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POSITION PAPER

EU CONSULTATION ON FAIR TAXATION OF THE DIGITAL ECONOMY

Prepared by the CFE Fiscal Committee

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The CFE (Confédération Fiscale Européenne) is the umbrella organisation representing the tax profession in Europe. Our members are 308 professional organisations from 24 European countries with more than 200,000 individual members. Our functions are to safeguard the professional interests of tax advisers, to assure the quality of tax services provided by tax advisers, to exchange information about national tax laws and professional law and to contribute to the coordination of tax law in Europe.

The CFE is registered in the EU Transparency Register (no. 3543183647-05).

We will be pleased to answer any questions you may have concerning CFE comments. For further information, please contact Stella Raventós Chair of the CFE Fiscal Committee, or Mary Dineen Advisor to the CFE Fiscal Committee, at brusselsoffice@cfe-eutax.org.

1 Introduction

This Opinion Statement by the CFE Fiscal Committee is in response to EU public consultation on the fair taxation of the digital economy.

We will be pleased to answer any questions you may have concerning our comments. For further information, please contact Ms. Stella Raventós, Chair of the CFE Fiscal Committee or Mary Dineen, Adviser to the CFE Fiscal Committee, at brusselsoffice@cfe-eutax.org.

2 General remarks on the EU consultation

In circumstances where the OECD is in the advanced stages of completing its Report on the Tax Challenges of the Digitalised Economy (due to be published Spring 2018), the CFE believes the EU Commission is premature in proposing unilateral action in the context of fair taxation of the digital economy. Similarly, any proposed legislation within the EU before the OECD's Final Report on the Tax Challenges of the Digitalised Economy (expected 2020) would constitute a unilateral action, and be at variance with the view taken by the members of the OECD that the OECD taskforce on the digital economy should focus on internationally agreed long-term solutions and that short-term or unilateral action is not the best way forward.

The CFE believes the format of this public consultation is too rigidly framed and does not reflect the level of technical refinement the issues require, nor does it encourage meaningful engagement with stakeholders or enable detailed debate about the merits of the various proposals. Many of the questions do not relate to technical aspects but rather are more akin to political statements (e.g. at 4.2 *"Social fairness is impacted because some digital companies do not pay their fair share of tax"*). Such a technically complex subject as the taxation of the digital economy cannot, and should not, be distilled down into overly simplified statements. In addition, multiple choice is an inappropriate tool for examining complicated tax proposals. Given the huge importance of this topic and the effect any proposed EU legislative action will have on the single market, meaningful engagement beginning from a neutral position should take place.

3 Digital economy should not be ring-fenced

CFE supports the conclusion reached by the BEPS Action 1 Report¹ that because *"The digital economy is increasingly becoming the economy itself, it would be difficult, if not impossible, to ring-fence the digital economy from the rest of the economy for tax purposes"*. The BEPS process involved long and

¹ Addressing the tax Challenges of the Digital Economy, OECD BEPS Action 1 Final Report , published October 5th 2015

detailed consultations with a broad spectrum of stakeholders, but none of the three options identified in the BEPS Report were recommended at that stage nor was a ring fencing the digital economy endorsed. This conclusion echoes the conclusion in the Report of the Commission Expert Group on Taxation of the Digital Economy² which found that *“There should not be a special tax regime for digital companies. Rather, the general rules should be applied or adapted so that ‘digital’ companies are treated in the same was as others”*. In addition, any proposed solutions targeted at the digital economy in isolation would violate the principle of neutrality espoused under the internationally agreed Ottawa Framework.

4 Timing of the proposals

Ideally, CFE believes the sensible approach is to allow the BEPS Project take effect and subsequently assess how problems which persist can be addressed in light of the new post-BEPS taxation framework. In practice we recognise the imperative that the certain larger EU Member States are under enormous political pressure to be seen to “be doing something” but we would strongly recommend that the EU not take unilateral steps to tax the digital economy but work within the OECD framework to build a clear international consensus on the best way forward. Not to do so would risk undermining all the consensus building that has surrounded the BEPS project itself.

It is simply too early to assess how the BEPS project has addressed the BEPS risks and the broader tax challenges raised by digitalisation. Great uncertainty still exists as to how new guidance, principles and practices espoused under the BEPS Action Plan will work in practice, be interpreted by tax authorities or ruled upon by the courts. It needs time to take effect, to assess its impacts, positive and negative. Imposing a whole new legislative framework, whilst jurisdictions are still in the process of implementing BEPS and the MLI will distort the BEPS process and may not achieve the intended aims as measures were prematurely adopted without proper consideration.

Significant changes have been made to the threshold for the creation of a PE in light of BEPS Action 7 – targeting mainly BEPS relating to commissionaire structures and the use of the preparatory and auxiliary exemption contained in Article 5(4) of the OECD Model Treaty. These changes affect the digital economy and the business models being operated. Time should be allowed to assess how effective these new rules will be. Similarly, great uncertainty exists over the profit allocation rules in light of the changes made by BEPS Action 7 and the interaction with BEPS Actions 8-10. Introducing new rules for

² Report of the Commission Expert Group on Taxation of the Digital Economy, published 28 /05/2014. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/gen_info/good_governance_matters/digital/report_digital_economy.pdf

the creation of a PE for digitalised companies and/or new methods for allocating profits to those PEs would lead to further confusion without having a clear view of how the changes under the BEPS project may have impacted the digital economy. In addition, it would violate the principle of neutrality.

More specifically, within the EU the Anti-Tax Avoidance Directives³ (“ATAD”) and the proposed amendments to ATAD pursuant to the second Anti-Tax Avoidance Directive⁴ (“ATAD 2”) have not yet been implemented in Member States, and will not be for a number of years⁵. Once again, the various provisions contained in the ATAD (e.g. CFC rules) could alleviate some of the issues experienced with effective taxation of the digital economy, and time should be allowed in order to assess the issues which prevail after implementation in Member States.

5 Adverse effect on competitiveness

It is important that any new taxes do not stifle the growth of the digital economy or discourage innovation within the EU. The EU must also focus its policy initiatives on the formulation of growth-orientated approaches, which exploit the opportunities of digitalisation for economic growth, particularly for start-ups and SMEs to flourish within the EU rather than focusing solely on taxing successful digital companies which have developed outside the EU.

6 Tax Certainty

In addition, any new tax which deviates from settled tax practice and the international tax framework will inevitably lead to great tax uncertainty for all stakeholders. Net income taxation within digital economy structures should be pursued to the maximum extent possible. Uncertainty will result in non-uniform application to entities and practices beyond the anticipated scope of the new laws. To mitigate this risk, any new legislation should be aligned, as much as possible with existing international practice and norms.

Double non-taxation is a problem, this is indisputable, equally indisputable is the problem of double taxation – and its negative effect on the world economy, consumers and taxpayers. It is extremely difficult to design a new tax that is not going to have unintended consequences and lead to double taxation. Any new tax must be designed in a manner to avoid double taxation, and must come within

³ Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

⁴ Council Directive amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries

⁵ ATAD provisions must be implemented in Member States before 1 January 2019, or 1 January 2020 in the case of exit taxes. The provisions of ATAD 2 must be implemented by 1 January 2020 or 1 January 2022 for reverse hybrid mismatches.

the ambit of double taxation treaties, otherwise the whole tax treaty system, which international taxation is built upon and tax treaty network will be completely undermined.

In the event that any new measures are implemented, it is vital that more robust dispute resolution measures are implemented as envisaged in Action 14 of the BEPS project. Access to effective dispute resolution mechanisms has been identified by all stakeholders as a significant problem for taxpayers. The addition of one of these new taxes will further exacerbate scarce resources to deal with disputes, increase waiting lists before appropriate fora and ultimately contribute to increased tax uncertainty.

Finally, taxpayers' rights must be safeguarded. Implementation of any new tax must be done in a manner to avoid uncertainty for taxpayers, ensuring that sufficient information is provided. New tax obligations should not be overly onerous on taxpayers and proper controls should be exercised over tax obligations (particularly in the context of a withholding tax).

7 Short-term solutions

CFE does not agree with a two-step approach. This concept is at variance with the conclusion reached by the BEPS Action 1 Final Report, which CFE agrees with, that the digital economy cannot be isolated from the economy as a whole.

It believes that short-term solutions will add huge tax uncertainty and create administrative burdens for business, and in particular, SMEs. In addition, given the time it takes to agree and implement new legislation (e.g. the ATAD originates from a 2015 BEPS Report but the earliest implementation will be 2019) long-term solutions could be identified and agreed within this time frame – negating the need for the so called stop gap “short-term” solutions by the time of implementation at Member State level.

As regards the four proposed short-term solutions in this section no comment can be made given the complete lack of detail provided on each of the proposals.

If the EU Commission concludes that it will propose a two-step approach, full details of the form the short-term solutions should be provided to the stakeholders.

8 Long-term solutions

8.1 General Comments

CFE believes that the EU should not act unilaterally in respect of proposing long-term solutions, but rather should operate within the framework of the OECD to reach agreement on an international level. Given the highly mobile and globalised business models operating within the digitalised economy it is not practical to have an EU solution alone.

Corporation tax is a direct tax rather than an indirect tax based on consumption. Corporation tax is a tax on the income of a company. The BEPS process focused on aligning this taxation with where the value is created. Many of the new long-term solutions proposed contradict this basic principle and focus instead on consumption – not value creation – completely undermining and contradicting the whole premise of the BEPS project.

If the EU wishes to raise more revenue from the digital economy it should focus on developing tax policies which encourage indigenous digital companies to operate within the EU and tax the income of those companies. Any new tax should be confined to only very large digital companies and should not affect start-ups or SMEs.

As with the short-term solutions above, the CFE cannot provide detailed comments on the five suggested long-term proposals given the absence of detail on salient aspects such as scope, definition, and mechanics of operating the proposals.

8.2 Specific Comments

“Digital presence in the EU”

It will be very difficult to select the extent a transaction must be “digital” and fall within the scope. It would be very important to clarify the relation between digital presence and significant economic presence. Every website, digital transaction and element of a digital transaction has at some point human involvement at a physical location. When deciding what transactions should be included within the scope equal consideration should be given to start-up companies and SMEs which also rely on digital platforms to carry out their business.

Further, it should be noted that any possible changes and increased administrative and compliance cross-border burdens will disproportionately affect the ability of smaller enterprises to carry out and expand their business domestically and cross-border. Similarly, the cost of double taxation will adversely affect SMEs far more than MNEs. In this context, at EU level new minimum thresholds are being introduced as part of the changes to the MOSS system to alleviate the compliance burden for small business providing online B2C e-commerce services across borders. Further simplification measures are also proposed to alleviate the burden on SME.

Defining or imposing a threshold under which a digital presence in the EU will be established will be problematic. Regardless of how it is measured or determined, once it is based on the concept of “significant economic presence” it will lead to a two-tier system of taxation with a complete divergence on the basic principles underlying that taxation of the digital economy and “traditional economy”. This will also violate the neutrality principle of the Ottawa Convention.

In relation to attributing value, emphasis purely on where goods are supplied to, deviates from the current OECD and international tax principles that value should be attributed to criteria such as where functions are performed, risks assumed and assets utilised.

CFE believes that the imposition of taxes based on something as vague and imprecise as a “digital presence in the EU” will result in double taxation. In the case that this option is pursued it is vital that the issue of double taxation is equally addressed.

Destination-based corporate tax & Unitary Tax

Proposed taxes such as a Destination-based corporate tax and unitary taxation are completely at variance with the concept of corporation tax and deviates completely from the underlying principle of the BEPS process that taxation should be based on where the value is created.

Residence tax base with destination tax rate

This proposal to define the applicable rate of tax based on the “*turnover-weighted average of the tax rates of the countries where the turnover is created*” will unduly encroach upon the sovereignty of Member States to set their own tax rate.