



October 13, 2017

Mr. Pascal Saint-Amans  
Director, Center for Tax Policy and Administration  
OECD, 2, rue Andre Pascal  
74775 Oarus/ Cedex 16  
France

Dear Mr. Saint-Amans,

The Information Technology Industry Council (ITI) hereby submits feedback on your ongoing work examining the tax challenges raised by digitalisation. ITI represents 62 of the leading information and communications technology (ICT) companies from around the world.<sup>1</sup> ITI is the voice of the high-tech community, advocating for policies that advance technology, promote innovation, open access to new and emerging markets, protect and enhance consumer choice, and foster increased global competition. ITI's member companies include wireless and wireline network equipment providers, computer hardware and software companies, Internet and digital service providers, mobile computing and communications device manufacturers, consumer electronics, and network security providers.

The global economy is digitised and data-driven. Digital commerce is exceptionally broad as it encompasses any economic activity involving the movement of digital information, services and products across borders. Indeed, digital commerce often yields the greatest impact in business-to-business contexts outside of the technology industry and is fundamental to the success and competitiveness of the private sector, including SMEs and startups in developing countries. Whether it is in the automotive, construction, energy, financial services, healthcare, manufacturing, or other sectors, business owners rely on cross-border data flows for their daily operations. As ITI members build hardware, develop software, and provide services that enable the business operations across all sectors, resolving ICT-related tax challenges in the global economy is a critical concern.

Increasingly tax policy is one such area where jurisdictions attempt to influence the technology sector and the use of ICT more broadly. We recognize the OECD has been heavily engaged in these policy debates and we appreciate your leadership on these issues. Further, we understand the modern digitalised economy has created a desire to revisit international tax norms. Overall, we feel strongly that such complex cross-border tax issues are best confronted through continuing multilateral engagement, especially given the OECD's recognition that these issues will impact all cross-border trade and

---

<sup>1</sup> For more information on ITI, including a list of its member companies, please visit: <http://www.itic.org/about/member-companies>.



investment. As interest in this area increases, it is important to recognize the OECD's role in not only providing policy insight into the taxation of technology firms or ICT-related business activities, but appropriate application of its policies and guidance in jurisdictions around the globe.

***Ring-fencing digital from the rest of the economy is impossible:*** In terms of taxation of technology firms or ICT-related business activities specifically, we agree with your conclusion in your BEPS Action 1 report on the impossibility of “ring-fenc(ing) the digital economy from the rest of the economy for tax purposes”. The European Commission Expert Group on Taxation of the Digital Economy similarly found in its 2014 report that relegating the digital economy to a subset of the broader global marketplace has been problematic due to the “widespread diffusion of the digital economy within the whole economy.” Acknowledging both the impossibility of isolating the digital economy and the need for a simple, stable international tax regime, the report concludes that rather than create a separate tax system for “digital” businesses, general tax rules should be applied or adapted to treat these businesses as any other in the mainstream economy.

As your Action 1 report elaborates, the convergence of the growing global economy and evolution of business models through digitalisation has resulted in companies navigating foreign markets in a fundamentally different way. The rapid development of digital technologies enables companies to conduct business across borders and deliver their products and services to consumers more efficiently and effectively across the world, increasing quality and reducing costs. By allowing for the central management of myriad operations that previously required a physical presence, the traditional framework of doing business has evolved. Companies are able to compete in the global marketplace at a much earlier stage in their development. Furthermore, as innovative technologies are embedded in, and integral to, operations of firms across the global marketplace, attempts to isolate business models with a predominant digital component as a separate sector of the economy would “require arbitrary lines to be drawn between what is digital and what is not”.

***Address the concerns, don't target the business model:*** Broadly speaking, we agree that the best way to address tax challenges in an increasingly digital global economy involves honing in on specific features of the relevant business models that raise tax concerns, and developing approaches to address those concerns. Policymakers should be mindful that the evolution of all digitalised business models will continue to accelerate, so approaches should be developed at a sufficiently high level to be sustainable for the future.

A good example of such an approach is the European Union's Electronically Supplied Services (ESS) rule. As you know, in 2008, the European Commission amended its VAT regulation and changed the place-of-supply rule for digital services to the place-of-consumption. Following the change in rules, the Commission did a number of things we would consider best practices. Critically, it allowed for a long and thoughtful transition—the effective date was set for January 2015. Commission officials used this time to form a working group to clarify the scope, administrative procedures and implementation guidelines. Several positive aspects of the rule resulted from this process. First, the ESS rule followed and adopted



OECD guidelines to limit the scope of business-to-business supplies and recommended the use of reverse charge for B2B transactions. Next, the rule simplified the administrative procedures to allow offshore companies to register with a single Member State to remit taxes due to all Member States. The tax agencies also invested in their systems to enable online registration, submission of tax returns and remittance of tax collected. These provisions have eased compliance for business and collection for EU countries.

However, such an approach is not always deployed, resulting in mixed policy outcomes. Overall, a significant challenge ITI members face in the tax space is the rush by countries to develop their own policy approaches, especially concerning digital goods and services. Continuing with the VAT example, seeing the success of the ESS approach, South Africa rushed to enact a similar provision. The quickness of its process led to issues that resulted in two rounds of additional clarifications and amendments. We have seen a similar dynamic as India has migrated to a Goods and Services Tax (GST) system. It announced the change in April 2017 and set the implementation for July 1, just three months later. Numerous problems have resulted.

***Continue favouring multilateral engagement rather than unilateral approaches on cross-border tax issues:*** Efforts to enact changes to direct tax rules focused on the “digital” economy have also resulted in complicating the international tax landscape. Though countries are free to establish their own tax laws, such laws have historically been accompanied by treaties to reduce double-taxation and streamline cross-border transaction. When economies take unilateral action, it not only puts these agreements into question; this individual movement across markets also impedes progress on a consistent, organized global tax conversation. As stated above, we agree with your preliminary conclusions and appreciate the attention and engagement with which you continue to analyze these issues; however, we also recognize that the process has created a short-term vacuum that jurisdictions seem eager to fill. Since the BEPS reports were issued in 2015, we have seen a number of countries move forward with various policies such as the Argentinian turnover tax (2015), Indian equalization levy (2016), Australian updated diverted profits tax (2017), and the United Kingdom diverted profits tax (2015) and updated withholding tax (2017), to name but a few.

One of the clear goals of the BEPS process, and the reason to pull it under the G20 banner, was to develop multilateral solutions to complex problems with the backing of the largest economies in the world. We recognize that the BEPS process was exhaustive and its conclusions hard fought. In the digital space the consensus was to continue the work and issue recommendations in 2020. We appreciate that this work continues but we must also recognize many economies have moved forward above and beyond the OECD’s work and conclusions. Perhaps the most significant example comes out of the European Union. As you know, recently, a block of EU Member States proposed a number of policies explicitly targeting technology firms and ICT-related business activities. These developments are precisely what the BEPS process tried to prevent.



***Equalisation levies and gross withholding taxes present numerous policy and legal issues:*** While our members are opposed to any special measures targeting the digital economy, they have immediate concerns about the notion of adopting such interim policies prior to the completion of the Action 1 Report mandated review. First, broadly speaking, we dispute the underlying notion that such taxes are levied on value where it is created. Tax law has long reinforced the idea that consumption of goods and services does not create value—development and production of goods and services does. Second, a tax imposed on gross revenue has no relationship to net income, which is the only appropriate base for a corporate income tax. Third, we believe these proposals inherently take tax revenue from one country (the country of production) and transfer that tax revenue to the market country. If such an approach is pursued it will require economies to agree between themselves to give up taxation on production.

An equalisation levy could have a number of unintended consequences for businesses and consumers. First, assuming the levy does not include an input credit, long supply chains could create a cascading tax which would multiply the base and amount of tax due. Further, we have heard concerns about the impact of such a tax on small- and medium-sized businesses, especially startups that have not achieved profitability—the very companies many policymakers that are focused on developing countries hope to assist. We also have concerns about the effect on the pricing of services and the impact that could have on consumers. A tax focused on digital services would likely raise the cost of services available in the cloud, for example, which we believe will be a major engine of growth for small and large businesses and developed and emerging economies across the world. Lastly, it is reasonable to believe that, ultimately, the tax would be borne by consumers, which raises questions about the fairness of such a policy.

We also have administrative and legal concerns about such a levy. Any such tax needs to be simple for tax authorities to administer, audit and enforce- and for enterprises to comply with (as noted in our above discussion of the EU’s ESS VAT rules.) We would flag particular concerns of non-resident entities that may not have a local infrastructure, versatility with the native language, local bank accounts, etc. Then we have pressing legal questions. First, any new taxes would need to be fully compliant with European Union laws and international trade obligations. Most critically, any corporate income tax must be fully compliant with tax treaty commitments. As this tax is intended to be a tax on corporate profits, it would be precluded by all existing intra-EU tax treaties. We believe any attempt to override tax treaties to impose taxes on a single industry or sector of the economy would be highly damaging to the integrity of the international tax treaty network.

***Efforts to create a special “digital” permanent establishment (PE) rule depart from reaffirmed long-standing international tax standards:*** Some have proposed creating a new PE nexus to target digital presence within jurisdictions. The notion of a digital PE runs counter to the fundamental agreements reached between countries on residence versus source taxation that underpin the international tax system. Even if such a concept could be delineated in any rational and administrable manner, how could profit be attributed to a digital presence under PE attribution rules (AOA or non-AOA)? In many ways, such profit attribution would operate as formulary apportionment, and therefore be a radical departure from the arm’s length standard that you reconfirmed through the BEPS reports.



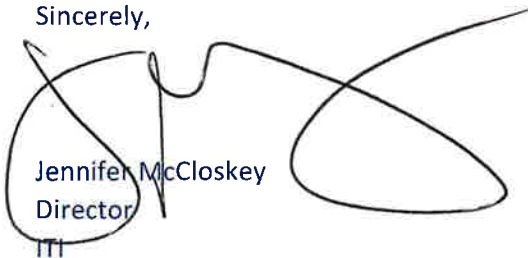
\* \* \*

As you continue your work on digital taxation, we ask you to keep the following points in mind:

- There is no such thing as a “digital economy.” The global economy is digital – data flows and other digital activities permeate virtually every aspect of modern international commerce – and should be treated as such for tax purposes.
- The best way to address tax challenges in relation to technology firms and ICT-related business activities is to hone in on specific concerns raised by such firms and business activities and develop targeted approaches to address those concerns, recognizing the need for solutions to be sustainable for evolving business models.
- These proposals inherently take tax revenue from one country (the country of production) and transfer that tax revenue to the market country. There needs to be agreement between countries that they are willing to give up taxation on production.
- Unilateral approaches are counterproductive for everyone. Complex cross-border tax issues are best addressed through multilateral engagement.
- Targeted levies could have unintended consequences adverse to economic growth and present legal challenges.

Thank you for your consideration of these points. We look forward to your continued focus on these critical issues.

Sincerely,

A handwritten signature in black ink, appearing to read "Jennifer McCloskey". The signature is fluid and somewhat abstract, with a large loop on the right side.

Jennifer McCloskey  
Director  
ITI