ICC Comments on EU consultation on fair taxation of the digital economy

ICC appreciates the opportunity to provide input on the European Union (EU) consultation regarding the fair taxation of the digital economy. ICC fully supports a harmonised approach to ensure that international tax rules remain relevant and applicable in an increasingly digitalised global economy. As digitalisation continues to increase in importance as a driver for global economic growth, it is imperative that any measures on the taxation of the digital economy be developed with the recognition that the digital economy is the economy so any changes will impact the entire corporate international tax system. Therefore, alignment with global efforts to address the challenges and opportunities the digital economy is essential.

The digital economy is not only revolutionising the way businesses operate but also creates new opportunities for global growth and prosperity. If nurtured appropriately, technological advances and digital connectivity can spur innovation in business models, business networking and knowledge transfer while also facilitating access to international markets for businesses of all sizes. Ensuring that the digital economy is taxed effectively and in a way that ensures fairness and supports growth is clearly high on the European Commission (EC) agenda. This commitment is evidenced by the Commission‟s recent communication to the European Parliament and Council on a Fair and Efficient Tax System in the European Union for the Digital Single Market. ICC respectfully acknowledges the commitment to establish a common EU approach on the taxation of the digital economy that would provide an efficient tax framework that stimulates economic growth and job creation in the region.

ICC reiterates, however, that a harmonised and collaborative global approach, together with the OECD and business, is highly recommended in order to fully grasp the challenges, implications, opportunities and solutions that the digital economy presents.

In this regard, ICC welcomes the EC public consultation on the fair taxation of the digital economy as an integral part of this process and is pleased to submit international business‟ views with respect to the taxation of the digitalised economy.

<u>A consistent and coherent global approach that fosters cross-border trade and investment</u>

ICC supports the OECD Base Erosion and Profit Shifting (BEPS) Action 1 Report conclusions 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 digital economy and its business models present however some key features which are potentially relevant from a tax perspective.*" As the digital economy is increasingly becoming the economy itself, goods and services, including digital services, have become intrinsically woven into the fabric of everyday international trade. As such, it would not be preferable or practical to consider measures targeted specifically at what is currently understood to be the „digital economy‟. It is ICC‟s view that a separate taxation system for digital companies could be fraught with challenges that would create uncertainty and negative consequences for economic growth and cross-border trade and investment. As all businesses become digitalised, these "targeted" measures would apply to all businesses and effectively become the basis for a new international business tax system. ICC welcomes the fact that the EC seems to have embraced this position as well.

For the ICC business community, the integrity of the international tax system is of critical importance - coherent and co-ordinated implementation of international guidelines is essential in establishing a consistent global tax system that better facilitates cross-border trade and economic growth. ICC notes that the EC appears to be advancing its efforts rapidly in an endeavour to address the growing tax challenges that the digital economy presents. ICC strongly recommends, however, that any measures being considered by the EC be aligned with the international OECD tax framework to ensure a consistency and coherence that would go a long way in assuring a level international playing field for business as well as co-ordinated implementation at global level. International tax co-operation, as opposed to EU-wide action or counter-productive unilateral action, is essential to ensure that any tax reforms should be both practicable and effective. It would, in the view of ICC, be the only way to effectively deal with the issue of fair taxation in the digitalised economy, while not increasing the compliance burden and risk of double taxation for businesses, as well as to foster cross-border trade and investment and economic growth.

Short term actions vs. long-term solutions

In view of the perceived urgency to find practicable solutions to fairly tax the digitalised economy, ICC respectfully urges the EC to carefully consider the broader implications of implementing targeted temporary actions in favour of long-term comprehensive solutions.

Of particular concern are the EC‟s proposals to, in the short term, develop a turnover based tax, where businesses would be taxed based on revenue as opposed to profits, which would not only negate generally accepted principles of taxing corporate profits (where value is created in excess of costs) but could also have a negative impact on solvency or investment opportunities for business. A unilateral levy would be a cost to business, require separate administrative intervention and compliance and make the taxation system more onerous. In addition, there is a risk of double taxation if one country imposes a turnover-based tax, such as an equalisation levy, which is outside the framework of double tax agreements. Furthermore, a turnover-based tax would create cost-based barriers to entry, undoubtedly penalising European start-ups and stifling innovation. This in turn would have a knock-on effect on jobs and growth. Tax costs would likely be recovered from consumers in larger markets and prevent entry into smaller markets. Adopting an equalisation levy would also adversely affect EU competitiveness and risk economic growth in the region.

The same concerns can be voiced with respect to some other short term options proposed by the EC, such as a withholding tax on digital transactions. Such a withholding tax would conflict with double taxation treaties‟ general principle under which business profits shall only be taxable in the State where the provider of the service is located.

ICC believes in long-term comprehensive solutions and in the importance of staying true to the basic principles of taxation because, as business becomes increasingly digitalised, these solutions will apply to the entire economy. Inventing an entire new system could lead to greater disruption than making significant changes to an existing system – implementing the BEPS action items are expected to address most of the perceived challenges of the digitalised economy. Great disruption would be counter-productive for all stakeholders including businesses, governments and consumers. ICC underscores the need to ensure that profits are taxed where true economic activity and value is created, as determined within the OECD BEPS recommendations.

The rapid evolution of digitalisation has permeated many spectrums of life, including the way that businesses operate today. However, to a large degree, these changes provide alternative means to completing commercial transactions which were traditionally undertaken physically. These activities do not simply create a presence that could lead to taxation in a country where the user or buyer would be located, but rather a significant presence in the location of product and service development and cloud computing infrastructure. ICC feels that a different means of achieving the same result should neither alter the conclusion on taxable presence, nor the characterisation of income. This aspect is an important consideration, given that the basic principle of taxation rests on the fact that activities give rise to incomes and such incomes should be taxable in the jurisdiction in which the activities are undertaken. Traditional taxation mechanics are applicable for the digitalised economy insofar as these require appropriate value to be allocated to these functions, which can be achieved through an improved and simplified application of the transfer pricing provisions.

It is clear that further discussion, currently on-going at the OECD, is required with respect to the definition of permanent establishment (PE) and, most importantly, around profit allocation. A „digital presence‟ (DP) concept, for instance, is a fundamental change to the existing permanent establishment framework and, as the digital economy is increasingly becoming the economy itself, would represent a significant change in taxation for all businesses. ICC holds the view that it should only be considered in connection with a broad and general review of the PE concept, including appropriate rules for attributing profit to the resulting PEs. The risk of double taxation and various interpretations is likely to increase tax uncertainty and must be adequately assessed and evaluated. Administrative simplification for PE reporting and tax payments will be critically important to minimise disruption for business. ICC believes that the on-going work at the OECD, with the active participation of the EU members and the European Commission, will accommodate solutions to this issue.

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The digitalisation of the economy raises challenging issues. A rush to address those issues could result in a large part of the economy, and eventually the entire economy, being subject to unilateral actions and consequently increased compliance and risk of double taxation. ICC remains concerned at the growing trend internationally to envisage taxation of foreign businesses and underlines the urgent need for countries to collectively discuss and resolve this issue through mutual consensus, as opposed to unilateral actions. ICC reiterates that any solutions should be long-term and should have broad adoption by countries to allow for a seamless application for business.

ICC finally notes that there is insufficient understanding of the incidence of direct and indirect taxes and believes that this would be worth researching further as work on the taxation of the digital economy progresses. ICC offers its knowledge and experience to assist in presenting business views on further issues in this area.

Commission on TAXATION

The International Chamber of Commerce (ICC)
Commission on Taxation

ICC is the world business organization, whose mission is to promote open trade and investment and help business meet the challenges and opportunities of an increasingly integrated world economy.

Founded in 1919, and with interests spanning every sector of private enterprise, ICC"s global network comprises over 6 million companies, chambers of commerce and business associations in more than 130 countries. ICC members work through national committees in their countries to address business concerns and convey ICC views to their respective governments.

The fundamental mission of ICC is to promote open international trade and investment and help business meet the challenges and opportunities of globalization. ICC conveys international business views and priorities through active engagement with the United Nations, the World Trade Organization, the Organisation for Economic Co-Operation and Development (OECD), the G20 and other intergovernmental forums.

The ICC Commission on Taxation promotes transparent and non-discriminatory treatment of foreign investment and earnings that eliminates tax obstacles to cross-border trade and investment. The Commission is composed of more than 150 tax experts from companies and business associations in approximately 40 countries from different regions of the world and all economic sectors. It analyses developments in international fiscal policy and legislation and puts forward business views on government and intergovernmental projects affecting taxation. Observers include representatives of the International Fiscal Association (IFA), International Bar Association (IBA), Business and Industry Advisory Committee to the OECD (BIAC), Business Europe and the United Nations Committee of Experts on International Cooperation in Tax Matters.