Response from ICAS

Corporate tax and the digital economy: position paper

31 January 2018
About ICAS

1. The following submission has been prepared by the ICAS Tax Board. The Board, with its five technical committees, is responsible for putting forward the views of the ICAS tax community, which consists of Chartered Accountants and ICAS Tax Professionals working across the UK and beyond, and it does this with the active input and support of over 60 committee members. The Institute of Chartered Accountants of Scotland (‘ICAS’) is the world’s oldest professional body of accountants and we represent over 21,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors.

Overview

2. ICAS welcomes the opportunity to comment on the HM Treasury position paper “Corporate tax and the digital economy” published in November 2017. The paper is a helpful contribution to the discussions taking place around taxation of the digital economy (including the OECD and EU consultations) and provides some useful analysis of the issues.

3. ICAS agrees with the comments in paragraphs 4.1 to 4.7 of the position paper that taxation of the digital economy can only be addressed in the long run through multilateral reform. We recognise that there is public dissatisfaction with the current position and a need to tackle the stresses imposed on the international tax framework by digitalisation, but it is difficult to see how this can sensibly be achieved on anything other than an international basis.

4. We also agree with the comments in paragraphs 4.11 and 4.12 that if any interim solutions are to be introduced there would be value in coordinated implementation between countries. It would be important to include as many key jurisdictions as possible. One major disadvantage of introducing an interim solution is that it is likely to require changes now – followed by further changes later when an international approach is agreed. Both HMRC and businesses are currently under considerable pressure, not least from Brexit, so it would be undesirable to introduce changes now which would only have to be revisited in future.

5. Our preference would be that the UK should avoid taking further unilateral actions, along the lines of the Diverted Profits Tax (DPT) - and should instead push for an agreed multilateral approach within a reasonable timeframe. Further unilateral actions by the UK, particularly if other jurisdictions take similar steps, are likely to lead to double taxation and to distort competition. This would not enhance the UK’s attractiveness to business and would be likely to inhibit rather than support growth in the tech sector. A global economy requires global solutions.

6. It is important that the messages given by governments, in discussing proposals for a new approach to the taxation of the digital economy, make clear that this is predominantly a matter of looking at whether the current approach to allocating tax between countries needs amendment to reflect modern business practice and increasing digitalisation. It is unhelpful to undermine public confidence in digital businesses by suggesting that it is all about tax avoidance. The OECD BEPS project has already developed recommendations (which the UK is taking a lead in implementing) to address tax avoidance by all international businesses (including those in the digital sector).

Additional comments

7. The OECD produced a report on Addressing the Tax Challenges of the Digital Economy in 2015 as part of its work on BEPS. This recognised that the digital economy and some of its business models pose challenges for international taxation but also acknowledged that it would be difficult to separate the digital economy from the rest of the economy (for tax purposes) because digitalisation is increasingly pervasive.

8. As noted in the position paper, the G20 Finance Ministers subsequently requested that the OECD deliver an interim report on the implications for taxation of digitalisation. The OECD held a consultation last year on the impact of digitalisation on business models and value creation, challenges and opportunities for tax systems, the implementation of the measures outlined in the BEPS package and potential options to address the direct tax challenges of digitalisation. The interim report is due in April 2018.

9. The EU Commission has also held a recent public consultation, which closed in January 2018, to seek input on defining an approach to the taxation of the digital economy – with the objective of
identifying an approach which would meet the goals of fairer and more effective taxation, supporting public revenue and a level playing field across businesses. A report is also expected by April 2018

10. As noted above, we believe this HM Treasury position paper is a useful contribution to the OECD and EU discussions and that the government should carefully consider the OECD and EU reports and proposals for action, once they are available, with a view to joining other jurisdictions in an international approach. It would also be sensible for the UK to await data arising from Country-by-Country Reporting (CBCR) which would assist in clarifying the nature and extent of the problem to be tackled by any proposed UK legislation.

11. Paragraph 5.14 of the paper notes that the government will continue to monitor the progress of US tax reform. It is important that this happens, particularly as it seems likely that the US may need to consider addressing some unintended consequences of the changes. Again, this supports taking time to arrive at a multilateral approach, which can take account of the consequences of US changes as they become clearer.

12. We welcome the recognition (in paragraphs 3.7 and 5.1 of the position paper) that the issues identified are not specific to businesses operating in the digital economy; the first OECD report made a similar acknowledgement. However, we are concerned that key aspects of the proposals do concentrate on these businesses and do not differentiate between them sufficiently. We understand that discussions are taking place with businesses in the sector to discuss different business models.

13. Paragraph 4.3 of the position paper refers to value generated from user participation in jurisdictions where there is no permanent establishment. It suggests that profit could be allocated to countries, in which the company has a user base, based on a metric that approximates the value that the user base generates e.g. monthly active users. We do not think it can be assumed that whenever users provide content or data this will necessarily have value. The data usually requires significant analysis and processing by the digital business. How and where value is actually created will vary considerably from business to business, according to differing business models, so the suggested metric could be very misleading. This needs to be explored in depth with digital businesses.

14. Unilateral UK action would not enhance the UK’s attractiveness as a place to do business or support the continued growth and success of the UK’s tech sector. In view of the pervasive nature of digitalisation (and variety of business models) it is also likely to be very difficult to target any measures accurately and to restrict the impact to the small number of businesses the government appears to have in mind. In this context it is worth noting that DPT was only intended to affect a relatively small number of businesses, but far more businesses had to devote time and resources to analysing complex legislation, in order to determine whether or not it applied to them.

15. Preparing for Brexit (including planning for the different possible outcomes of the negotiations) is currently a top priority for most large businesses. We do not believe that the government should be adding further challenges until after the Brexit process, or at least until the outcomes have become clearer.

16. Leaving Brexit aside, there have been a number of major changes to the taxation of large and multinational companies over the last few years, some of which still require considerable work on implementation, by both HMRC and businesses.

17. The Public Accounts Committee, in its recent report on HMRC, identified that HMRC is also under considerable pressure. It is undertaking 15 major transformation programmes and with the additional pressures arising from Brexit it is having to consider how to change its priorities.

18. From HMRC’s perspective, as well as a business perspective, it would therefore make sense to take the time to ensure that the kind of major changes suggested in the position paper are developed on an international basis, in a sensible timeframe. This would also allow time for proper assessment of the likely economic impact of any changes and the possible effect on business investment in the UK. Rushing to implement unilateral, piecemeal changes is likely to result in complexity, double taxation and additional administrative burdens which will tie up HMRC and business resources, at a time when these would be better directed at other challenges.