Taxation of the digital economy: Latest developments

There is an important ongoing debate on the direct and indirect taxation of the digital economy. Proposals on digital taxes, which are under negotiation in the OECD, are inter-linked with European Commission proposals on the same subject. As the Council did not reach an agreement on the Commission proposal for a digital services tax, national initiatives appeared in the interim until a global solution in the area of direct taxation could be found in the OECD. On 1 December 2020, the Council endorsed the text of amendments to the Directive on Administrative Cooperation between the Member States (known as DAC7), which will oblige digital platform operators to provide information on the operations they intermediate. If an agreement is not achieved at global level by July 2021, it could trigger an EU response in the form of a digital levy. There is also a debate on whether that levy should be similar to the Commission proposal that failed to get political backing or not.

Overview

Taxing the digital economy is difficult to regulate. There are many types of digital businesses and each specific case has to be considered individually. The corresponding taxable services should be differentiated as well: between those provided by a digital platform to the user and those which can originate between users. Then, it is necessary to distinguish between direct taxation and indirect taxation. In both areas, there is an important debate about the formal obligations of economic operators in general, and those of digital platforms in particular.

Platforms, although not exclusively, are the main subject in the debate on the direct taxation of the digital economy. The idea is that the distribution of sovereign taxation rights among countries should take into account the market on which a provider operates, unlike in the present system, where physical presence is the key criterion for distribution. In essence, the taxing rights would become assigned to the countries in which the consumers or users of digital companies are located. This could imply the modification of current double taxation agreements and principles. It requires an international solution, especially since the countries in which large tech companies are located and taxed need to agree with the countries where these companies generate their profits; hence the global approach in the ongoing negotiations on the subject at the OECD. In this respect, the failed Commission proposal on a significant digital presence envisaged that any EU or non-EU company, located in a country where a double tax treaty is not applicable, and having a significant digital presence in an EU Member State, should be taxed on its digital activities.

In the field of indirect taxation falls the failed Commission proposal for a digital services tax. There is some controversy as to whether the proposed tax is a direct or an indirect one; this distinction has particular importance when considering whether such a tax would affect double taxation agreements focused on direct taxation. Such a tax would not apply to the underlying service provided by a platform to its users, such as the act of sale itself, but to profits generated from user data or from providing the platform for commercial activities among its users. For instance, when the service provided to the users is free, the digital platforms obtain benefits from advertising. Therefore, this tax is to be levied on income from advertising and fees charged to the users, but it does not cover the underlying transactions enabled by the online platform. The Member State that has the right to collect this tax is that in which the target of the advertisements or the users of the platform are located.

Focusing on the service that a digital platform provides to its users for the operations that it intermediates, it is necessary again to clearly determine the nature of the operation in order to establish which Member State has the right to levy VAT for that particular service. More specifically, there are some unresolved doubts related to whether these are purely electronic service transactions or auxiliary transactions to the underlying transactions; if the latter, they are considered to have the same nature as the underlying transaction. The action plan for fair taxation, adopted by the Commission in July 2020, where future work is
The European Commission submitted the **Fair Taxation of the Digital Economy** package of legislative proposals in March 2018. These included two proposals – on an **interim (digital services) tax** and on a **long-term (significant digital presence) taxes** – which received the support of the European Parliament in its consultative role, but not the Council’s, as it failed to reach political agreement. Subsequently, some countries, such as France, Italy and Spain, adopted a national tax similar to the interim digital services tax; others, such as Czechia, are still deliberating on one. Almost all of the countries that have adopted such a tax insist that it is an interim solution until a global one in the area of direct taxation is found.

Meanwhile, the Council reached agreement on adopting a Commission proposal on amending the Directive on Administrative Cooperation (**DAC7**) on 1 December 2020, pending the European Parliament’s opinion. The revised directive would oblige digital platforms to provide information on the operations they intermediate; this information would be exchanged automatically between Member States. So far, such information has been difficult to obtain, since digital platform operators insist that they do not take part in the operations that take place on their platforms, but are mere intermediaries.

### e-Commerce package

When it comes to the underlying operations in the form of sales of goods or services through platforms, the 2017 **VAT e-commerce package**, further developed in 2019, will come into force in July 2021 rather than in January 2021 as originally scheduled. The package introduces two important measures for platforms:

- **Article 14a of the VAT Directive**: Platforms that intermediate in an operation are normally not recognised as taxpayers because they are not those who sell; they are recognised as taxpayers when they carry out: i) imports of less than €150; and ii) sales in the EU when the seller is not established in the EU;

- **Article 242a of the VAT Directive**: Platforms are obliged to save the data on the operations they intermediate in order to keep sufficiently detailed records on the supplies of goods or services, when the recipient is a consumer (not a company). These records should be made available electronically on request by Member States. This is similar, in fact, to DAC7.

### OECD

Negotiations on introducing global digital tax measures are ongoing in the OECD. The OECD proposal is based on two pillars: **pillar one** addresses the business location-taxation nexus rules, reviews the current profit allocation and proposes the grant of new taxation rights. It is mainly based on sales, rather than on physical presence as is the case in the currently binding rules. **Pillar two** aims to establish a minimum corporate taxation level worldwide in order to combat profit-shifting and to reduce tax competition. It does not specifically relate to digital businesses.

The Trump administration has reacted strongly against the idea of a digital tax and has launched an international trade offensive against the countries that have implemented digital services-type taxes, arguing these are a protectionist measure against US tech companies. The opposing stance of the US is making the negotiations very difficult and the target calendar has recently been postponed by six months. The current reference date is July 2021.

If an agreement is reached within the OECD, those EU Member States that have adopted digital taxes would replace them with the globally agreed ones. In fact, the original 2018 proposals and the application of a tax on digital services in some EU countries could be considered an attempt to exercise international pressure to secure progress in the OECD negotiations. The shortcoming is that it may lead to companies having to fulfil different sets of obligations, which would increase their administrative burden and costs. The EU and OECD proposals are inter-related. If global consent is not achieved by July 2021, the EU will respond with fresh proposals. However, it is yet unclear if these would be similar to the 2018 package or not.