BRIEFING

Initial Appraisal of a European Commission Impact Assessment

European Parliament

Better cooperation against tax fraud and evasion

Impact assessment (SWD(2020) 131, SWD(2020) 130 (summary)) accompanying a Commission proposal for a Council Directive amending Directive 2011/16/EU on administrative cooperation in the field of taxation, COM(2020) 314

This briefing provides an initial analysis of the strengths and weaknesses of the European Commission's impact assessment (IA) accompanying the above-mentioned proposal, adopted on 15 July 2020 and referred to the Economic and Monetary Affairs Committee (ECON) of the European Parliament (EP). The proposal, at whose core is the rapid growth of online platform sales, is featured in the Commission's 2020 work programme and is part of the broader EU tax package of July 2020, aimed at making taxation simpler, fairer, more effective and more efficient. The IA points out that these objectives have become even more urgent in the context of the coronavirus crisis (IA, p. 4). Their increasing relevance is also evidenced by the recent creation of a special EP Subcommittee on Tax Matters (FISC).

Alongside the proposal that is the subject of the present analysis, the Commission also presented an Action plan for fair and simple taxation and a communication on tax good governance, laying out a comprehensive tax policy agenda for the coming years. As for the proposal, it focusses on the reporting and transfer of information on the earnings of online platform sellers to the tax authorities in their country of residence.[1] As the IA clarifies, it does not deal with the actual direct tax levied on businesses, which is the subject of other proposals under the above-mentioned action plan (IA, pp. 6-7).

Problem definition

The IA presents a concise and clear analysis of the two main problems to be tackled, including their drivers and consequences, and their relevance to the Member States' ability to trace and prevent tax evasion. The **first problem** is the **lack of reporting of revenues and income of sellers generated by digital platforms**, leaving these 'sizeable' unreported earnings untaxed (IA, pp. 9-12). The causes of the underreporting are diverse, including a lack of incentives for both the taxpayers and the platforms to report the earnings, the fragmentation of income originating from several, be it cross-border or worldwide-operating online platforms, and differing national reporting standards (12 Member States have national reporting requirements while others have none) (IA, pp. 13-15).

The latter issue is also linked to a great variety when it comes to the implementation of the current Directive on Administrative Cooperation in Direct Taxation (DAC) by the Member States, which leads to the **second problem: the lack of efficiency in the cooperation and information exchange between EU Member States** (IA, p. 16). Besides the diversity in national practices and the often ineffective monitoring and evaluation, the IA points to unclear provisions in the current DAC, including legal uncertainties around the concepts of 'foreseeable relevance', group requests and joint audits (IA, pp. 13-16).

The problem analysis is substantiated by several recent stakeholder consultations (see section below) and a thorough Commission ex-post evaluation of the DAC. Based on these sources and own calculations, the IA estimates the total value of services and goods transacted in the EU-27 on digital platforms in 2018 at €55 billion (€34.3 billion in services and €20.7 billion in goods) (IA, p. 11). The

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corresponding resulting **tax gap for 2018 is supposed to be between €2.7 billion and €7.1 billion (**based on an assumed tax rate of 20-40 % on a taxable income of 65 %, and on the assumption that 50 % of taxes are currently not paid, IA, p. 11). The IA notes from the start the data scarcity both on the exact size of the income and revenues of digital platform sellers and on the share of unreported income, owing to multiple issues, starting with the generally uncertain and 'sensitive' definition of a platform[2] and the diverse reporting systems across the EU (IA, pp. 5, 9).

It is therefore welcome that the IA compares its own estimates to those of the TADEUS project on 'Digital and Data' (gathering together the heads of the Member States' tax administrations), which are based on a 2016 study (IA, pp. 11-12).[3] However, these results cannot be checked because, as the IA admits, the above study is not publicly available – only the general TADEUS 2019 outcomes statement is, covering all aspects of tax cooperation in rather general terms (IA, p. 7). Notwithstanding this caveat, the IA's estimates appear to be based on sound methods.

The IA expects the already significant size of the problem to triple by 2025, considering the quick pace at which the digital economy is growing and therefore the ever-increasing loss of tax revenues for the Member States. It also highlights another important consequence: the distortion of (fair) competition and the single market, with financial disadvantages for sellers who do pay their fair share of taxes (IA, p. 16). Annex III to the IA presents the broad groups of citizens/consumers, businesses and administrations as the most affected stakeholders, but it does not explain more specifically how exactly these groups are affected by the problems.

Subsidiarity / proportionality

Taking into account the nature and scope of the problems, as well as the outcome of the consultations and the ex-post evaluation, the IA considers the current cooperation of the national tax authorities insufficient to ensure that taxes due on revenues and income generated by digital platform sellers are indeed paid (IA, p. 18). It notes that even for the 12 Member States that have some reporting requirements (with four more planning to introduce such legislation or guidance),[4] it is currently highly uncertain that they receive information from platforms that are not registered in the respective country and/or from sellers operating on several platforms, be it cross-border and/or global.

Without EU action, the inefficient cooperation among tax authorities in the EU would persist and tax losses would increase. Therefore, to ensure the proper functioning of the internal market and prevent tax avoidance and evasion effectively, the IA considers EU legislative action to be necessary and proportionate at the same time, based on Articles 113 and 115 of the Treaty on the Functioning of the European Union (TFEU), while also minimising negative consequences (IA, p. 19). According to the Commission, the added value of the initiative – compared to a 'patchwork' of national reporting requirements – was confirmed by the public consultation and the 'Digital and Data' report[5] (IA, p. 19).

Objectives of the initiative

Against the backdrop of the expanding digital economy, the IA defines **two general objectives** of the initiative: 1) ensuring a fair and consistent functioning of the internal market; and 2) safeguarding EU Member States' tax revenues (IA, pp. 20-21).

While these objectives are directly linked to the problem definition, their further breakdown into specific and operational objectives is less evident and does not seem to follow the requirements of the Better Regulation Guidelines and Toolbox. In particular, the distinction between general and specific objectives is not entirely clear. The **three specific objectives** are:

- ensure access of tax authorities to the relevant information to tax resident and/or relevant sources of income and/or turnover;
- improve the ability of Member States to detect and counter cross-border tax avoidance and evasion (by making their administrative cooperation more effective and requiring platforms to provide the necessary information to the tax authorities);

- deter taxpayers from tax avoidance or evasion, and foster voluntary compliance.

The distinctions between these objectives and the actions mentioned to achieve them are not clear. In addition, Figure 7 (IA, p. 58), illustrating the intervention logic of the IA, does not feature specific objectives at all, but refers to two 'activities' (new reporting obligations for digital platforms and clarifications to current EU framework for administrative cooperation), omitting the third specific objective.

Furthermore, and contrary to the Better Regulation Guidelines, the IA does not mention any 'operational objectives'. In the chapter on monitoring, it presents indicators in relation to the last two of the three above-listed specific objectives (IA, p. 59).[6] Also, the objectives as presented in the IA do not seem to correspond to all of the specific, measurable, achievable, relevant and time-bound (S.M.A.R.T.) criteria. The overall lack of specification of the objectives and the inconsistencies between the denominations in the text and the illustration do not support a clear understanding of the different levels of objectives there are. In the future, this might make it difficult to effectively monitor and evaluate whether the objectives have been achieved, because it is not clear against what deliverables the achievement of the objectives should be measured ex-post.

Range of options considered

In a **first step**, the IA provides the following policy options:

1) **Baseline scenario** ('doing nothing', taking into account the ongoing yet limited efforts of the OECD to provide non-mandatory advice for reporting by digital platforms);
2) **EU non-legislative action** (recommendations);
3) **EU legislative action** (providing a legal framework to encompass reporting by digital platforms and the exchange of such information).

The preference for the legislative option becomes quickly evident, since the baseline is considered ineffective and inefficient, and the non-legislative approach has been discarded at an early stage. According to the IA, the latter would have no added value compared to the OECD framework under the baseline, leaving the responsibility for the implementation equally to each Member State (IA, pp. 28, 30).

In a **second step**, the IA outlines **a multi-layered, complex package of legislative actions under the legislative option** (IA, pp. 23-27). The IA speaks of 'activities' or 'building blocks' instead of providing a clear list of 'options' and sub-options (IA, Figure 4, p. 23). There is no numbering or other classification of the altogether 14 legislative '(sub)options' discussed in the IA. Table 1 below attempts to provide such a classification of the 'building blocks' presented in the IA to facilitate their visualisation for the reader. The Commission's preferred 'options' are deduced, where possible, from the IA's analysis and the concluding chapter (IA, pp.55-56), and are marked here in grey.

Table 1. Overview of (legislative) policy options

A. Scope of the action
- Option 1.1: Limited scope – selected services
- Option 1.2: Intermediate scope – all services provided via platforms
- Option 1.3: **Full scope – all services and sales of goods**
B. Which platforms should report revenues? (potential exemptions from reporting)
- Option 2.1: **No exemption** – all platforms that facilitate the transaction within the scope should report
- Option 2.2: Exemption based on a threshold – reporting exemption for a platform, the revenue of which does not exceed €100 000 for a three-year period
- Option 3.1: Applies only to platforms established in the EU

- Option 3.2: Applies to **all platforms active in the EU regardless of where they are established**
C. Which platform sellers should report? (potential exemptions for certain reportable platform sellers and transactions)
- Option 4.1: No exemption – digital platforms should report on all sellers regardless of the number and value of the transactions - Option 4.2: Exemption linked to a monetary threshold for each of the sellers, so that platforms would not have to report on the registered sellers that fall below that threshold (discarded option, IA, p. 28) - Option 4.3: Exemption linked to a combined monetary and transaction threshold
- Option 5.1: Only cross-border transactions (i.e. transactions involving two or more Member States) would fall within the scope of the rules - Option 5.2: All transactions taking place within the EU, which would imply that platform operators would report on all transactions linked to a reportable seller, regardless of whether they involve different Member States or are purely domestic
D. Practical aspects
How should the exchange take place? - Option 6.1: Spontaneous exchange (discarded option, IA, pp. 28-29) - Option 6.2: Automatic exchange of information (once a year)
Dataset There are no options – the IA presents the dataset to be provided regarding the platform, the seller and the transaction: 'Within the framework of the "Digital and Data" group led by Member States, later complemented by the discussions at Working Party IV, consensus has been reached that the following set of data [Table 4] would be indispensable to ensure the effectiveness of the system and that the information could reliably be used for taxation purposes' (IA, pp. 26-27, Table 4).
Data checks The IA does not provide any information on the data checks.

Source: IA and authors' own compilation.

The IA does not fully explain all options, for example, what sectors 'option 1.1' (the limited scope) actually includes. The reader is left alone to figure out and make sense of the various 'activities' or 'building blocks' presented, including their order, structure and the links between them. The IA could have also elaborated on the way the options would help achieve the general and specific objectives it identifies earlier. It is, for instance, unclear how the third specific objective (deterrent effect) would be achieved by the various actions discussed.

The IA states that the legislative option (not clear which 'building blocks' this corresponds to) would also 'cover minor fixes to the current administrative cooperation framework to ensure it becomes more effective. These changes to the framework mainly concern: a clarification of the concept of foreseeable relevance; explicitly mentioning that group requests for information are in scope of the directive; and joint tax audits are possible under the directive' (IA, pp. 27-28). More detailed information, especially on the group requests, would have been useful. At the end of the analysis of impacts (see below), the baseline scenario, under which the problem is expected not only to persist but to grow significantly, is used as a benchmark for the comparison of the main legislative activities analysed in the IA in terms of their effectiveness, efficiency and coherence with other EU policies (IA, pp. 53-54). The preferred measures are also deemed to be proportionate (IA, p. 56).

Assessment of impacts

The IA mainly outlines the **economic** impacts of the legislative 'building blocks', while considering the social and environmental impacts only briefly. From the start, it openly acknowledges the

scarcity of data, which 'prevents us to reliably estimate the economic impacts' (IA, pp. 31-32).[7] Keeping in mind this uncertainty, the IA expects **benefits in the form of increased tax revenues** from the reporting of revenues of only selected services (accommodation and transport sectors, as well as other on-demand services) between €1.1 billion and €3.8 billion, whereas the reporting of revenues of all online sales of all services and goods (the preferred option of the IA) would yield significantly larger tax revenues, ranging **between €2.7 billion and €7.1 billion** (IA, p. 36). The IA highlights that it expects these positive effects to be even higher by 2025, as the platform economy grows in importance across the EU (IA, p. 36).

At the same time, the IA points out that requirements for platforms to report data and for tax administrations to exchange them will entail **costs** for both. These would consist of one-off substantive compliance costs and recurrent administrative and enforcement costs (IA, pp. 38-39). As about the benefits, the IA is transparent about the assumptions and methods underlying the analysis, in particular the limitations of the extrapolations and cost calculations. (IA, pp. 43). It estimates that the **one-off, substantive compliance costs** for platforms across the EU vary between €250 million in the case of a limited reporting of selected online sales revenues and €875 million in case of a full reporting of all platform sales revenues. The estimated costs per platform, on average, are about €400 000. One-off costs for all tax administrations are estimated at between €2 million and €7 million per tax administration on average and depending on the scope of reporting. The one-off costs for the Commission are estimated at €0.8 million for the development and the first five years of operation of the system (IA, pp. 40-41). According to the IA, the **recurrent administrative costs for platforms** would vary between €30 million in the case of a limited scope to about €100 million in the case of a full scope. The administrative costs per platform, on average, would range at €50 000 per year. For tax administrations, the recurrent costs of the system are estimated approximately between €6 million (limited scope) and €21 million (full scope) per year, or approximately €200 000 to €800 000 per Member State (IA, p. 42). Overall, **recurrent enforcement costs** (labour costs for sorting and exploiting the data) are estimated to vary between €3 million and more than €10 million, or about €100 000 to €400 000 per tax administration (IA, p. 42). In conclusion, even considering the uncertainty of the estimates reflected in the wide range of possible tax revenue gains and anticipated costs, the Commission states that 'regardless of methodology, the benefits derived from implementing automatic EU-wide reporting seem to be in the order of billions of euros per year', estimating the current level of underreporting to be as high as 50 % for all sectors (IA, pp. 36-37). More importantly, these benefits exceed clearly the anticipated total costs for businesses and administrations (€1.2 billion under the preferred option, IA, p. 80).

The **strengthening of administrative cooperation is expected to improve the effectiveness of EU-wide tax cooperation** (IA, pp. 47-50). In line with the findings of the 2019 ex-post evaluation of the implementation of the existing DAC, the proposed new directive clarifies 1) the concept of 'foreseeable relevance' (tax administrations have to cooperate to exchange information foreseeably relevant for tax administration and enforcement); 2) the explicit possibility of 'group requests' (the IA mentions 'tidying up' the legislation for a request for information concerning a group of taxpayers sharing certain characteristics, but does not specify any further); and 3) the explicit provision for 'joint audits' in the legislation (joint audits are expected to save tax administrations and taxpayers time and money).

What the effects would be from the tax authorities' improved cooperation is difficult to quantify, as are the **social impacts** – the expected increase in tax revenues, tax fairness and transparency – that the IA assesses as positive (IA, pp. 50-51). According to the IA, two **fundamental rights** may be affected by the intervention: personal data protection and the freedom to conduct a business. The IA points out that the specific provisions and safeguards on data protection in the current DAC will continue to be respected in line with the General Data Protection Regulation (GDPR), as the data that would be collected on sellers would be limited and proportionate to the aim of achieving better enforcement of tax laws, but would not include data on consumers (IA, p. 51). In addition, the IA specifies that the intervention does not negatively affect the freedom to conduct a business (IA,

pp. 50-52). Finally, the IA considers that 'the total **environmental effects** are unclear but likely to be minor' (IA, p. 52). This claim would have deserved further elaboration and explanation.

SMEs / Competitiveness

According to the IA, the preferred legislative option would ensure the 'broadest possible level playing field', increase fair competition and trust and improve **competitiveness** in the fast-growing and expanding sector of the digital platform economy (IA, pp. 43-44). As another positive consequence, consumers would benefit, as they 'appreciate the convenience of having a wide range of services and goods at their immediate disposal' (IA, p. 44).

Fairer competition would also benefit **SMEs** as reporting platforms because standardised rules would facilitate their expansion across the border (IA, p. 46). While the IA expects SME platforms to face some compliance burden, it concludes that most users use large platforms so that the burden for SMEs would only be a 'fraction of the overall compliance costs generated by the intervention' (IA, p. 47). A more detailed substantiation of this claim, which is not supported by specific quantifications, would have been helpful. The IA evaluates the direct impact of the intervention on SME sellers (estimated to be one third of reportable sellers) as 'negligible' and positive, and even states that SME online sellers 'are not assumed to bear any particular burden or cost' of the initiative (IA, pp. 39, 45-46). They would 'most likely' only have to share data they have shared anyway to register on the platform. Overall, the IA considers that the 'better business environment' would benefit SMEs more than the potential costs that would burden some of them, especially since these costs are high under the baseline scenario (IA, p. 47).

Simplification and other regulatory implications

In the context of **simplification** that is expected to be achieved by the harmonisation and clarification of rules, the IA highlights the **coherence** of the initiative with the EU's comprehensive VAT e-commerce package that will enter into force on 1 January 2021, obliging platforms to keep records of online transactions and to make them available to the tax authorities on request (IA, p. 50). The explanatory memorandum of the proposal stresses that it is designed to reduce regulatory burdens for digital platform operators, taxpayers and tax administrations (p. 8).

Monitoring and evaluation

Contrary to what the IA states, it only identifies monitoring indicators for specific objectives 2) and 3). It also does not identify any operational objectives. As a measurement tool, the IA indicates 'a yearly assessment of the automatic exchange of information' (AEOI) to be presented by the Member States' tax administrations and discussed in the Administrative Cooperation in Direct Taxation Commission expert group. In addition, the IA speaks of 'statistics on administrative cooperation other than AEOI' and 'a yearly questionnaire on the functioning of the directive' (IA, p. 59). However, it is not clear who will provide this information. Despite the repeatedly highlighted lack of data, the presented indicators do not seem to significantly improve future specific data collection, for instance, regarding the size of platforms, SMEs and cross-border transactions. The IA leaves the question of the ex-post evaluation of the initiative open. It will take place as part of the third report on the application of the directive, either by 1 January 2023 or by 1 January 2028, depending on the beginning of its implementation before or after 2022 (IA, p. 60).

Stakeholder consultation

The Commission made considerable efforts to consult broadly with stakeholders and refers to their views fairly consistently throughout the IA. These views include feedback received through the inception impact assessment; several targeted consultations (with Member States' public authorities and the businesses involved (platforms)); and an online open public consultation. The latter, to which the Commission received 37 replies, lasted from 10 February to 6 April 2020, thus eight and not 12 weeks as required by the Better Regulation Guidelines, following an exemption granted to make it possible to 'respect the overall political timeline of the initiative', (IA, p. 68). While

the synopsis report in Annex II to the IA provides more detailed information on the different stakeholder consultations, at times it remains vague on specific aspects (e.g. 'most Member States have conducted compliance activities [...], or 'some Member States were favourable to an exemption for start-ups [...]', IA, Annex II, pp. 71 and 73). Annex III of the IA provides a summary of the costs and benefits for the main stakeholders under the legislative activities assessed in the IA (IA, pp. 78-80).

Supporting data and analytical methods used

The IA is based on sound sources and methods and, as indicated before, openly acknowledges the scarcity of relevant data and thus, uncertainties of the exact costs and benefits, which are duly taken into account in the analysis.[8] The IA is in particular transparent with regard to estimations and calculation methods (for instance, the EU standard cost model), and explains the underlying assumptions well. Annex IV provides additional information on the categories of costs and benefits and on the assumptions made.

The IA has taken into account the findings of its thorough 2019 ex-post evaluation of the implementation of the DAC, itself based on an extensive external study. Annex V sets out the OECD model rules for sellers in the sharing and gig economy, Annex VII contains a bibliography, and Annex VIII provides references to the Commission's evaluation of the existing DAC.

Follow-up to the opinion of the Commission Regulatory Scrutiny Board

The European Commission's Regulatory Scrutiny Board (RSB) delivered a positive opinion 'with reservations' on the draft IA on 5 May 2020, noting that the report still contained significant shortcomings. The RSB criticised 1) the lack of a complete and clear problem analysis, highlighting the costs of containing tax evasion in transactions on digital platforms; 2) the lack of sufficiently specific objectives to fully match the problem analysis; 3) the lack of a sufficiently substantiated and justified preferred option.

The IA explains how the RSB's comments were addressed in its Annex I (pp. 61-62). While it appears that the problem definition has substantially improved, the objectives would have deserved further attention (see section on objectives above). The final IA also seems to elaborate more on the activities under the preferred legislative option in a concluding section 8 (IA, pp. 55-57). However, since there is no clear and structured presentation of the options, the exact components of the preferred legislative option are not entirely clear. The IA discusses the proportionality of the preferred 'building blocks', but more information on the proportionality of the other considered measures could have been provided. It is surprising that the RSB did not comment on the quality of the section on the options in the draft IA.

Coherence between the Commission's legislative proposal and the IA

The legislative proposal appears to correspond overall to the preferred actions identified in the IA.

Key Findings

The IA provides a good problem definition overall, taking into account the Commission's evaluation findings and stakeholder consultations. It is based on solid research and sources, and is fully transparent as regards the methods and assumptions underlying the analysis. In particular, it openly acknowledges the scarcity of relevant data, which is taken into account in the cost and benefit estimates. Another strength of the IA is its accessibility for non-specialist readers. However, the objectives of the initiative are not sufficiently differentiated and specified. Furthermore, the presentation of the options lacks clarity and structure, because instead of a clear list of options, the IA presents different sets of measures and actions. The IA mainly assesses the economic impacts of the actions under the preferred legislative option, concluding that the benefits would significantly exceed the costs. Social and environmental effects are considered briefly, the former namely in terms of tax fairness and transparency, and data protection safeguards.

ENDNOTES

1 The EPRS' Directorate B is currently also preparing a European implementation assessment on tax evasion and fraud ('EU requirements for exchange of tax information: progress, lessons learnt and obstacles to overcome'). See also A. Scherrer, Fighting tax crimes – cooperation between Financial Intelligence Units, Study, EPRS, European Parliament, March 2017.

2 In the context of the current proposal, the IA offers the following definition: 'The concept of a Platform does not include software exclusively allowing the (i) processing of payments, (ii) listing or advertising, or (iii) redirecting or transferring of users to a Platform' (IA, p. 5, footnote 13).

3 In addition, the IA corroborates its own estimates in Annex IV, by comparing them to other sources, including those of the ex-post evaluation and two other IAs, one by the UK government and one of the Commission (due to incoherent referencing, the latter is not easy to find), IA, pp. 82-85).

4 See Annex II, p. 71, of the IA.

5 The published 'outcomes statement' is too general to corroborate this claim, see point 11.

6 Figure 7 was added following the RSB opinion on the draft IA (IA, p. 58). It does not contain operational objectives, but features 'outputs' instead (for instance 'Harmonized interpretation & application of admin cooperation framework'), which could be understood as expected deliverables, even though they still remain rather vague.

7 As reasons for the data scarcity in this context, the IA lists the following: underreporting of income and revenues of the digital platform economy, different reporting requirements across jurisdictions or no requirements, and privately held digital platforms not publishing their annual financial reports (IA, p. 32).

8 It makes clear that the estimation of costs 'involves significant uncertainty regarding each parameter' (IA, p. 43).

This briefing, prepared for the ECON committee, analyses whether the principal criteria laid down in the Commission's own Better Regulation Guidelines, as well as additional factors identified by the Parliament in its Impact Assessment Handbook, appear to be met by the IA. It does not attempt to deal with the substance of the proposal.

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