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PLATFORM FOR TAX GOOD GOVERNANCE

LONG-TERM SOLUTIONS TO THE TAXATION OF THE DIGITAL ECONOMY

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Overview (as set out in the Communication)

One solution is to embed the taxation of the digital economy in the general international corporate tax framework. Fundamental reform of the international corporate tax framework currently applicable to the digital economy would ensure the consistency and coherence of tax rules worldwide, and ensure stability and certainty for businesses. The EU expects a high level of ambition as regards the interim report on the taxation of the digital economy that the OECD will present to the G20. It is essential that the report comes forward with meaningful policy options to address the issues at stake.

In particular, new international rules specific to the challenges raised by digital economy are needed to determine where the value of businesses is created and how it should be attributed for tax purposes. This would entail reform of international tax rules on permanent establishment, transfer pricing and profit attribution applicable to digital technologies.

The **permanent establishment rules** are used to determine the threshold of activity that needs to be carried out in a country in order for a business to be taxable in that country, and are largely based on physical presence. However, thanks to digital technologies, businesses are now able to have a significant economic presence in a market jurisdiction without necessarily having a substantial physical presence. Alternative indicators for significant economic presence are therefore required in order to establish and protect taxing rights in relation to the new digitalised business models.

Once the business is taxable in the country, the profits generated by this business still need to be determined and allocated to this country. The **transfer pricing rules** are used to attribute the profit of multinational groups to the different countries based on an analysis of the functions, assets and risks within the value chain of the group. However, these rules were developed for traditional business models and economic environment. The digital economy relies heavily on intangible assets, which are becoming more and more the value drivers within multinational groups and which are difficult to value. The challenge of identifying and valuing intangible assets as well as determining their contribution to value creation requires alternative methods for attributing profit that better capture value creation in the new business models, which should therefore be considered alongside changes to the permanent establishment rules. Furthermore, as profits can be shifted across countries through misuse of permanent establishment and transfer pricing rules, anti-abuse rules could be considered to enforce compliance and ensure that profits earned in the EU are taxed in the EU.

At EU level, the Common Consolidated Corporate Tax Base proposal offers a basis to address these key challenges. The Commission continues to believe that the CCCTB provides an EU framework for revised permanent establishment rules and for allocating the profit of large multinational groups using the formula apportionment approach based on assets, labour and sales that should better reflect where the value is created. There is scope within the current CCCTB proposal to examine further enhancements to ensure that it effectively captures digital activities. Discussions are already underway on this in the Council under the Estonian Presidency and in the European Parliament. The Commission stands ready to work with Member States in examining these options within the ongoing CCCTB negotiations, to find an ambitious and EU-law compatible approach for the Single Market.

Questions

Platform members are asked to consider the following questions:

- How should a business's "digital presence" be measured and determined?
- How could meaningful income be attributed to the "digital presence"?
- What companies / transactions should be included within scope?