A REVIEW OF SOUTH AFRICA'S APPROACH TO THE TAXATION OF THE DIGITAL ECONOMY IN LIGHT OF INTERNATIONAL DEVELOPMENTS

by

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ABSTRACT

The emergence and progression of the digital economy has distorted the core principles of international taxation. Foreign multinational companies now have the ability to fundamentally operate in market jurisdictions without having a "physical presence". This poses a various challenges to the current international tax regimes because it enables businesses to have a "significant economic presence" without a taxable nexus. Therefore, it becomes extremely difficult to "ring-fence" the digital economy.

The Organisation of Economic Co-operation and Development (OECD) has attempted to address these challenges in Action 1 of its Base Erosion Profit Shifting (BEPS) Plan report entitled "Addressing the Tax Challenges of the Digital Economy - Action 1: 2015 Report". Action 1 recommended a few proposals to address the challenges presented in taxing the digital economy, but they were not agreed upon. In the absence of a consensus on the proposals in Action 1, especially from a direct tax perspective, a number of countries began to explore unilateral measures in order to protect their tax base.

South Africa is referred to as the "getaway to Africa" and considering South Africa's importance in the global economy, it is imperative to ascertain South Africa's approach to taxing the digital economy. This study will assess South Africa's approach to taxing the digital economy within the international tax spectrum. This assessment will be based on a review of the unilateral approaches taken by other jurisdictions, to determine whether South Africa has taken the correct stance in not taking direct tax measures so far, as well as to assess whether there is anything else South Africa can do to protect its tax base as it awaits global consensus on the taxation of the digital economy. The observations of this study discovered that the unilateral measures taken by the various countries have caused retaliations by trade partners, impractical implementation issues and has created greater uncertainty. This study affirms that South Africa's subtle approach to taxing the digital economy was correct and that the expansion of its current source taxation rules should be considered in order to protect the South African tax base whilst a "global consensus" on taxing the digital economy is still to be reached.

Key words: Digital economy, digital services, significant economic presence, unilateral measures, taxable nexus.

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1 INTRODUCTION

1.1 BACKGROUND

During the 1920s the “League of Nations” had already understood that the interaction between domestic tax systems could cause a situation of double taxation (OECD, 2013, p. 7). This would potentially lead to the detriment of the economic growth and prosperity of a country (OECD, 2013, p. 7). Nations recognised that there was a need for the creation of international tax regimes that are clear, predictable and easy to understand and provide the government and the taxpayers with a level of certainty (OECD, 2013, p. 7). However, the economy has evolved to become more globally integrated and large corporations followed suit. This “globalisation” has resulted in certain multinational enterprises (MNEs) having to alter their country-specific operating models to have a more globalised operating model (OECD, 2013, p. 7). An example of how this has been executed is through the ability of servicing customers around the world via the internet. This “World Wide Web” (www) was developed by Sir Tim Berners-Lee in 1998; but neither he nor his generation could have fathomed that he had opened up the “Pandora’s box” of the digital revolution (Berners-Lee & Fischetti, 1999, p. 22). The internet has enabled companies to easily carry out business activities in remote locations that are different to the geographical location of their consumers (OECD, 2013, p. 7). These developments, combined with the sophistication of tax planning, have enabled MNEs to manipulate the legal arbitrage and to aggressively pursue tax avoidance schemes to minimise their tax liability (OECD, 2013, p. 8).

This has drawn unprecedented attention to antagonistic international tax planning that has unsettled the most powerful players in a world of international tax policy design (OECD, 2013, p. 8; Brauner, 2014, p. 55). It has forced the leaders of developed and emerging economies to take action and demand the revision of the international tax rules that would generate tax revenue and restore public trust in the system, hence the birth of the “Base Erosion and Profit Shifting” (BEPS) Project by the Organisation for Economic Co-operation and Development (OECD) (OECD, 2013, p. 8; Brauner, 2014, p. 55). The OECD has been examining ways to equalise the playing field by promoting solutions to assist with taxing the digital economy (OECD, 2013, p. 14). The digital economy is the consequence of information and communication’s transformative (ICT) process which can be defined as

"the economic output that comprises solely or mainly of digital technologies with a business model based on the sale of digital goods and/or services" (Bukht & Heeks, 2017, p. 1). One of the key attributes of the digital economy is that it has unparalleled reliance on intangible assets (OECD, 2013, p. 10; OECD (a), 2015, p. 16). This characteristic is a platform for the exploitation of personal data and manipulation of the multi-faceted business models which have the ability to capture value from the generation of "free" products which presents difficulty in determining the jurisdiction in which the value was created (OECD, 2013, p. 10; OECD (a), 2015, p. 16). In this case, BEPS becomes a challenge based on the complex nature of digital business models and its ever-evolving landscape which requires an in depth understanding of the generation of value within this industry (OECD, 2013, p. 14; OECD (a), 2015, p. 16).

The progression of business models and the evolution of the digital economy has resulted in foreign companies having the ability to fundamentally operate in market jurisdictions without having a "physical presence" in that jurisdiction (OECD (a), 2015, p. 98). The main difficulty that this causes is that the current application of international tax regimes enables businesses to have a "significant digital presence" and earn revenue without the liability of tax in the economy of another jurisdiction (OECD (a), 2015, p. 98). This poses further tax challenges regarding attribution of value creation from the characterisation of income, collection of marketable relevant data through the utilisation of products and services, and the application of source rules (OECD (a), 2015, pp. 98-99). Another issue that has been raised with taxing the digital economy is the fact that modern business models rely profusely on data (OECD (a), 2015, pp. 98-99). This presents a number of challenges in terms of characterising and attributing the value of data in terms of adjusting the way in which users and consumers interact with enterprises (OECD (a), 2015, pp. 98-99). Furthermore, the innovation of new digital products or services creates a level of uncertainty in the characterisation of payments made in new business models, especially in the "cloud computing" spectrum (OECD (a), 2015, p. 99). Therefore, it becomes extremely challenging to regulate the digital economy (OECD, 2013, pp. 14-15).

The OECD has attempted to address some of these challenges in Action 1 of its BEPS Reports entitled "Addressing the Tax Challenges of the Digital Economy - Action 1: 2015 Report" (Action 1) (Olbert & Spengel, 2017, p. 3). Even though Action 1 provided guidance on taxing the digital economy, the notion of taxing revenue according to value creation was

still viewed as an anomaly in the international tax field (Olbert & Spengel, 2017, p. 3). Action 1 recommended the following proposals for taxing the digital economy, but they were not agreed upon (OECD (a), 2015, p. 13):

- From an indirect tax perspective, Action 1 recommended that countries should apply International Value Added Tax (VAT)/Goods and Services Tax (GST) Guidelines and introduce collection mechanisms on cross border transactions, especially those between businesses and customers (OECD (a), 2015, p. 13).
- From a direct tax perspective, the Task Force on the Digital Economy (TFDE) noted that although measures recommended in the OECD's BEPS Reports would have a substantial effect on addressing BEPS issues in the digital economy, there are broader tax challenges regarding how tax will be levied in a market country (OECD (a), 2015, p. 13). Therefore, Action 1 suggested that countries come up with new international tax rules for taxing the digital economy.

The OECD recommended that countries could adopt these proposals at a domestic level if they honoured existing bilateral and/or multilateral tax treaty obligations (OECD (a), 2015, p. 148). However, the adaptation of domestic law measures would require consideration to ensure consistency with existing cross-border legal provisions and commitments (OECD (a), 2015, p. 148).

In the absence of a consensus on the proposals in Action 1 on the taxing of the digital economy, especially from a direct tax perspective, a number of countries began to explore unilateral measures in order to protect their tax base (OECD, 2018, p. 212). On 16th of March 2018, the OECD issued an Interim Report entitled the "Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project" (Interim Report) (OECD, 2018, p. 3). This Interim Report analysed a few interim measures that were introduced by various countries to protect their tax base (OECD, 2018, p. 134). Most countries' interim measures included alternative applications of permeant establishment (PE) thresholds, withholding taxes, turnover taxes and specialised laws for targeting large multinational digital businesses (OECD, 2018, p. 134). Some of these measures are explored in detail in this study.

The member countries of the OECD/G20 Inclusive Framework on BEPS (OECD Inclusive Framework) did not reach a conclusion on the analysis performed in the Interim Report. They planned to continue working towards delivering a final report in 2020 which provides a long-term solution to the digital economy conundrum, and they promised to come up with an update in 2019 (OECD (a), 2019, p. 6). On the 23rd January 2019 the OECD issued a Policy Note for "Addressing the Tax Challenges of the Digitalisation of the Economy", by which the OECD Inclusive Framework agreed to review and develop the following proposals that were grouped into two pillars (OECD (a), 2019, p. 6). Firstly, Pillar One which focused on the allocation of taxing rights and a review of nexus and profit allocation rules. Secondly, Pillar Two which focused on other lingering BEPS issues so as to establish rules where jurisdictions had rights to "tax back" where other countries had not exercised their preferential taxing rights (OECD (a), 2019, p. 6).

1.2 PROBLEM STATEMENT

International tax rules that date back to the 1920s have not been able to keep up with the evolving business environment, which has an important emphasis on intangibles and its digital economy (Li, 2018, p. 479). Digitisation poses difficulties to the collection of direct taxes, specifically for corporate income tax (CIT) (Li, 2018, p. 479). It enables digital businesses to tap into foreign markets without having a taxable nexus system based on traditional international tax standards (i.e. PE). This enables digital companies to engage in aggressive tax planning practices which erode countries' tax bases and shift profits to low tax jurisdictions, since this relies heavily on mobile and intangible assets (Olbert & Spengel, 2019, p. 3). The tax bases of developing countries are ostensibly more at risk than the OECD member countries.

The CIT numbers are more prominent in developing countries than in developed countries, in terms of total tax revenues (Thaçi & Gërxhaliu, 2018 , p. 215; Li, 2018, p. 482). CIT is especially important because collecting taxes at a business level is less burdensome than taxing at an individual tax level (Davis Tax Committee (a), 2015, p. 13). CIT is necessary to prevent excessive income shifting between capital and labour income and it acts as a withholding tax on equity income earned by foreign shareholders, which could potentially result in taxes being eroded in a source country (Davis Tax Committee (a), 2015, p. 13). Therefore, any form of erosion to the CIT tax base would have profound consequences to

revenue capacity in a developing country (Li, 2018, p. 482; Davis Tax Committee (a), 2015, p. 13).

An empirical analysis performed by Bakari, indicated that even though South Africa has made remarkable improvement to its infrastructure and abundance of goods and resources, it is still ranked as a developing country (Bakari, 2017, p. 1). The United Nations (UN) still classifies South Africa as a developing country with a 0.5% growth rate in its real Gross Domestic Product (GDP) for 2019 (United Nations, 2020, p. 178). To protect its tax base whilst embracing the evolution of the digital economy, South Africa participates in deliberations on the "globalisation of a tax policy" with international organisations to ensure that its interests as a source or market jurisdiction are protected (Li, 2018, p. 480).

In an attempt to preserve the South African tax base, South Africa introduced legislation that became effective from 1 June 2014 (National Treasury , 2014, p. 4). This legislation relates to a VAT on the inbound supply of digital services which essentially shifted the onus on the taxpayer and the non-resident supplier (National Treasury , 2014, p. 4). The introduction of the VAT on "electronic services" does not protect the country's income tax base, as it can still be eroded due to the fact that South Africa is predominantly a market jurisdiction that faces the impact of BEPS (Li, 2018, p. 480). The focus of this work is therefore not on the VAT measures, but on CIT measures. South Africa is yet to design a direct tax measure for taxing the digital economy.

South Africa is referred to as the "getaway to Africa", meaning that it is seen as the economic hinge between Africa and the rest of the world. The Johannesburg Stock Exchange (JSE) is a channel for various financial flows from the rest of the world to the African continent (Scholvin & Draper, 2012, p. 390). South Africa is the European Union's (EU) top economic partner in the Sub-Saharan region (Grimm & Hackenesch, 2017, p. 161). South Africa's strong banking and telecommunication sector is an attraction for MNEs to expand into the Southern Africa region with ease (Scholvin & Draper, 2012, p. 392). The country also has a strong transport and logistic system for the import and export of goods and services (Scholvin & Draper, 2012, p. 392).

Considering South Africa's importance in the global economy it is imperative to ascertain South Africa's approach to direct taxes regarding the digital economy. This would be ideal to address the direct tax issues that the indirect tax cannot resolve. South Africa needs to protect its tax base whilst embracing the digital economy. Most multinational digital companies that operate in South Africa are based in the US, Europe and Asia, and are based on the Forbes "Top 100 Digital Companies" list (Forbes, 2019, pp. 1-5). The basis of taxation that South Africa would apply to tax the income of such non-resident companies is the source basis of taxation. However, applying source rules for taxing non-residents is an old and outdated way of taxing the digital economy (Li, 2018, pp. 480-482). These source rules are based on "physical presence" tests, for example the PE concept, which is easily circumvented by the digital economy. According to Article 5(1) of the OECD Model Tax Convention on Income and on Capital, 2017 (OECD MTC), read with Article 7(1), the basic definition of a PE is "a fixed place of business through which the business of an enterprise is wholly or partly carried on" (OECD (a), 2017, p. 49). This poses a problem because most of Articles 5 and 7 of the OECD MTC and most countries' domestic laws require a level of "physical presence" before an entity's business profits are subject to tax (Cockfield, 2003, p. 402). Even though countries have withholding taxes, which is a "tax imposed by a source country at a flat rate on the gross amount", if countries have double tax agreements (DTAs), the withholding taxes are reduced, which leaves room for treaty shopping when MNEs create shell companies located in jurisdictions with advantageous treaty networks (OECD (a), 2015, p. 80). The BEPS Action 6 which deals with "Preventing the Granting of Benefits of Treaty Benefits in Appropriate Circumstances" describes treaty shopping as "typically involving persons who are residents of third States attempting to access indirectly the benefits of a treaty between two Contracting States" (OECD (b), 2015, p. 9).

South Africa's participation in the global dialogue to enable consensus on the taxation of the digital economy provides it with a platform to project its views on the new international tax rules that will ensure that its interests as a market jurisdiction are protected.

1.3 THE PURPOSE OF THE STUDY

From the emergence of the digital economy, there has been a considerable amount of uncertainty when it comes to taxing the economy. As mentioned above, the OECD has

been involved in attempting to solve the problem by coming up with ways to ensure global consensus on the taxation of the digital economy.

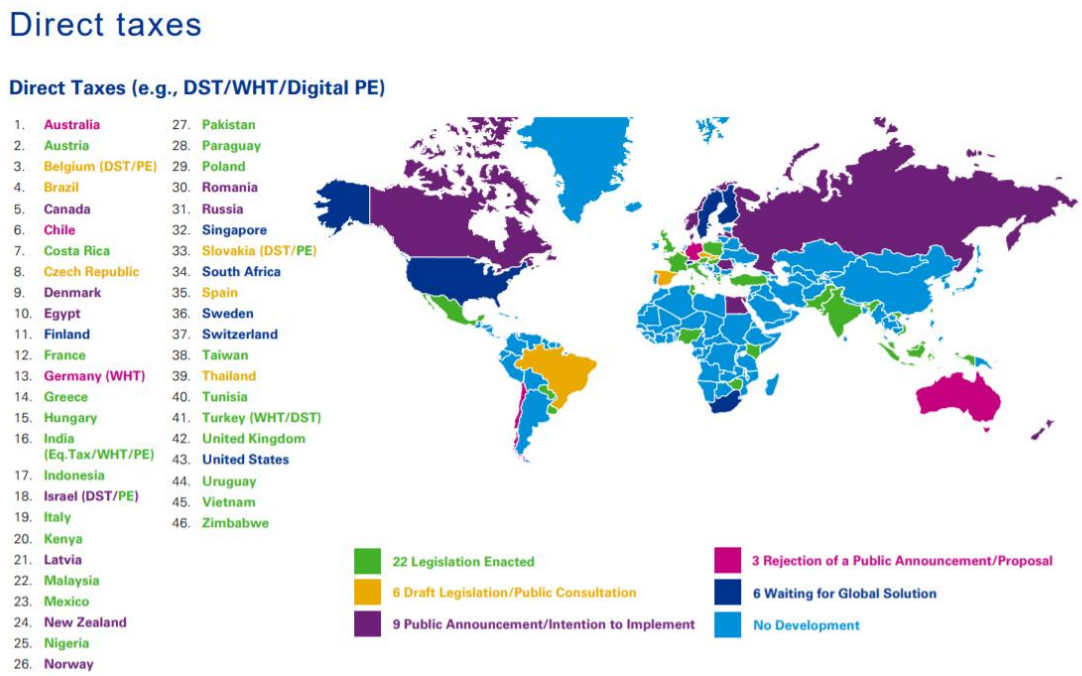
The main objective of this study is to assess South Africa's approach to taxing the digital economy within the international tax spectrum. This assessment will be based on a review of the unilateral approaches taken by jurisdictions, to determine whether South Africa has taken the correct stance in not taking direct tax measures so far, as well as to assess whether there is anything else South Africa can do to protect its tax base as it awaits global consensus on the taxation of the digital economy.

1.4 COMPARATIVE STUDY

As indicated above, South Africa plays a great role in linking Africa with the rest of the world. This study does not evaluate some of the temporary measures that some developing countries and developed countries have put in place to address the tax challenges of the digital economy until a "global consensus" is reached. This evaluation forms the synopsis for assessing South Africa's approach towards the digital tax challenge.

The image below illustrates the international developments in introducing interim measures to tax the digital economy.

Figure 1: Taxation of the digitalised economy – Direct Taxes (as at September 2020)



Source: (KPMG LLP, 2020, p. 5)

The study considers interim measures that have been implemented in selected developed countries and developing countries in their respective tax regimes. The developed countries selected are the United States (US), the United Kingdom (UK) and France.

The UK was selected as one of the developed countries in Europe due to the following reasons:

- South Africa and the UK are party to a DTA which was published in the Government Gazette on the 31st of January 2003 with the intent of promoting and strengthening the economy over and above preventing double taxation and fiscal evasion for South Africa and the UK (The Government of the United Kingdom of Great Britian and the Republic of South Africa, 2003, p. 2).
- A number of UK multinational companies have investments in South Africa. The most notable online platform is eBuyGumm which is a UK based online shopping platform without a “physical presence” in South Africa (eBUYgumm Ltd, 2020, p. 4). The Vodacom Group, which is a subsidiary of Vodafone in the UK, was ranked tenth as one of the biggest multinational companies based on capitalisation, with approximately R213 billion in annual turnover (IG Markets South Africa Limited, 2019, p. 2).

France was chosen as one of the developed countries in Europe due to the following considerations:

- France and South Africa have a DTA that was published on the 27th of September 1995 with the objective of avoiding double taxation and fiscal leakage for both of these countries (The Government of the French Republic and Republic South Africa , 1995, p. 2).
- France is ranked as the fourteenth largest foreign investor in South Africa with a recorded 370 subsidiaries of French companies (Ministère de l'Europe et des Affaires étrangères, 2018, p. 1). One of the digital services that is used in Africa (including South Africa) without a "physical presence" is the film downloading service platform called "My French Film Festival" (MyFFF) which was launched in 2017 (l'Institut Français d'Afrique du Sud, 2017, p. 2). Users of this account are able to upload their films for an audience to watch as well as watch all movies that are available on the website anywhere in the world (l'Institut Français d'Afrique du Sud, 2017, pp. 2-3).

The US was chosen as one of the developed countries due to the following considerations:

- The US and South Africa signed a DTA on the 15th of December 1997 for the avoidance of double taxation and prevention of fiscal evasion from both of these nations (The Government of the United States of America and Republic of South Africa, 1997, p. 1).
- Large multinationals from the US dominate the South African market without a "physical presence". Google, YouTube, Facebook, Netflix, Wikipedia and WhatsApp are the top consumed service offerings in the digital market in South Africa, based on monthly data traffic and time spent by active users located in South Africa compared to other digital services and platforms (Hootsuite, 2019, p. 25).

The study also compares the unilateral approaches taken by developing countries to tax the digital economy. India was chosen as one of the developing countries to be reviewed, based on the following considerations:

- The DTA that was published in the Government Gazette on the 12 December 1997 had the intent of preventing double taxation and fiscal evasion for these two

emerging economies (The Government of the Republic of India and Republic of South Africa, 1997, p. 1).

- India offers a range of software applications that are used by business in South Africa i.e. AVG Anti-virus software and XBRL software which is an accounting application used by small to medium business (IndiaMart, 2020, p. 1). These software services have the ability to be granted without a physical nexus within South Africa.

Pakistan was chosen as one of the developing countries based on the following:

- Pakistan has a DTA with South Africa that was published in the Government Gazette on the 9th of March 1999 with the intent of preventing double taxation and fiscal evasion for these two nations (The Government of the Islamic Republic of Pakistan and Republic of South Africa, 1999, p. 1).
- There aren't notable companies with a digital presence in South Africa but there are software applications such as Cubix, Hashe Computer Solutions and Avaib, which are business solution software applications that provide business analytic services, IT development software and data processing. These are used by businesses around the world and in South Africa (GoodFirms, 2020, pp. 2-3). In addition, these two countries are seen as market countries with a similar tax system that have the potential to be eroded, especially in the application of international tax agreements for taxing business income for source or market countries (OECD, 2020, p. 20).

Nigeria was chosen as one of the developing countries to be reviewed based on the following considerations:

- Nigeria and South Africa have a DTA that was established on the 22nd of July 2008 with the same intention of protecting their respective tax bases (The Government of the Federal Republic of Nigeria and Republic of South Africa, 2008).
- One of the most notable Nigerian exports within the digital economy is Nollywood. This Nigerian online streaming film service is a popular business amongst the internet users in South Africa. iROKOtv was launched in 2011 which primarily showcased Nollywood movies. It stopped for a while and then was relaunched as a downloading service in 2016, since the boom of Africa having the ability to use Wireless Fibre Internet (Wi-Fi) (PwC South Africa, 2019, p. 24). This downloading service is expected to have a Compound Annual Growth Rate (CAGR) within the African (including South African) market and the global market (PwC South Africa,

2019, p. 85). In addition, these two countries have vulnerable tax systems to the digital economy, especially international tax agreements for taxing business income for source countries such as these two nations (OECD, 2020, p. 20). It is also key to note that Nigeria and South Africa are part of the African Tax Administration Forum (ATAF).

The developed countries were selected based on their strong trade ties and investments in South Africa. With regard to the developing countries, not only were they chosen due to their economic ties to South Africa, but also due to their country profiles. South Africa is a developing country and it was also important to evaluate how these emerging countries would deal with the taxation of a digital economy as a market country. The combination of evaluating how both developing and developed countries have taken interim measures to address the tax challenges of the digital economy will assist in judging whether South Africa has taken the right decision not to introduce interim measures to protect its tax base, but to rather wait for a "global consensus' on the matter.

1.5 SCOPE OF STUDY

It is important to acknowledge the limitations of the study in order to focus the reader on the research problem statement (Connelly, 2013, p. 325).

The research study does not cover the indirect tax measures taken by other countries. The study covers only the OECD Pillar One proposals. It does not cover the Pillar Two proposal (also referred to as the "GloBE" proposal) (OECD (a), 2019, p. 6).

1.6 METHODOLOGY

The study follows a pragmatic approach as it analyses the different viewpoints of various scholars and industry specialists on the topic. Therefore, the study explores different perspectives to comprehend how the world, but especially South Africa, has approached the taxation of the digital economy (Wagner, et al., 2012, pp. 223-225). It reviews policy

documents by international bodies such as the OECD, the legislative provisions of the countries covered in the study and double tax treaty provisions.

1.7 BREAKDOWN OF STUDY

The study is divided into the following segments:

Part 1

This part provides an introduction to the study, the purpose of the study and why it is important to understand where South Africa stands in addressing the tax challenges of the digital economy.

Part 2

This part analyses the unilateral measures put in place by selected developed countries as they endeavour to address the challenge of taxing the digital economy. It also evaluates the impact of these measures before a "global consensus" is reached. This will provide insights as to why South Africa has not implemented these measures from a direct tax point of view.

Part 3

This part analyses unilateral measures taken by selected developing countries as they also try to address the taxation of the digital economy before the "global consensus" is reached. Since South Africa is a developing country, the study evaluates whether these measures could be adopted by South Africa and what their impact could have on the economy.

Part 4

This part explains South Africa's involvement with the OECD in developing "global consensus" on taxing the digital economy. In this section the OECD's "Unified Approach under Pillar One" is explained.

Part 5

This part assesses initiatives taken by South Africa to help establish steps in the direct taxation of the digital economy. It examines the commentaries by South African institutions on the Pillar One proposals for taxing the digital economy to gauge where South Africa stands in addressing this international tax problem.

Part 6

This section provides recommendations of steps which South Africa should take to protect its tax base, while it awaits international consensus on the taxation of the digital economy. It concludes the study.

2 INTERIM APPROACHES TAKEN IN SELECTED DEVELOPED COUNTRIES

This section of the study analyses the unilateral measures taken by selected developed countries.

2.1 UK'S APPROACH TO TAXING THE DIGITAL ECONOMY

On the 29th of October 2018, the UK Budget Speech was presented in preparation of the UK leaving the EU. The UK government took steps to safeguard a prosperous future by investing in public services, support enterprises and enhanced living conditions across the country (Her Majesty's Treasury, 2018, p. 1).

2.1.1 UK DIVERTED PROFITS

One of the mechanisms used to prevent the erosion of the UK tax base is the Diverted Profits Tax (DPT) provision (HM Revenue & Customs, 2018, p. 3). DPT aims to discourage and counteract the diversion of profits from the UK by large multinationals that avoid creating a "physical presence" (i.e.PE) which would allow these multinationals to fall within the UK tax net or capitalise on certain arrangements that have a "lack of commercial substance", in order to manipulate tax mismatches by diverting income and expenditure within the group (HM Revenue & Customs, 2018, p. 3). This measure was first introduced in the UK Finance Bill of 2015, but only became legislated and enacted after the 29th of October 2018 through the UK Finance Act of 2019 (Her Majesty's Treasury, 2019, p. 220).

Sections 80 and 81 of the UK Finance Act of 2019 explain the criteria of UK based companies that are captured by this provision, whilst Sections 82 – 85 explain the rules applicable in the calculation of taxable diverted profits (HM Revenue & Customs, 2018, p. 9). The segments applicable to foreign multinationals operating in the UK are in Section 86 and the calculation for those taxable diverted profits are in Sections 88 to 91 (HM Revenue & Customs, 2018, p. 9). Essentially, the DPT is applicable to these diverted profits at the normal corporate tax rate of 25% plus a "true-up interest" (which is a component of the tax charge) however, where diverted profits are ring-fenced especially in the old sector, the rate is 55% plus "true-up interest" (HM Revenue & Customs, 2018, p. 4).

2.1.2 THE UK'S PROPOSED DIGITAL SERVICE TAX (DST)

Another mechanism that has been proposed by Her Majesty's Treasury (HM Treasury) to protect the UK fiscus is to ensure that large digital service enterprises pay their fair share of taxes by introducing a 2% of "digital service tax" on revenues derived by large multinational companies that reflects the value which they acquire from UK users (Her Majesty's Treasury, 2018, p. 41).

This DST was introduced in the United Kingdom's Finance Bill 114 of 2020 (UK Finance Bill). The 2020 Budget that was held on the 11th of March 2020 confirmed that the DST will come into force upon the royal assent of the 2020 Finance Bill (Her Majesty's Treasury (a), 2020, p. 91). In accordance with Clause 60(2) of the UK Finance Bill, the DST will be applicable for a multinational group that is "in-scope" with a financial year that commences on or after 1 April 2020 (Parliamentary House of Commons, 2020, pp. 47-48). Clause 38(1) of the UK Finance Bill states that "a tax (to be known as a 'digital services tax') is charged in accordance with this Part on UK digital services revenues arising to a person in an accounting period" (Parliamentary House of Commons, 2020, p. 35). In addition, Clause 38(2) of the UK Finance Bill indicates that the Commissioner of Her Majesty's Revenue and Customs (HMRC) will be responsible for collecting these taxes (Parliamentary House of Commons, 2020, p. 35). Clauses 39 – 44 define what is perceived as "UK digital service revenues" and other key concepts in detail (Parliamentary House of Commons, 2020, p. 35).

Clause 42(2) of the UK Finance Bill provides that "digital service activity" "means providing social media service, an internet search engine or an online marketplace" (Parliamentary House of Commons, 2020, p. 38). Clauses 42(3) – (5) provide critical definitions of these "business activities":

- Clause 42(3) defines a "social media service" as "an online service that meets the following: the main purpose, or one of the main purposes, of the service is to promote interaction between users (including interaction between users and user-generated content), and making content generated by users available to other users is a significant feature of the service" (Parliamentary House of Commons, 2020, p. 38);
- Clause 42(4) defines an "internet search engine" as not including "a facility on a website that merely enables a person to search the material on that website, or the material on that website and on closely related websites" (Parliamentary House of Commons, 2020, p. 38); and
- Clause 42(5) defines an "online marketplace" as "an online service that meets the following conditions; the main purpose, or one of the main purposes, of the service is to facilitate the sale by users of particular things, and the service enables users to sell particular things to other users, or to advertise or otherwise offer particular things for sale to other users" (Parliamentary House of Commons, 2020, p. 38). Clause 42(5) also defines a "thing" to mean "any services, goods or other property; and any reference of the sale of a thing includes hiring it" (Parliamentary House of Commons, 2020, p. 38).
- Clause 43 defines the terms "user" and "UK user". According to Clause 43(2), a "user" is "any reference to a user, in relation to a digital services activity of a person (the "provider"), which does not include — (a) the provider or a member of the same group as the provider, or (b) an employee of a person within Paragraph (a), acting in the course of that person's business" (Parliamentary House of Commons, 2020, p. 39). The term "UK user" is defined under Clause 43(3) to mean "any user who it is reasonable to assume — (a) in the case of an individual, is normally in the United Kingdom; (b) in any other case, is established in the United Kingdom" (Parliamentary House of Commons, 2020, p. 39).
- Clause 45(7)-(9) describes "associated online advertising" that is included as part of digital business activities (Parliamentary House of Commons, 2020, p. 38).

These DST provisions will be applicable in relation to a multinational group for the accounting period under Clause 45(1) of the UK Finance Bill on "that the total amount of digital services revenues arising in that period to members of the group exceeds £500 million, and that the total amount of UK digital services revenues arising in that period to members of the group exceeds £25 million" (Parliamentary House of Commons, 2020, p. 39). Clause 46(2) of the UK Finance Bill indicates that each group member is liable to pay tax in respect of "UK digital services revenues" in that period. Clause 46(3) provides a step by step process for applying the 2% charge of the DST which includes: taking the total amount of "UK digital services revenues arising to members of the group in the accounting period", deducting £25million from the amount and applying the 2% DST and thereafter each group member is liable for the 2% DST based on its contribution to the group amount from "UK digital services revenues" (Parliamentary House of Commons, 2020, p. 40). There is a "safe harbour" for low profit and loss-making entities, which allows for a reduced rate of the DST rate calculated at 0.8 multiplied by the operating margin and then multiplied by the net revenues under Clause 47 of the UK Finance Bill (Parliamentary House of Commons, 2020, p. 40).

The HMRC's Explanatory Notes of the UK Finance Bill on DST provide details on how this DST will be applied, however it emphasises the fact that the UK government will participate in the international co-operation with regard to taxing large international companies in the future (Her Majesty's Treasury (b), 2020, p. 96). The UK government is still committed to the development of a multilateral solution to addressing the tax challenges of digitalisation and it has stated in its 2020 Budget that the DST will be repealed once an appropriate global solution is in place (Her Majesty's Treasury (a), 2020, p. 92).

2.2 FRANCE'S APPROACH TO TAXING THE DIGITAL ECONOMY

France's approach to taxing the digital economy has taken its cue from the EU's guidance. In 2014, the European Commission (EC) released a "Report of the Commission Expert Group on Taxation of the Digital Economy" that discussed the key principles of taxing the digital economy under the international taxation realm (European Commission, 2014, p. 5). The EC High Level Expert Group on Taxation of the Digital Economy" (Expert Group) identified that distributional equity, economic efficiency and effectiveness of tax

enforcement coupled with tax administration were fundamental principles in considering a new tax regime to address the challenges presented by taxing the digital economy (European Commission, 2014, p. 5). This report emphasised the need for elaborating on more fundamental tax reform options to address the technological changes of the digital economy, and it encouraged the continuous examination of income tax based on a formulary approach, and a destination based imposed tax system (European Commission, 2014, p. 5). The EC published a Council Directive on the 21st March 2018 on the "Proposal on the common system of a digital services tax on revenues resulting from the provision of certain digital services" (European Commission, 2018, p. 1). This Council Directive considered proposing an interim solution to the current corporate tax rules that were deemed inadequate to tax the digital economy. The proposal was in the form of a tax on certain digital services (European Commission, 2018, pp. 2-3).

In 2019, the French government released a proposal to charge a 3% levy on revenues generated by businesses that provided specific digital services (United States Trade Representative, 2019, p. 5). The French Parliament passed a DST Bill on the 9th of April and on the 21st of May 2019, and the final bill was agreed on the 4th of July 2019 (United States Trade Representative, 2019, p. 5). On the 24th of July 2019 the President of France, Emmanuel Marcon, signed the bill to become law under "LAW n ° 2019-759 of 24 July 2019 creating a tax on digital services and modifying the trajectory of reduction in corporate tax" (Légifrance, 2019, p. 1). Article 299 – I - A of the French Tax Code (FTC) provides that the tax is "payable on the revenues received by the companies in the digital sector defined in Paragraph III, resulting from the provision in France, during the calendar year, of the services defined in Paragraph II" (Légifrance, 2019, p. 1).

Paragraph II (A) of Article 299 of the FTC defines services as "the provision, by electronic communications, of a digital interface which allows users to enter into contact with other users and to interact with them, in particular for the delivery of goods or the provision of services, directly between these users. However, the provision of a digital interface is not a taxable service: when the person making this provision uses the 'digital content', 'communications services' or 'payment services' within the meaning of article L. 314-1 of the Monetary and Financial Code" (Légifrance, 2019, pp. 1-2).

Paragraph of II (C) of Article 299 of the FTC defines digital activities as "when the digital interface is intended to allow the purchase or sale of services aimed at placing advertising messages under the conditions provided for in Paragraph II (Légifrance, 2019, p. 2). It should be noted that services marketed to advertisers or agents that are aimed at placing targeted advertising messages on a digital interface based on data relating to the users are excluded from this definition (Légifrance, 2019, p. 2). For example here are services related to purchasing, storing and broadcasting advertising messages, and the management and transmission of data relating to users (Légifrance, 2019, p. 2). The DST will apply to a taxpayer that meets the following thresholds according to Paragraph III of Article 299 of the FTC:

- If the multinational company has a consolidated worldwide turnover of €750 million derived from digital services (Légifrance, 2019, p. 2); and
- If the multinational company earns €25 million on digital services from French users (Légifrance, 2019, pp. 2-3).

The amount of tax calculated is determined by applying 3% on the tax base (excluding VAT). The tax base consists of the revenue generated by the digital services provided in France, but only adjusted to keep the share of this turnover that is connected to the digital services utilised by French users as per Paragraph I and II of Article 299 – a quarter of the FTC (Légifrance, 2019, pp. 4-5).

2.3 THE USA'S APPROACH TO TAXING THE DIGITAL ECONOMY

In December 2017, the US enacted a minimum tax policy which is called the "Global Intangible Low Taxed Income" (GILTI) and "Base Erosion and Anti-Abuse Tax" (BEAT) as part of its expansion of its Controlled Foreign Company (CFC) in an attempt to address the tax challenges of the digital economy. This was part of its Act to "Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, Pub. L. No.115–97, which is also known as the Tax Cuts and Jobs Act of 2017

(TCJA)" (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—1; Herzfeld, 2019, p. 504).

Section 951A of the TCJA contains the GILTI rules that require a 10% US shareholder of a CFC to include in current income the shareholder's pro rata share of the GILTI income of the CFC (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—155). The GILTI rules apply to "specified corporations" as defined in Section 965E (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—148) and partnerships and individuals (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—155).

The annual GILTI inclusion would amount to the aggregate "net CFC tested income" of the US shareholder, reduced by the US shareholder's "net deemed tangible income return" (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—155). The "net CFC tested income" generally includes a CFC's gross income subject to certain exclusions and the net deemed tangible income return is a 10% return on the US shareholder's share of the adjusted tax basis of tangible depreciable property of CFCs that earn tested income and is deducted by the allocable interest expense to the extent that such expense reduces tested income (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—155/156). As a result, US shareholders will need to assess whether they have GILTI inclusions every year.

The BEAT provisions are contained in Section 59A of the TCJA which was enacted on the 22nd of December 2017, which limits the ability of multinationals to shift profits from the US orchestrating deducible payments to their subsidiaries or affiliates in low tax jurisdictions (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—173/174). Therefore, US companies will calculate their regular tax liability by applying a 21% rate on taxable income and then the US company would have to recalculate its taxable income without the deductible payments multiplied by the BEAT which is 10%. If the BEAT is higher than the normal tax which that company must pay, the difference between the normal tax and BEAT amount is an addition to its normal tax liable (One Hundred Fifteenth Congress of the United States of America, 2017, p. H. R. 1—173/174).

2.4 CONCERNS ABOUT THE APPROACHES IN THE US, UK AND FRANCE

It is worth noting that both the US GILTI and BEAT regimes were enacted in the Federal TJCA three years ago (in 2017), but the Federal US government is yet to issue guidance on explaining how these provisions would apply to international income (U.S. Tax Foundation , 2019, p. 1). The US GILTI/BEAT regime has increased the level of uncertainty in taxing the digital economy (U.S. Tax Foundation, 2019, p. 1) for which clear guidance is required. Only 17 US states have issued some guidance as an initial step towards a significant foray into the taxation of international tax (U.S. Tax Foundation, 2019, p. 1). During 2020, the US' Department of Treasury and the Internal Revenue Service (IRS) released the Final Regulations (TD9885) for certain sections that were included in the TCJA, which included Section 59A in the Federal Register (Department of Treasury and Internal Revenue Service, 2020, pp. 2-3). These Regulations aimed to provide detailed guidance on how to make BEAT calculations for groups of related taxpayers. This document also contains certain provisions that permit the waiving of deductions for the purposes of BEAT and additional guidance regarding partnership on anti-abuse rules (Department of Treasury and Internal Revenue Service, 2020, pp. 4-5).

Even though the IRS and the Department of Treasury published the BEAT Regulations, the BEAT provision is contradictory to the US Model Income Tax Conventions (including the OECD and UN Model Tax Conventions) from where tax treaties are rooted (Rosenbloom & Shaheen, 2018, p. 54). The BEAT provision is computed in such a way that without deductions for payments to non-resident related persons, it does not apply the same disallowance rules for domestic related questions which introduces an element of discrimination (Rosenbloom & Shaheen, 2018, p. 54). Therefore, this Section 59A BEAT provision will be subject to the rules of Article 24(4) of the US Model Tax Convention which allows for foreign related parties to be allowed the deduction regardless due to the discriminatory nature of this provision (The Federal Government of the United States of America, 2016, p. 54; Rosenbloom & Shaheen, 2018, p. 54). This BEAT fails to adhere to US tax treaty obligations and therefore this provision increases the lack of certainty which applies to this interim measure.

The DST regimes that countries like France and the UK have enacted or are proposing to enact have received direct criticism because they bear a substantial risk of creating double

taxation, increasing legal uncertainty for taxpayers and distorting the international trade regulations amongst jurisdictions (Olbert & Spengel, 2019, p. 11). The DST approach has the potential to severely limit international competition between countries; and it would effectively restrict the economic growth of these countries (Confédération Fiscale Européenne, 2018, p. 8; Olbert & Spengel, 2019, p. 11).

The UK's proposed DST includes a "safe harbour" provision that would exempt loss-making entities and reduce the effective tax rate for digital companies with a low profit margin (Her Majesty's Treasury, 2018, p. 44). However, the French DST does not have a similar provision for low margin and loss-making entities.

One of the main concerns of the DST regimes is that they violate several goals of good tax policy (OECD, 2014, p. 63; Choudhury & Petrin, 2019, p. 347). The OECD set out a guideline of core overarching traits that a good tax policy should have which are: "neutrality, efficiency, certainty and simplicity, effectiveness and fairness, and flexibility" (OECD, 2014, p. 63; Choudhury & Petrin, 2019, p. 347). Achieving all of these goals can often conflict, as not all of these traits can be included in a tax policy. Neutrality is more important than the others, because treating similar transactions differently distorts economic decisions (Kennedy, 2019, pp. 14-15). Ideally, a tax policy should be neutral with regard to several factors, including business function, nationality and market size. The DST clearly violates this key principle, creating legislation that will negatively impact growth and innovation of the global economy (Kennedy, 2019, pp. 14-15).

This is was one of the key reasons why the US conducted an investigation into the French DST. In December 2019 the US Trade Representative (USTR) published a "Report on France's Digital Services Tax Prepared in the Investigation under section 301 of the Trade Act of 1974" (the USTR Report). It found that the introduction of the French DST was discriminatory against the US companies and that it was inconsistent with the prevailing principles of a tax policy (the US Treasury Secretary, 2019. P. 1). Furthermore, it was found that the French DST was unusually burdensome for potentially affected US companies (United States Trade Representative, 2019, pp. 1-3). The US argued that the new French DST was particularly orchestrated to tax the US headquartered digital companies such as Google and Facebook, which undermines the OECD key principles of a good tax policy (United States Trade Representative, 2019, pp. 3-5). In retaliation, the

USTR authorised by its section 301 Trade Act of 1974, proposed to impose duties of up to a 100% on specific French products. Following this investigation, the USTR released a Federal Notice on the 6th of June 2020which initiated section 302(b)(1)(A) of the Trade Act of 1974 investigations on the DST provisions of other countries, including the UK (United States Trade Representative, 2020, pp. 4-5). These investigations focus on the key concerns that the DST raises: discrimination to the taxpayer (mainly US headquartered companies), divergence from the US tax system and the international tax regimes, and the fact that revenue is taxed rather than income, which may paralyse the commercial success of digital companies that are subjected to the DST (United States Trade Representative, 2020, p. 5).

Following this investigation, the US Treasury Secretary wrote a letter to the Secretary General of the OECD noting that: “We have already held two public consultations attended by stakeholders from around the world and like you, while noting broad support for existing rules, clearly identified the need for greater tax certainty and administrative ability. This is why the OECD proposal on a ‘Unified Approach’ contains a very strong tax certainty dimension. Without it, there would be no conditions for achieving a consensus” (the US Treasury Secretary, 2019. p. 1). The US Treasury Secretary noted that the Pillar One “Unified Approach” did appear to be a “safe harbour” regime, which is concerning because the DST would impact over 135 countries (the US Treasury Secretary, 2019. P. 1). On the 12th of June 2020, the US Treasury Secretary wrote a letter to the Finance Ministers of France, Spain, Italy and the UK stating that they would not agree to the proposed Pillar One and suggesting that these discussions be suspended for the time being, as this Pillar One would change the core principles of international tax regimes such as the taxable nexus on “physical presence” and the arm’s length principle. The letter goes further, expanding upon the fact that since the “safe harbour” approach has been rejected, the chances of resolving this complex multilateral issue are becoming more challenging (Secretary of the Treasury, 2020, p. 1). This letter does emphasise the fact that retaliatory action will be taken against the unilateral measures that are taken by these countries (i.e. the DST) (Secretary of the Treasury, 2020, p. 2). It further emphasises the concern that unilateral measures will have detrimental effects on trading relations within the wider economy, which is a great concern, especially for a source country.

3 INTERIM APPROACHES TAKEN IN SELECTED DEVELOPING COUNTRIES

3.1 INDIA'S APPROACH TO TAXING THE DIGITAL ECONOMY

India introduced an "equalisation levy" of 6% on "specified services" through its Chapter VIII, specifically Clause 162(1), of the Finance Bill of 2016 (The Central Government, 2016, p. 53). This levy of 6% is applicable to the non-resident that has received or has accrued a consideration from a resident of India and the non-resident that has a PE (as defined in Clause 162(g) of India's Finance Bill of 2016) in India from rendering a "specified service" (The Central Government, 2016, p. 53). The definition of a "specified service" according to Clause 162(i) means "online advertisement, any provision for digital advertising space or any other facility or service for the purpose of online advertisement and includes any other services which may be notified by the Central Government on this behalf" (The Central Government, 2016, p. 53). In accordance with Clause 163, the "equalisation levy" essentially provides an obligation to Indian residents to remit the amount of the "equalisation levy" to the government in terms of the consideration due for the "specified services" to non-residents (The Central Government, 2016, p. 53).

From 1 April 2020, India widened its scope on the "equalisation levy" through its Finance Bill 26 of 2020 (India's Finance Bill of 2020). Clause 84 of India's Finance Bill of 2020 seeks to introduce a new section, Section 194O, into India's Income-tax Act of 1961 (The Central Government, 2020, p. 86). This clause widens the scope of imposing a 2% "equalisation levy" by indicating that "where sale of goods or the provision of services of an e-commerce participant is facilitated by an e-commerce operator through its digital or electronic facility or platform (by whatever name called), such e-commerce operator shall, at the time of credit of amount of sale or services or both to the account of an e-commerce participant or at the time of payment thereof to such e-commerce participant by any mode, whichever is earlier, deduct income-tax at the rate of 1% of the gross amount of such sales or services or both" (The Central Government, 2020, p. 31). The provisions of India's Finance Bill of 2020 were passed by the Lok Sabha on 23 March 2020 and have become enacted and legislated in Finance Act No 12 of 2020 which included the introduction of a new Section 194O (Ministry of Law and Justice, 2020, pp. 43-44). This section will come into effect on the 1st day of October 2020 (Ministry of Law and Justice, 2020, p. 43).

Clause 84 of the India Finance Bill of 2020 provides further explanation of definitions of "electronic commerce" and "e-commerce participant". For purposes of this clause, the definition of "electronic commerce" means "the supply of goods or services or both, including digital products, over digital or electronic network" (The Central Government, 2020, p. 31). Therefore, the "equalisation levy" will apply to "e-commerce supply of services" provided by a foreign resident/"e-commerce operator" or the online sale of goods and services facilitated by this "e-commerce operator" (providing a platform for the sale of goods and provision of services) or the combination of all aspects mentioned to a resident (The Central Government, 2020, pp. 86-87). An "e-commerce operator" is "a person resident in India selling goods or providing services or both, including digital products, through digital or electronic facility or platform for electronic commerce" (The Central Government, 2020, p. 31). The abovementioned provision will not be applicable to foreign suppliers providing "e-commerce supply or services" to its PE in India (The Central Government, 2020, p. 31). Furthermore, the "equalisation levy" of India's Finance Bill of 2016 falls within the ambit of "specific services" and to the revenue in respect of goods/services provided to residents utilising internet protocols addressed in India and is less than 2 crore rupees (approximately R4.5 million) (The Central Government, 2020, pp. 46-47).

India also adopted the "significant economic presence" test to tax the digital economy as was proposed in Action 1. The India Finance Act of 2020 (Ministry of Law and Justice, 2020, p. 12) stated that from the 1st day of April 2022 this provision would be applicable. Section 9 of the Income Tax Act of 1961 defines "significant economic presence" as "a transaction in respect of any goods, services or property performed by a foreigner in India including the download of data or software which will be subject to a payment threshold or the continuous or systematic soliciting of business undertakings or engaging in the interaction with the number of users in India via digital means" (Ministry of Law and Justice, 2020, p. 12).

3.2 PAKISTAN'S APPROACH TO TAXING THE DIGITAL ECONOMY

In 2018, Pakistan published its Finance Act of 2018 (Pakistan's Finance Act of 2018) that came into force on the 1st of July 2018, providing for a withholding tax on offshore "digital

services" (Government of Pakistan, 2018, p. 461). Section 8(1) of the Pakistan Finance Act of 2018 states that the Income Tax Act of 2001 would be amended to include Clause 22B which provides that a "fee for 'offshore digital service' means any consideration for providing or rendering services by a non-resident person for online advertising including digital advertising space, designing, creating, hosting or maintenance of websites, digital or cyber space for websites, advertising, e-mails, online computing, blogs, online content and online data, providing any facility or service for uploading, storing or distribution of digital content, including digital text, digital audio or digital video, online collection or processing of data related to users in Pakistan, any facility for online sale of goods or services or any other online facility" (Government of Pakistan, 2018, p. 461).

The Pakistan Finance Act of 2018 explains how the fee on the "digital offshore services" will apply in Section 8(19). In terms of Clause 12A that was included in the Income Tax Act of 2001, the fee for "offshore digital services" is deemed as source income if it is "paid by a resident person, except where the fee is payable in respect of services utilised in a business carried on by the resident outside Pakistan through a permanent establishment" or "borne by a permanent establishment in Pakistan of a non-resident person" (Government of Pakistan, 2018, p. 467). Section 8(36) of the Pakistan Finance Act of 2018 indicates that Clause 1C will allow banking or financial institutions to deduct the fee on offshore digital services that remit payments outside Pakistan on behalf of a resident or a PE of a non-resident in Pakistan (Government of Pakistan, 2018, p. 480). Division III of the Pakistan Finance Act of 2018 indicates that the gross amount earned on "offshore digital services" will be subject to a levy of 5% (Government of Pakistan, 2018, p. 494).

3.3 NIGERIA'S APPROACH TO TAXING THE DIGITAL ECONOMY

The enactment of the Nigeria Finance Act of 2019 on the 14th of January 2020 introduced a provision that creates a "taxable presence" for a foreign company that is in the business of carrying digital activities (Federal Republic of Nigeria (a), 2020, p. A4). This provision is included as a key amendment to section 13(2) of the Corporate Income Tax of Nigeria (CITA) which is meant to be aligned to the international digital taxation doctrine of "significant economic presence" (Federal Republic of Nigeria (a), 2020, p. A4). Paragraph (c) of section 13(2) was modified to subject a foreign company to tax on its profits where these profits are deemed to be derived in Nigeria where it "transmits, emits or receives

signals, sounds, messages, images or data of any kind by cable, radio, electromagnetic systems or any other electronic or wireless apparatus to Nigeria in respect of any activity, including electronic commerce, application store, high frequency trading, electronic data storage, online adverts, participative network platform, online payments and so on, to the extent that the company has significant economic presence in Nigeria and profit can be attributable to such activity" (Federal Republic of Nigeria (a), 2020, p. A4). The Nigeria Finance Act of 2019 does not provide a definition of what constitutes "significant economic presence" (Federal Republic of Nigeria (a), 2020, p. A5). However, Paragraph of 4 section 13 includes CITA that provides that "the Minister may by order, determine what constitutes the 'significant economic presence' of a company other than a Nigerian company" (Federal Republic of Nigeria (a), 2020, p. A5).

During 2020, the Nigerian Minister of Finance issued a "Companies Income Tax (Significant Economic Presence) Order, 2020 (the Order)" which would be effective from 3 February 2020 that would assist in clarifying the concept of "significant economic presence" (Federal Republic of Nigeria (b), 2020, p. B115). According to Paragraph 1(1) of this order, it provides that a foreign company would be deemed to have "significant economic presence" in Nigeria for any financial year where it generates gross turnover or income of more than ₦25 million from "any or the combination of streaming or downloading services to persons in Nigeria or transmitting data to Nigerian users which has been generated from activities on a website or mobile application, providing goods or services directly or indirectly through a digital platform to Nigeria, or providing intermediation services through a digital platform linking suppliers and customers in Nigeria" (Federal Republic of Nigeria (b), 2020, p. B113). The paragraph further explains that a foreign company will be deemed to have a "significant economic presence" in Nigeria if that business "uses a local domain name or registers a website address in Nigeria; or has a purposeful and sustained interaction with persons in Nigeria through a digital page or platform that targets persons in Nigeria, including pricing products in Naira or providing billing or payment options in Naira" (Federal Republic of Nigeria (b), 2020, p. B113). Non-resident companies that fall within the ambit of this scope will be subject to a corporate income tax rate of 30% on the income earned on rendering of such digital services (Federal Republic of Nigeria (a), 2020, p. A4).

3.4 CONCERNS ABOUT THE APPROACHES IN INDIA, PAKISTAN AND NIGERIA

One of the main concerns with the "equalisation levy" that was introduced in India, is that that same revenues earned would be subject to corporate income tax and this levy. This would result in a situation where a non-resident suppler is subject to this tax at source and to the income tax in its country of residence, or the foreign supplier is subject to both the levy and income tax of the source country (OECD (a), 2015, p. 117). As mentioned in Part 2 of the study, when the USA issued the USTR Federal Notice which initiated Section 302(b)(1)(A) of the Trade Act of 1974 investigations on the DST provisions of other countries, India was amongst the countries investigated (United States Trade Representative, 2020, pp. 4-5). These investigations focused on the key concerns that the "equalisation levy" raises. These include: discrimination to the taxpayer, possible divergence from key international tax regimes and the economic effects it will have on the commercial success of digital companies that are subject to this "equalisation levy" (United States Trade Representative, 2020, p. 5).

The Pakistan withholding tax on "offshore digital services" raises a concern that the imposition of a standalone gross-basis final withholding tax on non-resident suppliers of offshore digital services has the probability to raise significant conflicts with trade obligations (OECD (a), 2015, p. 115). Trade obligations may deviate depending on whether or not a particular digital transaction occurs, because this tax on digital services, namely the General Agreement on Trade in Services (GATS) would apply. This agreement generally requires a non-resident supplier of services to be taxed no less favourably than domestic suppliers (World Trade Organization, 2005, p. 298; OECD (a), 2015, p. 115). The Asia Internet Coalition Council drafted a letter to the Minister of Pakistan that addressed the challenges present with implementing the withholding tax on "offshore digital services" (Asia Internet Coalition Council, 2019, p. 3). One of the main issues that was raised is that digital services present challenges in distinguishing territorial boundaries on the provision of such services, especially when these services are provided by or to a "trans-provincial entity". In addition, there is no adequate safeguard in Pakistan's current withholding tax regime to prevent imposition of sales tax by multiple provisions or territories to a specific single transaction (Asia Internet Coalition Council, 2019, p. 3). For example, if an advertising space is sold to a reseller (located in a province of Pakistan) and it is further sold to a customer located in a different province to the reseller, the single transaction will

be taxable in both provincial states which increases the overall tax liability of such a service (Asia Internet Coalition Council, 2019, p. 3). This imposition of multiple taxes on a single digital service will increase the cost of digital services available in the local market which will significantly hinder the success of a local digital company in the global technology market (Asia Internet Coalition Council, 2019, p. 3).

The Order that was issued by Nigeria's Minister of Finance introducing the "significant economic presence" provision presents challenges in attempting to resolve the taxable nexus issue. One of the main concerns is the practicality of the profit allocation rules and tax treaty impacts it will have on the treaties that Nigeria is a party to that were established on the basis of traditional concepts of physical presence (Nwodo & Omoniyi, 2020, p. 2). This concern would also apply to India's "significant economic presence" rules. The "significant economic presence" creates a greater level of uncertainty for taxpayers and tax administrators and raises a number of practical issues that have not necessarily been dealt with. Firstly, the "significant economic presence" rule does not provide any formula or guidelines on how profits would be attributable to a specific foreign company. In determining the revenue attributable to "significant economic presence", the attribution of profits is a crucial element in developing a nexus based on "significant economic presence". Considerations must be given to possible changes to profit attribution rules that would apply to the "significant economic presence", while ensuring the fair taxation treatment to foreign companies with "physical presence" and those that do not have such presence (OECD (a), 2015, p. 111). Secondly, this issue has an impact on DTA's that were entered into prior to the enactment of this "significant economic presence". The allocation principles established in Article 7 and 9 of the OECD Model Tax Convention and the United Nations Model Tax Convention are based on a taxable nexus that is created through a PE or a "fixed base" (OECD (b), 2019, p. 8). Therefore, if a non-resident qualified for this "significant economic presence' regime the current treaty provisions would override this rule because a Source state would only receive taxing right for the business profits of a non-resident company if there is a taxable nexus which is established by means of having a "physical presence" (OECD (a), 2017, p. 33). Due to the lack of guidance, it would be difficult to enforce compliance without an international consensus with other jurisdictions. In addition these provisions are particularity contradictory to the OECD's principles when it comes to enacting a good tax policy, which are "neutrality,

efficiency, certainty and simplicity, effectiveness and fairness, and flexibility" (OECD, 2014, p. 63; Choudhury & Petrin, 2019, p. 347).

4 OECD'S CONTRIBUTIONS TO DRIVE A CONSENSUS BASED SOLUTION

4.1 OVERVIEW OF WORK DONE BY THE OECD

As alluded to above, Action 1 of the OECD BEPS Report provided guidance on taxing the digital economy. Action 1 proposed provisions that could be in place to assist with taxing the digital economy, but they were not agreed upon. In 2018, the OECD issued an Interim Report on the "Tax Challenges arising from Digitalisation" with an extensive analysis of a few interim measures that were introduced by various countries to protect their tax base (OECD, 2018, p. 134). Most countries opted to propose or implement interim measures which included alternative applications of PE thresholds, withholding taxes, turnover taxes and specialised laws for targeting large multinational digital business (OECD, 2018, p. 134). The member countries of the OECD Inclusive Framework did not reach a conclusion on the analysis performed in the Interim Report. The plan was to continue to work towards delivering a final report in 2020 that provides a long-term solution to the digital economy conundrum with an update in 2019 (OECD (a), 2019, p. 6).

The OECD issued a Policy Note for "Addressing the Tax Challenges of the Digitalisation of the Economy" on the 23rd of January 2019, whereby the OECD Inclusive Framework agreed to review and develop proposals for taxing the digital economy which were grouped into two pillars. Pillar One focuses on the allocation of taxing rights and attempts to undertake a coherent review of nexus and profit allocation rules. Pillar Two focuses on remaining BEPS issues and to develop rules where jurisdictions have the right to "tax back" where other countries have not exercised their principal taxing rights (OECD (a), 2019, p. 6). The focus of this study is on Pillar One.

4.2 PILLAR ONE

The 2019 OECD Policy Note proposed the following options for taxing the digital economy: "user participation", "marketing intangibles" and "significant economic presence" (OECD (a), 2019, p. 11). The character of the relocation of taxing rights differs amongst these three approaches.

- The "user participation" is a doctrine that attempts to correlate taxation with the presence and activities of the users of digital services in a tax jurisdiction (OECD (b), 2019, pp. 9-11; Schön, 2019, p. 1004).
- The concept of "significant economic presence" aims to amend the PE threshold and to ultimately allocate profits to market countries based on a formula (OECD (a), 2015, p. 107; Schön, 2019, p. 1006).
- A "marketing intangible" as defined in the "OECD Transfer Pricing Guidelines for Multinationals of July 2017" (OECD Guidelines) is "an intangible (within the meaning of Paragraph 6.6 of the OECD Guidelines) that relates to marketing activities, aids in the commercial exploitation of a product or service and/or has an important promotional value for the product concerned" (OECD (b), 2017, p. 27). According to this concept it is argued that intangible assets are a key contributor to the value creation and economic enhancements for multinationals in the digital economy (OECD (a), 2015, p. 65).

This Policy Note indicated that the above proposed solutions would go beyond the "arm's length principle". The core principles of taxing rights in international taxation are profit allocation and nexus (OECD (b), 2019, p. 4). Later on in the year, the OECD issued a "Programme of Work to Develop a Consensus Based Solution to the Tax Challenges Arising from the Digitalisation of the Economy" (Programme of Work), which recognised the commonalities between the three proposals which were introduced to the TFDE to facilitate a the global based solution (OECD (b), 2019, p. 4). The Programme of Work highlighted the fact that without a bridge between these three proposals it would be virtually impossible to develop a globally consented approach to tax the digital economy (OECD (b), 2019, p. 4).

The key features of Pillar One that need to be addressed are the scope, the new nexus and the new profit allocation rule to reach a consensus based solution (OECD (b), 2019, p. 5). The allocation of the new taxing right to a market country through the new nexus and profit attribution rules would enable a market jurisdiction to tax a business that interacts

with its customers (users) in that country and creates a substantial amount of economic value without a traditional "physical presence" within that country (OECD (b), 2019, p. 7). These types of features would be most relevant for a digital business that remotely interacts with its users, collects and exploits data and drives marketing and branding from a remote location through the use of technology to develop this customer base (OECD (b), 2019, p. 7). This anchors that the ideology of the "Unified Approach" should focus on large consumer facing business that provides digital goods and services to its consumers which would carve out certain industries (i.e. commodities and extractive business activities). A further step would be to articulate the "business within scope" requirement to exclude intermediates and businesses operating in the financial sector (OECD (b), 2019, p. 7).

According to the current international tax rules, a foreign company's profits are taxable within that jurisdiction if that foreign company has a PE which means having some form of a "physical presence". However, as discussed earlier, digitalisation has nullified the applicability of this rule, especially for "digital centric" businesses (OECD (b), 2019, p. 7). The new nexus rule would essentially address this issue by becoming applicable to businesses that have a "sustained and significant involvement" in a market country's economy through consumer interaction irrespective of "physical presence" in that jurisdiction (OECD (b), 2019, p. 8). The OECD proposed that the best way to operate this rule would be to define a revenue threshold (depending on the market size) as a primary indicator for determining "sustained and significant involvement" of a business within scope in a market jurisdiction (OECD (b), 2019, p. 8). This revenue threshold would take into consideration the type of activities performed (i.e. online advertising services) and this rule would have to be introduced as a standalone provision to prevent potential overlaps to other existing tax regimes (OECD (b), 2019, p. 8). The intention is that this revenue threshold will not only create a nexus for business models that are driven by remote sales to customers, but will also apply to group companies that tap into a market through a distributor. This will ensure neutrality between various business models that have a remote involvement in the market county's economy (OECD (b), 2019, p. 8).

Once a market country has the taxing right to the profits of a foreign business that falls within this scope, the next step would be to allocate the appropriate profits to this jurisdiction (OECD (b), 2019, p. 8). The current traditional allocation principles lie within Article 7 of the OECD Model Tax Convention and Article 7 and 9 of the United Nations

Model Tax Convention. However, those allocation rules are based on the "physical presence" concept which does not apply in the digital economy (OECD (b), 2019, p. 8). The OECD's "Unified Approach" takes this dilemma into account. It encompasses three types of mechanisms to allocate the appropriate profits that a market jurisdiction is entitled to which can be described as "Amount A", "Amount B" and "Amount C":

- "Amount A" – is a share of "residual profit" that would be allocated in the market jurisdiction by applying a formula to the MNE business line or group level. This new taxing right would apply regardless of the existence of "physical presence," especially in the context of digital services (OECD (b), 2019, p. 12; OECD, 2020, p. 8). It would reflect the revenue associated with the active and consistent participation of an enterprise in the economy of the specific market jurisdiction through remotely directed or direct activities in the particular country. Therefore, this constitutes the prime response of the "Unified Approach" to the tax challenges associated with the digital economy (OECD (b), 2019, p. 12; OECD, 2020, p. 8).
- "Amount B" – is a fixed remuneration based on the "arm's length principle" for the defined baseline marketing and distribution function that takes place in a market jurisdiction (OECD (b), 2019, p. 9; OECD, 2020, p. 8).
- "Amount C" – is the return that covers any excess profit where in-country functions exceed the baseline remuneration of "Amount B" (OECD (b), 2019, p. 12; OECD, 2020, p. 8). "Amount C" gives emphasis to the need for an improved dispute resolution process (OECD (b), 2019, p. 12; OECD, 2020, p. 8). Nonetheless, the scope of "Amount C" is still under discussion, as it's a crucial element in reaching an overall consensus on the "Unified Approach" under Pillar One (OECD (b), 2019, p. 12; OECD, 2020, p. 8).

From the above, "Amount A" has received a greater response due to the fact that it introduces a new taxing right, whereas "Amount B" and "Amount C" are existing allocation rules within the international tax spectrum (OECD, 2020, p. 8). The "Amount A" approach is limited to MNEs that meet the new nexus test, where a market jurisdiction is concerned and the portion of income that should be attributed to that particular jurisdiction (OECD, 2020, p. 8). These aspects need to be designed in a simple way that prevents double taxation and is aligned to the "arm's length principle" with the presentation of "Amount B" and "Amount C" (OECD, 2020, pp. 8-9). "Amount A" is rooted from the idea that taxing

profits cannot be bound by “physical presence” rules, but rather following allocable business activities such as baseline marketing and distribution (OECD, 2020, p. 9). The policy issue impacts on businesses that can benefit with or without local “physical presence” and that can sustain a significant manner in the economy in a market jurisdiction (OECD, 2020, p. 9). These are businesses that provide automated digital services to a large and/or a global user base, exploit powerful users and customer networks that generate a substantial amount of value from their interaction with customers and users, utilising intensive monitoring of users’ activity and capitalising on the corresponding data (OECD, 2020, pp. 9-10). This is also relevant for other enterprises that generate profits from selling goods or services; whether it is done directly or indirectly which is mainly consumer facing business that sells connected products using online platforms as a way to sell and market to customers (OECD, 2020, p. 10). This now shines new light on “consumer facing” and highly digitalised businesses, however there is a debate that most enterprises across all industries are leveraging on new technologies to no longer rely on “physical presence” for serving customers and the dichotomy between “consumer facing” versus “business to business” models are a few crucial factors that need to be considered as the global consensus is evolving (OECD, 2020, p. 10).

There are concerns over double taxation since this approach follows a three-tier approach but “Amount A” is only concerned with the residual profit of an MNE and “Amount B” is only designed to remunerate the market country with a fixed line for distribution and marketing activities and there will not be an overlap (OECD, 2020, p. 16). The issue would be the overlap between “Amount A” and “Amount C”. This overlap will only occur if the MNE falls within the “Amount A” scope and has a transfer pricing re-assessment (OECD, 2020, p. 16). For instance, the transfer pricing re-assessment would significantly change the profitability of different entities, which have been used to identify the entities that would have to pay “Amount A”. To ensure that these entities receive relief from double taxation, further work needs to be done to address any discrepancies (OECD, 2020, p. 16).

A few concerns have been raised by the OECD Inclusive Framework itself. Implementing this approach would require amendments to the domestic legislation and tax treaties (OECD, 2020, p. 19). This would entail a new multilateral convention that requires negotiation to establish a modified multilateral solution that will regulate companies that fall “in-scope” of the “Amount A” presented thresholds (OECD, 2020, pp. 19-20). This would

ensure that all jurisdictions apply this “Unified Approach” on a consistent and sustainable basis. The outcome of a true multilateral convention postulates strong backing at the highest government level to achieve acceptability from most jurisdictions (OECD, 2020, p. 20). The implementation of the “Unified Approach” should also be contingent upon the acceptance of new disputes and resolutions, especially where “Amount A” and “Amount C” may overlap (OECD, 2020, p. 20). In principle, the “Unified Approach” under Pillar One seeks to amend the historical interpretation of the PE through these new nexus and profit allocation rules, especially in the application of international tax agreements for taxing business income for source and market countries (OECD, 2020, p. 20).

5 SOUTH AFRICA’S REACTION TO THE OECD’S WORK ON THE TAXATION OF THE DIGITAL ECONOMY

5.1 SOUTH AFRICA’S BACKGROUND WITH THE OECD

During May 2007, the OECD member countries agreed to invite non-OECD member countries to an open discussion of the organisation’s membership and offer enhanced engagement with a possibility of membership to Brazil, China, India, Indonesia and South Africa (OECD, 2008, p. 8; OECD (c), 2017, p. 18). Following that discussion, the OECD Council at ministerial level introduced a resolution which led to South Africa becoming one of its “Key Partners” to contribute to the OECD’s work in a comprehensive and sustainable manner (OECD, 2008, p. 74). South Africa become the 37th country to ratify the OECD’s Convention in 2007 (OECD, 2008, p. 64) and is now a part of the OECD’s Development Centre (DEV) which is a programme that allows for policy makers to share expertise that contributes to the growth and sustainability of developing and emerging economies (OECD, 2008, p. 104).

South Africa participates in approximately 21 OECD bodies and projects. It has adhered to 19 legal instruments and consistently participates in the OECD initiatives (OECD (c), 2017, p. 18). South Africa, as Vice Co-chair, has continuously contributed to the work of the “NEPAD-OECD Africa Investment Initiative”; the activities of the “Southern African Development Community (SADC) Regional Investment Policy Framework” Project, and the “OECD African Development Bank (AfDB) Initiative” which combats bribery efforts by supporting business integrity in Africa (OECD (c), 2017, p. 17). South Africa is an

Associate in the BEPS Project and a crucial and active member of the OECD Inclusive Framework on BEPS by contributing its own perspectives to the BEPS process, as well as championing the efforts of developing countries to provide input through the ATAF (OECD (c), 2017, pp. 13-14). Furthermore, South Africa benefits from the OECD's expertise in policy analytics and advice through its active participation in the OECD projects which includes regular qualification excises through the G20 umbrella that entails an impact analysis on policy reforms within the country (OECD (c), 2017, p. 19). As a member of the G20, South Africa was part of the G20 Finance Minister's Meeting that was held in March of 2017, which initiated the acceleration for the OECD Inclusive Framework working through its TFDE for the 2018 Interim Report on the "Tax Challenges arising from Digitalisation" to be released. This included an in-depth analysis of the evolution of business models and implications of the international tax system (OECD, 2020, p. 6). Even though the 2018 Interim Report has similar conclusions to Action 1 about not being able to reach a global based consensus, it was agreed that further work was required in the development of reaching a long term consensus based solution (OECD, 2020, p. 6).

5.2 OVERVIEW OF SOUTH AFRICA'S APPROACH ON TAXING THE DIGITAL ECONOMY

The Action 1 Report, as indicated above, set out indirect and direct tax recommendations for taxing the digital economy. As a developing country, South Africa was in favour of the International VAT/GST Guidelines and implementation modified collection mechanisms on cross border transactions, especially those between business and customers (OECD (a), 2015, p. 13). South Africa implemented the OECD's suggestion to apply the modification of International VAT/GST Guidelines and implementation by revising collection mechanisms on international transactions, especially those between business and customers (OECD (a), 2015, p. 13). The South African government published "Regulations Prescribing Electronic Services for the purpose of the definition of 'electronic services' in Section 1(1) of the VAT Act, 1991 in terms of Government Notice No.R221 in Government Gazette No. 37489" (VAT Regulations) on the 24th of March 2014, which altered the way that specific imported "electronic services" were taxed (National Treasury, 2014, pp. 3-6). This provision shifted the onus of the VAT from the in-country recipient to the supplier of "electronic services" that is located in an export country which came into effect on the 1st of June 2014 (National Treasury, 2014, p. 7; National Treasury, 2014, p. 4). Fast-forward to

2018 where new VAT Regulations were released to widen the scope of "electronic services" to apply to all "services" as defined in the VAT Act No. 89 of 1991 (the VAT Act) that are provided by means of an "electronic agent, electronic communication or the internet for any consideration" (National Treasury, 2018, p. 5). The policy's intention was to mitigate the risk of distortions in trade between non-resident suppliers and local suppliers where VAT is one of the reasons for such distortions (National Treasury, 2018, p. 5). As indicated above, this work does not focus on the VAT matters but on the direct tax matters. It was also indicated in Part 1 above that the introduction of the VAT on "electronic services" does not protect the country's income tax base, as it can still be eroded due to the fact that South Africa is predominantly a market jurisdiction that faces the impact of BEPS (Li, 2018, p. 480).

With regard to direct taxes, the discussion above has shown that Action 1 set out options for taxing the digital economy, but they were not agreed upon by the international community (OECD (a), 2015, p. 13; Latif, 2019, p. 104). However, both developed and developing countries went ahead and enacted unilateral measures. Fellow developing countries such as India, Pakistan and Nigeria enacted an "equalisation levy", a "withholding tax on offshore digital services" and the "significant economic presence" principles (respectively) into their domestic law. However, South Africa did not introduce such measures.

Some of the disadvantages of introducing such measures as discussed in Part 3 above are that they would not only be in conflict with tax treaty principles, but they have the potential to negatively impact foreign investment (Davies, et al., 2010, p. 24). Tax treaties foster the probability of investment whilst having the ability to reduce the likelihood of investments if the tax regimes in a country are stringent (Davies, et al., 2010, p. 24). South Africa's approach during this time seems to be aimed at focusing on targeting the consumers of this economy, rather than focusing on taxing the value created, which the US, the UK and France have done (Latif, 2019, p. 105).

South Africa's policy on taxing the digital economy is also relevant to the international agreements which it has signed. South Africa is a party to the Council of Europe/OECD Multilateral Convention for Mutual Administrative Assistance in Tax Matters. It is also a member of the ATAF and has entered into a multilateral ATAF agreement with various

African countries for mutual assistance in tax issues and effective exchange of information between the revenue authorities and member states (SARS and National Treasury, 2014, p. 64). These agreements fall within the ambit of section 231(2) of the Constitution of the Republic of South Africa Act of 1996, in conjunction with section 108 of the South African Income Tax Act No 58 of 1962 which basically means that all international agreements are binding on South Africa once they are approved by Parliament (SARS and National Treasury, 2014, p. 67). South Africa's association with these organisations is a crucial element to determine where it stands with respect to the taxation of the digital economy. Therefore also reviewing the ATAF's response to the work done by the OECD can provide greater clarity on South Africa's perspective on taxing the digital economy.

The ATAF agrees with the OECD Inclusive Framework that fundamental changes need to be made to the core principle of international tax rules which is the nexus and profit allocation rules that determine how MNE's global revenues are allocated between jurisdictions (African Tax Administration Forum (a), 2019, p. 2). In January 2019, South Africa hosted the OECD, the United Nations (UN) Committee and the European Union (EU) to discuss the work conducted by the OECD Inclusive Framework proposals (African Tax Administration Forum (a), 2019, p. 2) and to emphasise that the proposed revision of the current international tax rules must significantly reduce the complex nature of the current nexus and profit allocation rules which hinder the efforts by the tax administrators and impair tax certainty for African corporate taxpayers and governments (African Tax Administration Forum (a), 2019, p. 4). The ATAF is of the view that BEPS outcomes do adequately address the risks for Africa to effectively protect its tax base from "artificial profit shifting" (African Tax Administration Forum (a), 2019, p. 5). Therefore the ATAF considers that work should be done to prevent "artificial profit shifting" and should focus on addressing base eroding payments that reduce a source country's right to tax (African Tax Administration Forum (a), 2019, p. 5). The ATAF believes that the Two Pillar approach should be anchored by this fundamental principle in order to achieve an equalised consensus based approach (African Tax Administration Forum (a), 2019, p. 5).

In May 2019, the ATAF and several African countries (including South Africa) participated in an OECD Inclusive Framework meeting to bridge the gaps between the proposals set out in the Public Consultation Document (African Tax Administration Forum (b), 2019, p. 2). In July 2019, the ATAF's Cross Border Taxation Technical Committee (CBT) and the

OECD held a technical discussion about the OECD's Programme of Work and how a consensus based approach could suit the needs of the African countries (African Tax Administration Forum (b), 2019, p. 2). This discussion gave rise to two critical points: one is that the new nexus rules need to be created in such a way that the value created by "user participation" is taxable in the market jurisdiction which requires domestic legalisation and tax treaties to be amended (African Tax Administration Forum (b), 2019, p. 2). The other one is that new profit allocation rules would need to reflect the value created for an MNE in a market country that is obtained through active and sustained participation of users, which is a key component of value creation for a highly digitalised company (African Tax Administration Forum (b), 2019, p. 3).

Further discussions were held on the 30th of September – 1st of October 2019 regarding the consensus based approach on taxing the digital economy. The ATAF agreed with the new nexus approach, but it indicated that the threshold must be country specific and be adjusted to the economic scale of that specific jurisdiction to ensure that smaller economies receive an appropriate allocation of taxing rights. The ATAF also indicated that measures should be in place to mitigate the risk of double taxation where high thresholds could lead to excluded jurisdictions taxing under "arm length principals" that have been already allocated under these new profit allocation rules (African Tax Administration Forum (c), 2019, p. 2). The ATAF noted that the distribution based approach under the new profit allocation rules would allow for a guaranteed fixed return for routine marketing and distribution activities within a market country, which would address the majority of transfer pricing disputes taking place in Africa over the appropriateness of the routine return achieved for marketing and distribution functions under the "arm's length principle" (African Tax Administration Forum (c), 2019, p. 2). The ATAF considers the inclusion of a fixed minimum return rule for such activities a high priority for African countries (African Tax Administration Forum (c), 2019, p. 2). The ATAF also supports the proposal to develop allocation rules that allow market jurisdictions to have the taxing rule to non-routine profits, but the determination of this non-routine return must be fairly apportioned to the marketing intangibles that the market country is contributing, as it is the ATAF's view that transfer pricing rules substantially undervalue the contribution of a market country to the MNE's profit (African Tax Administration Forum (c), 2019, pp. 2-3).

In January 2020, the ATAF held a meeting where it discussed its further views on the Pillar One proposal (African Tax Administration Forum, 2020, p. 2). In 2020, ATAF issued its technical note on the subject matter and the main concern is the application of the "Amount A" in scope businesses concept (African Tax Administration Forum, 2020, p. 2). ATAF is concerned that this concept may lead to more disputes due to its complexity, for example regarding how to distinguish between "automated digital services" or "consumer facing business" (African Tax Administration Forum, 2020, p. 6). There is also a concern that this "digital differentiation" does not accord with the previous OECD reports, as digital business will still be taxed differently to scope businesses (African Tax Administration Forum, 2020, p. 6). The ATAF is in favour of "Amount B's" "fixed minimum return rule," but it requires a clear definition of what is defined as "routine marketing and distribution activities" (African Tax Administration Forum, 2020, p. 7).

The ultimate concern for the ATAF is that the introduction of the "Unified Approach" under Pillar One should not decrease the prospects of foreign direct investments in Africa when "global consensus" is reached.

6 RECOMMENDATIONS AND CONCLUSION

From 2007 South Africa become a "Key Partner" to the OECD, which allowed South Africa to actively contribute to the work done by the OECD in a sustained and comprehensive manner through its various bodies (OECD (c), 2017, p. 18). South Africa has managed to increase its eminence in the OECD by becoming one of its most active "Key Partners" (OECD (c), 2017, p. 18) through its investment in the OECD's bodies and policies. South Africa has already been involved in the work conducted in the Action 1 Report that provided guidance on taxing the digital economy (Olbert & Spengel, 2017, p. 3). The OECD recommended that countries could adopt these proposals at domestic level if they honoured existing treaty obligations or bilateral tax treaties. However, the adaptation of domestic law measures would require consideration to ensure consistency with existing international legal commitments (OECD (a), 2015, p. 148).

During the course of 2020, the US's withdrawal from the international negotiations of Pillar One has caused a great concern in the international tax world. This withdrawal from the US is seen as a collective failure in the global attempt to prevent the erosion of tax by

large multinationals. The economy is becoming more and more digitalised and the longer it takes to reach a multilateral consensus, the longer large multilaterals remain with power to manipulate the traditional principles of international rules (Ministere De L'Economie et des Finances, Ministerio de Hacieda, Ministero dell'Economia e delle Finance & HM Treasury, 2020, p. 1). The Ministers of France, Italy, Spain and the UK responded to the US Secretary's letter that was released on the 12th of June of 2020, expressing disappointment in the US's decision to pull out of the discussions of Pillar One to reach a global consensus. However, it was indicated that the OECD and the G20 will carry on with their ambition of reaching a global consensus at the end of 2020 (Ministere De L'Economie et des Finances, Ministerio de Hacieda, Ministero dell'Economia e delle Finance & HM Treasury, 2020, p. 2). This objective has the potential of not being reached as this multilateral consensus requires all parties involved to participate.

In the absence of a consensus being reached, a number of countries enacted unilateral measures in order to protect their tax base (OECD, 2018, p. 212). From a direct tax perspective South Africa did not follow the approach of implementing unilateral measures, but rather pressed for the agenda by participating in the OECD Inclusive Framework meeting to bridge the gaps between the proposals set out in the Public Consultation Document and allowing for a Programme of Work to be in place (African Tax Administration Forum (b), 2019, p. 2). The OECD Inclusive Framework is continuing to work towards delivering a final report in 2020 that provides a long-term solution to the taxation of the digital economy (OECD (a), 2019, p. 6). South Africa has shown a considerable amount of investment in its relationship with the OECD and the ATAF. It is actively involved in hosting meetings pre and post the release of the OECD's policy documents by expressing its concerns with the OECD Inclusive Framework's proposals and their effect on developing countries in Southern Africa through the ATAF Technical notes (African Tax Administration Forum, 2020, p. 6).

Even though developing countries like India, Pakistan and Nigeria have decided to have temporary measure(s) in place to protect their tax base, South Africa has not adopted any unilateral measures. South Africa appears to have taken a risk-averse approach in dealing with the tax challenges of the digital economy by not introducing unilateral measures in an effort to afford the risk of discouraging foreign investment.

As discussed in Parts 2 and 3, the unilateral measures taken by the various countries have caused retaliations by trade partners. In addition, they have caused impractical implementation issues and created greater uncertainty which is contradictory to South Africa's fiscal objectives. These objectives are to prioritise Africa's industrialisation; pursue market development integration, maintain trade and investment relations with developed economies; open trade relations with more countries and strengthen the macroeconomic framework to deliver certainty (Department of Trade and Industry – Republic of South Africa, 2019, p. 4; National Treasury, 2020, p. 8).

This study affirms that the approach that South Africa has followed to tax the digital economy is the correct approach. Implementing temporary direct tax legislation to tax the digital economy would not be practical. By the time a unilateral measure is enacted in law a "global consensus" could be reached. What South Africa could do in the interim to protect its source tax base is to adopt the recommendation of the Davis Tax Committee to strengthen its source taxation rules (Davis Tax Committee (b), 2015, p. 4). Even if these rules are not that effective, they could at least preserve some taxing rights. Strengthening these rules would not go against South Africa's tax and trade treaty obligations such as the US's reaction to the UK and French DST and the Indian "equalisation levy". Strengthening source rules would also help prevent the uncertainty caused by the Indian and Nigerian "significant economic presence" and the US' GITLI and BEAT provisions and reduce possible drawbacks of the Pakistan withholding tax regime. These unilateral provisions can harm the trade relationships with other countries which will have a negative effect on the overall economy.

The Davis Tax Committee recommended that South Africa needs to adopt the OECD's recommendations because taxing of the digital economy is an international tax matter (Davis Tax Committee (b), 2015, p. 4). In order to enable South Africa to impose tax on foreign suppliers of digital services, new source rules would have to be implemented (Davis Tax Committee (b), 2015, p. 4). The existing scope of the "source rules" included in Section 9 of the South African Income Tax Act No. 58 of 1962 would need to be extended to cover proceeds generated from the supply of digital services that are originated from a source in South Africa (Davis Tax Committee (b), 2015, p. 4). The Davis Tax Committee recommended that practically this new tax rule could be implemented based on a payer principle. This would enable the tax administrator to track where the digital service is

sourced by a resident who is “physically present” in a jurisdiction (i.e. South Africa) at the time of the supply (Davis Tax Committee (b), 2015, p. 4). Enacting these rules could be a starting point from which South Africa can apply the proposals of the OECD from a direct income tax perspective and level the playing field between local and foreign suppliers of e-commerce services (Davis Tax Committee (b), 2015, p. 4).

These recommendations do not necessarily address the tax challenges of the digital economy but they would preserve the tax base of South Africa, which is ostensibly more at risk than its other OECD counterparts (Thaci and Gerxhaliu, 2018, p. 215; Li, 2018, p. 482). This way, South Africa would protect its fiscus as a developing country whilst embracing the evolution of the digital economy by its participation in the “globalisation of a tax policy” with international organisations (Li, 2018, p. 480), so as to ensure that its interest as a source and market jurisdiction are protected until a “global consensus” is reached.

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