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Digital Economy Taxation Developments: A Marker for the Future of Taxes (Part 1)

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The digitization and globalization of the economy have created a challenging environment to enforce tax rules and ensure tax compliance. Ever since the OECD's release of the Action Plan on Base Erosion and Profit Shifting (BEPS)[1], the taxation of the digital economy has been under scrutiny from both a direct and indirect tax perspective. The rules and regulations that apply to the digital economy sector are changing rapidly and many more initiatives are expected to be proposed and implemented in the years to come. The common denominator between new regulations that will soon enter into force, such as the amended VAT rules for e-commerce transactions and DAC7, is that platforms will more-and-more be confronted with tax liabilities as well as record-keeping and data-sharing obligations. Based on the important role that platforms fulfil in generating, facilitating and executing online sales, this trend was also signalled in the OECD's work on the effectiveness of VAT / GST collection in the digital economy[2] and the European Commission's Action Plan for Fair and Simple Taxation.[3] The broad scope of these newly adopted tax liabilities and data-sharing obligations has created uncertainty in the market and (fiscal) pressure on the business model of platform operators. The impact on parties that use the platform to carry out transactions must also not be underestimated.

In our blog, we will discuss this digital economy tax trend of increased platform involvement in the levy of direct and indirect taxes.

Platform-centred levy of taxes

VAT liability

From 1 July 2021, taxable persons 'facilitating' supplies of goods to EU non-taxable persons through the use of an electronic interface will be deemed to purchase and on-sell these goods. The platform will effectively become liable for the collection and remittance of VAT due on these sales. This VAT liability will apply to (1) distance sales of imported goods with an intrinsic value of less than EUR 150 and (2) sales of goods by non-EU taxable persons. Services are not (yet) covered under this liability.

In order to qualify as a deemed-seller, the platform must be 'facilitating'; i.e. connect a customer with a supplier offering goods for sale through the electronic interface, which results in a supply of those goods.[4] Generally, for e-commerce transactions this is reflected in the actual ordering and

the checkout process being carried out by or with the help of the electronic interface.[5] The facilitator definition is open and formulated broad.

Based on the above, we think the platform must fulfill two activities in order for it to 'facilitate'. First, the platform must be both consumer- and seller-facing. This means that, in our view, technical infrastructure and back-office service suppliers will in principle not be covered by this liability. Second, the platform must fulfill a linking / connecting activity, which results in a supply of goods.

The new VAT regulation will also include an 'escape' provision to the facilitator definition. A taxable person will in all cases not be considered to 'facilitate' if it does not (in)directly set the terms and conditions of the supply, is not (in)directly involved in authorising the payment charge to the customer and is not (in)directly involved in the ordering or delivery of the goods.

What is interesting about this is that some companies that do not meet the two basic characteristics of the facilitator definition simultaneously do not meet the conditions of the escape provision. This seems contradicting. For example, technological infrastructure and back-office service providers will in our view not be considered to 'facilitate', but they are generally involved in the payment processing and/or ordering of goods. Technically they would therefore not meet the escape criteria. The facilitator definition and the escape provision do not seem to align very well with each other.

Further, the VAT liability will also not apply to a taxable person that provides any of the following activities without any further intervention in the supply; payment processing services, listing or advertising of goods or redirecting customers to other electronic interfaces where the goods are offered for sale.

We note that the UK will adopt similar rules as of 1 January 2021. However, there is one relevant difference that we would like to stress. Based on current HMRC guidance, the UK platform liability will only apply to online marketplaces that set the terms and conditions of the supply, are involved in authorising or facilitating customers' payments and are involved in the ordering or delivery of the goods.[6] These are cumulative requirements. Basically, the escape provision under the EU platform definition will be the constitutive requirement under the UK platform definition. In our view, it would be desirable if the EU would adopt a similar definition because the UK definition aligns better with the basic characteristics of platform models.

Joint-and-several liabilities

The EU VAT directive also offers Member States the possibility to hold other persons than the taxable person jointly and severally liable for the payment of VAT.[7] The UK was the first state to use this option and implemented joint-and-several liability rules in 2016. Since then the number of states adopting similar rules has been growing. At this moment Austria, Germany, France, Italy and the UK apply joint-and-several liabilities for VAT due by platform sellers and record-keeping obligations for platforms that generally cover a broader range of transactions than the deemed supplier provision.

It can be argued that these joint-and-several liabilities are not in all cases proportional. For example, the European Commission already sent a letter of formal notice to Germany in relation to its national platform liability stating that the measure is inefficient and disproportionate and hinders the free access of EU businesses to the German market in violation of EU law.[8]

Some of these unilateral VAT liabilities also capture B2B- and C2C-supplies and in some cases also import VAT, whereas the deemed supplier provision only relates to B2C-supplies[9]. Generally, there are two options in which a platform can be waived from these joint-and-several VAT liabilities; either by actively demonstrating that the sellers are compliant (collecting and sharing VAT identification numbers with the tax authority) or by indefinitely banning incompliant sellers from the platform.

What we notice in practice is that these VAT liabilities have created market uncertainty which has forced platforms to change their business model and to make sure to educate, facilitate and enforce tax compliance of platform sellers. Another interesting development is that these VAT liabilities are often extended to B2B and C2C transactions, thus creating a multitude of national platform liability rules that platforms should adhere by.

Customs Action Plan

A possible next step in the future could be that platforms will also become liable for customs duties. Recently, the Council of the European Union approved the cornerstones of the Customs Action, in which the Council encourages the European Commission to further examine the use of VAT collected data for customs purposes.[10]

More reporting obligations

DAC7

New tax transparency measures will be imposed in the form of DAC7, which will amend Directive 2011/16/EU on administrative cooperation in the field of taxation.[11] DAC7 will impose a data-sharing obligation on (EU and non-EU) platforms to report the turnover realized by sellers of goods and services through the platform. DAC7 is further aimed at preventing income tax and VAT shortfalls. To achieve this result, the scope of Directive 2011/16/EU will be broadened to also capture VAT and other indirect taxes.[12]

Reportable activities will include (1) the rental of immovable property, (2) the provision of personal services, (3) the sale of goods, (4) the rental of means of transport and (5) investment and lending in the context of crowdfunding. The reporting obligations also apply in purely domestic situations. Hence, it could be challenged whether prevention of income tax shortfalls in purely domestic situations has sufficient legal basis for harmonization on EU level.

Under DAC7, the concept of a ‘platform’ is defined as “any software, including a website or a part thereof and applications, including mobile applications, accessible by users and allowing Sellers to be connected to other users for purpose of carrying out a Relevant Activity, directly or indirectly, to such users”. In our view, this definition does not significantly differ from the EU VAT definition due to the emphasis on connecting sellers and users through a digital interface. Similarly, platforms will not be subject to DAC7 if they only allow processing of payments in relation to Reportable Activity, list or advertise a Reportable Activity or redirect users to a Platform.[13]

A relevant question is whether an overlap exists between the information that a tax authority will receive under DAC7 and the VAT e-commerce Directive. Although the goal of both regulations is the same, how the information is submitted differs. DAC7 relates to the yearly income realized by the platform seller, whereas platforms will be confronted with a 10-year record-keeping obligation at transactional level under the VAT e-commerce Directive.

DAC8

The emergence of alternative means of payment and investment, such as crypto-assets and e-money, threaten to undermine the progress made on tax transparency. Because of this, the European Commission issued a roadmap on a proposal amending Directive 2011/16/EU to include crypto-assets and e-money (DAC8) at the end of last year.[14] Public consultation is planned for the first quarter of 2021 and adoption by the Commission is currently expected in the third quarter of 2021.

Payment service providers

In order to cross-check the VAT information declared by distance sellers, platforms and other online marketplaces, the European Commission also adopted record-keeping obligations for payment service providers (PSPs), such as credit institutions, e-money institutions and other payment institutions.[15] In summary, EU based PSPs should keep record of payment information relating to cross-border e-commerce transactions, such as details of the payee, the location of the payer, and the payment transaction itself. This information will be aggregated per payee for each EU Member State. PSPs will need to store this information in the Central Electronic System of Payment Information (CESOP), which will be available to all EU Member States. Based on the information made available through CESOP, the Member States should be able to verify whether the remote seller or platform has fulfilled its VAT obligations. These regulations will enter into force on 1 January 2024. At this stage PSPs are not confronted with similar tax liabilities like platforms.

Where are we headed?

As shown in our blog, the levy of taxes is becoming increasingly platform centered. If the 2021 deemed supplier rules or the local joint-and-several liability rules prove successful in closing the VAT-gap, considering also the increasing number of countries adopting joint-and-several liability of platforms, it should be expected that the liability of platforms will be increased further to cover more activities and other taxes as well.

Also, we notice that more reporting obligations are imposed on companies that possess information that is valuable for tax authorities, like platforms and PSPs. If the measures applied to platforms are successful, it would only be a small step to apply similar obligations and liabilities to other parties where tax-relevant information is concentrated. This would entail a significant change of traditional taxation models applied, as tax authorities would become dependent on a few very large parties. This could also create a risk of tax authorities becoming (too) dependent on a select number of large parties for securing tax revenues.

In part 2 of this blog, we will focus on another tax trend: the shift of taxation rights between jurisdictions.

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[1] OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing. http://dx.doi.org/10.1787/9789264202719-en.

[2] OECD (2019), The Role of Digital Platforms in the Collection of VAT/GST on Online Sales, OECD, Paris. www.oecd.org/tax/consumption/the-role-of-digital-platforms-in-the-collection-of-vat-gst-on-online-sales.pdf

[3] European Commission, AN ACTION PLAN FOR FAIR AND SIMPLE TAXATION SUPPORTING THE RECOVERY STRATEGY, COM(2020) 312 final.

[4] Article 5b of COUNCIL IMPLEMENTING REGULATION (EU) 2019/2026 of 21 November 2019 amending Implementing Regulation (EU) No 282/2011 as regards supplies of goods or services facilitated by electronic interfaces and the special schemes for taxable persons supplying services to non-taxable persons, making distance sales of goods and certain domestic supplies of goods.

[5] European Commission, Explanatory Notes on VAT e-commerce Rules, paragraph 2.1.6.

[6] HMRC, Policy Paper Changes to VAT treatment of overseas goods sold to customers from 1 Janaury 2021, updated 3 december 2020, Changes to VAT treatment of overseas goods sold to customers from 1 January 2021 – GOV.UK (www.gov.uk).

[7] Article 205 COUNCIL DIRECTIVE 2006/112/EC of 28 November 2006 on the common system of value added tax.

[8] European Commission, October 2019 Infringement Package: key decisions, October infringements package: key decisions (europa.eu).

[9] In this context, B2C also includes transactions to non-taxable persons.

[10] Council of the European Union, Council Conclusions regarding Taking the Customs Union to the Next Level: a Plan for Action, approved through a written procedure completed on 18 December 2020.

[11] European Commission, Proposal for a COUNCIL DIRECTIVE amending Directive 2011/16/EU on administrative cooperation in the field of taxation, COM(2020) 314 final.

[12] By amending article 16 of Directive 2011/16/EU on administrative cooperation in the field of taxation.

[13] Annex 5, Section I(A)(1) of the DAC7 proposal.

[14] Inception Impact Assessment, Proposal for a Council Directive amending Directive 2011/16/EU as regards measures to strengthen existing rules and expand the exchange of information framework in the field of taxation to include crypto-assets and e-money, Ref. Ares(2020)7030524 – 23/11/2020.

[15] European Commission. Proposal for a COUNCIL REGULATION amending Regulation (EU) No 904/2010 as regards measures to strengthen administrative cooperation in order to combat VAT fraud, COM(2018) 813 final.

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