakhstan may import, free of duty and VAT, goods having a value of up to US$2,000, with a weight not to exceed 70 kilograms. Additional goods are subject to special duty rates but do not appear to be exempt from VAT. *Id*. paras. 5 - 8. Goods shipped to a physical person in Kazakhstan by international postal "dispatch" or "parcel" are exempt from customs duties and VAT up to US$200 in value and 7 kilograms in weight. *Id.* paras. 16(a), 17. Duty-free import of goods subject to excise tax (alcoholic beverages, tobacco products, fuels, etc.) are subject to individual quotas, and included within the general limitation described above. *See* Supplement 2 to Decree No. 907 of the Government of the Republic of Kazakhstan May 30 1997, "The Quotas Exempt from Excise Duty for the Conveyance of Excisable Goods Through the Customs Boundary of the Republic of Kazakhstan by Physical Persons."

[58]Kaz. Tax Law, *supra* note 18, art. 57; Kyrg. Tax Code, *supra* note 18, art. 147; Uzb. Tax Code, *supra* note 18, art. 71. Some exemptions that might apply include exemptions for financial services, educational materials (books, etc.) and services, pharmaceuticals and prosthetics, medical services, legal services. *Id*. Uzbekistan's VAT exemptions include payments for licenses, fees and registration relating to the acquisition of "rights to intellectual properties." Uzb. Tax Code, *supra* note 18, art 71.9. That section expressly exempts "licensing payments". Whether consumers' payments to a copyright holder for the right to use digital products are exempt is not certain. Reasonable arguments can be made both for and against such an interpretation.

[59]Kaz. Tax Law, *supra* note 18, art. 5.13.f). *See also id*., art. 5.37 (definition of "royalty"). In a U.S. publication attributed to the U.S. Embassy in Almaty, that interpretation is stated as being a fixed rule. *See* U.S. Department of Commerce, BISNIS Bulletin (Aug. 2000), at p. 6. No authority is there cited, but is it highly likely to be based on actual practices. The same source asserts that no documentation is required "for the import of digital products over the Internet." *Id*.

[60]Kaz. Tax Law, *supra* note 18, arts. 62, 70-1.1; Kyrg. Tax Code, *supra* note 18, art. 119; Uzb. Tax Code, *supra* note 18, art. 74 ("socially significant food item" 10% VAT). There are some lower rates that apply to particular industries or sales (primarily food commodities), none is likely to apply to an Internet-related transaction. Kaz. Tax Law, *supra* note 18, arts. 62.3, 70-1.3.

[61]A recent news report stated that the Kazakhstan legislature has approved a bill reducing the VAT to 15%. Whether that has been approved by the President and implemented is not known by the author at publication time. The VAT rate is not particularly important for this article, despite its importance to taxpayers. *See* Interfax-Kazakhstan, *Kazakh Parliament Passes Bill to Cut Vat and Social Tax Rates*, *published in* THE TIMES OF CENTRAL ASIA [INTERNET ED.] (Apr. 17, 2001), *found at* <http://www.times.kg/?D=article&aid+1017121> (May 27, 2001).

[62]Kaz. Tax Law, *supra* note 18, arts. 64 - 66.

[63]*See id*., art. 55 [treaties], 70 [CIS countries].

[64]*Id*., art. 70-1. *See also* Kaz. Inst. No. 37 - VAT, *supra* note 53, para. 54. A three-month extension can be obtained if the goods are raw materials or consumables imported for industrial processing. *Id*.

[65]*Id*., art. 70-1

[66]*Id*., art. 54.5; Kaz. Inst. No. 37 - VAT, *supra* note 53, para. 9-2. There may also be an added 50% fine. See note 43, *supra*

[67]*Id*.

[68]*Id*. This particular provision might be considered ambiguous because of its similarity with the provision exempting such payments from the withholding at source requirement for income tax purposes. See discussion at note ?, *supra*. However, it does not exempt the transaction from VAT, only from this particular payment method. VAT on imported items are payable in conjunction with import duties. *Id*., art. 70-1.

[69]One result of the withholding requirements is the reduction of the number of tax returns from individuals. Persons with income consisting of only wages/salary, interest, and/or dividends have their exact taxes paid and need not file returns. Reducing the number of returns certainly has administrative benefits but it also may make it more difficult to identify individuals that underpay.

Under that regime, the fact that a person does not file a return does not raise any suspicion of tax evasion, since that is normal. Some of the "evasion" might be totally innocent, especially in countries where individual tax payment is not an established practice. The fact that government officials are equally inexperienced in collecting taxe s make it even less likely that individuals who should pay additional taxes are identified. One can easily understand why *elected* government officials did not spend a great amount of time and effort educating taxpayers about their obligations.

[70]*See* Kaz. Tax Law, *supra* note 18, art. 50.3, 163-4; Kyrg. Tax Code, *supra* note 18, art. 50.2; Uzb. Tax Code, *supra* note 18, art. 42, 63.

[71]*See* Kaz. Tax Law, *supra* note 18, art. 137, 171.1.1; Kyrg. Tax Code, *supra* note 18, art. 13; Uzb. Tax Code, *supra* note 18, art. 13. Empowering government employees to audit taxpayers also creates the possibility of collusion. During difficult economic, political, and administrative times, paying the "tax man" to look the other way might be easier and less expensive than paying taxes, especially if the tax man suggests the payment and describes potential alternatives. This is not intended to imply that such things are more likely to happen in these republics than anywhere else.

[72]Kaz. Tax Law, *supra* note 18, art. 137; Kyrg. Tax Code, *supra* note 18, art. 13.2; Uzb. Tax Code, *supra* note 18, art.12.3 . Under the Kyrghyz Tax Code, if the Tax Service obtains, after an audit is completed, documentation that the taxpayer has understated its tax obligation, the audit can be reopened, but for no more than 10 days and limited by the newly discovered evidence. Kyrg. Tax Code, *supra* note 18, art. 13.2. The Kyrghyz Tax Code also requires that all audits be authorized by the head of the State Tax Committee. Kyrg. Tax Code, *supra* note 18, art. 13.2. Kazakhstan's tax rules limit audits with respect to any one tax to once per half-year and "integrated" audits to once per year. Kaz. Tax Law, *supra* note 18, art. 137.2

[73]*See* Kaz. Tax Law, *supra* note 18, art. 143; Kyrg. Tax Code, *supra* note 18, art. 23; Uzb. Tax Code, *supra* note 18, art. 12, 41, 62. This, too, is another "innovation" in the post-U.S.S.R. world; far fewer persons understand the basics of accounting than understand the basics of capitalist enterprise. The persons with the greatest experience in "business" are the ones selling products in open markets or on the street, who have had no need for, or experience with, accounting records. The cost of creating and maintaining such records could significantly reduce their net income.

[74]*See* Kaz. Tax Law, *supra* note 18, art. 142; Kyrg. Tax Code, *supra* note 18, art. 27 (warrant required for entrance to business premises without notice, and limited to business hours).

[75]Kaz. Tax Law, *supra* note 18, art. 138-1. The term "prices" should not be treated as limiting this authority to the taxpayer's sales prices. The clear import of art. 138-1 as a whole is that the tax authorities can adjust any accounting entry.

[76]*Id*. *See also* Kyrg. Tax Code, *supra* note 18, art. 127 (general right to revise submitted figures considered inaccurate, with notice to the taxpayer).

[77]*See* Kaz. Tax Law, *supra* note 18, art. 147.2; Kyrg. Tax Code, *supra* note 18, art. 28.1(2), (3), (5).

[78]*See* Kaz. Tax Law, *supra* note 18, art. 147.4 - 147.6; Kyrg. Tax Code, *supra* note 18, art. 28.1(5).

[79]Kaz. Tax Law, *supra* note 18, art 171.1; Kyrg. Tax Code, *supra* note 18, art. 28.2 (commodity exchanges and stock exchanges).

[80]Kaz. Tax Law, *supra* note 18, art. 146, 171; Kyrg. Tax Code, *supra* note 18, art. 27.1. *Cf.* Uzb. Tax Code, *supra* note 18, art. 12.2 (taxpayers' obligation to submit documents not expressly limited to ones relevant to their own taxes).

[81]*See, e.g.* Kaz. Tax Law, *supra* note 18, art. 154 - 159; Kyrg. Tax Code, *supra* note 18, art. 51 - 56. The Uzbekistan Tax Code contains very general authorizations to apply the taxpayer's assets to tax debts "pursuant to decisions of the court." Uzb. Tax Code, *supra* note 18, art. 130, 134. With respect only to legal entities, tax authorities can administratively take collection actions and impose sanctions. *Id*. Customs officials can detain goods in the import or export process, as security, prior to a court decision. *Id*.

[82]*Id.* Some tax treaties may authorize or require cooperation in collecting taxes due to the party-states. However, those procedures are controlled by the individual treaty's provisions and are probably unrealistically expensive except when a particular taxpayer owes very substantial sums.

[83]Many tax officials of the states of the United States are stating very loudly that their inability to tax Internet-related transactions however they choose will soon result in the states' total bankruptcy. Those statements should be placed in the category of political campaign speeches, which they essentially are. When placed in context of all state tax revenues (which these officials never do), it is apparent that their rhetoric is very much ado about slightly more than nothing.

[84]The European Union recognizes the potential impact on small businesses in its proposals for VAT enforcement vis-a-vis non-EU sellers. Its February, 2001, proposal would exempt non-EU sellers with less than 100,000 Euros in sales to EU residents. *See*

European Union Commission, EU Doc. 500PC0349(02), *Proposal for a Council Directive amending Directive 77/388/EEC as regards the value added tax arrangements applicable to certain services supplied by electronic mean*, Expl. para. 5.2, and prop. art. 24(2a) (Feb. 2001) (herein "EU Comm'n. VAT Proposal"), *available at* <http://europa.eu.int/eur-lex/en/com/dat/2000/en_500PC0349(02)>, *visited* May 30, 2001. That proposal has been withdrawn because of significant objection to its registration provisions, which relate only indirectly to its suggested *de minimis* exemption.

[85]*See* note 57, *supra*.

[86]*See* EU Comm'n VAT Proposal, *supra* note 84.

[87]He does not withhold deduct income tax because the item was not in Kazakhstan when it was sold and its purchase is a non-deductible personal expense. *See* text at note 40, *supra*.

[88]Since collection costs would probably exceed the amount to be collected ($80 in the example), and the Wyoming seller would probably have no idea about how to go about collecting, the full selling price would never be received on a COD shipment.

[89]The total VAT cost to the purchaser may be reduced by VAT payments made in other countries, provided the necessary documentation is available. At least on their face, VAT requirements are not intended to have a protectionist purpose. Specific provisions in tax treaties can lessen this impact, as will global standardization of VAT documentation requirements.

[90]However, one could read the Kazakhstan Tax Code as allowing the VAT-withholding exemption for "foreign trade contracts" only when the subject items are processed through a customs entry point. *See* Kaz. Tax Law, *supra* note 18, art. 73.2.

[91]One might argue that no VAT is payable because neither to the Code-defined events (transaction in Kazakhstan or passage through Customs) occurred. It is likely that the tax authorities would take the position that the transaction did come through the national customs boundary, just not through an established checkpoint.

[92]See U.S. Internal Revenue Code § 7701(a)(30).

[93]*See, e.g.*, Kaz. Tax Code art. 5.36; Kyrg. Tax Code, *supra* note 18, art. 9.24; Uzb. Tax Code, *supra* note 18, art. 14. Therefore, a joint stock company organized in Kazakhstan with its principal office in Bishkek would be a "resident" of both Kazakstan and the Kyrghyz Republic.

[94]If the business owner (individual or entity) is a tax resident or has a physical "permanent establishment", the question of whether there is an electronic permanent establishment never arises.

[95]Current technology allows a person or entity to establish a website in any computer with appropriate capacity, programming and connections. That computer can be in the owner's office or in any other location in the world. Website programming can be accomplished through the Internet and can allow the website to function without continuing human intervention. It is not uncommon to establish "mirror" sites at various geographic locations to minimize transmission delays and errors. When that is done, the practical result is a single website "located" in more than one jurisdiction.

[96]Kaz. Tax Code art. 5.31; Kaz. Inst. No. 33 - Entities, *supra* note 21, paras. 27 - 33. The Kazakhstan rules conform, in large part, to international norms, particularly those published by the OECD. A multi-national group, the Organization for Economic Co-operation and Development (OECD), has published a "Model Tax Convention" that is used in whole or substantial art by many countries, including Kazakhstan. That Model is available at <http://www.oecd.org/daf/fa/treaties/treaty.htm>. The OECD Model Convention and related "Commentaries" represent a consensus among a major portion of trading nations.

[97]*See, e.g.*, Andrea Wilson, *E-Commerce Goes to Bermuda*, E-COMMERCE TIMES (visited Feb. 8, 2000) <http://www.ecommercetimes/news/special_reports/bermuda.shtml>. The author is co-founder and Senior V-P of First Atlantic Commerce Ltd., which consults and assists businesses that are interested in moving to Bermuda. The article claims that Bermuda-based operations are not required to collect or remit some transaction taxes, including VAT. That claim may or may not be supportable in any particular context.

[98]Despite the general rule, conducting an "exhibition" creates a permanent establishment if there is a charge for admission or goods are sold. Kaz. Inst. 33 - Entities, *supra* note 21, para. 33. This particular provision is probably inconsistent with the more general rule that prepatory activities do not create permanent establishments. *See, e.g.*, OECD Model Treaty, *supra* note 96, art. 5. It is also not consistent with some Kazakstan treaties, which are similar to the OECD model. *See, e.g.*, The Convention Between the Republic of Kazakhstan and the Hungarian Republic on the Avoidance of Double Taxation and Prevention of Fiscal Evasion with Regard to Taxes on Income and Capital, art. 5, para. 4.

[99]There is no quantification of the length of term necessary to create a permanent establishment. The Kazakhstan Tax Code defines a long-term contract as one requiring work for more than one year. Kaz. Tax Code, art. 5. Various treaties require that an

operation exist for more than one year to be a "permanent establishment" under the treaty. *See, e.g.*, Treaty with Hungary, *supra* note 98, art. 3. The fact that the Instructions studiously avoid using quantified time terms, and includes operations that could easily exist for less than one year, makes it inadvisable to assume that there is some minimum time requirement.

[100]Kaz. Inst. 33 - Entities, *supra* note 21, para. 38[2].

[101]*Id*. at para. 33[11].

[102]For example, a local company might "subscribe" to a stock-exchange database. If the database is accessible via Internet, it could be seen as having, in effect, a continuous presence in the jurisdiction. A small minority of U.S. courts have reached such a conclusion.

[103]*See* OECD, Committee on Fiscal Affairs, *Clarification on the Application of the Permanent Establishment Definition in E-Commerce: Changes to the Commentary on the Model Tax Convention on Article 5* (Dec. 22, 2000), <http://www.oecd.org/daf/fa/e_com/public_release.html>, *download from* <http://www.oecd.org/daf/fa/e-con/ec_1_PE_Eng.pdf> (May 30, 2001).

[104]Kaz. Inst. No. 33 - Entities, *supra* note 21, para. 38. That result is consistent with the OECD position. *See* OECD Commentary, *supra* note 103.

[105]OECD Commentary, *supra* note 103.

[106]*Id*., comment 42.6, p. 6.

[107]OECD Commentary, *supra* note 103, comment 42.2, p. 5.

[108]*Id*., para. 2.

[109]An interesting philosophical question is whether a computer program exists when it is not operating on some computer — similar to the traditional question about trees falling in the forest. That is, obviously, beyond the scope of this discussion.

[110]This obviates the need to address an essentially insoluble question concerning whether a copy of the website program on the server is an "original," especially if there are copies on several servers. Can one website have more than one permanent establishment, particularly if the programs are identical and a visitor has no way (or incentive) to determine which server she is contacting? Should a website be considered something capable of having a legal location separate from its owner, *i.e.*, an entity, and if so, which copy or copies of the website program has that status? The OECD Commentary takes the position that computer programs have no tangible existence. OECD Commentary, *supra* note 103, comment 42.10, p. 7.

[111]See Kaz. Inst. 33 — Entities, *supra* note 21, para. 29.

[112]There is a potential for significant conflict between developing rules in the United States and the European Union. For example, U.S. rules generally treat standardized computer programs as tangible goods, even if they are delivered electronically. The E.U., however, treats electronically delivered computer programs as services. *See* EU Commission VAT Proposal, *supra* note 84, Expl. memo. para. 1.2. The characterization ("goods" or "services") generally controls which jurisdiction (buyer's or seller's) can impose a transaction tax. In the U.S., the characterization usually determines *if* it will be taxes, not where.

[113]It is inevitable that some countries will opt out of any such agreement solely for the potential benefits, just as there are "tax havens." However, before reaching a conclusion about the effect of "cyberhavens", one should contemplate the number of persons and business that do not have accounts or establishments in tax havens.

[114]*See* note 28, *supra*.

[115]It should be noted that none of these questions seem to be unique to these republics.

[116]The person who initiated the transaction may be the only person who knows the event took place. Programs exist that allow a person to use the Internet without leaving a record traceable to that user. "Electronic cash" can be used to transfer funds to the seller; again without leaving a record traceable to the buyer. The computer memory where the original video is stored is not altered by sending the copy and the copy stored in the receiving computer may not reveal the source from which it is copied, or may not be discovered by government enforcement personnel.

[117]Note, however, that Kazakhstan's rules might be read as placing the source of the Taiwan company's income as Kazakhstan even when the manager traveled to Taiwan. *See* Kaz. Tax Law, *supra* note 18, art. 5.13(c)[4].

[118]See text at note 40, *supra*.

[119]As indicated in the prior discussion, a transfer is generally considered to take place where the seller delivers the goods or services to the purchaser. Kyrghyz rules specifically provide that the transfer occurs where the seller delivers the goods to a carrier. If the "goods" are digital videos, they can reasonably be considered "delivered" to the carrier when the electronic impulses enter the communication system from the server-computer.

[120]Of course, there is still the philosophical question of where electronic analogs of physical objects exists (if they do "exist"), particularly when the "transfer" is the creation of a copy, not a movement of the original.

[121]A government may try to create a customs point of entry between cyberspace and the physical world. That might appear attractive and possible, if all electronic transmissions were transmitted through transmission lines that physically cross real-world borders. Unfortunately for that idea, electronic communications often do not follow transmission lines, but are sent by radio-or micro-wave, via satellite. Those transmissions can avoid crossing physical boundaries in any form that can be intercepted. Even with existing technology, creating a controllable "gateway" to and from cyberspace has proven extremely difficult. With easily foreseeable future technology (or even more widespread use of today's more advanced technology) creating such a gateway will be impossible.

[122]The OECD treaty comments also indicate that delivery of standard programs should be given equal treatment, whether they are delivered on physical media or electronically. *See generally* OECD, Comm. on Fiscal Affairs, Tech. Adv. Group on Treaty Characterization of Electronic Commerce Payments, Final Report, *Treaty Characterization Issues Arising From E-Commerce* (1 Feb. 2001), <http://www.oecd.org/daf/fa/e_com/ public_release.htm>, *download at* http://www.oecd.org/daf/fa/e_com/ec_2_TREATY_CHAR_Eng.pdf.

[123]*See, e.g.*, Edmund L. Andrews, *Europe Plans to Collect Tax on Some Internet Transactions*, New York Times (2 March 2000), <<http://www.nytimes.com/library/tech/00/ 03/biztech/articles/02tax.html>> (6 April 2000); U.K. Inland Revenue, *Electronic Commerce: The UK's Tax Agenda*, (Nov. 1999), <<http://www.inlandrevenue.gov.uk/taxagenda/executive.htm (15 March 2000); European Commission, Directorate General XXI, *Working Party No. 1, Harmonization of turnover taxes* (8 June 1999) <<http://www.europa.eu.int/en/comm/dg21/publicat/databases/ecommerce.EN.pdf>> (16 April 2000); OECD, Committee on Fiscal Affairs, *Electronic Commerce: A Discussion Paper on Taxation Issues* (17 Sept. 1998), <<http:// www.oecd.org/daf/fa/e_com/discusse.pdf>> (16 April 2000); OECD, Committee on Fiscal Affairs, *Electronic Commerce: The Challenges to Tax Authorities and Taxpayers*, (18 Nov. 1997), <<http://www. oecd.org//daf/ fa/e-com/turku_e.pdf>> (16 April 2000).

[124]The non-resident receiving the income has little reason for concern, unless it has a domestic presence or assets. There is no income tax obligation unless the buyer deducts the cost (which the seller has know way of determining) and the tax authorities will collect both the VAT and the income tax from the domestic purchaser. Thus there is no reason for the foreign seller to reprogram the sales price to account for the VAT or income tax, even if the "obligation" to pay those is known.

[125]The payment is republic-sourced income only if it is deducted in a resident's income tax calculations. *See* note 40, *supra*.

[126]Taking the deduction = 100 - 20 tax savings + 20 income w/h + 20 VAT = 120. Not taking the deduction = 100 + 20 VAT = 120.

[127]*See* Elizabeth de Bony, *IBM, Others Seek EU Tax Reform for E-Commerce*, Infoworld (Feb. 5, 2000) <http://www2.infoworld.com/articles/ic/>>

[128]Inland Revenue, *Tax Agenda 2000*, Exec. Summ. paras. 8 - 12 (pub. 1999), <http://www.inlandrevenue.gov.uk/taxagenda/-executive.htm>.

[129]Kaz. Tax Law, *supra* note 18, art. 36.1. At various places, this has also been interpreted as "foreign commercial contract" or "foreign economic contract". In the VAT context, the exact intent is not important if the VAT-taxable event occurs outside the jurisdiction.

[130]It would probably be necessary to engage in some definitional "fine tuning" to preclude tax avoidance in situations which do not justify exemption. It may also be appropriate to add a requirement that a resident provide information to the tax authorities if he/she/it pays more than a cumulative minimum amount from one non-resident, or a higher cumulative amount from more than one non-resident. That would enable tax authorities to contact non-residents with significant domestic-source income for registration and collection purposes.