



Global Tax Webcast

Taxation of the Digital
Economy: an Asia Pacific
perspective on the recent
developments

KPMG Asia Pacific Tax Centre


May 15, 2018



Speakers

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Agenda

- Digital tax proposals
- A transfer pricing approach to the concept of digital presence
- Observations and looking ahead
- Indirect Taxes
- Future directions
- Q&A



Digital tax proposals

How did we get here?

Overview

2013: Collin & Colin Report in France



October 2015: BEPS Action 1 report



2016: Equalisation Levy in India



2016: Emergence of unilateral measures



November 2017: OECD public consultation



March 2018: Delivery of OECD & EU report/draft

The terms of the debate

Why Ireland faces a fight on the corporate tax front

New charge chips away at the tax package which Ireland offers to foreign investors

© Wed, Mar 14, 2018, 06:00



Cliff Taylor

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IN THE SPOTLIGHT



Fair Taxation for the Digital Economy

Digital tax deepens EU-US trade rift

opposes plans for digital levy • Brussels prepares counter-measures to tariffs

The European Commission is preparing to unveil its "digital tax" plans next week, hooding calls led by France to force tech companies to make bigger contributions. They would change a longstanding consensus to tax companies on the basis of profits by instead targeting revenues in Europe, according to draft proposals seen by the Financial Times.

"Some of these companies are among the greatest contributors to US job creation and economic growth," Mr Mnuchin said.

While he did not specifically refer to the Brussels proposals, his comments

add to tension with the EU days before Donald Trump's administration is set to impose a 25 per cent tariff on steel and a 10 per cent tariff on aluminium.

Brussels yesterday published a draft list of close to 200 US products that would be targeted for higher duties if the EU failed to secure an exemption from the tariffs. The list covers some €2.8bn of US exports ranging from whisky to motorbikes. Its publication is a legal step that gives companies 10 days to raise concerns before Brussels adopts the measures.

The commission still hopes to avert an outright clash with the US over



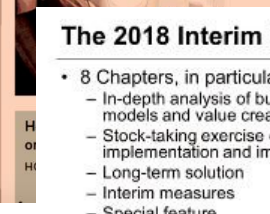
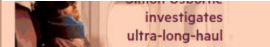
Steven Mnuchin: "Some of these [tech] companies are the greatest contributors to US job creation"

tariffs. Peter Altmaier, Germany's economy minister, will head to Washington tomorrow, while Cecilia Malmström, the EU's trade commissioner, is set to meet US commerce secretary Wilbur Ross next week.

Brussels said publication of the retaliation list was needed to respect tight timelines set by the World Trade Organization for countermeasures to be put in place. "We need to be sure that we protect our rights," one official said.

Mr Mnuchin's words laid down a marker from the US before next week's G20 meeting in Buenos Aires.

What political risk? page 7



- 8 Chapters, in particular:
 - In-depth analysis of business models and value creation
 - Stock-taking exercise on BEPS implementation and impact
 - Long-term solution
 - Interim measures
 - Special feature
 - Next steps





Where are we now?

OECD 2018 Interim Report

OECD 2018 Interim Report

DE tax concerns

- Nexus – exploitation without traditional nexus
- Data – how to attribute value
- Characterization – digital revenues

User value creation

- No consensus
- Attempt to set out analysis of value creation processes, which will be further refined

Organisation for Economic Co-operation and Development

Long-term solution

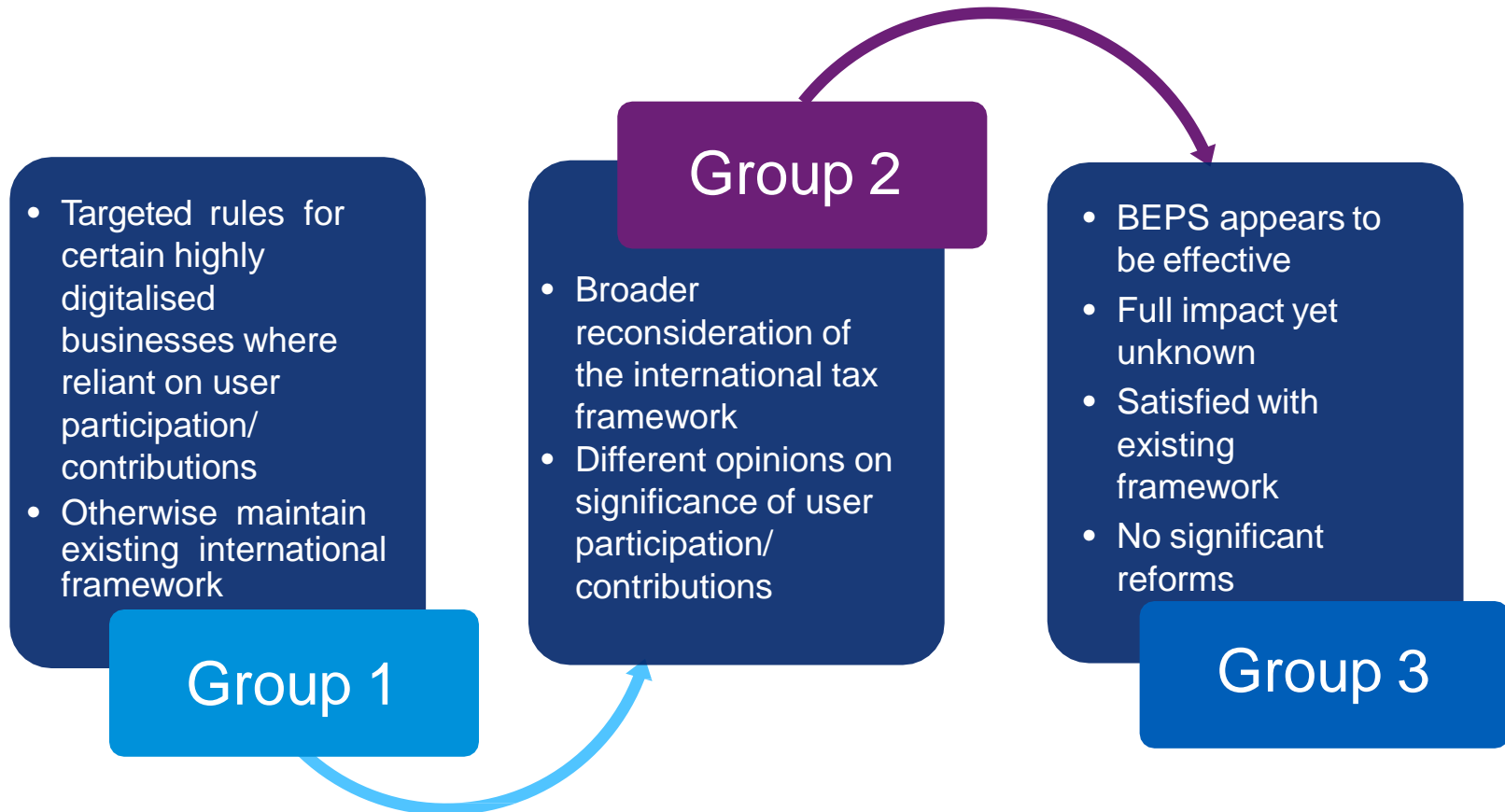
- No consensus
- Nexus – jurisdiction to tax nonresidents
- Profit allocation – how to allocate profits to jurisdictions

Interim measures

- No consensus
- No recommendations
- Framework agreed as to design of interim measures

OECD 2018 Interim Report - Three views on the way forward

Country views are categorized into three groups



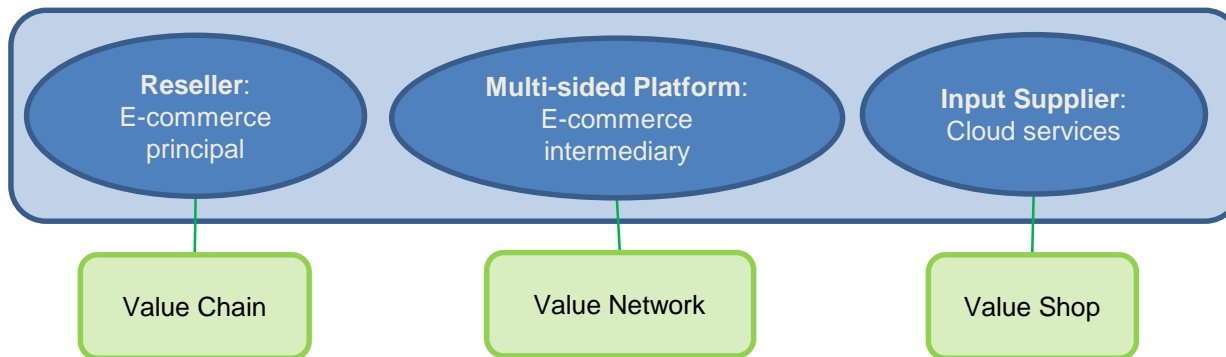
OECD 2018 Interim Report – Value Creation categories

	Multi-sided Platforms	Reseller	Input Suppliers	Vertically-integrated Firms
Indirect Network Effects	Yes	Yes	No	Yes
Intermediary	Yes	Yes	No	No
User Affiliation	High	Low	-	Low
Price Control and Liability	End-users	Reseller	Firm	Firm
Production of Final Good	No	No	No	Yes



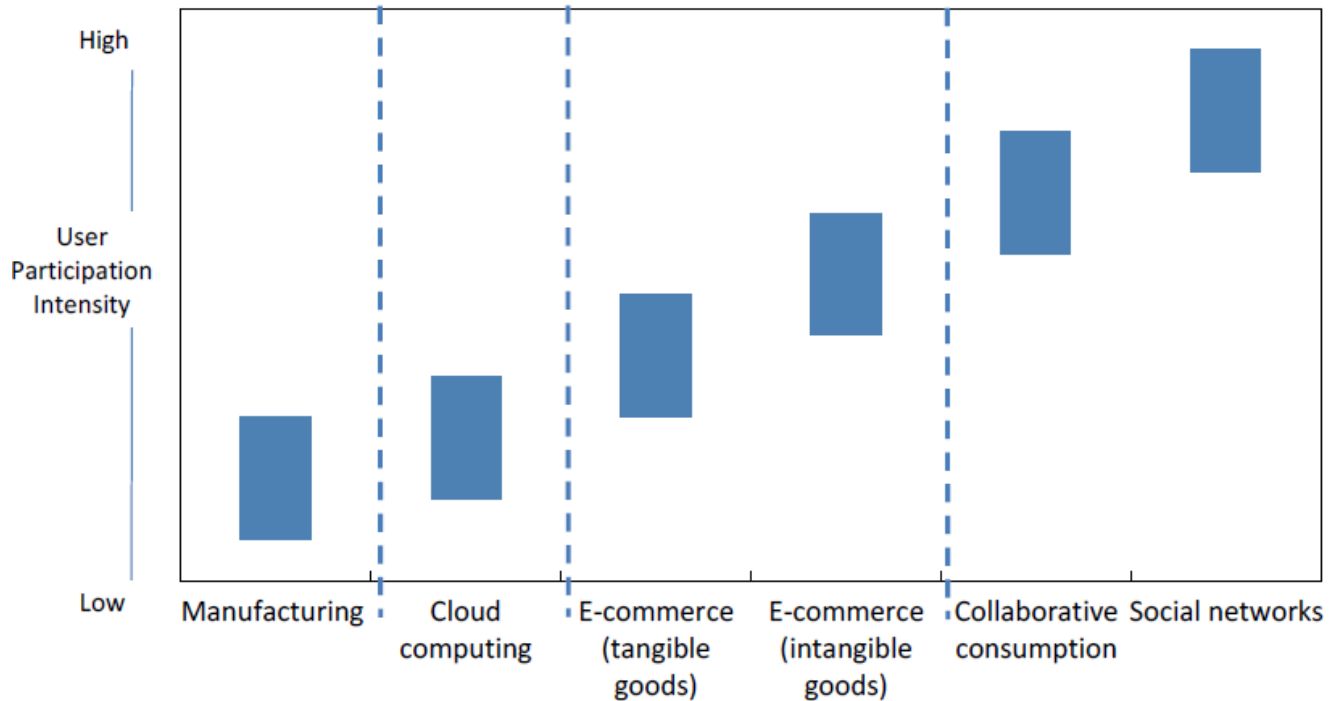
Interim Report 2018, p.31

MNE group



OECD 2018 Interim Report - Intensity of User Participation

Figure 2.8. Intensity of user participation



Interim Report 2018, p.58

Unilateral DE measures

Summary of unilateral country measures

Alternative PE thresholds

- Significant economic presence test (e.g., Israel, India)
- Virtual service PE (e.g., Saudi Arabia)

Withholding taxes

- Broader royalty definitions
- Technical service fees
- Online advertising

Turnover taxes

- Targeted sectors such as digital ads (e.g., Hungary)
- Levy on digital transactions (Italy)
- Equalization levy (e.g., India)

Specific regimes for large MNEs

- Diverted profits tax (e.g., U.K and Australia)
- BEAT (U.S.)

Interim measures

Countries favoring interim measures observe design considerations

- Compliance with international obligations (treaty, WTO, EU, EEA, etc.)
- Temporary
- Targeted (e.g., digital ads, platform services)
- Minimizing over-taxation
- Minimizing impact on start-ups and SMEs
- Minimizing cost and complexity





Where are we now?

EU Proposal & UK Position Paper

Digital Services Tax - Interim solution



A. Scope

- (i) Transmission of Data: website publishers, App developers, Advertisers
- (ii) Intermediation Services: platforms that bring consumers and suppliers together
- (iii) Supply of advertising
- (iv) Out of scope?: supply of digital content, e-commerce ex intermediation, payment services?



B. Tax

- (i) Tax on gross revenues
- (ii) 3% single tax rate
- (iii) Annual worldwide revenues > EUR 750M and digital revenues in the EU > EUR 50M
- (iv) Tax due where users are located
 - Allocation key depending on the digital services
 - One-stop-shop simplification system



C. Observations

- (i) No difference between purely domestically operating companies and international companies
- (ii) Pay the tax also when it is making a loss or paying a “normal” effective tax rate?
- (iii) Is the DST deductible as an expense or creditable as a foreign tax credit?

Digital PE - Long term solution

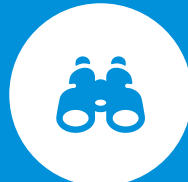
A. Standalone directive on the taxation of digital activities

- (i) Taxpayers incorporated or established in the EU and outside of the EU but with no relevant double tax treaty, AND with a **significant digital presence** in the EU
- (ii) Outside of scope: Situations where a double tax treaty with the relevant Member State applies



B. Taxable nexus in addition to the existing PE concept

- (i) Rely on a large user base, user engagement and user's contribution
- (ii) Revenues from digital services in a MS > EUR 7 million, or no. of users in a MS > 100,000, or no. of online contracts with in a MS > 3,000
- (iii) Digital service delivered over the internet or an electronic network, the nature of which renders its **supply essentially automated** and involving **minimal human intervention**



C. Profit allocation relying on the current OECD framework applicable to PE

- (i) OECD arm's-length principle based on significant people functions relevant to the attribution of risk and to the economic ownership of assets, AND
- (ii) Tailored framework for economically significant functions





A transfer pricing
approach to the concept
of digital presence

Value?

“Where is value created?”

Underlying principle for transfer pricing is that profits should be taxed where value is created.

However, in a digitalized world, it is not always clear:

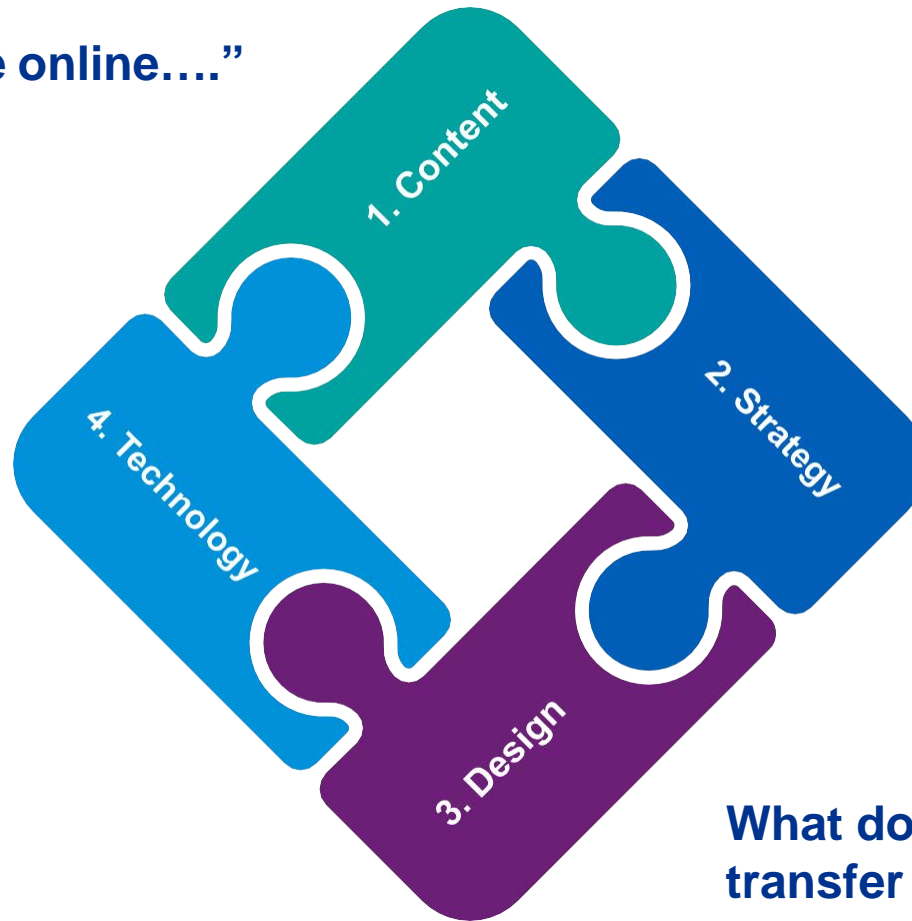
- What the value is,
- How to measure it,
- or where it is created

“How to capture activities which are increasingly based on intangible assets and data?”

Development
Enhancement
Maintenance
Protection
Exploitation

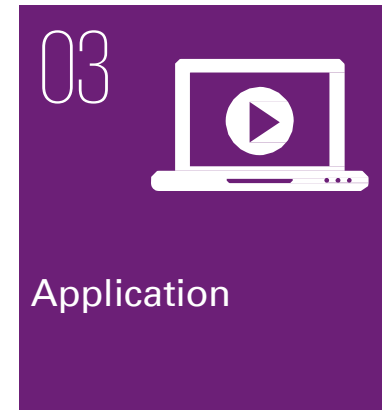
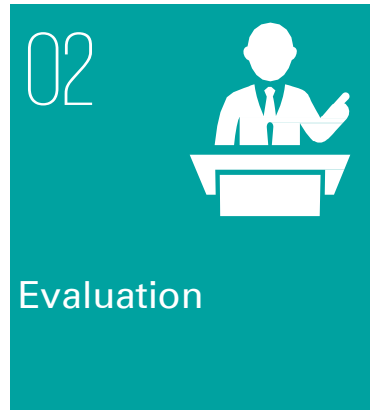
What is digital presence?

“Occupy space online....”



What does this mean for transfer pricing?

Approach: where do you start?





Observations and what lies ahead

Observations and design challenges

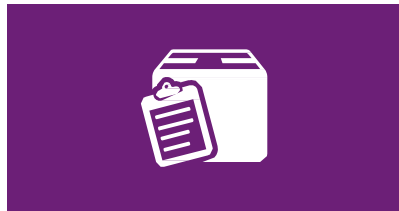
Both long-term and interim measures raise a number of design and implementation issues. Consensus on these considerations will be difficult and time consuming.



International obligations

How do you design a digital tax consistent with treaty obligations?

What are the implications?



Transfer pricing

Consistent with arm's-length principle?

Challenges with a "modified" authorized OECD approach (AOA)

The "U.K. approach"

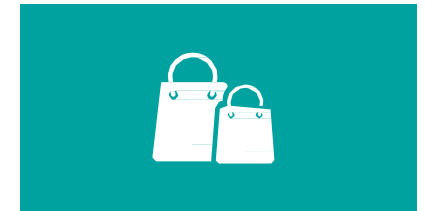


Design considerations

Party to tax

Sourcing profits and revenue

Assessment and collection



Scope concerns

How to define what's in and what's not?

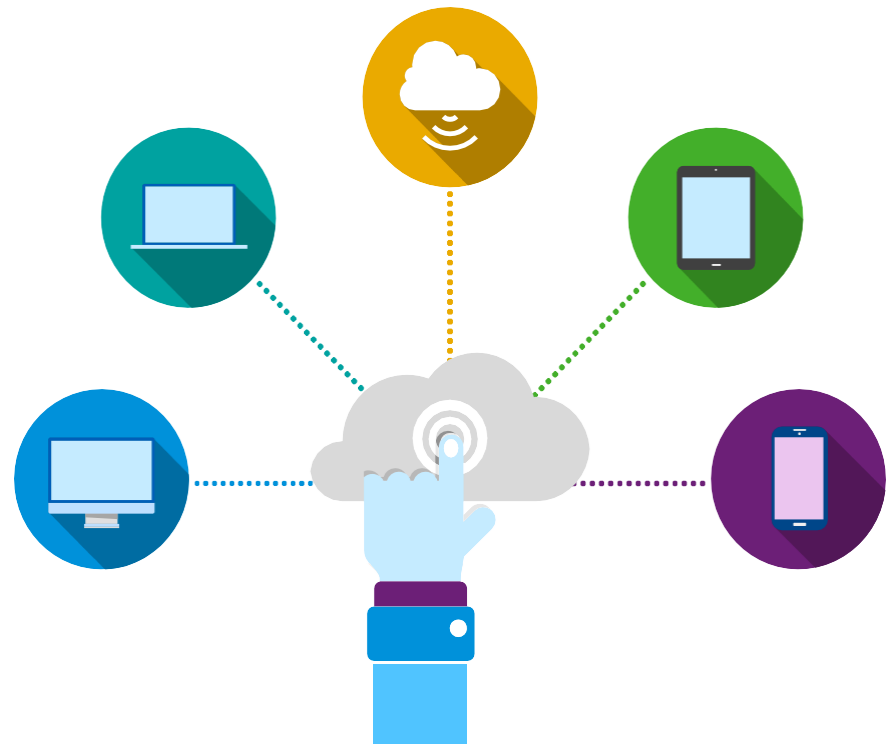
Flexibility for future DE business models

Big picture and looking forward

Will these proposals really become reality and what will it mean to international tax norms?

- What is this debate really about?
- Is consensus possible for a long-term solution that singles out the DE possible?
- Are there broader trade implications?
- Where will we be in the future (one year out? five years out?)

[Read our latest report 'Observations on OECD Interim Paper and EU Commission Digital Tax Proposals'](#) for our initial thoughts.



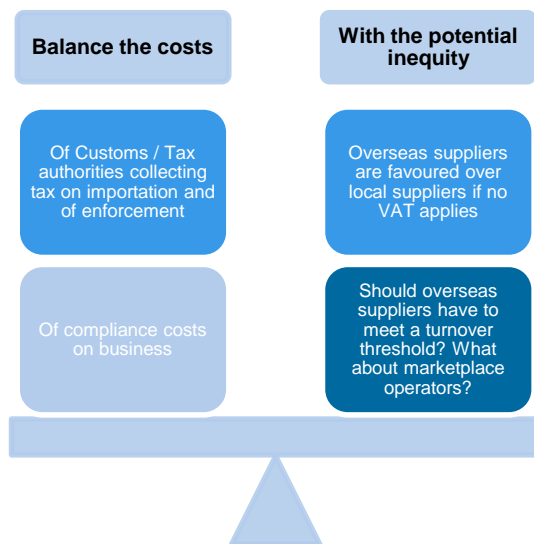


Indirect Taxes

The digital economy – indirect tax policy issues

Problem 1 – low value imports of goods are not subject to VAT/GST, and online shopping has grown























The problem:



Recommendations:

- Thresholds below which VAT/GST does not apply should be lowered
- Tax authorities to significantly improve efficiency of processing imports
- Introduce simplified registration systems to enable non-residents to register for VAT/GST

Problem 1 - low value goods - collection method

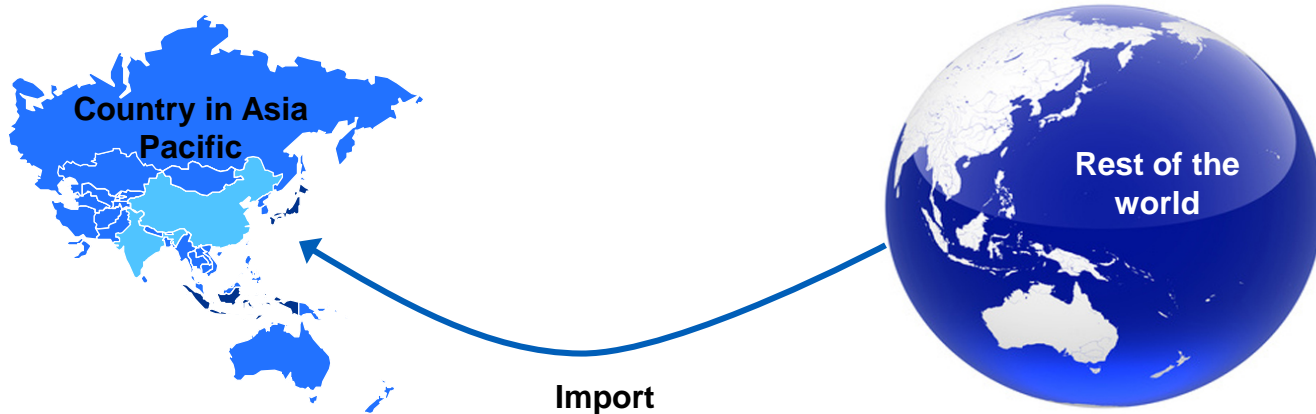
VAT regulatory change		Examples of jurisdictions		
		Currently applicable	Legislative phase	Policy discussion / consultation phase
Goods	Vendor liable – withdrawal of import relief for low value consignments		   	  
	Marketplace operator liable (in certain circumstances)		 	  
	Marketplace operator jointly & severally liable			
	Logistics provider liable under merged VAT/Customs e-commerce model			
	Collection from debit/credit card issuers facilitating transactions	 		
	Split payment method			
	Deeming a PE through imposing VAT registration obligations			

The digital economy – indirect tax policy issues

Problem 2 – how to collect the VAT/GST on importation of digitized services supplied Business-to-Consumer (B2C)

The problem:











- Overseas service provider may have no PE in country and is not registered for VAT
- No VAT or GST is currently being paid on importation
- Collecting the VAT from end consumer is impractical



OECD recommendations:

- Require non-resident suppliers to register for VAT/GST and account for output tax. Allow for simplified registration processes.
- No point in imposing VAT/GST collection obligations on end-consumers. Improve information exchanges, assistance with audits and recovery to enforce.

Problem 2 - digitized services B2C - models

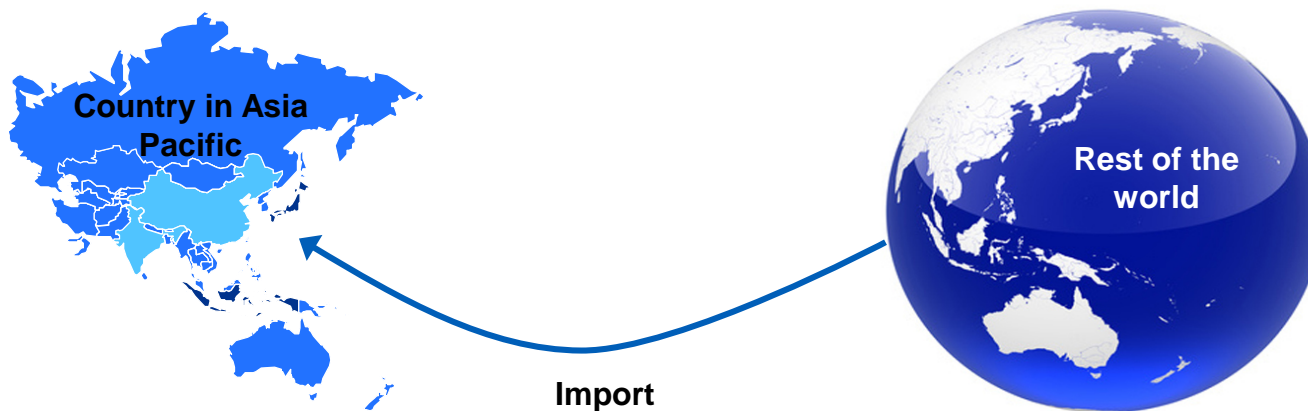
VAT regulatory change		Examples of jurisdictions		
		Currently applicable	Legislative proposals	Policy discussion / consultation
Services	Non-resident vendor liable			
	Marketplace operator liable			
	Customer withholds or assessed			
	Split payment method (including goods)			
	Deeming a PE through imposing VAT registration obligations			

The digital economy – indirect tax policy issues

Problem 3 – how to collect the VAT/GST on imported intangibles and services supplied Business-to-Business (B2B)

The problem:










- No VAT or GST is paid on importation
- If recipient business is not eligible for a full credit, creates a bias in favour of procuring from offshore service providers rather than domestic service providers
- Largely affects banks and other FS service providers (not fully creditable)



OECD recommendations:

- B2B: introduce reverse charge rules

Problem 3 - B2B models

VAT regulatory change		Examples of jurisdictions		
		Currently applicable	Legislative proposals	Policy discussion / consultation
Services	Reverse charge on all supplies			
	Reverse charge where leakage only	 (electronic services only) 		
	VAT withholding by recipient			
	Split payment method	 (transactions with public agencies only)		
	Nothing	 		

Other ASPAC DE examples

Taiwan

- 20% tax rate
- applicable to cross border e-services (e.g. online games, ads and streaming) and services utilised in physical location in Taiwan
- May apply to both B2B and B2C services
- Net basis taxation applies, with deduction for either actual costs or by applying deemed profit ratio
- Collection on WHT basis through domestic and foreign platforms

India

- 6% equalisation levy applicable to online B2B advertising by foreign entities earned in India since June 2016
- Proposal now to apply “virtual PE” where “significant economic presence” in India. Applies where (1) foreign company provides goods, services into India, including through downloads and exceeds a threshold (TBD); and (2) foreign company engages in solicitation of business in India through digital means on a sustained basis. Intended to take effect from April 2019

Thailand / Indonesia

- At various stages, both have proposed variations of ‘deemed PE’ measures – though currently in abeyance
- Thailand has not progressed further at this stage, favouring VAT measures
- In 2016 Indonesia proposed requirement to establish a PE if providing digital services, and in 2017 issued Circular Letter proposing enhanced PE measures around servers/data centres

Australia - income tax changes

Multinational Anti-Avoidance Law (MAAL)

- Effective 1 Jan 2016- Deemed PE, plus penalties
- Applies to significant MNEs (AUD1B+ turnover) supplying goods or services to Australian customers, and recording revenue overseas
- Arrangements with “a principal purpose” of avoiding tax in Australia or reducing foreign tax liability
- Target 30 unnamed multinationals, but will have broader impact
- Restructuring to MAAL compliant structures

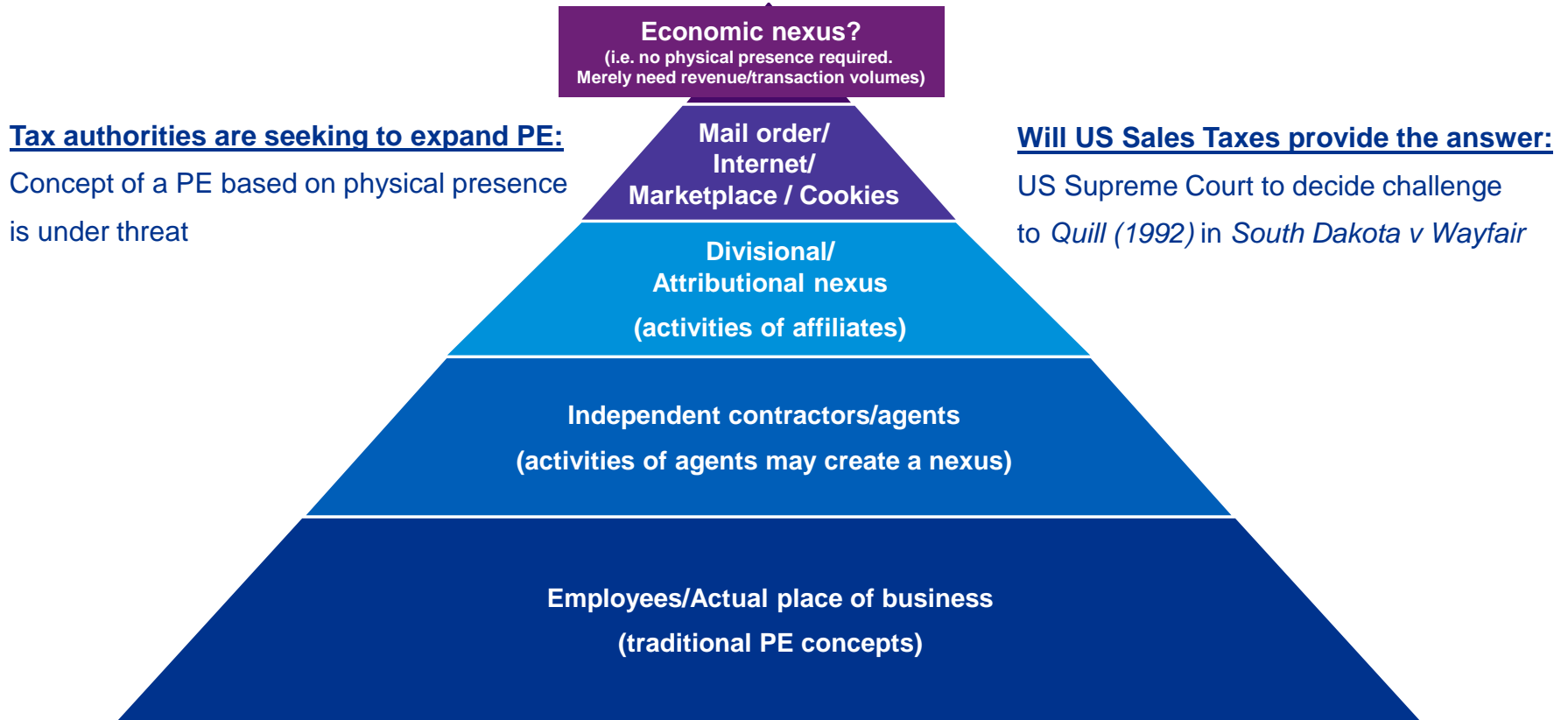
Diverted Profits Tax (DPT)

- Effective from income years commencing on or after 1 July 2017
- 40% tax rate
- Applies to significant global entities (AUD1B+ turnover)
- Arrangements entered into or carried out for a principal purpose of avoiding Australian tax
- Primarily relevant where payments made to a jurisdiction with a tax rate significantly lower than Australia.



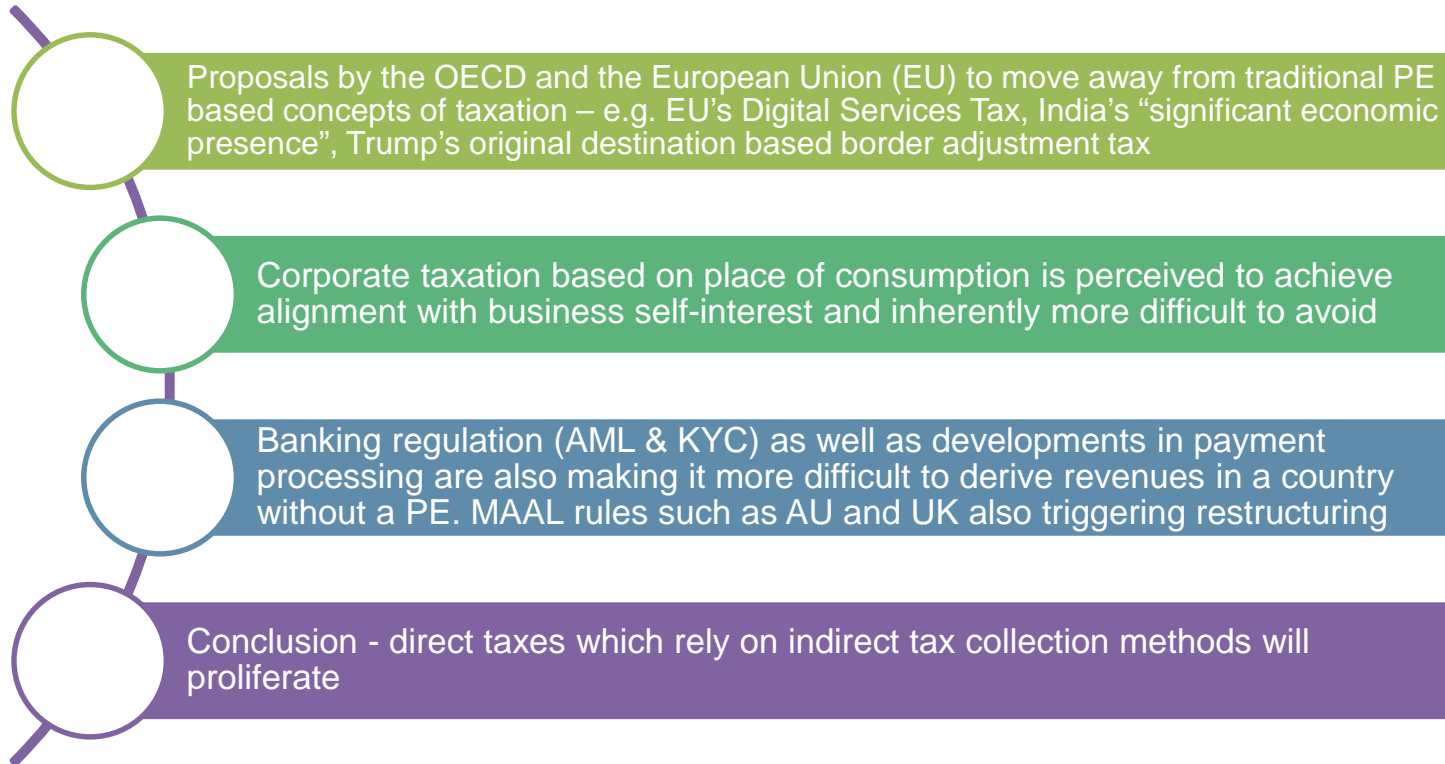
Future directions

Direct taxes and indirect taxes are morphing



Direct tax and indirect taxes are morphing

Consider the following:



Key takeaways - what it means for clients

1

Clients are required to comply with new taxes based on where their customers may be located. They require our help since they may not have tax teams and resources in country

2

Indirect tax collection methods and resources will need to be deployed for new direct taxes too – who should take 'ownership' of them?

3

A big challenge of the tax function amongst many digital economy clients right now is in managing the data. We need to help them get the information to meet their obligations

4

These measures are currently focused on digital economy clients. How will this affect the next wave of clients – such as FinTech, traditional retailers with e-commerce business etc.

5

Direct taxes will increasingly be destination based – this has the potential to alter effective tax rates and the resourcing required to manage those taxes

6

Assisting our clients requires greater member firm collaboration than normal in managing multijurisdictional obligations

7

Watch developments in other taxes as a guide to the future direction of PE based concepts

8

We need to ensure we communicate developments to clients and throughout the network on a very timely basis. Providing a global proposition is key



Q&A

Today's Presenters



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