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Business Principles for Addressing the Tax Challenges of the Digitalizing Economy

January 2019
Paris, France

The digital revolution is transforming economies, business models, and the lives of billions of citizens. It is dramatically impacting every aspect of economies including the tax base and governments' ability to raise revenues.

At the international level, the OECD/G20 project on Base Erosion and Profit Shifting (BEPS) remains at the forefront of tax policy discussions. As the digital transformation impacts economies as a whole, the BEPS project has recognized that it would be difficult, if not impossible, to ring-fence the digital economy from the rest of the economy for tax purposes. Furthermore, the project has emphasized that while some digital business models can exacerbate BEPS concerns, digitalization itself presents no unique BEPS issues.[1]

We welcome the OECD Task Force on the Digital Economy's March 2018 Interim Report, and the opportunity that this project has provided Inclusive Framework (IF) countries, with input from relevant stakeholders, to contribute to addressing these challenges together. By 2020 we expect the OECD to publish a final report reflecting the outcome of the continued work in relation to taxation of the digitalized economy.

Set out below are a set of 11 policy recommendations we believe should be considered when developing modifications to the underlying international taxation norms to update them for the modern economy.

These principles will help ensure that any reforms to existing tax principles are coherent, pro-growth, and do not inhibit the innovation and digitalization that is transforming our world.

The reforms should:

1. **Be based on long-standing and well-founded underlying principles of international taxation**
   The long-standing and well-founded underlying principles of international taxation including taxation of net income, nexus, permanent establishment, and transfer pricing based on the arm's length standard should remain, and any changes should be to improve these underlying principles. The revised framework should be applicable to all digitalizing businesses and be flexible to accommodate future business model evolution.

2. **Not ring-fence the digital economy**
   The "digital economy" cannot be ring-fenced and attempts to do so will simply be distortive and harmful to the digitalization of the whole economy. The economy is now the digital economy. Changes to underlying international tax rules should be principle based and flexible for further changes to the economy that we cannot predict today.

3. **Respect the Ottawa Taxation Framework principles**
   In 1998 the OECD developed the principles for the Ottawa Taxation Framework for the then-emerging technology sector. The principles of neutrality, efficiency, certainty, simplicity, effectiveness, fairness and flexibility are well founded. Further we support the principles of proportionality and sustainability recommended in the OECD BEPS Action 1 Report. These remain core principles to be adhered to.

4. **Be grounded in the concept of value creation**
   During and since the BEPS Project, international tax policy has sought to align taxing rights with the location of value creating activities undertaken by enterprises. We support this approach, and where activities undertaken by enterprises that create value are identified as not being currently reflected in the international framework, we support amendments to ensure that they are. However, this examination must be undertaken within and against the existing (i.e., non-digital) principles of value creation to ensure that all value creating activities undertaken by enterprises are rewarded appropriately and proportionately.

5. **Reduce instances of double taxation**
   Agreement over the allocation of taxing rights should ensure that profits are allocated in a consistent and clear way to reduce the potential instances of double taxation. This principle aligns with a key objective of the BEPS initiatives.

[1] OECD/G20 Base Erosion and Profit Shifting Project, Addressing the Tax Challenges of the Digital Economy, Action 1: 2015 Final Report.

6. **Be introduced as a comprehensive package**
   The issues of nexus and attribution must be dealt with simultaneously, and recommendations on both made together to ensure coherency and certainty.

7. **Be reflected in model treaties and commentary**
   Uniform model treaties with comprehensive commentary that reflect transactions, in today's and tomorrow's world, are imperative. Domestic rules should be discouraged before relevant treaties have been amended.

8. **Provide tax certainty for taxpayers and tax administrations, including strong dispute resolution mechanisms**
   As important as reducing double taxation is the inclusion of mechanisms that will eliminate instances that do occur. Any changes to the international tax rules increase the potential for double taxation, so *Business at OECD* supports arbitration mechanisms and further strengthening of Mutual Agreement Procedures (and other initiatives such as ICAP).

9. **Have global agreement**
   We understand the urgency with which many governments wish to address their concerns and agree that a realistic balance must be struck between the required timeframe for action and comprehensive engagement.

   We strongly counsel against fragmentation in international taxation and encourage all countries to avoid action outside of an IF-led consensus, particularly within the already agreed international timeframe of reaching consensus by 2020. The reforms must be affirmatively agreed by all IF member countries. The OECD is the only organization that garners such global support, and an agreement should reflect and balance the concerns of all nations – large and small, developed and developing, importers and exporters.

10. **Minimize the administrative burden on taxpayers and tax administrations**
    The permanent establishment thresholds provided a clear line in the industrial age to ensure that administrative burdens on taxpayers and tax administrations were only incurred where the tax due was likely to be substantial. Such clear lines are an essential part of any threshold. Where a taxable presence does exist, coordination between tax administrations and aligned simplified compliance rules are welcomed.

11. **Be developed through inclusive consultation with all businesses and other stakeholders**
    The best and most coherent solutions will be found if the conversation is broadened beyond the taxation of a small number of perceived "digital" businesses to include more stakeholders with different experiences and ideas.

    Businesses themselves have been at the forefront of driving digitalization – and businesses across all sectors are increasingly seeing new ways in which digitalization can add value for their stakeholders. They are harnessing digital technology to create value first hand, and they have the best insight as to how, where and why this happens, how that changes over a business lifecycle, and how future developments could impact this analysis.

    It is critical to fully engage business in the sustained conversation to more fully review current and future business models to determine the means and location of value creation, and thereby to address concerns in a forward-looking, coherent, global agreement. *Business at OECD* continues to stand ready to work constructively to help reach a true multilateral agreement that establishes a new, pro-growth tax framework that meets the needs of **all** stakeholders.

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