

# Taxation of the digital economy and development

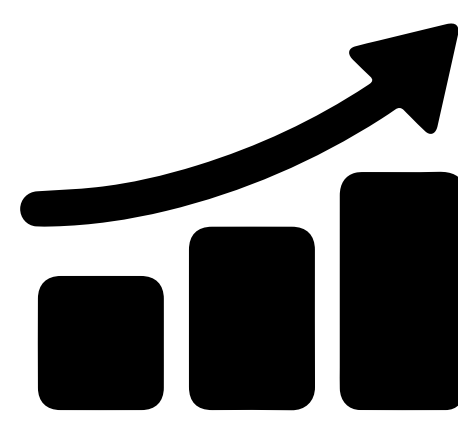
A critical assessment of Art. 12B UN-MTC

## The baseline: Where do we depart from?

### Status quo: PE

Nexus and profit allocation rules in international tax law rely on physical criteria. The PE concept is adapted to the economic reality of brick-and-mortar business models.

8x



from 110.46 billion in 2003 to 891.69 billion in 2021

ICT service exports

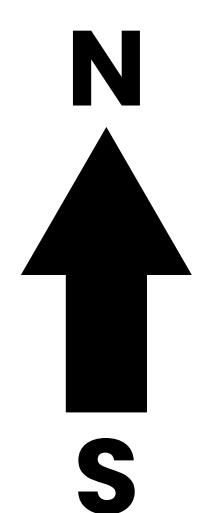
### New Economy

- Decreasing relevance of a physical presence
- Increasing reliance on intangible assets
- Change of the value creation chains: Reliance on data, user participation and network effects

Developing countries are typically market states.



Global ICT service exports



Data flows

## Tax challenges

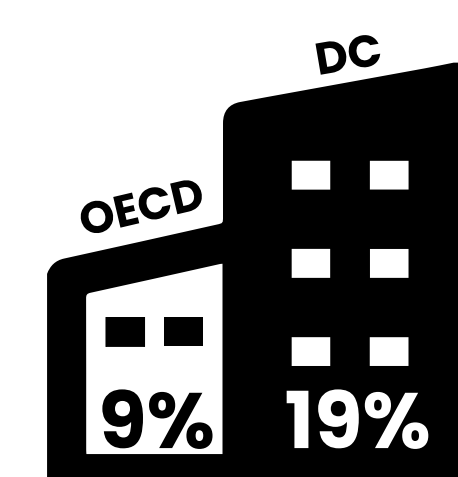
- Existing tax (nexus) rules and principles outdated
- Increased BEPS risks
- Shift of tax revenue away from market states

Developing countries face structural challenges exacerbating BEPS risks.

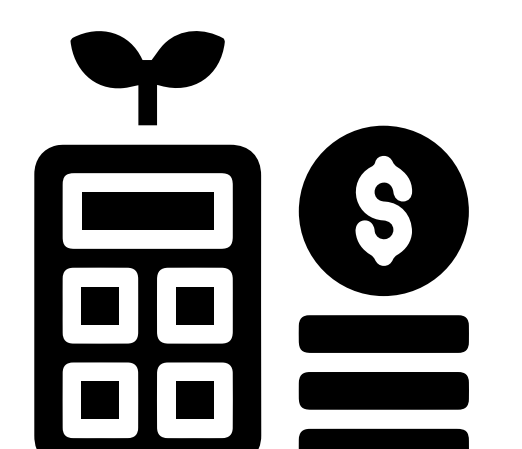
Reform debate is primarily framed by fiscal and economic interests of developed countries.



Inclusive (?) Framework on BEPS



Reliance on CIT revenue



Lack of administrative resources

## The solution: Art. 12B UN-MTC?



Does Art. 12B UN-MTC provide a reasonable, fair and inclusive system to tax profits of MNE in the digital era?

### Art. 12B - Taxation of ADS



#### Allocation of taxing rights

- (1) General rule: Taxing right of residence state
- (2) Gross withholding taxation of income from ADS in source state
- (3) Option to net taxation based on formulaic approach
- (4) Definition of MNE group

#### Scope: Automated digital services

- (5) Definition: Service provided on the Internet or another electronic network, requiring minimal human involvement from the service provider
- (6) Exemplary positive list includes inter alia online advertising services, supply of user data, social media platforms

#### Subsidiarity

- (7) Precedence of Art. 12 and 12 A UN-MTC
- (8) Permanent establishment reservation

#### Revenue sourcing rule

- (9) Nexus: Location of the payer for ADS
- (10) Exception to source rule
- (11) Anti-abuse clause

## Normative analysis

- Gross basis taxation as a simple and effective method of tax collection vs. risks of excessive taxation
- Administrability: Need for alternative collection mechanisms in B2C context and missing thresholds for application
- Ring-fencing of the digital economy?
- Neutrality and efficiency of allocation mechanism
- Relation to Art. 12 and 12A UN-MTC: Consistent delineation?
- Practicability vs. missing the policy rationale of reallocating taxing rights to market states
- Does the allocation mechanism provide for a fair global share of taxing rights?

[...] find a solution which is relatively simple to comply with [...], and at the same time, results in a definite share for market jurisdictions.

- UN Commentary to Art. 12B

## Further issues . . .

- . . . Implementation of Art. 12B UN-MTC in the tax treaty network
- . . . Comparative analysis to the Pillar I Model
- . . . Compatibility with unilateral DST, specifically the Indian Equalization Levy

## Methodology

### Interdisciplinary approach

- Doctrinal analysis of Art. 12B UN-MTC
- Developing a normative framework with reference to principles and theories of public finance, economy and political philosophy from the perspective of developing countries

What principles should govern international tax law on a normative basis?

What are the specific needs of developing countries?

Is there a normative claim for global distributive justice?

What principles should govern a fair reallocation of taxing powers?