

Table of Contents

Foreword

xv

Part 1 Value Creation

Chapter 1: OECD Consultations on the Digital Economy: “Tax Base Reallocation” and “I’ll Tax If You Don’t”? 3

1.1.	Introduction	3
1.2.	Corporate tax systems have become outdated	5
1.3.	BEPS action package seems not to be enough	6
1.4.	Solutions in the consultation document: Two-pronged approach	8
1.5.	Transfer pricing? Or formulary apportionment, after all?	9
1.6.	GLOBE: A “BEPS 2.0”?	13
1.7.	Levyng extra tax then, like the Americans? That means the end of import neutrality	14
1.8.	So what exactly are the Americans doing?	19
1.9.	Could other countries actually do that too?	22
1.10.	And so, lastly, what would be a better way forward?	23

Chapter 2: Transfer Pricing for Data Businesses: How to Apply the Arm’s Length Principle to the Digital Economy 27

2.1.	Introduction	27
2.2.	Tax challenges of the digital economy and recent policy developments	29
2.2.1.	Overview of tax challenges of the digital economy	29
2.2.2.	Recent developments at the OECD and proposals by the European Commission	30
2.2.3.	Critical review of the current debate	32
2.3.	Value creation in the digital economy and data-driven businesses	38
2.3.1.	Conceptual considerations on the usage of big data in business models	38
2.3.2.	Data mining process in business models	41

Table of Contents

2.3.3.	Functional analysis of digital business models for transfer pricing	44
2.4.	Conclusions	46
Chapter 3:	User Contribution to Value Creation: The Benefit Principle in the Spotlight	49
3.1.	Introduction	49
3.2.	The benefit principle	52
3.2.1.	Benefit principle as the basis for source-based taxation	52
3.2.2.	Benefit theory in a domestic setting	54
3.2.3.	Benefit theory in an international setting	56
3.3.	User contribution to value creation: Some considerations	62
3.4.	Benefit principle considerations and users as a new nexus	65
3.5.	Conclusion	68
Chapter 4:	Taxation of the Digital Economy: A New Dawn for Multilateralism and Mutual Recognition	71
4.1.	Introduction	71
4.2.	The crisis of the territoriality principle on taxation of business profits in the digital era	71
4.3.	Reconsidering value creation: The OECD approach	75
4.4.	A new perspective on value creation: Value co-creation	77
4.5.	Reshaping the international tax framework through a mechanism of mutual recognition	83
4.6.	Conclusion	87
 Part 2 Significant Digital Presence		
Chapter 5:	New Nexus for the Digital Economy: An Analysis of Digital, Revenue-Based and User-Based Factors	91
5.1.	Introduction	91
5.2.	The quest for new income tax nexus for digital economy: Framing the policy discussion	95

5.2.1.	Clearing the theoretical mist: Tax equity, value creation, economic allegiance and justification to tax	97
5.2.2.	The Gordian knot: Justification to tax, physical presence and the market	99
5.2.3.	A view through the looking-glass: Territorial income tax jurisdiction and the problem of localization in the digital realm	102
5.3.	Redefining taxable presence for the digital age: An overview and assessment of some new proposals	107
5.3.1.	SDP as proposed by the European Commission	108
5.3.2.	Notion of SEP under Indian domestic law	110
5.3.3.	SEP in Israeli domestic law	111
5.3.4.	Assessment	112
5.4.	Conclusion	117
Chapter 6:	Solving the Allocation of Taxing Rights Debate for the Digitalized Economy: Shortcomings of the Digital PE Proposal and Reconsideration of the Base-Eroding Payments Proposal	119
6.1.	Introduction	119
6.1.1.	Key characteristics of digital businesses and their corresponding tax challenges	119
6.1.2.	The response of international organizations and unilateral measures in the domestic tax law	122
6.1.2.1.	The response of international organizations	122
6.1.2.2.	Unilateral measures in the domestic tax law	124
6.1.3.	The purpose of this chapter	125
6.2.	The shortcomings of the digital PE concept	125
6.2.1.	The structure of this section	125
6.2.2.	BEPS Action 8-10: Profit allocation under the ALP	126
6.2.2.1.	Control over risk and ownership of intangibles (DEMPE activities)	126
6.2.2.2.	The transactional profit split method (PSM)	128
6.2.2.3.	Application of the PSM to digitalized businesses – Selected illustrations	129

Table of Contents

6.2.3.	BEPS Action 7: Transactions between head office and PEs	130
6.2.3.1.	Changes to the PE threshold	130
6.2.3.2.	Profit allocation to PEs: Arm's length and non-arm's length approaches	131
6.2.3.3.	Application of the changes (including PSM) to digitalized businesses – Selected illustrations	132
6.2.4.	Lessons from BEPS Actions 8-10 and Action 7: Enhanced profit allocation to the source (market) states and tax uncertainty	136
6.2.5.	The digital PE proposal	138
6.2.5.1.	New nexus rules	138
6.2.5.2.	New profit allocation rules	139
6.2.5.3.	Our perspective on whether an EU SDP-type proposal should be pursued?	140
6.3.	A WHT on services as a rational long-term solution	144
6.3.1.	Introductory comments	144
6.3.2.	A stand-alone final WHT	145
6.3.3.	A broad WHT with pragmatic restrictions: A WHT on all business-to-business services	145
6.3.4.	A creditable WHT on cross-border and domestic services	148
6.3.5.	A WHT on gross payments for services	150
6.3.6.	A simple and therefore easily enforceable WHT	152
6.3.7.	A WHT compliant with international obligations	155
6.4.	Conclusion	157

Part 3 EU Digital Services Tax

Chapter 7: Unilateralism in Taxing the Digitalized Economy: Comparing the EU Digital Services Tax Proposal and the Indian Equalization Levy 161

7.1.	Introduction	161
7.2.	Object, purpose and legal basis	162
7.3.	Taxable revenues and taxable person	166
7.3.1.	Taxable revenues	166
7.3.2.	Taxable person	168
7.4.	Place of taxation and revenue allocation	170

7.5.	Interaction between the measures: A case study	172
7.6.	Concluding remarks	174

Chapter 8: Comments on the Digital Services Tax: A Panacea or Placebo for the Taxation of the Digital Economy? 177

8.1.	Introduction	177
8.2.	Setting the scene	179
8.2.1.	The tax challenges of the digital economy	179
8.2.1.1.	Cross-jurisdictional scale without mass	180
8.2.1.2.	Reliance upon intangible assets	181
8.2.1.3.	Data and user participation	181
8.2.2.	The digital services tax proposal	184
8.2.2.1.	Material scope	184
8.2.2.2.	Subjective scope	186
8.2.2.3.	Territorial scope	187
8.2.2.4.	Chargeability and rate	188
8.3.	The DST as panacea, a remedy to the tax challenges of the digital economy in the EU and global tax framework	189
8.3.1.	Meeting the objectives of the DST	189
8.3.2.	The DST and the principle of non-discrimination	192
8.3.3.	The DST and DTCs	195
8.4.	The DST as a placebo, a flawed proposal in light of certain tax principles	199
8.4.1.	Issues under the principle of equity	200
8.4.2.	Issues under the principle of neutrality	201
8.4.3.	Issues under principles of international tax law	203
8.5.	Conclusion	208

Chapter 9: Some Critical Remarks about the DST Proposal 211

9.1.	Introduction	211
9.2.	Behind the DST Proposal	211
9.2.1.	The general picture	211
9.2.2.	The phenomenon of stateless/taxless income	212
9.2.3.	The digital tax package	214
9.3.	The DST Proposal	214
9.3.1.	The basic rules	215
9.3.2.	The targeted outcome	215
9.3.3.	Areas with potential for improvement	216
9.3.3.1.	The temporary character of the DST Proposal	216

Table of Contents

9.3.3.2.	Limited scope	217
9.3.3.3.	User location – Tax allocation	220
9.3.4.	The ongoing discussion – Key developments	221
9.4.	Conclusion: An international policy perspective	223
Chapter 10: Digital Services Tax: A Critical Analysis and Comparison with the VAT System		225
10.1.	Introduction	225
10.2.	Key features of the DST and comparison with the VAT system (and other indirect taxes where relevant)	227
10.2.1.	Overall objective of the tax	227
10.2.2.	Taxable revenue	229
10.2.2.1.	Tax base	229
10.2.2.2.	Taxable amount	231
10.2.2.3.	Intra-group transactions	231
10.2.3.	Taxable persons	232
10.2.4.	Taxable rate	233
10.2.5.	Place of taxation	233
10.2.6.	Remitting of the tax	236
10.2.7.	Time limit	237
10.2.8.	Summary and brief comments regarding overall compliance with the general tax principles	238
10.3.	Is the DST an indirect tax at all?	240
10.4.	Recent developments: National initiatives	241
10.5.	Conclusions	243
Chapter 11: The Compatibility of the EU Digital Services Tax with EU and WTO Law: <i>Requiem Aeternam Donate Nascenti Tributo</i>		247
11.1.	Introduction	247
11.2.	Rationale behind the Commission's intervention in this area	249
11.3.	Main features of the DST	251
11.4.	Compatibility with EU law	253
11.4.1.	Introduction	253
11.4.2.	Compatibility with State aid rules	254
11.4.3.	Compatibility with fundamental freedoms	256

11.4.3.1.	Scope of fundamental freedoms and the EU Commission proposal	256
11.4.3.2.	Restriction	257
11.4.3.2.1.	The deduction system	257
11.4.3.2.2.	Worse treatment of non-EU service providers	258
11.4.3.3.	Justifications and proportionality	261
11.4.3.3.1.	Regarding the deduction system	261
11.4.3.3.2.	Regarding de facto discrimination	263
11.4.4.	Fulfilment of the requirements connected with the DST's legal basis	264
11.4.4.1.	Introduction	264
11.4.4.2.	DST in the case of profits: The emergence of the market state	264
11.4.4.3.	Internal market	267
11.4.4.4.	Avoid distortion of competition	271
11.4.5.	Subsidiarity and proportionality	273
11.4.5.1.	Introduction	273
11.4.5.2.	Subsidiarity and a gap in the effective average tax rates	274
11.4.5.3.	Proportionality and less restrictive approaches	276
11.5.	Compatibility with WTO law	278
11.5.1.	Introduction	278
11.5.2.	Covered digital services and WTO schedules	279
11.5.2.1.	Advertisement services	279
11.5.2.2.	Other services	281
11.5.3.	Discrimination	282
11.5.3.1.	De facto discrimination created by the threshold	282
11.5.3.2.	Compatibility of the deduction system stated in the preamble	283
11.5.4.	Exceptions to the national treatment clause	284
11.6.	Conclusions	285

Part 4
Other Insights

Chapter 12: Taxing the Digital Economy: The Italian Digital Services Tax	289
12.1. Introduction	289
12.2. Setting the framework for the analysis: Tax and digitalization in Italy	290
12.2.1. Key features of the updated definition of a PE as laid down in article 162 of the TUIR	292
12.2.2. The DST provisions	293
12.2.2.1. Subjective scope of the Italian DST	293
12.2.2.2. Objective scope of the Italian DST	294
12.2.2.3. Technical features of the Italian DST	294
12.2.2.4. Critical aspects	295
12.3. Conclusions	296
Chapter 13: The One-Stop Shop for VAT and Digital Services Tax	297
13.1. Introduction	297
13.2. Great oaks from little acorns grow	298
13.2.1. The first set of measures	299
13.2.2. The second set of measures	300
13.3. All that glitters is not gold	301
13.3.1. The limitations of the OSS for VAT	301
13.3.2. The OSS for DST and its limitations	302
13.3.2.1. The characteristics of the DST	302
13.3.2.2. The limits of the OSS for DST	304
13.4. Conclusion: One swallow does not make a summer	305
Chapter 14: The Blockchain Revolution for Transfer Pricing Documentation: If Not in 2020, Then When?	307
14.1. Introduction	307
14.2. Transfer pricing documentation and the goals of BEPS Action 13	308
14.2.1. The OECD Guidelines and BEPS Action 13	310
14.2.2. Issues with transfer pricing documentation in a post-BEPS era, and efforts at automation by MNEs' transfer pricing departments	312

14.3. Blockchain and smart contracts revolution	314
14.3.1. Blockchain: What does the hottest tech disruption buzzword mean?	315
14.3.2. Smart contracts: A perfect match for blockchains	318
14.4. How could blockchain technology be a game changer for transfer pricing documentation?	320
14.4.1. Setting arm's length policies through smart contracts	320
14.4.2. The second leg of the OECD/G20's transfer pricing documentation tripod: Transparency as one of the most valuable characters of blockchains	324
14.4.2.1. Transparency, tamper-proofing, immutability and confidentiality: The most valuable characteristics of the blockchain	324
14.4.2.2. Risk assessment, audit and blockchain revolution for transfer pricing matters	327
14.4.3. Reducing compliance issues through blockchain: The third leg of the transfer pricing documentation tripod and related issues	329
14.4.3.1. The potential of blockchain to reduce compliance costs and time spent on transfer pricing documentation	329
14.4.3.2. Access and retention of data on blockchain: Material and temporal issues involving transfer pricing documentation	332
14.5. Final remarks: Agenda for a revolution	334
List of Contributors	335