

The Relations Between the Tax Authorities and Non-established VAT Taxpayers in 2020. Are We Using 20th Century Rules for a 21st Century Digital World?

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The digital economy in the 21st century

New business models associated to the so-called digital economy are blossoming in all type of economic activities all over the globe. Among many other examples of increasingly digitalized business we can find online goods sellers, streaming television services, remote PC repairs, food delivery, accommodation or transport services ordered through a digital platform, online/apps gaming, etc.

Digital platforms have become a major source for customers to easily and quickly gain access to many types of supplies of goods and services, most of them subject to taxation in VAT/GST in the country where the consumption is made.

The possibilities of modern Information Technologies in many cases allow the digital platform to provide and/or facilitate the underlying supply with very limited physical presence in the country of consumption or with no presence at all.

At the same time, this blooming of the digital economy business models is competing with domestic "traditional" sellers or service suppliers.

To preserve fair competition amongst more digitalised and less digitalised business models, governments must assure that the applicable tax rules and obligations for economic activities are the same regardless of where the supplier is established.

To preserve a level playing field is not only a matter of the taxes to pay, but also of fulfilling administrative regulations in areas such as public security, health and food regulations measures, security of passengers transport, financial market regulations, etc.

Digital economy, non-established business and VAT/GST

As for the specific issues of taxation in the digital business models, hot discussions are going on worldwide about where the profits of a company with a highly-digitalised business should be subject to corporate taxation.^[1]

In the case of consumption taxes (VAT/GST), generally speaking, taxation rights for business to consumer transactions (B2C) will be allocated to the jurisdiction where the actual consumption takes place.^[2] In the digital economy, where many goods or service suppliers are not established in the country of consumption, the traditional way of relation between the Tax Authorities and the established taxpayers may not work properly, for a number of reasons:

- The taxpayer may not be aware of the very existence of a tax obligation to pay VAT/GST or to provide information to the Tax Authorities. For digital business established in a single one or in a few countries but providing supplies of goods and/or services in multiple jurisdictions, the taxpayer could not be familiar with the domestic tax rules of each and every jurisdiction where their activity is carried out. Even when the non-established taxpayer has some indications that he is subject to VAT/GST obligations in a certain jurisdiction, he may face difficulties in understanding the VAT/GST rules (tax returns periods, VAT rates, exemptions, etc.) in foreign languages.
- The different domestic means to fulfil VAT/GST obligations (electronic formats, invoicing, record keeping obligation, information provision to the Tax Authorities, etc.) may notably vary from one country to another, making voluntary compliance a complex task.
- The Tax Authorities may face difficulties to contact the non-established taxpayer. Even something as simple as sending a communication or an email to the taxpayer to the accurate address may be challenging for the Tax Authorities. Requests of information may be also sent to the wrong address or to the wrong persons, as the Tax Authorities may not be aware of who the legal representative is or where the legal address of the company is located.
- In the case of non-compliance with the VAT/GST domestic rules, either with the obligation to pay the VAT/GST or with a reporting obligation, it is not easy for the domestic Tax Authorities to enforce the VAT/GST law, as the taxpayer is not established in its jurisdiction.

The relation between Tax Authorities and non-established taxpayers through administrative cooperation tools

In a "traditional" international tax framework, as it was designed in the 20th century, the relations of the Tax Authorities and non-established taxpayers subject to VAT/GST obligations in the absence of a fiscal representative in the jurisdiction of consumption were channelled through international administrative cooperation between the Tax Authorities.

Under this traditional relation framework, the Tax Authorities of the country of consumption should request in principle the cooperation of the Tax Authorities where the taxpayer is established to send a request of information, to carry out tax control procedures or to recover unpaid tax debts.

To request the international administrative cooperation an agreement providing the commitment of both Tax Authorities to cooperate must be in place between the concerned jurisdictions. In the case of administrative cooperation for VAT/GST purposes, the typical International cooperation tools are the Convention on Mutual Administrative Assistance in Tax Matters^[3], where currently 137 worldwide jurisdictions are participating, the bilateral double taxation agreements including administrative cooperation, and the Tax information exchange agreements (TIEAs).^[4]

However, the quick evolution of the digital economy business models in the 21st century reveals that the traditional way of contact and relations between the Tax Authorities and the non-established taxpayers for VAT/GST purposes is not efficient enough in some cases, due to a number of reasons:

- The request of administrative cooperation based on international agreements is highly focused on direct taxes, such as personal income tax or corporate taxation. In fact, the OECD bilateral model convention for tax matters typically covers direct taxes on income and capital rather than consumption taxes. Thus, the capacity to exchange of information for other types of taxes, such as VAT/GST, will depend on the wording of Article 26 of the specific Bilateral Tax convention.
- To grant administrative cooperation, a foreseeable relevance of the requested information is generally demanded. Fishing expeditions - this is to say - the request of bulk data with no foreseeable relevance for tax purposes may be rejected by the requested Tax Authority. In the case of digital business models run by non-established companies in the shape of thousands of supplies (software/apps downloads, access to digital content in streaming, intermediation fees, etc.) of little value in individual terms, a request of administrative cooperation where there is no immediate and clear indication of a tax shortfall may be rejected as "fishing".
- The time to obtain the requested administrative cooperation will depend on the requested Authority's capacity to handle the request. In many cases, it could take longer than what it is reasonable to react to tax shortfalls (and distortions of competition due to tax reasons) in an efficient way. In some cases, the time needed to obtain administrative cooperation to react to non-established companies' VAT/GST infringements may have damaged fair domestic competition to the extent that some honest domestic businesses have been expelled from the market.
- The requested non-established taxpayer may invoke different legal exceptions to cooperate with the Tax Authorities compared with the legal framework where the consumption is to be taxed, for instance in terms of data protection rules. This will create an additional element to distort competition detrimental to established taxpayers.

This dichotomy between global business models and domestic VAT/GST rules is a real mess, as at the time of writing in 2020, both for taxpayers willing to comply with VAT/GST rules in all the jurisdictions where their business is carried out and to the Tax Authorities trying to preserve not only tax revenues but also a level playing field for all economic activities regardless of where the business is established.

The challenges of the 21st century digital economy world deserve solutions of the 21st century, even for the means of interaction between Tax Authorities and taxpayers.

Some of the ideas for improving the relations between the domestic Tax Authorities and the non-established taxpayers and to preserve a level playing field for all competing business models in the digital economy are:

- To facilitate as much as possible voluntary VAT/GST compliance to non-established taxpayers using IT tools. Websites easy to access and to use, simplified registration systems, electronically filed tax returns, website information available in foreign languages, remote means of contact, fluent electronic channels for taxpayer assistance, etc., will ease VAT/GST compliance to non-established taxpayers willing to do so.
- To improve international administrative cooperation in VAT/GST matters. The current international tools should be improved, making sure they cover cooperation for consumption taxes and shortening the time to respond to the cooperation requests. The traditional requirement of foreseeable relevance and the differences in data protection regulations may deserve a revision in the 2020 economic environment.
- To initiate direct contact between Tax Authorities and non-established VAT/GST payers. Where there is no administrative cooperation tools in place between the jurisdiction of consumption and the jurisdiction of establishment or where the existing ones are not working fluently, a direct contact between the Tax Authorities and the non-established taxpayer must be used. Through this direct contact, the Tax Authority could send to the taxpayer requests of information and perform remote tax controls, while the taxpayer could send to the Tax Authorities questions about the domestic legal framework and its interpretation and request of them a written and binding answer. A mutual consent for these bilateral direct contacts may be required by the Tax Authorities and the taxpayer.
- To develop mechanisms to enforce VAT/GST rules. If the non-established taxpayer is not willing to comply with the VAT/GST rules of the jurisdiction where the tax is due, the Tax Authorities must impose monetary penalties, but it is likely that to enforce penalty collection they need to request international administrative cooperation. A second tool to enforce domestic VAT/GST rules would be to make public the identity of non-established taxpayers who are reluctant to comply. Thus, potential consumers and the civil society in general would be aware of the company's non-compliance. For the most serious cases of VAT/GST fraud or deliberate non-compliance, extreme reactions may be applied, such as prohibiting the economic activities of that company in the country^[5] or seizing any asset or money the company could have in the country, even forcing the payment services intermediaries to seize any money transfer to the identified company.

[1] See the discussion at the OECD about the Pillar I and Pillar II, and the different domestic approaches on taxing the digital services.

[2] OECD *International VAT / GST Guidelines* (OECD Publishing, Paris, 2017)

[3]
<https://www.oecd.org/tax/exchange-of-tax-information/convention-on-mutual-administrative-assistance-in-tax-matters.htm>

[4]
<https://www.oecd.org/tax/exchange-of-tax-information/taxinformationexchangeagreements.htm#:~:text=The%20purpose%20of%20this%20Agreement,to%20address%20harmful%20tax%20practices.>

[5] The Mexican Authorities have announced recently that they are considering to block apps/websites of companies non-compliant with domestic tax rules