Recent Developments in Digital Services Taxes: The UK Debate

John Vella
Faculty of Law & Centre for Business Taxation
This presentation

- UK DST’s stated policy rationale and design issues arising from it

- Many other issues:
  - Economic perspective: distortions, incidence, etc
  - Enforcement
  - DTT, WTO, EU law issues
  - Impact on international cooperation
  - Alternative rationales
Context

• Huge public/political/media pressure to ensure companies pay “fair share of tax”
  – Non-tax concerns with digital giants

• UK’s general position on Int’l Tax reform (March 2018, Updated Position Paper)

• Policy rationale
  – Mismatch represents a “fundamental challenge to the fairness, sustainability and public acceptability of the corporate tax system.”

  → to ensure digital businesses pay tax that reflects value they derive from UK users

• By basing reform preferences on value creation:
  – UK can claim that not departing from principle underlying existing system
  – But affects particular design of UK DST
UK’s proposals

• DST
  – Announced in Budget October 2018
  – Despite “acknowledging the limitations and challenges of revenue-based taxes”
  – Consultation: November 2018 – February 2019
  – Final legislation expected by July 2019
  – Effective from April 2020

• Preferred long-term solution: User Participation
  – Modify nexus and allocation rules
  – Currently discussed by OECD’s Inclusive Framework
UK DST in brief

• **2% tax on revenues** of *certain* digital business models if linked to UK users
  – Not a tax on online sales or advertising revenues

• **Double threshold:**
  – £500m global annual revenues from in-scope business activities; &
  – £25m in annual revenues from in-scope business activities linked to UK users

• **Exemption:** £25m of UK taxable revenues not taxable

• **Safe harbour:** Very low profit margins businesses can elect for alternative calculation

• **Deductible:** against UK CIT as an expense

• **Temporary:** Formal review in 2025 but disapplied before if “appropriate international solution” in place

• **Expected revenue:** £1.5bn over four years
Design issues stemming from policy rationale

“In scope business”

- Businesses for which users are “significant value drivers”
  - search engines; social media platforms; and online marketplaces
- Reverse engineered?
- Why only if users are significant value drivers? Fine distinctions - e.g. wine app
- What is “significant”?
  - HMT needs to “reflect further” on online gaming
- In a fast-moving digitalised world list will require regular updating
- Each business model defined
  - Is business within definition?
  - Website providing professional content allows users to upload content/interact with other users etc: “ancillary” or “incidental” to website’s offering?
Design issues stemming from policy rationale

“In scope revenue”

→ All 3rd party revenues linked to UK users (“whatever the character”, e.g. advertising, fees, commissions, data sales)

→ Irrelevant if realised in UK entity or not

• Highly integrated in and out of scope businesses
  – e.g. advertising revenues both on market place and sales of own services
  - “just and reasonable apportionment” (diff. businesses reach diff. conclusions)
Design issues stemming from policy rationale

UK Users

→ Basic rule: UK user if “normally resident”

• Businesses can take different approach if “just and reasonable having regard to facts”
  • – e.g. search engine could use IP address

• Issues:
  • Diff companies have different views on “just and reasonable”
  • Will all companies have data? How will HMRC review it?
  • VPN
  • Data protection