

Digital Economy & Defining Taxable Presence

Mr Simon Poh,
Board Member
Singapore Institute of Accredited Tax Professionals
Assoc Professor (Practice),
National University of Singapore

24 October 2014, Friday

Asia-Oceania Tax Consultants' Association
International Tax Conference
Taipei



**Professional
Development**



Industry News



Outline

1. What is the Digital Economy?
2. What constitutes a Permanent Establishment?
3. Milestones for BEPS Action 1 – Address the Tax Challenges of the Digital Economy
4. Key Principles governing the Digital Economy Discussion
5. What is Singapore's position?
6. Beyond BEPS, what next?

What is the Digital Economy?

- Digital economy is the result of a transformative process brought by information and communication technology (ICT).
- Electronic commerce is borderless, and can be contracted to be delivered in a paperless and faceless format.
- Advances in ICT have enabled businesses to move their “place of business” from one place to another quickly.
- Businesses can potentially avoid tax by choosing a low-tax jurisdiction to “source” and record their transactions.

What is the Digital Economy?

- Despite its advantages, electronic commerce raises many questions relating to the concept of permanent establishment (PE):
 - Where should profits be recognized and paid if consumers in different jurisdictions make on-line purchases?
 - Can a website or presence of server constitute a PE?
 - Can an internet service provider be regarded as an agent for a foreign seller in a tax jurisdiction?
 - The list goes on.

What constitutes a Permanent Establishment (PE)?

- Concept of PE is becoming more complicated as tax regulators struggle to grapple and keep pace with a rapidly developing digital economy, and have different stance on taxing e-commerce.
- PE may be created in many ways:
 - Fixed place of business (includes server, virtual PE?)
 - Service PE
 - Agency PE – (includes virtual agency PE?)
 - Equipment PE (includes server PE with digital operations?)
 - New – “Economic Presence” PE covering digital activity
- Related issue is how tax is collected – impose withholding tax on digital transactions?

Milestones for BEPS Action 1 – Address the Tax Challenges of the Digital Economy

- 19 Jul 2013 – OECD published Action Plan to address Base Erosion and Profit Shifting (BEPS)
- 6 Sep 2013 – Leaders of G20 countries publicly endorsed the outline proposals to address BEPS
- Sep 2013 – The Task Force on the Digital Economy (TFDE) established.
- Oct 2013 – TFDE had first meeting
- Mar 2014 – Discussion Draft released
- 23 April 2014 – Public Consultation held
- 16 Sep 2014- OECD released its first set of report and recommendations, addressing 7 out of the 15 actions in the BEPS Action Plan

Key Principles Governing the Digital Economy Discussion

- Difficult to ring-fence the digital economy for special tax treatment. It is neither appropriate nor feasible. Conclusion - digital economy is so widespread that it represents not a special part of the economy but the economy itself. Hard to isolate it for the purpose of creating tax rules.
- Action Plan tries to identify unique features of the digital economy and consider whether these features exacerbate potential for BEPS.
- Key driver behind this Action Plan – whether existing international rules have kept pace with the emergence of new business models caused by rapid developments in ICT.
- Main goal is to restore taxation and this is expected to be delivered also by the other BEPS focus areas, e.g. treaty abuse, PE, Transfer Pricing, CFC rules. Hence, response to this Action Plan seen as part of BEPS package. Also, try to adhere to “Ottawa Principles” - neutrality; efficiency; certainty and simplicity; effectiveness and fairness; flexibility.

What is Singapore's position?

- Although neither a member of OECD or G20, Singapore supports the BEPS initiatives – agrees with the broad principles that profits should be taxed where the real economic activities driving the profits take place.
- It does not condone tax avoidance, especially artificially contrived arrangements and will not support structures that aim to shelter tax evasion or tax avoidance without substantive activities.
- Remains committed to providing the best environment for substantive businesses to thrive in Singapore, hence it maintains its sovereignty right to keep tax rates competitive and provide tax incentives to companies.

What is Singapore's position?

- Singapore adopts modified territorial basis of taxation, i.e. in addition to taxing income sourced in Singapore, foreign income derived by Singapore companies are subject to tax when they are remitted to Singapore, unless they are specifically exempted.
- Except for capital gains, the possibility of double no taxation is unlikely to happen for trading profits.
- Like Hong Kong, Singapore adopts the operations test to determine whether income is derived in Singapore, i.e. need to examine the business model and extent of operations (including presence of personnel) to determine whether income is liable to tax in Singapore.

What is Singapore's position?

- Singapore issued an e-commerce tax guide in 2001 to state that the mere presence of a physical server in Singapore will not amount to trading in Singapore.
- It regards the server as a communication tool and will instead look at the extent of business activities conducted in Singapore to determine if a person is trading in Singapore.
- However, since the announcement of the BEPS action plan, the Singapore tax authorities have not officially made any explicit statements on how it will respond to the tax challenges of the digital economy.

Beyond BEPS, what's next?

- Harmful tax competition is at the root of the international avoidance problem.
- BEPS provides an opportunity for the global tax community to move to revolutionise the international tax framework to address weaknesses in the international tax rules.
- How far will BEPS go?
- Will BEPS Action Plan be the end?
- What happens after 2015? May need to survive the end of the BEPS process to deal with a recurrence of the issues which it identifies.

Thank You

This presentation has been prepared for general guidance and discussion purpose on matters of interest only. It does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice and this presentation, in part or in whole, shall not be copied, reproduced or distributed.