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AHEAD OF TAX

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Fraudulent AI as an Agent PE

by Lucas de Lima Carvalho

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In this installment of Ahead of Tax, Carvalho argues that permanent establishment tax issues caused by fraudulent use of AI in business may not be far away.

The internet was taken by storm when, in mid-February, OpenAI released the first samples of videos produced by its new platform, Sora.[1] Sora is a new artificial intelligence model that can create "realistic and imaginative scenes from text prompts," and the results are quite stunning (the video of a 20-year-old man sitting "on a piece of cloud in the sky, reading a book,"[2] spread like wildfire on social media). As stated on OpenAI's website, Sora can "generate complex scenes with multiple characters, specific types of motion, and accurate details of the subject and background. The model understands not only what the user has asked for in the prompt, but also how those things exist in the physical world."[3]

OpenAI claims that they will be taking "several important safety steps ahead of making Sora available in [their] products." They assure us that their text classifier will check and reject "text input prompts that [violate] usage policies, like those that request extreme violence, sexual content, hateful imagery, celebrity likeness, or the [intellectual property] of others."[4] If they are anything like the guardrails around DALL-E 3 (OpenAI's text-to-image system),[5] they should prevent Sora from being used as a tool to spread misinformation. This applies to Sora, not all forms of AI — which will only become more sophisticated and democratized from this point onward.

Let me switch gears for a moment. About a year ago, a heavily edited clip of Joe Rogan interviewing Andrew D. Huberman on his podcast went viral on social media. It featured out-of-context remarks from Huberman followed by a semi-robotic, "deepfake"[6] Rogan advertising a brand of supplements available on Amazon.[7] This was a deceptive "AI-infused" ad that might have generated thousands or even millions of dollars' worth of sales for the person or company behind those supplements. Assuming the supplements were actually delivered to their customers, this sort of fraud would differ from outright scams, like those committed using AI content with the images of billionaire investor Warren Buffett and popular YouTuber MrBeast. The fake video with Buffett directed viewers to a website that would ask them to make a "minimum deposit" of 0.005 bitcoin so that they could later claim a bonus worth 0.31 BTC — their deposit would then be stolen, with no bonus paid out

[1] *See* OpenAI, "Introducing Sora" (Feb. 15, 2024).

[2] *Id.*

[3] *Id.*

[4] *Id.*

[5] *See* OpenAI, "DALL-E 3 System Card" (Oct. 3, 2023).

[6] "Deepfakes are synthetic media in which images/sounds captured from certain people are replaced by those of others through advanced machine learning techniques and [AI] to manipulate visual and/or sound content, with enormous potential for falsifying reality." *See* Patrícia Fonseca Fanaya, "Deepfake e a Realidade Sintetizada," Revista Digital de Tecnologias Cognitivas, No. 23, at 106 (2021) (unofficial translation from Portuguese).

[7] *See* Mashable, "Tiktok Removes Viral Video Ad of Suspected Joe Rogan AI Deepfake," Feb. 15, 2023.

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afterward.[8] MrBeast, whose real name is Jimmy Donaldson, denounced a fake video of his offering $2 iPhones to 10,000 people on TikTok.[9]

The mere existence of Sora indicates that AI videos will become increasingly undistinguishable from reality. Our hope is that OpenAI and other responsible platforms will protect us from the onslaught of "deepfake" misinformation soon, but it is just as plausible that bad-faith actors will continue to use AI to deceive us, whether in the realm of trade, investment, or others. The economic implications of these frauds, like of any fraudulent activity, are relevant for international tax purposes. Particularly within tax treaties, AI can disrupt even our most contemporary views about taxable nexus, the most obvious of which are permanent establishments.

In this article, I focus on nonresident persons that create (or use) AI videos with false endorsements of their products on social media to generate sales made to resident customers. All the examples I use below will be based on tax treaties following the 2017 OECD model convention, particularly article 5(5),[10] which follows the non-minimum standard recommendations of the final report of base erosion and profit shifting action 7.[11]

False Endorsements via AI

False endorsement is the act of someone that uses the image or likeness of a particular person, company, or brand to endorse their product without authorization.[12] One recent example can be found in the complaint of actor Sacha Baron Cohen against Solar Therapeutics Inc., a company that is accused of having used his image to advertise cannabis products on a billboard on an interstate highway in Massachusetts. The actor, who is depicted on the billboard as his famous character Borat, said he never gave them permission to do so.[13]

In the age of social media, false endorsements can reach millions of people across several countries in a matter of seconds. Fraudulent posts can be taken down, yes, but others appear elsewhere, not necessarily on the same platform. As written by Samuel Greengard in a recent article, "combatting deepfakes resembles a game of whack-a-mole," with companies offering to clone a person's voice or image for $10 or less.[14] Notice how this is in and of itself a sign of entropy: an entire industry emerging (or maybe reinventing itself) before our eyes and selling the opportunity to defraud people for a few bucks.

Though it is true that false endorsements predate AI, AI is what really blurs the lines between them being false or real. Consider Baron Cohen's case, for example. The actor was made aware of the billboard and declared that he had no association with the company behind it. But what if an AI video — a sufficiently sophisticated one, let us assume[15] — surfaced on the web showing a fake interview in which the actor "endorsed" the same product? He could be made aware of the video, then publish the same statement, only to witness AI generate a second video claiming that his statement is false (and that the original video is genuine). Even the argument that a victim of "AI cloning" would just be able to issue a statement claiming that whatever media it produced is false is based on the premise that they are a public person. But what if the direct victim of such a scheme is someone like Banksy,[16] or Satoshi Nakamoto,[17] or a person that is well-known but has decided to live a reclusive

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[8] *See* Thomas Orsolya, "Don't Fall for the Warren Buffett Bitcoin Promo Code Giveaway Scam," Malware Tips, Jan. 23, 2024.

[9] *See* Kalhan Rosenblatt, "MrBeast Calls Tiktok Ad Showing an AI Version of Him a 'Scam,'" NBC News, Oct. 3, 2023.

[10] *See* OECD, "Model Tax Convention on Income and on Capital," at M-20 (2017).

[11] *See* OECD, "Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 — 2015 Final Report" (2015).

[12] A more complete definition can be found in Title 15, Section 1125 (also Section 43(a) of the Lanham Act).

[13] Baron Cohen is reported to have recently dropped the lawsuit. *See* "Sacha Baron Cohen Drops Lawsuit Over Somerset Cannabis Dispensary's 'Borat' Billboard," CBS News, May 18, 2022.

[14] *See* Greengard, "The Campaign Against Deepfakes," Communications of The ACM, Feb. 15, 2024.

[15] My point being that I want to put aside the possible counterargument that current versions of AI are easily distinguishable from reality (a disputable counter, even at this stage, but some could have that opinion). The premise of this article is that AI will soon reach that stage of verisimilitude.

[16] On Nov. 21, 2023, several news reports claimed that the true identity of Banksy was finally revealed. *See, e.g.*, Carita Rizzo, "Banksy's Identity Finally Revealed in Lost BBC Interview?" *Rolling Stone*, Nov. 21, 2023.

[17] The pseudonym used by the person (or the group) that created and developed Bitcoin up until late 2010. *See* Michael Adams, "Who is Satoshi Nakamoto?" Forbes, Mar. 18, 2023.

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lifestyle? Indirect victims of false endorsements involving these figures — people who appreciate them and would respect their advice — could be scattered across the globe, and it is doubtful whether (a) any of these figures would be willing to come forth to denounce their AI representation as false or (b) people would even believe them if they did.

This distinction between direct and indirect victims of false endorsements is important because it highlights that legal protections can be afforded not just to the people whose image rights were exploited, but to bona fide buyers as well. In Peru, for instance, article 948 of the Civil Code says that, with minor exceptions, bona fide buyers have the right to keep the things they purchased even when whoever transferred their possession lacked the power to do so.[18] True, the type of purchase I focus on in this article is not fraudulent in itself (the means used to effectuate the deal are), but the Peruvian legal system recognizes buyers as having good faith if their purchase is justifiable considering the amount of information they have.[19] In Brazil, the Consumer Protection Code says in article 37 that all forms of misleading or abusive advertising are prohibited by law,[20] and courts have awarded damages to customers in many of those cases. In a ruling issued in 2017, the Brazilian Superior Court of Justice decided that customers were entitled to moral damages[21] owed by a dealer that resold products from one distributor while using the trademark of another.[22] In the majority vote, Minister Luis Felipe Salomão said that consumer protection requires fighting against "disguised objectives of deviousness, easy profit and causing harm to vulnerable parties."[23]

[18] *See Código Civil — Decreto Legislativo 295*, (July 24, 1984, updated Feb. 29, 2024) (in Spanish).

[19] *See* Salvador del Solar Labarthe, "Protección a terceros adquirentes en el Código Civil: orientaciones y desorientaciones," Revista Ius et Veritas, p. 162-163 (1994) (in Spanish).

[20] *See Lei nº 8.078, de 11 de setembro de 1990*, (Sept. 12, 1990) (in Portuguese).

[21] Which differ from punitive damages in the sense that they compensate nonmaterial damages. *See* Jarrod Wong, "Making a Muddle of Moral Damages," Kluwer Arbitration Blog, Oct. 13, 2014.

[22] *See Recurso Especial nº 1.487.046/MT*, Superior Court of Justice, Fourth Chamber, (May 16, 2017) (in Portuguese).

[23] *Id*. at 33 (unofficial translation from Portuguese).

Apparent Agency and Fraudulent AI

Intuitively, there seems to be a key difference between an endorsement and an agency relationship. If I see a billboard with a celebrity wearing a fancy watch next to the watchmaker's brand and logo, I might be tempted to find a store that sells that watch and purchase it for myself. A sales agent, on the other hand, would approach me (or I approach them), show me the watch, and then sell it to me if I decide to buy it. The celebrity endorser might have incentivized me to buy the watch, but it was the agent who served as the *channel* through which I bought it.

I have made this point in a previous *Tax Notes* article;[24] in the realm of social media, certain endorsers are virtually (pun intended) equivalent to sales agents. If a person with millions of followers of their own social media account posts a story or a reel endorsing a product and telling viewers to click on a link to buy it with a special discount, they are not just incentivizing people to buy the product — they are effectively within the *channel* that effectuates the sale. Tech channels on YouTube are part of my daily media consumption: Some post "reviews" of smartphones, or rings, or watches, accompanied by "promo codes" that give people a discount if bought using their links. Aside from the specs of these products, what makes me buy them is a combination of the trust I have in the reviewer (which can be misplaced if the review is not genuine) and the promotional links they share with me in their platforms, which are the locations (web-based, internet-based) in which I conclude my purchase.

The point I am making is not that there is a clear principal-agent relationship between sellers and influencers on social media — you might have noticed that this is the first use of the word "principal" in this article. My point is that consumers will interact with those influencers and their platforms, discount codes, and links much like they would with a sales agent. There is no doubt that the support given by an influencer to a product or a company is an endorsement (and that using AI to falsify it would be a case of false endorsement), but their activities can be far more

[24] *See* Lucas de Lima Carvalho and Larissa Falkowski, "The 'Principal Role' of Social Media Influencers as PEs," *Tax Notes Int'l*, Nov. 22, 2021, p. 875.

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crucial for the conclusion of each sale. Put it this way: The fact that YouTube creators were sued for "soliciting the sale of unregistered securities" because of their promotion of FTX cryptocurrency shows how customers viewed their videos as the channel through which they decided to invest in FTX.[25]

Having built the bridge between endorsements and agency in social media, I can now refer to a common-law form of agency known as "apparent agency."[26] This is when person A acts as an agent for person P in their dealings with person C (a customer or a client). If P, by their actions and words, leads C to believe that A is their agent, C should have a right to treat A as the "apparent agent" of P, their "principal." Notice that in this example, A has no authority to act on behalf of P — there is no contract between P and A; they might not even know one another.[27] Notice also that this form of agency is not premised on C having suffered any sort of loss;[28] C might have successfully purchased something from P as a result of A's actions, and P could later claim that they had no agreement giving powers to A to represent them in the first place. What matters is that a business transaction took place in the context of P leading C to believe that A — the channel through which the transaction was effectuated — was their agent. A business transaction concluded in the context of "apparent agency" is a transaction concluded by or through an agent.

In section 267 of Restatement (Second) of the Law of Agency, the American Legal Institute defined apparent agency as a situation in which one party represents another as their servant or agent, leading a third party to reasonably rely on "the care or skill" of the apparent agent. The definition added that whoever makes such a representation becomes liable for any harm "caused by the lack of care or skill of the one appearing to be [their agent]."[29] There is a clear connection between this definition and the one for apparent authority featured in section 2.03 of Restatement (Third) of the Law of Agency, which says that apparent authority "is the power held by an agent or other actor to affect a principal's legal relations with third parties when [they] reasonably [believe] the actor has authority to act on behalf of the principal and that belief is traceable to the principal's manifestations."[30] The common thread between the two notions is (a) the "principal" represented to a third party that someone was their agent, and (b) the reliance of the third party on that representation must have been reasonable.[31]

Those guideposts can accommodate AI. Think of a Belgian start-up eager to sell its products into the Brazilian market but short on funds to recruit influencers as their social media agents. The start-up chooses instead to create a viral AI campaign featuring a video of a Brazilian celebrity that shows their product on Instagram and claims that viewers can click on a link to purchase it with a special discount. Millions of viewers click on the link, purchase the start-up's products, and those are shipped to their homes in Brazil. If you put aside the sophistication of the AI content produced by the start-up in my example (assume that it is true to life), it would be hard not to qualify this as a form of agency: Clients reasonably relied on a representation made by a principal (the start-up) that somebody in their jurisdiction (the Brazilian celebrity) acted as their agent (the channel through which they purchased the start-up's products). True, the clients in this case never thought that they were interacting with AI, so the "thing" that acted as an agent was never

[25] *See* André Beganski, "YouTube Influencers Slapped With $1 Billion Lawsuit for Promoting FTX," Decrypt, Mar. 16, 2023. The case was apparently settled out of court. *See* James Hunt, "Ben 'Bit Boy' Armstrong Dismissed From FTX Case as Three Celebrities Settle," The Block, Sept. 18, 2023.

[26] *See* Jonathan E. Schultz "You Can't Have Your Cake and Eat It Too: The Standards for Establishing Apparent Agency," 60 *S. C. L. Rev.* 999 (2009).

[27] This being the marked difference between apparent agency or authority and "implied authority," a situation in which an agent exercises "implied rights" as an extension of the express authority granted to them. *See* Raimonda Bubliene and Vaidas Jurkevicius, "Interaction Between Apparent and Implied Authority in the Implementation of Sustainable Business Relationships," *Contemporary Issues in Business, Management and Economics Engineering* 93 (May 2021).

[28] *See* Robert Brand Stone, "Agency-Recovery in Tort Under the Theory of Apparent Authority or Agency by Estoppel," 69 W. Va. L. Rev. 187 (1967).

[29] *See* Restatement (Second) of the Law of Agency, section 267 (1958).

[30] *See* Restatement (Third) of the Law of Agency, section 2.03 (2006).

[31] *See* Schultz, *supra* note 26. *See also* Chad P. Wade, "The Double Doctrine Agent: Streamlining the Restatement (Third) of Agency by Eliminating the Apparent Agency Doctrine," 42 *Val. U. L. Rev.* 348 Volume 42 (2007).

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"evident" to them, and the person that AI emulated had no involvement with the start-up at all. Having said that, whoever the clients believed they were interacting with (the local celebrity) became an apparent agent in their relationship with the start-up. AI depicted a person they trust, and this is likely the main reason they clicked on the link.

PE Standard: Dependent and Independent Agents

PEs are the result of a political compromise between treaty signatories. They enable source jurisdictions to tax the business profits of nonresident enterprises after a certain level of economic activity is reached in their territory. As said in the commentary to article 5 of the OECD 1963 Draft Double Taxation Convention, PEs were designed as a concept within tax treaties after "a good deal of discussion and much careful thought and consideration."[32] Apart from the definition of PEs as a "fixed place of business" — the text you will find in most treaties and in article 5(1) of the OECD model — the draft adds that "certain groups of persons" should be treated as PEs "on account of the nature of their business activities, even though the enterprise may not have a fixed place of business."[33] The PE provision referring to dependent agents, article 5(4), currently article 5(5) of the 2017 OECD model, comes from this.[34]

Since 1963, the OECD said that a dependent agent would be qualifiable as a PE if they had "and habitually [exercised] in [the PE jurisdiction], an authority to conclude contracts in the name of the enterprise, unless [their] activities [were] limited to the purchase of goods or merchandise for the enterprise."[35] This is quite a limited range. Not all agents, only the dependent ones; not all dependent agents, just the ones with the authority to conclude contracts in the name of the enterprise; not all the agents with that authority, but specifically the ones that "habitually" exercise it, and only if the contracts in question pertain to activities beyond the mere purchase of goods for the enterprise. As the commentary said back then, a PE qualification should only be recognized for those agents if their principals, "in view of the scope of their agent's authority or of the nature of their agent's business dealings, [took] part to a particular extent in business activities in the other State."[36]

Article 5(5) of the 1963 draft, now article 5(6) of the 2017 model, said that independent agents cannot be regarded as PEs,[37] of course (because even most of those labelled as dependent agents are not PEs as well). An independent agent like a broker or a commissionaire is just a person acting in the ordinary course of a separate business, in which case it would "stand to reason" that they should not be treated as a PE of whoever their client abroad is.[38] That said, even back then the OECD recognized that if a person calling themselves an independent agent not only sold merchandise of their client in their own name "but also habitually [acted], in relation to that enterprise, as a permanent agent having an authority to conclude contracts," they would be viewed as a PE for this activity, something that would be regarded as "outside the ordinary course of [their] own trade or business."[39] I mention this because article 5(6) of the 2017 model says that an agent will not be treated as independent if they act "exclusively or almost exclusively on behalf of one or more enterprises to which [they are] closely related."[40] While this is a product of the final report of BEPS action 7, which is also found in article 12(2) of the BEPS multilateral instrument,[41] my point is that it comes from a concern that was expressed by OECD members decades earlier.

Until October 5, 2015 (when the OECD released the final reports of its BEPS action plan); June 7, 2017 (when they published the BEPS MLI); or November 21, 2017 (when the current OECD model convention was finalized), agents

[32] See OECD, "Draft Double Taxation Convention on Income and Capital," (1963).

[33] *Id*. at p. 75.

[34] *See* OECD, *supra* note 10.

[35] *See* OECD, *supra* note 32 at p. 44.

[36] *Id*. at p. 75.

[37] *Id*. at p. 44.

[38] *Id*. at p. 76.

[39] *Id*.

[40] *See* OECD, *supra* note 10.

[41] See OECD, "Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting" (2017), p. 19.

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qualifiable as PEs were dependent agents (formally or otherwise) that had and habitually exercised the power to conclude contracts binding nonresident enterprises. This standard changed — for both dependent and so-called independent agents — after the BEPS action plan, because the text of article 5(5) today says that a dependent agent can also generate a PE link if they "habitually [play] the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise."[42] You can find this clause in several tax treaties signed since late 2015, for example between Brazil and Uruguay in 2019[43] and between Bangladesh and Iran in 2022.[44]

To describe the "playing the principal role leading to the conclusion of contracts" test, the OECD states that it is aimed at "situations in which the conclusion of a contract directly results from the actions that the person performs in a [state] on behalf of the enterprise even though, under the relevant law, the contract is not concluded by that person in that State."[45] In paragraph 89 of the commentary, the OECD says that the test is met if the agent "solicits and receives (but does not formally finalise) orders" that are "sent directly to a warehouse from which goods belonging to the enterprise are delivered and where the enterprise routinely approves these transactions."[46] They add that article 5(5) refers not only to contracts that create rights and obligations legally enforceable on the enterprise and third parties, but also to those that create obligations to effectively be performed by the enterprise abroad.[47] As for the "habituality" of the agent's role, they claim that it is "not possible to lay down a precise frequency test,"[48] deferring instead to a facts and circumstances analysis depending on the business activity of the enterprise.[49]

I have discussed this in my previous piece,[50] but the references of the OECD to "mere promotion or advertising"[51] in paragraph 83 as well as "merely promotes and markets"[52] in paragraph 89 are not applicable to the work of certain influencers on social media. These are referred to by the OECD as exceptions to the agent PE standard, but certain influencers play a role far more crucial than that of an endorser or a marketer — they are part of the channel that facilitates sales, sometimes in the ballpark of millions of products to their followers. Though it is true that not all agents are qualifiable as PEs and that independent agents generally are not PEs, if an influencer uses their platform to sell merchandise of a nonresident business, and if this business exerts significant authority over the influencer's activities,[53] they might be qualifiable as PEs. It would all hinge on how "principal" their role is in the conclusion of each sale, and as my coauthor and I argued in the previous piece, "habituality" on social media is different from habituality in real life: One single post might be viewed, shared, and reshared countless times, years on end, reaching waves upon waves of new customers.[54]

Finally, when it describes the PE exception for "independent agents," featured in article 5(6) of the 2017 model, the OECD commentary says that an agent shall not be treated as independent if their activities are subject to "detailed instructions or to comprehensive control" by the nonresident enterprise.[55] If the agent does not bear entrepreneurial risk, they should not be treated as independent.[56] Although reliance on the agent's

[42] *See* OECD, *supra* note 10.

[43] *See* "Brazil — Uruguay: 2019 Income and Capital Tax Convention and Final Protocol" (signed June 7, 2019, in force July 21, 2023) (in Spanish).

[44] *See* "Bangladesh — Iran: 2022 Income Tax Agreement" (signed Oct. 8, 2022, effective July 1, 2023 (Bangladesh) and Mar. 21, 2024 (Iran)).

[45] *See* OECD *supra* note 10 at p. C(5)-37.

[46] *Id*. at p. C(5)-38.

[47] *Id*. at p. C(5)-39.

[48] *Id*. at p. C(5)-41.

[49] The OECD points to paragraphs 28-30 of the commentary to article 5(1), which explain how "fixed" a place of business must be to be considered a PE of the nonresident enterprise. Id., at p. C(5)-10-11.

[50] *See* Carvalho and Falkowski, *supra* note 24.

[51] *See* OECD *supra* note 10, p. C(5)-36.

[52] *Id*. at p. C(5)-38.

[53] *Id*. at p. C(5)-43-44.

[54] *See* Carvalho and Falkowski, *supra* note 24, p. 856-857.

[55] *See* OECD, *supra* note 10, p. C(5)-43.

[56] *Id*.

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"special skill and knowledge" is labelled by the OECD as "an indication of independence,"[57] it is the extent of their freedom "in the conduct of business on behalf of the principal"[58] that will determine whether they are actually independent. Also, if an agent says that they are independent but acts on behalf of one enterprise that represents a "predominant" part of their business (if the lion's share of their earnings comes from a single nonresident principal), then that form of economic control should prevent them from being treated as independent under article 5(6).[59] Influencers that play the principal role to conclude online sales might be effectively dependent on certain nonresident enterprises, and it is a case-by-case investigation of whether their status as independent content creators translates to independent agents for PE purposes.[60]

Fraudulent AI on Social Media as a PE

You might be wondering why I made this apparent detour into the world of social media influencers, but it is all tied to the main topic of this article. Influencers are just people with a huge following on these social media platforms — some have a degree of fame outside the internet, but (many) others cultivate their entire persona and their fame on the web. Their content can make or break entire businesses overnight, with one recent example being Marques Brownlee's scathing review of a new automobile, the Fisker Ocean, on the YouTube channel "Auto Focus." This is a 20-minute video aptly titled "This is the Worst Car I've Ever Reviewed."[61] Fisker's stock price, which had been declining in the previous year, halved from USD 0.75 to roughly USD 0.38 per share a month after the video aired.[62] For reference, Brownlee's follower base on social media is higher than the subscriber count of *The New York Times*, *The Washington Post*, *The Wall Street Journal*, and *USA Today* combined.[63]

I will first lay out my claim, then test it with a few counterarguments. If a nonresident enterprise uses AI to fraudulently exploit the image of a person on social media and if that fraudulent AI is then used as their sales channel in a given jurisdiction, the fact that the person "mimicked" by AI resides in that jurisdiction may trigger a PE risk for the enterprise under the equivalent of article 5(5) of the 2017 OECD model. This is far from obvious, so here are some counterpoints to be considered by tax authorities and taxpayers if, or when, they discuss real cases involving fraudulent AI.

Actual Agency vs. Apparent Agency

The first counter to my claim is that the agency referred to in article 5(5) is premised on "a person [acting] in a Contracting State on behalf of an enterprise."[64] They could go on to say that while article 3(1)(a) provides only a non-exhaustive list of what "persons" are,[65] paragraph 2 of the OECD commentary implies that they are individuals or corporate bodies that have their personhood recognized as such by tax laws.[66] So, if a person recognized as such by tax laws is not acting on behalf of an enterprise, they must not be treated as an agent (dependent or independent) for PE purposes. And in my claim — or in the hypothetical on which I stake my claim — the person depicted by AI gave no authorization to the nonresident enterprise for their likeness to be used on social media. They are not acting on behalf of anyone: AI is, but I am not claiming that AI is the territorial link between the nonresident enterprise and the PE jurisdiction, and as of today, AI is not generally recognized as a "person" (so even if I argued that AI should be treated as the person that it is cloning on social media, the system itself is not a person, and thus it is not qualifiable as an agent under article 5(5)).

[57] *Id*. at p. C(5)-44.

[58] *Id*.

[59] *Id*.

[60] *See* Carvalho and Falkowski, *supra* note 24, p. 854-855.

[61] *See* Auto Focus, "This is the Worst Car I've Ever Reviewed," YouTube (Feb. 17, 2024).

[62] *See* "NYSE — Nasdaq Real Time Price in USD: *Fisker, Inc. (FSR)*," Yahoo Finance (last updated Mar. 8, 2024).

[63] *See* Harry McCracken "Inside Marques Brownlee's tech review studio: The YouTube star on gadgets, growth, and staying chill," Fast Company (Nov. 14, 2023).

[64] *See* OECD, *supra* note 10.

[65] *Id*. at p. M-10.

[66] *Id*. at p. C(3)-1.

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Before I address the counterargument, let me flesh out what I see as the *hybrid nature* of fraudulent AI as an agent PE. On one hand, the nonresident enterprise is using AI as its *actual agent* with *actual authority*: They are employing AI to sell their products to local customers (or to "play the principal role" in every sale). The robot has a master, and that relationship is known and accepted by both (figuratively or not).[67] On the other hand, AI is only selling products to local customers because it is masking itself as a local influencer who has unwittingly become an *apparent agent* with *apparent authority* on behalf of the nonresident enterprise. Yes, the person depicted by AI never "acted" on behalf of anyone, but AI, using their likeness to generate sales, did — and I contend that this transforms the depicted person, the direct victim of this instance of AI fraud, into an apparent agent of the nonresident enterprise. Think of it this way: It is as if the nonresident enterprise was able to manufacture a human clone of a celebrity in the PE jurisdiction to then use them to sell products to local customers (a rather boring sci-fi movie plot, no doubt). The clone is their actual agent, but it is their appearance as a local celebrity — the apparent agent — that drives sales to local customers.

I can address the counter by reminding us of the purpose of the PE clause in tax treaties: to justify the taxing rights of a PE jurisdiction on a nonresident enterprise's business profits if the enterprise carries on business in its territory via a fixed place or a local dependent agent. If local customers bought products from the enterprise believing that they were being endorsed by a local influencer on social media, it is fair to assume that it was that belief that facilitated every sale. In other words, if customers engaged in business transactions with the nonresident enterprise because of the actions of a thing or entity that they reasonably believed was a local person acting on its behalf, then a person "acted" on its behalf within the scope of article 5(5). This is the PE version of "apparent agency is [agency],"[68] and it is irrelevant that in my hypothetical the agent is unwitting. Tax authorities of the PE jurisdiction should care that business transactions were effectuated through a channel with sufficient ties to their territory, which in turn makes the nonresident enterprise a candidate for a PE connection under article 5(5).

Also, suppose tax authorities were unable to build a PE link based on the hypothetical I presented. So no PE because (a) AI is not a person, (b) even if AI was a person, AI is not physically connected to the PE jurisdiction (for instance) and (c) even if it were, local customers purchased goods from the nonresident enterprise because they were misled — they thought they were endorsed by a local influencer on social media, but because that never happened, then no agency relationship exists and no PE can be established under article 5(5) of the 2017 OECD model. How convenient, right? So the nonresident enterprise, which would have had an "agent PE" if they had hired the local influencer (as a person that "plays the principal role" on each sale), scores back-to-back points for their cashflow. Not only are they paying a fraction of the cost of hiring a local influencer (paying for the AI clone instead), but they are also dodging a PE qualification under article 5(5). They get the benefit of "hiring" the social media equivalent of a local sales agent with little actual cost and no source taxation.

It would be odd if a nonresident enterprise tried to claim that the reason it does not have a PE in the PE jurisdiction is that the person depicted in their promotional videos on social media never authorized the use of their image. In Latin, the maxim *Nemo auditur propiam turpitudinem allegans* ("no one can be heard to invoke his own turpitude") has become a general principle of international law, also known as "unclean hands".[69] It says that claimants should be barred from obtaining relief if they acquired or retained

[67] *See* Carvalho and Victor Guilherme Esteche, "Sentience as a Prerequisite for Taxing AI," *Tax Notes Int'l*, Dec. 5, 2022, p. 1263 (discussing the implications of sentience for the taxability of AI).

[68] *See Advanced Sec. Servs. Evaluation & Training, LLC v. OHR Partners Ltd.*, No. M2017-00249-COA-R3-CV (Tenn. Ct. App. Mar. 20, 2018) ("apparent agency is agency by estoppel. . . . Thus, a finding of apparent agency does not hinge on any actual agency agreement").

[69] *See* Lodovico Amianto, "The Role of "Unclean Hands" Defences in International Investment Law," 6 *McGill J. of Dispute Resolution* 13 (2019-2020).

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their right by inequitable means,[70] and it has been invoked by tax courts in many countries.[71] If a case can be made for the qualification of local influencers as actual agents (if they had been formally hired by the nonresident enterprise) and therefore as PEs, then their false endorsement via AI — turning them into apparent agents of the nonresident enterprise — should similarly raise the risk of a PE link under article 5(5) of the 2017 model.

AI Residency vs. False Endorser's Residency

Arguably, if a nonresident enterprise uses AI as its agent, then it is AI that must be tested for "residency" in the PE jurisdiction, not the person that AI is mimicking. Tax authorities would have to build the case that the target AI resides in their territory, which is a tough task. The AI Act recently approved by the EU Parliament says that in-scope AI is that which is "[placed] on the market or [put] into service . . . in the Union, irrespective of whether [its] providers are established or [located] within the Union or in a third country."[72] It also states that the regulation applies to providers and deployers of AI established elsewhere if "the output produced by the [AI] system is used in the Union."[73] None of these definitions speaks to the residence of AI itself.[74]

This is untenable in my view. Again, the question is whether customers believed they were interacting with an AI platform or with a local influencer, the person who they would trust to buy products from. If a customer who bought a product from a nonresident enterprise through fraudulent AI had known that it was AI that endorsed it and sold it to them, not the famous person that AI mimicked, it is fair to assume that they would not have made the purchase. The PE definition of article 5(1), "a fixed place of business through which the business of an enterprise is wholly or partly carried on," is a clear guideline for what makes an agent eligible for a PE qualification: doing business. If business took place (i.e., the sale was concluded and the purchased goods were received by the customer) and it was facilitated by an agent (fraudulent AI), it is the agent's trait that facilitated it (AI's appearance as the local influencer) that can turn it into a PE.

For contrast, if a nonresident enterprise used an AI system that was clearly identified (like an AI influencer on Instagram)[75] as a sales channel for its products, it should only be qualified as having a PE in the PE jurisdiction if the servers used by the AI itself are located in its territory (or, alternatively, if the company hired by the enterprise to build it and maintain it is).[76] That said, this argument is not the same as the argument that I am making for qualifying fraudulent AI as an agent PE in the PE jurisdiction. My claim is that the person depicted by AI has connections in the PE jurisdiction that lead to sales for the nonresident enterprise, and that is what ties them to its territory. If customers are aware that they are dealing with AI and they purchase products following its endorsement, it seems odd to argue that these purchases have been made just because AI is using servers located in the customers' jurisdiction of residence (or because the company that built the AI system is a resident). This is decidedly a case within article 5(1) as opposed to 5(5); the tax authorities would have to argue that either the servers used by AI or the company that built it and maintains it are the fixed place of business "through which" the business of the nonresident enterprise is wholly or partly carried on.[77]

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[70] *See* Richard Kreindler, "Corruption in International Investment Arbitration: Jurisdiction and the Unclean Hands Doctrine," *Between East and West: Essays in Honour of Ulf Franke*, p. 316 (Mar. 2010).

[71] *Acórdão nº 9101-003.663*, First Chamber, Superior Chamber of Tax Appeals (July 4, 2018) (in Portuguese). *See also Sentencia T-332 de 1994*, Sixth Chamber, Constitutional Court (July 19, 1994) (in Spanish).

[72] *See* EU, "Interinstitutional File: 2021/0106(COD)," (Jan. 26, 2024) p. 94.

[73] *Id*.

[74] A subject that I covered in a previous paper regarding autonomous AI systems. *See* Carvalho, "Spiritus Ex Machina: Addressing the Unique BEPS Issues of Autonomous Artificial Intelligence by Using 'Personality' and 'Residence'" 47 *Intertax* 425 (2019).

[75] See Ryan Hogg, "AI influencers are making their secretive creators tens of thousands of dollars a month—now an OnlyFans rival is betting on the lucrative virtual girlfriends," Fortune (Feb. 21, 2024).

[76] For further analysis on whether servers can create PEs under article 5 of the OECD model, see Jerôme Monsenego, "May a Server Create a Permanent Establishment? Reflections on Certain Questions of Principle in Light of a Swedish Case," 21 International Transfer Pricing Journal 247 (2014).

[77] *See* OECD, *supra* note 10, p. M-19.

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You could say that I am playing both sides of the PE game: defining AI as a PE but looking to the residence of the person imitated by it to examine whether AI is an agent within the scope of article 5(5) of the OECD model. I explained above why I believe that the link fraudulently created in the PE jurisdiction by using the image of a local influencer on social media is what "does business" for the nonresident enterprise and therefore is the link enabling the application of article 5(5). However, I never stated that the qualification under article 5(5) means that the human being depicted by AI is or should be considered liable for the actions of their apparent principal, whether in a civil or commercial setting. In other words, I am not claiming that a victim of AI mimicry can become liable for the fraudulent, criminal agency relationship that it created. Once again, what matters is that, in the eyes of the customers who purchased products from the nonresident enterprise, a local influencer acted as its sales channel on social media. The key component of this apparent agency relationship "for PE purposes" is that business deals were executed via what the customers believed was a local agent.

Reasonability in Social Media

My comments so far have been based on the idea that AI is or will become so sophisticated that customers will not be able to differentiate it from real life. Apparent agency requires that level of trust — a reasonable assessment of the situation must lead a regular person to believe that the "agent" is actually the principal's agent and is acting on their behalf. If the customer's reliance on the "agent" is considered unreasonable under the circumstances, then it follows that they cannot claim apparent agency.

The problem in social media is that customers will probably have access to a plethora of resources to either test or double-check the AI video they watched — many of these companies, these "AI checkers," are emerging on the web now.[78] If one of those is providing their services for free, can it be argued that customers should have used them to verify the authenticity of what they saw? In other words, if you buy a fake Audemars Piguet and there is a free tutorial on YouTube on how to distinguish fake from genuine Audemars Piguet watches, should your reliance on the seller's representation be deemed unreasonable?

The annoying answer is that it depends. Deception is an art: It is a collection of data, impressions, subtle cues, and biases that lead someone to believe a fake thing or person is in fact real. Weaving those cues as threads that tie you up and then manipulate you is a criminal, yet somewhat admirable craft (look up the name Wolfgang Beltracchi — you will likely be as amazed as I was).[79] If well-executed, AI mimicry can deceive even the most discerning audiences, and it might be relevant for tax authorities to try and find the extent to which the nonresident enterprise invested in the narrative that its AI clone was in fact a video of the local influencer endorsing its products (e.g., did the company use bots to reshare the AI clone so that it would be viewed by more people? Did the bots publish posts or messages saying the clone was genuine?).[80] AI representations that are rapidly and extensively debunked as fakes are probably less qualifiable as PEs, but I go back to my point about unclean hands: If someone ends up buying the products endorsed by AI and tax authorities claim that this created a PE link in their jurisdiction, it would be strange for a court to accept the argument coming from the nonresident enterprise that reliance on their AI by local customers was unreasonable because their fraud was quickly debunked.

Beyond the OECD: U.N. and Into the Future

Article 5 of the 2021 U.N. model departs in important ways from its source of inspiration in the 2017 OECD model. For instance, it features a type of PE known as "services PE," which is "the furnishing of services by an enterprise through employees or other personnel . . . where such activities continue for a total of more than 183 days in any twelve-month period commencing or

[78] *See* Elijah Clark, "The 10 Best AI Content Detector Tools," Forbes, (Dec. 14, 2023).

[79] *See* Ana Bambic, "The Art of Forgery — Wolfgang Beltracchi," Widewalls, (Mar. 4, 2014).

[80] *See* Patrick Collinson, "Fake reviews: can we trust what we read online as use of AI explodes?" The Guardian, (July 15, 2023).

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ending in the fiscal year concerned."[81] It also contains a specific PE provision for insurance services, something that was described as "inappropriate" for the OECD model by the final report of BEPS action 7.[82] Article 5(5) is not meaningfully different between the two models, or perhaps not different in a way that affects my comments thus far: The U.N. model divides it into 5(5)(a) and 5(5)(b), the latter being an addition that refers to persons that neither "habitually conclude contracts" nor "play the principal role leading to the conclusion of such contracts" but habitually keep in the PE state "a stock of goods or merchandise from which [they] regularly [deliver] goods or merchandise on behalf of the enterprise."[83]

It is still early days, but in November 2023 U.N. members adopted a landmark resolution to establish what is called a "framework convention on international tax cooperation."[84] The hope of some organizations is that this convention will empower the U.N. to take over the role of (principal) global tax policy forum that currently resides within the OECD,[85] so to an extent it might be fruitless to refer to OECD commentary as a baseline for PE definitions under article 5(1) or 5(5). There is little difference between the OECD and U.N. commentaries on article 5(5) — most of the section in the U.N. commentary is just a copy-paste of what the OECD stated.[86]

As the U.N. model becomes possibly more independent from the OECD, the key question is whether this means anything for the PE qualification of fraudulent AI. It is expected that handing more power over to non-G20 members (the majority of the U.N. membership) is going to broaden the scope of the PE clause or of whatever replaces it in the future. Whether it is the PE clause or something else, typical source jurisdictions are still going to push for source taxing rights, and the justification for those rights will still be some sort of local connection, like a fixed place of business, an agent, or some sort of significant economic presence.[87] I do not foresee that updates to the concept of what a PE is will affect my observations in previous sections of this article — in fact, I expect that AI representations of local influencers, if engineered or paid for by the nonresident enterprise that benefits from them, will be more and more targeted as potential PEs by local tax authorities and courts.

Final Remarks

In his book titled "Superintelligence — Paths, Dangers, Strategies," Nick Bostrom says that our standards for what is impressive keep adapting to the advances made in the field of AI.[88] As new AI models improve their learning and adaptive abilities, their form of interacting with us will also evolve. These interactions are relevant for legal systems in general and, within those, for taxation and international taxation. If nothing else, this article is my attempt to cast my mind years into the future (but not many) to ask complex questions and attempt to find some answers.

The OECD finalized the BEPS action plan nearly 10 years ago (I know, I can barely believe it myself), and since then, numerous tax treaties have incorporated its proposals either via the MLI or on a bilateral basis. It is likely that court cases involving influencers being challenged as PEs will appear soon,[89] which might then lead to cases referring to AI as PEs (fraudulent or not). So far, the OECD has not proposed any sort of harmonization of court precedents on the application of BEPS minimum standards, and if they have not done so for those, it is even less probable that they will be concerned about

[81] *See* U.N., "United Nations Model Double Taxation Convention Between Developed and Developing Countries," (Sept. 2021) p. 11.

[82] *See* OECD, "Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 — 2015 Final Report," (Oct. 2015) p. 44.

[83] *See* U.N., *supra* note 81, p. 12.

[84] *See* U.N., "Promotion of inclusive and effective international tax cooperation at the United Nations," General Assembly (Nov. 15, 2023).

[85] *See* Mark Bou Mansour, "UN Adopts Plan for Historic Tax Reform," Tax Justice Network (Nov. 22, 2023).

[86] *See* U.N., *supra* note 81, p. 233-241.

[87] Referring to the Colombian PES standard (in Spanish, "presencia económica significativa"); *see* José Manuel Castro Arango, "Reforma a las normas de tributación internacional en la Ley 2277 de 2022," *Análisis Crítico de la Reforma Tributaria: Ley 2277 de 2022* (2023) p. 194-212 (in Spanish).

[88] *See* Nick Bostrom, "Superintelligence — Paths, Dangers, Strategies," (2014).

[89] *See* Carvalho and Falkowski, *supra* note 24.

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asymmetrical precedents related to BEPS action 7 (not a minimum standard).[90] It will be interesting to see whether those tax audits and court cases about article 5(5) will naturally converge toward some of the remarks that I made here, essentially that a PE link is not reliant on actual agency only and can be created by the use of fraudulent AI mimicking a local influencer on social media. ■

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[90] I have proposed a more structured solution for this elsewhere, which I named the Database of Approved Precedents; *see* Carvalho, "The Database of Approved Precedents (DAP): a Proposal to Steer the Application of the BEPS Action 6 Minimum Standard Towards Global Harmonization," (Jan. 30, 2023).

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