

**THE APPROACH OF THE ORGANISATION FOR ECONOMIC CO-
OPERATION AND DEVELOPMENT TO THE CHALLENGES OF
INTERNATIONAL DIGITAL TAXATION AND DISPUTE RESOLUTION**

by

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SUMMARY

The world's economy has shifted and evolved in such a manner that embraces and largely relies on the use and application of technology. This imputes a duty on each country and the worldwide regulatory bodies to implement legislative measures which are designed to control the digital implications of the economy and ensure equal applications of such regulations.

In order to effectively regulate the advent of the digital economic system, the world's recognised international regulatory body has proposed a number of solutions relating to the taxation of digital economic activities. These solutions are to be applied and adopted to countries that voluntarily undertake to be bound by them. This raises a number of concerns relating to the uniformity of tax regulations internationally, as well as the resolution of tax disputes that may arise from lack of uniform interpretation of the concerned regulations.

This dissertation analyses the proposed solutions to digital taxation by the OECD, paying attention to the responses to those solutions from the EU and SADC region with a particular focus on South Africa. It also explores dispute resolution mechanisms proposed by the OECD in their application to digital taxation and the digital economy. These are intended to ascertain the potential effectiveness of the solutions in a world that does not have a set international tax adjudicating body and/or tax authority.

The SADC has thus far made no attempt to address the implications of digital taxation which raises concerns as it is a recognised fact that African countries' economies are largely reliant on taxes. As such, focus is paid to any other solutions that may assist the SADC region in order to propose solutions that can be of benefit to its member countries.

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ACRONYMS

ALP	Arms-Length Principle
APA	Advance Pricing Agreement
ATAF	Africa Tax Administration Forum
B2C	Business-to-customer
BEPS	Base Erosion and Profit Shifting
BIAC	Business at OECD
DTA	Double Tax Agreement
DTC	Davis Tax Committee
EU	European Union
FTA	Forum on Tax Administration
GST	Goods and Services Tax
IMF	International Monetary Fund
MAP	Mutual Agreement Procedure
MNE	Multinational Enterprise
OECD	Organisation for Economic Co-operation and Development
PE	Permanent Establishment
SADC	Southern African Development Committee
SARS	South African Revenue Services
TFDE	Task Force on the Digital Economy
U.N	United Nations
UNCTD	United Nations Centre for Trade and Development
VAT	Value-Added Tax

TABLE OF CONTENTS

Plagiarism policy.....	i
SUMMARY.....	ii
Declaration of originality	iii
Acronyms	iv
Chapter ONE – An Introduction to the OECD’s Approach to the challenges of international digital taxation and dispute resolution	1
1.1 INTRODUCTION AND BACKGROUND TO STUDY	1
1.2 PROBLEM STATEMENT.....	3
1.3 Chapter exposition.....	4
1.3.1 Chapter Two.....	4
1.3.2 Chapter Three	4
1.3.4 Chapter Four	6
1.3.5 Chapter Five	8
1.4 RESEARCH METHODS.....	8
1.5 LIMITATIONS	8
1.6. CONCLUSION.....	9
CHAPTER TWO –The OECD’s proposed solutions to digital taxation.....	10
2.1 Introduction	10
2.2 An analysis of the OECD’s approach to problems arising from digital taxation	10
2.3 Proposed solutions – Direct digital tax challenges	12
2.3.1 Establishing a significant economic presence.....	12
2.3.2 Withholding tax on digital transactions.....	16
2.3.3 Introduction of an equalisation levy	17
2.4 Proposed solutions – Indirect digital tax challenges.....	19
2.5 Conclusion.....	23
Chapter THREE – Application of the OECD’s proposed solutions to SADC.....	25
3.1 Introduction	25
3.2 Taxation of the digital economy in developing countries – Broader direct tax challenges.....	26
3.2.1 Change in the definition of PE status and new source rules	26
3.2.2 Administration of unregistered companies	29

3.2.3 The DTC’s proposed solutions to the administrative challenges of the digital economy in South Africa	29
3.2.4 Davies Tax Committee legislative recommendations	30
3.3 Taxation of the digital economy in developing countries – Indirect tax challenges	32
3.4 Recommendations for SADC and developing countries	34
3.5 Conclusion	35
Chapter FOUR – Dispute resolution in the digital economy	37
4.1 Introduction	37
4.2 Dispute Resolution – the OECD’s position	38
4.3 Dispute resolution and digital taxation	41
4.4 Dispute resolution between jurisdictions	42
4.4.1 Dispute resolution for the taxpayer (individuals and businesses)	46
4.5 Conclusion	47
Chapter Five –The public’s response to the OECD’s proposed solutions	49
5.1 Introduction	49
5.2 General responses to the OECD’s Action 1 project.....	49
5.2.1 BEPS Monitoring Group – Comments submitted to the OECD.....	51
5.3.2 Deloitte Touche Tohmatsu Limited (Deloitte) – Comments submitted to the OECD.....	52
5.3.3 Ernst and Young (EY) – Comments submitted to the OECD.	53
5.3.4 Klynveld Peat Marwick Goerdeler (KPMG) – Comments submitted to the OECD 2017 & 2019).	54
5.3.5 Pricewaterhouse Coopers International (PwC) – Comments submitted to the OECD	55
5.3.6 The United Nations (the UN)	56
5.4 Conclusion	57
BIBLIOGRAPHY	59

CHAPTER ONE – AN INTRODUCTION TO THE OECD’S APPROACH TO THE CHALLENGES OF INTERNATIONAL DIGITAL TAXATION AND DISPUTE RESOLUTION

1.1 INTRODUCTION AND BACKGROUND TO STUDY

The advancement of digital economics is inevitable with the rapid improvement of technology on a global basis. This means that the developing digital economy needs to have an effective monitoring system with special focus being taxation.¹ The digital economy has developed rapidly such that it has become an essential part of every aspect of the economy due to its fast developing nature and the cheaper manner in which it enables businesses to be run.²

One of the main problems international tax institutions like the OECD and the UN grapple with when attempting to propose tax policies on the digital economy is the fact that the digital economy is not a stagnant practice upon which tax jurisdiction is easily ascertained.³ It is important that countries find simpler and effective solutions to the application of taxation on digital transactions within one country’s jurisdiction in a way that does not infringe another country’s taxing rights. This, if unchecked, could give rise to problems; the main problem being the application and interpretation of an operating tax treaty under which no adjudicating body exists, thus giving rise to non-effective “dispute resolution”.⁴

This dissertation will focus on the proposed solutions as outlined by the Organisation for Economic Co-operation and Development (OECD) and the application of these solutions to South Africa and the Southern African Development Community (SADC), with comparisons being drawn with the European Union (EU). All of the Base Erosion and

¹<https://taxinsights.ey.com/archive/archive-articles/tax-administration-continues-to-go-digital.aspx> accessed on 25 September 2018.

²United Nations Conference on Trade and Development [2017]. *Technical Note No.8. The New Digital Economy and Development*. Page 2.

³<https://www.nautadutilh.com/en/information-centre/news/taxation-and-the-digital-economy-european-and-international-initiatives-to-create-a-fair-tax-system> accessed on 29 June 2018.

⁴OECD [2007]. *Improving the Resolution of Tax Treaty Disputes*.

Profit Shifting (BEPS) 15 Actions are closely related to each other and it can be said that the successful implementation of the actions is dependent on one another. Thus far, the OECD has not yet made any recommendations and has instead only published proposed solutions to BEPS.⁵

The digital economy was historically prevalent in large companies but it has since spread to small enterprises.⁶ This calls for effective regulations to be implemented in the digital sector. The OECD has identified a number of problems that are associated with digital taxation which contribute largely to BEPS and acknowledges that the problems it identified are not exhaustive.⁷ There is a possibility that these problems are wider and bound to become even more so given the ever-improving and developing digital economy models within the business sector. An outline of the issues will be discussed in order to ascertain the results of the OECD's approach to the challenges of international digital taxation and dispute resolution from an international and southern African perspective.

The OECD proposed a number of solutions to BEPS in an action plan that contained 15 actions, under which each action was expected and/or designed to play a role in countering BEPS in its own way. These action plans were developed from the OECD's model tax convention, which is mostly applied to member countries in the EU and many other developed countries and not by most African countries. The action plans include addressing the tax challenges of the digital economy (Action 1) and making dispute resolution mechanisms more effective to prevent BEPS (Action 14).⁸

Chapter 7 of Action 1, Addressing Digital Tax⁹ outlines a number of proposed solutions which encompass identifying a new nexus based on the concept of significant economic presence, determining the income attributable to the significant economic presence,

⁵OECD/G20 [2019]. *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy*. Page 5.

⁶Oguttu AW *et al.* [2005] *Electronic Commerce: Challenging the Income Tax Base*. page 321.

⁷OECD/G20 [2015]. *Base Erosion and Profit Shifting Project. Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*.

⁸<http://www.oecd.org/ctp/beps-actions.htm> accessed on 13 June 2018.

⁹OECD/G20 [2015]. *Base Erosion and Profit Shifting Project. Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*.

withholding tax on digital transactions and introducing an equalisation levy.¹⁰ The OECD is of the view that the action plan proposed as Action 1 (Addressing Digital Tax) will be of particular benefit to all countries. Although they are not proposed as laws they are, however, considered to be possible solutions to digital taxation.¹¹ Developing countries cannot rely on OECD models (and now possibly solutions to BEPS) because these models are inequitable in their application.¹² This means that developing countries cannot apply OECD models and expect the same results as developed countries. This dissertation will explore the OECD's proposed solutions and their application to the EU including discerning how these have been received and applied by the countries that have implemented the recommended solutions to BEPS in the digital economy.

1.2 PROBLEM STATEMENT

This dissertation outlines the BEPS solutions proposed by the OECD from both developed and developing countries' perspectives. There are also solutions to the taxation of the digital economy for developing countries which have been proposed by African-based organisations. This dissertation will analyse the OECD's approach to digital economics and how the digital economy is most likely to lead to an unprecedented rise in international tax disputes. There will be focus on the opinions of some key entities in the OECD's tax department like Business at OECD (BIAC).

This dissertation identifies that although digital taxation has been an issue for a number of years, SADC and South Africa have paid very little attention to it. This raises non-taxation risks on a large scale, as the digital economy is fast becoming a gateway to the world's economic future.¹³

¹⁰OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 107 – 117.

¹¹*Ibid.*

¹²Rohatgi R. 2005. *Basic International Taxation*. Page 29.

¹³ OECD [2019]. *Tax and Digitalisation*.

1.3 CHAPTER EXPOSITION

Chapter One of this dissertation contains an introduction of the study. Chapter One introduces the issues that will be discussed in this dissertation as well as a brief structure of the next chapters.

1.3.1 Chapter Two

This chapter will explore the solutions that the OECD proposed in its BEPS project. Special focus will be paid to Action 1 – Addressing Digital Taxation. This chapter will also focus on how the EU has responded to the proposed solutions by introducing new tax legislation within their countries. This chapter will address the following issues and will answer them as described above:

- a) The OECD's approach to these problems – this will explore the solutions that the OECD has published.
- b) An overview of the EU's approach to BEPS.
- c) Conclusion.

1.3.2 Chapter Three

This chapter will explore the significance of the OECD's proposed solutions to digital taxation in South Africa and the SADC. Literature on the SADC's tax database¹⁴ reflect that minimum attention is paid to digital taxation in the SADC region. This chapter will also endeavour to explore how the OECD's proposed solutions will fit in with the South African and SADC tax system(s). This chapter will answer the following sub-questions:

- a) Proposed solutions for developing countries.
- b) Identify working solutions for South Africa and SADC.
- c) Consider other methods of effectively regulating the digital economy.
- d) SADC's approach to digital taxation.

¹⁴<https://www.sadc.int/themes/economic-development/investment/tax-coordination> accessed on 1 October 2018.

African countries are hesitant to follow the OECD's tax proposals for a number of reasons due to higher administrative burdens on African countries (which the OECD has promised to address).¹⁵ The United Nations (UN) has attempted to address any inequalities in the model tax conventions by publishing its own convention that is tailored for developing countries as well as developed countries.¹⁶ It is very likely that the proposed solutions could be difficult to apply to the developing countries' tax legislation and systems. It is still to be seen whether these solutions have been developed to suit the African countries' tax systems themselves. This poses an application problem for South Africa and Africa at large; an easier solution would be to tailor the provisions of the OECD in such a manner that works for South Africa's tax system without disrupting its international relations.

The Davis Tax Committee (DTC) stated in its report¹⁷ that South Africa faces the challenge of understated incompetence, as it failed to establish working rules for permanent establishments regarding digital economics.¹⁸ Chapter Three will therefore explore the BEPS solutions and their application to the South African and SADC tax system.

Most of the OECD's proposed approaches to BEPS have been considered by several African countries. In South Africa, the DTC has made a number of legislative recommendations, especially encouraging domestic digital tax laws to adhere to international tax guidelines.¹⁹ The DTC's recommendations have been made in order to promote uniformity as the digital economy is not focused entirely on one jurisdiction. The African Tax Administrative Forum (ATAF) has published an ATAF Model Tax

¹⁵A.W. Oguttu [2016]. *Tax Base Erosion and Profit Shifting in Africa – Part 1: Africa's Response to the OECD BEPS Action Plan*. ICTD Working Paper 54. Page 19.

¹⁶United Nations Model Double Taxation Convention between Developed and Developing Countries 2017.

¹⁷Davis Tax Committee: *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa - Summary of DTC Report on Action 1: Address the Tax Challenges of the Digital Economy*.

¹⁸Ibid page 54.

¹⁹Davis Tax Committee: *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa - Summary of DTC Report on Action 1: Address the Tax Challenges of the Digital Economy* page 13

Convention²⁰ and has encouraged African countries to be signatories of the convention in order to address the imbalances between the international community and Africa.²¹

The DTC has refined the OECD's recommendations and suggested that a number of legislative provisions be enacted by South Africa. The South African government responded by including the term "electronic services" in the Value-Added Tax Act (VAT Act).²² Section 1 of the VAT Act defines "electronic services" as "those electronic services prescribed by the Minister by regulation in terms of this Act", while the definition of "enterprise" has also been expanded to include electronic services. This, however, does not adequately address the problems raised by the digital economy in tax-related matters as this was not all that was recommended by the DTC. Chapter Three will explore how South Africa can go further in order to effectively regulate digital taxation without overlooking the OECD's proposed solutions, as it is an observer of the OECD.

This dissertation will also focus on SADC's approach to digital taxation. South Africa is a part of the SADC region and as such, it would be important to consider SADC's approach to digital taxation. Although Africa largely has developing countries, it contains a platform for digital economics, therefore, more regulations must be enacted within the countries' ambits to regulate digital tax and enable economic development.²³ Even though digitalisation of the economy is of particular advantage, it brings with it a particular set of risks which must be identified and addressed.²⁴

1.3.4 Chapter Four

The above chapters will focus largely on digital taxation and potential solutions thereto. This chapter will explore the relationship between digital taxation and dispute resolution

²⁰African Tax Administration Forum. The ATAF Model Tax Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income.

²¹A.W. Oguttu [2017]. "Tax Base Erosion and Profit Shifting in Africa – Part 2: A Critique of Some Priority OECD Actions from an African Perspective." ICTD Working Paper 64. Page 24.

²²Act 89 of 1991.

²³Gillward A. [2017]. *Beyond Access: Addressing Digital Inequality in Africa*. (Global Commission on Internet governance – accessed on 4 August 2018).

²⁴Simms R, Juswanto W [2017]. *Fair Taxation in the Digital Economy*. Asian Development Bank Institute (accessed on 25 June 2018).

as a by-product of the OECD's proposed solutions to digital taxation. This chapter will also explore whether methods highlighted in the OECD's Action 14 will be effectively applied in line with the proposed solutions contained in Action 1. This chapter will include the following sub-sections:

- a) An overview of digital taxation and dispute resolution.
- b) The OECD's approach to effectively address problems identified in dispute resolution mechanisms connected with digital taxation.
- c) An in-depth analysis of the OECD's approach to dispute resolution and how these will influence the application of digital taxation mechanisms.

One of the OECD's approaches to BEPS is creating a more effective platform for dispute resolution. This was proposed in 2015 through one of the BEPS action plans titled Action 14.²⁵ There has not been an international tax adjudicating body in recent years, countries instead rely on their local courts to settle tax disputes with international entities. Chapter Four will explore the problems surrounding establishing dispute resolution mechanisms in the digital sector which will become essential at an international level, as disputes will likely arise from matters relating to the proposed solutions of digital taxation. Other forms of dispute resolution focusing on continental application thereof will also be explored.

The digital economy is a popular concept which dominates the international business economy and as such, it is more likely to attract its fair share of international tax disputes. Any recommendations regarding dispute resolution are more clearly outlined in the OECD's Action 14 report.²⁶

Chapter Four will outline how dispute resolution and the digital economy are intertwined. The digital economy is fast becoming an important economic sector which will lead to many disagreements between countries, much of which will need to be adjudicated upon

²⁵OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report.* Page 94.

²⁶OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Making Dispute Resolution Mechanisms More Effective. Action 14.*

by an impartial body. This chapter will outline how digital taxation will bring about a number of international disputes which have been highlighted by the OECD and will serve to highlight the relationship between dispute resolution and digital taxation in context.

1.3.5 Chapter Five

This chapter will be a consolidation of the four chapters mentioned above. It will contain a proposed solution to any identified problems and outline any further work and research that needs to be done in order to make digital taxation more effective. Chapter Five will contain the conclusion and outline proposed and potential solutions to identified problems.

1.4 RESEARCH METHODS

This dissertation will be based on a desktop research method as it is concerned with analysing and highlighting the OECD's work on digital taxation and dispute resolution. A comparative legal analysis will also be used as this dissertation will focus on the EU and SADC's responses to the OECD's proposed solutions.

The comparative literature study will be focused on international source-based literature, legislation and academic articles relating to the application of taxation to the digital economy. Special focus will be given to the EU, in which the OECD is largely based and SADC as a smaller part of the African continent.

1.5 LIMITATIONS

The digital economy has existed for a long time. Up to now, there has not been primary material written on the digital economy, thus, reliance on articles and internet articles in this regard is extensive. Due to tax fluidity²⁷, no country has managed to put in place comprehensive digital tax legislations. Any international digital tax guidelines are tailored

²⁷The inability of a country's tax system to remain stagnant over long periods of time.

in such a way that enables countries with the capacity to fund any resources that may need to be put in place.

1.6. CONCLUSION

The OECD, with the assistance of a number of companies are working to propose solve any digital related tax challenges. This work will not be exhaustive and is more likely to require updates more frequently than any other legislation due to the constant changes within digitalisation. The solutions outline in the following chapters are therefore not exhaustive and are susceptible to change as often as the digital economy itself advances.

CHAPTER TWO –THE OECD’S PROPOSED SOLUTIONS TO DIGITAL TAXATION

2.1 INTRODUCTION

The OECD has outlined a number of solutions in response to the problems associated with imposing tax on the digital economy. These solutions address the problems associated with “broader direct tax challenges” and “broader indirect tax challenges” caused by the digital economy.²⁸ This chapter will explore these solutions and the likely outcomes thereof with special attention being paid to the responses of the EU. These solutions are largely based on the OECD’s *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report* and its 2018 interim report.

2.2 AN ANALYSIS OF THE OECD’S APPROACH TO PROBLEMS ARISING FROM DIGITAL TAXATION

The OECD identified a number of problems associated with the digital economy which largely contribute to the BEPS issues in tax matters. The digital economy is seen to create competitive inequality and also raises uncertainties relating to identifying a jurisdiction in order to establish tax accountability.²⁹ In light of this, the OECD has suggested a number of solutions which are contained in the BEPS action plans. The OECD’s analysis in Action 1³⁰ suggests that digital taxation is affected in almost every aspect of BEPS and can, therefore, be related to other actions including but not limited to Action 3 (strengthen CFC rules), Action 5 (counter harmful tax practices effectively) and Actions 8 – 10, which address transfer pricing.³¹

The OECD suggested that the manner in which the digital economy is capable of generating large profits with limited productive input in digital businesses, coupled with

²⁸OECD [2015]. *Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report*. OECD/G20.

²⁹Schenk A. *et al* 2015. *Value Added Tax: A Comparative Approach*. 2nd ed. Page 218.

³⁰OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. OECD/G20.

³¹ *Ibid* at 86.

increased easy access to the internet displayed through higher user participation, may justify a change in tax policy.³²The international community has thus far been attempting to implement their digital tax solutions through varied legislative reforms like the definition of electronic services in South Africa's VAT legislation. The OECD also realised that although the business systems may have different operating platforms, they are still the same businesses which are managed by the same people. This is done through a wide network which must be identified and considered when determining cross-border tax practices to determine permanent establishment status (PE) and related tax policies.³³

An interim report known as *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS* (the Interim Report) has been published by the OECD as a progress report for the proposed solution (published in 2015). This Interim Report contained more contributions to the solutions which will be highlighted below. These solutions are largely based on establishing the source of income-generating activities within a particular jurisdiction, digitally, and are subject to constant review and public comment.

The Task Force on the Digital Economy (TFDE) is commissioned to monitor the developments of the digital economy and propose new policies should they be required. This is indicative of an ever-developing area of taxation.³⁴ Digitalisation is ever-growing; it does not only focus on algorithms as in the past, hence continued growth is expected within the digital economy together with the emergence of new digital tax challenges.³⁵ There is therefore, a need for constant monitoring in order to address these challenges.

³²*Ibid* Page 101.

³³*Ibid*.

³⁴http://oecdobserver.org/news/fullstory.php/aid/5600/Tax_challenges,_disruption_and_the_digital_economy.html accessed on 19 March 2019.

³⁵OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 171.

2.3 PROPOSED SOLUTIONS – DIRECT DIGITAL TAX CHALLENGES

2.3.1 Establishing a significant economic presence

Establishing a significant economic presence is linked to the issues relating to PE status. The OECD described significant economic presence in a new light in its 2018 Interim Report. It is a concept that, through its non-physical presence establishes a sustained and purposeful economic interaction with a country through the digital platform.³⁶ This aspect can be determined by considering a number of factors listed below.

2.3.1.1 Revenue-based factor (nexus)

The digital platform allows for economic activities to be carried out without the actual need for physical presence within the economic environment by non-resident entities. In this respect, the OECD proposed that taxes be charged on any digital transactions by establishing a *significant economic presence* and not focus entirely on the non-resident company's physical presence within the concerned jurisdiction.³⁷ This solution was proposed with the intention of ascertaining revenue received from a particular jurisdiction in order to establish a nexus, thus making it certain that there is significant economic presence albeit through the digital platform.³⁸

This proposed solution attempts to establish the origins of a non-resident entity's profits within a particular jurisdiction in order to assign where the receipt of such profits should be taxed. This concept is yet to be adopted by the EU as the OECD noted that many countries have indicated their intention to modify their PE status in order to bring them in line with the recommendations of the Action 1 BEPS Report.³⁹ This indicates the

³⁶OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 135.

³⁷OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 107.

³⁸*Ibid.*

³⁹OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 136.

countries' willingness to implement effective tax solutions for the benefit of their administrations.

Although most EU countries have raised a few concerns relating to the proposed solutions, a number of them have tailored their interim digital tax solutions in line with the OECD's proposed solutions. It is difficult to establish "digital PE" and assign taxes, as digital entities prefer the advantages of fluidity and flexibility of the digital platform.

2.3.1.2 Digital-based factor

A number of considerations were proposed in order to establish significant economic presence under the digital factors. Some of these considerations are established through creating a local domain that contains that local country's domain name, a website that is designed to appeal to a particular country's market or ensuring easy local payment options for that particular user's jurisdiction.⁴⁰ The international tax community has been urged by the OECD to ensure that they are alert regarding any developments that may allow non-resident companies to conduct their businesses without the need for that particular country's domain name.⁴¹

Hungary, as part of the EU, introduced an advertisement tax in 2014. This advertisement tax can be compared with the concept of the nexus and digital-based factors contained in Action 1. Hungary's advertisement tax is focused on the destination of the advertisement and the location of the targeted audience.⁴² Tax liability in this regard would attach to the publisher of the content, who is expected to be registered before being able to supply the digital services.⁴³ The advertisement tax is Hungary's way of establishing a

⁴⁰OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 109.

⁴¹*Ibid.*

⁴²OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 145.

⁴³ *Ibid.*

nexus, as any outside entity wishing to advertise in Hungary is required to register and will be liable for tax in the event that the set threshold is met.⁴⁴

2.3.1.3 User-based factors

The user-based factors are based on the fact that the number of consumers visiting a certain company digital platform can be measured against the number of online contracts⁴⁵ concluded between a service provider and a consumer.⁴⁶ Significant economic presence can be established through the number of “monthly active users” that visit any particular company’s website.⁴⁷ Considering the uncertainties involved with digital technology, this could prove to be a difficult initiative as it would require the input of IT experts to counter any technological advances that may be used to disguise the company’s online presence in any jurisdiction in the future. The OECD has also proposed an approach where tax authorities can work to establish the jurisdiction by ascertaining where the data (consumer-related details) was collected and disregard where any such data is stored (company headquarters).⁴⁸

The user-based factors can be implemented by applying a country’s electronic communications legislations should there be any. In South Africa, there is an Electronic Communications and Transactions Act (ECT Act)⁴⁹. Section 10 of the ECT Act empowers the Minister of Communications to implement electronic transactions policies. These policies may be implemented in consultation with the different members of cabinet that may be affected by any such policies.⁵⁰In this regard, in order to access any user-based information in order to establish nexus, the South African tax authorities must work

⁴⁴<https://taxinsights.ey.com/archive/archive-news/hungary--advertisement-tax-amended.aspx> accessed 24 August 2019.

⁴⁵Agreed terms and conditions of the use of a certain website.

⁴⁶OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 110.

⁴⁷*Ibid.*

⁴⁸*Ibid.* This is data relating to consumers, that is what the consumer fills out as their details according to the company’s request (it could also lead to the collection of consumer privacy data).

⁴⁹Act 25 of 2002.

⁵⁰Section 10 (2) (a) of Act 25 of 2002.

together with the communications authority in order to obtain authorisation through policy considerations.

2.3.1.4 Revenue and other factors

This factor, according to the OECD, should be considered with any one of the above factors when attempting to establish a nexus/significant economic presence. It is important for authorities to establish a link between the revenue generated in a particular jurisdiction with the relevant digital factors that lead to a non-resident company gaining sufficient digital presence in the digital economy.⁵¹

The OECD recognised that the proposed solution to establish a nexus through profits derived from digital trade could be difficult to enforce and has therefore proposed another approach to address this potential problem. The OECD realised that there are rules relating to the taxation of profits (generally) and that such rules would need to be revisited to allow for the taxation of profits derived from the nexus based on significant economic presence in the digital economy.⁵² The conclusion was that “unless there is a substantial rewrite of the rules for the attribution of profits, alternative methods would need to be considered”.⁵³ The United Kingdom proposed that clarity must be established when determining the revenue which must be taxed by the government in any digital transaction, considering the lack of certainty of the consumer and the selling enterprise.⁵⁴

In order to address any misunderstandings relating to the location profits for tax purposes following the nexus proposal, the OECD moved to ensure that a profit allocation method was proposed.⁵⁵ Once it has been established that a country has a right to tax certain profits, the next step would be to determine how much of those profits that country can

⁵¹*Ibid* at 111.

⁵²OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 112.

⁵³*Ibid*.

⁵⁴HM Treasury [2017]. *Corporate tax and the digital economy: Position paper*. Page 12.

⁵⁵This is an attempt to control profit allocation in order to avoid double taxation on the same profits. It is only relevant to the solutions relating to significant economic presence and will therefore not be discussed further.

tax through profit allocation rules.⁵⁶ Establishing profit allocation is currently done under the Arm's Length Principle (ALP) which is provided for in Articles 7 and 9 of the OECD and UN model tax conventions. The OECD has indicated that a revision of the provisions relating to the ALP must be done in order to bring them in line with digital taxation and the nexus proposal.⁵⁷

2.3.2 Withholding tax on digital transactions

The OECD proposed that a withholding tax be applied to digital transactions when payments are made by local jurisdictional residents.⁵⁸ In order to successfully implement this solution, the OECD proposed that there should be a clear definition of the scope of the transaction and an effective method of ensuring that tax is declared in the concerned transactions.⁵⁹ This declaration must be made regardless of whether the transaction relates to non-resident entities and local resident entities or non-resident entities and individuals.⁶⁰

The TFDE in the OECD's interim report proposed that the withholding tax be broadened to encompass royalties. This proposal is based on the fact that a number of countries⁶¹ have responded to the 2015 report by suggesting taxes on royalties should be extended to include transactions that use what is akin to intellectual property through examples which include right to use software for payment.⁶² The OECD has highlighted that a number of countries have used different methods in order to implement this solution including the United Kingdom (UK), whose newly proposed source definition will most likely target digital transactions.⁶³

⁵⁶OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 168.

⁵⁷*Ibid* at 173.

⁵⁸OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 113.

⁵⁹*Ibid* at 114.

⁶⁰*Ibid*.

⁶¹Commonly EU countries. The OECD highlighted that the UK recently proposed a tax that is targeted at mostly digital transactions with intellectual property in low or no tax jurisdictions.

⁶²OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 140.

⁶³*Ibid*. It is a newly proposed new tax that will control intra-group tax planning that places intellectual property benefits in low tax jurisdictions.

2.3.3 Introduction of an equalisation levy

Equalisation levy is defined as “tax leviable on a consideration received or receivable for any specified service...”.⁶⁴ An equalisation levy in the context of digital taxation is meant to tax non-resident entities with a significant economic presence in one jurisdiction.⁶⁵ This would mean that an attempt can be made by the taxing jurisdiction to bring taxes to equal standing with a domestic entity and a non-domestic one. There are a number of alternatives relating to this proposed solution. One alternative is to establish the nature and scope of the transaction according to the concluded online agreement.⁶⁶ Another was to attribute the levy to the data relating to in-country users of the digital platform.⁶⁷ The levy may also be charged on the gross value of goods and services remotely supplied but paid for by in-country consumers and collected by foreign entities with no PEs or an intermediary of those foreign entities.⁶⁸

This solution has already received a number of responses world-wide. In 2016, the Policy Department A⁶⁹ noted that the introduction of this levy would allow for more tax to be retained within the market jurisdiction especially where advertisements are concerned.⁷⁰ Policy Department A notes with concern that there is a large tax revenue being lost by market jurisdictions when entities like Amazon, Facebook and Google allow advertisers to use their platforms and only remit tax to their jurisdiction of establishment.⁷¹ Italy introduced a levy on digital transactions in 2017 which operates on the destination principle. This levy is focused on transactions that are concluded digitally with the objective of the levy to “level the playing field by taxing digital transactions whose value,

⁶⁴[https://www.ey.com/Publication/vwLUAssets/Template_Equalisation_Levy_Alert.pdf/\\$FILE/Template_Equalisation_Levy_Alert.pdf](https://www.ey.com/Publication/vwLUAssets/Template_Equalisation_Levy_Alert.pdf/$FILE/Template_Equalisation_Levy_Alert.pdf) (accessed 9th March 2019).

⁶⁵OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 116.

⁶⁶The OECD recognised that the problem with this solution would be the inability to keep up with the constant technological changes; as such the levy would require constant updates and reviews.

⁶⁷OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 116.

⁶⁸ *Ibid.*

⁶⁹A department within the European Union Parliament which was commissioned by the Special Committee on Tax Rulings to issue a report on digital taxation.

⁷⁰Policy Department A: Economic and Scientific Policy [2016]. “Tax Challenges in the Digital Economy.” Page 36.

⁷¹*Ibid.*

generated by users and user-generated content, is currently not captured (or at least is only partially captured) by existing corporate tax rules.”⁷² This is not a direct response to the equalisation levy solution, however, similarities are clear in their principles of requiring equality to be established between two service providers, regardless of their methods of delivery. Italy’s current rules relate to the local providers of digital content and corporate content while the OECD’s equalisation levy applies internationally.

The OECD has indicated that it is difficult to measure the success of the broader tax challenges associated with the digital economy as these have not been practically applied.⁷³ The legislative measures that have been thus far implemented by different countries have been measured as a success by the OECD which indicated a rise in tax revenue since the implementation of some of the tax reforms related to BEPS.⁷⁴ The proposed solutions represent solutions to “loopholes” and “gaps” in the issue of double non-taxation rather than solving what is identified as a problem in digital taxation.⁷⁵ Due to this, the OECD called on public participation in response to its BEPS project and received numerous proposals from the international community.⁷⁶

After the release of the 2015 BEPS Action 1 Report, many countries have attempted to solve the problems associated with digital taxation by modifying their domestic laws to either fully or partially codify the OECD’s proposed solutions. These unilateral moves, although beneficial to the concerned jurisdictions, have raised concerns with the OECD. This has been largely due to lack of consensus on the proposed solutions amongst the international community.⁷⁷ The UK stated in its 2017 position paper that solutions will be successfully implemented if there are international consensus and acceptance of the outlined solutions as well as a set timetable of when these solutions should be

⁷²OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 143

⁷³*Ibid* at 108.

⁷⁴OECD/G20 [2018]. *Brief on the Tax Challenges Arising from the Digital Economy: Interim Report 2018*.

⁷⁵OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 108.

⁷⁶These responses will be discussed in Chapter Five.

⁷⁷OECD [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 134.

implemented.⁷⁸ The OECD acknowledges the UK's view and has indicated that it recognises the risk that is associated with a large number of uncoordinated and unilateral tax measures in a matter that affects the international community.⁷⁹ The EU agreed to this. In March 2018, the EU released two proposals directed at digital taxation; one was for the EU to adopt a uniform definition of a “digital PE”, while the other was to introduce a digital services tax which will be charged at 3% for any revenue derived from digital services.⁸⁰ A digital services tax would be one that ensures that revenues are taxed amongst countries in a fair manner according to the location of the consumer and the enterprise involved. BIAC stated that there should be clear thresholds attached to the proposed solutions (and policies should there be any) in order to reduce administrative burdens and avoid the rise of disputes caused by lack of uniformity.⁸¹

2.4 PROPOSED SOLUTIONS – INDIRECT DIGITAL TAX CHALLENGES

Chapter 8 of the OECD's Action 1 report outlines the indirect challenges that are present in the digital economy and provide options (in this case proposed solutions) to address these challenges. VAT has been the OECD's main focus in indirect challenges. The OECD has therefore issued proposed solutions directed at making VAT collection in the digital economy more effective. VAT is “the application to goods and services of a general tax on consumption”,⁸² and it is the predominant indirect challenge in the digital economy. With the advent of the digital economy and its ever-evolving technology, the collection of VAT is a difficult exercise whereby domestic entities face more complicated pressures when compared to non-resident entities.⁸³

⁷⁸HM Treasury [2017]. Corporate tax and the digital economy: Position paper. Page 11.

⁷⁹ OECD/G20 [2019]. *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy*. Page 7.

⁸⁰<https://files.taxfoundation.org/20181022090015/Tax-Foundation-FF618.pdf> (accessed 24th February 2019).

⁸¹Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

⁸²Schenk A. *et al* 2015. *Value Added Tax: A Comparative Approach*. Page 10.

⁸³OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 122.

The issue of VAT collection in the digital economy is not as simple to regulate as with non-digital transactions; non-resident suppliers may not be motivated to remit VAT to the consumer's jurisdiction.⁸⁴ The OECD suggested in its *E-Commerce Guidelines*⁸⁵ that non-resident suppliers register as vendors in the consumer's jurisdiction. This suggestion was a great concept which was taken up by a number of jurisdictions and complied with by a number of large non-resident entities.⁸⁶ However, this is not an effective solution as the OECD noted that there is not enough incentive to ensure that all digital suppliers register; there are also not enough resources for the tax authorities to make an effective follow-up.⁸⁷ Introducing punitive penalties should there be failure to address this could be incentive enough if governments have the capacity to follow up on the online suppliers.

The TFDE proposed that a simplified method of VAT/GST collection on digital services be implemented in relation to the digital economy and to simplify the collection of digital related revenue taxes. This simplification was proposed through the introduction of the idea of "digital platforms".⁸⁸ These were proposed to be implemented as intermediaries for the collection of only VAT/GST in the sale of digital goods and/or services in the digital economy.⁸⁹ The work of digital platforms is better described as online VAT/GST collection agents for revenue services around the world in digital related services. The OECD has stated that it is important to ensure that a digital platform complies with VAT/GST requirements before any VAT/GST related duties can be assigned to them in line with the VAT/GST guidelines.⁹⁰ These requirements are i) that the digital platform has sufficient and accurate information to make an appropriate VAT/GST determination, and ii) that the digital platform has the capacity to collect the VAT/GST on the supply.⁹¹

⁸⁴ *Ibid.*

⁸⁵ <https://www.oecd.org/sti/consumer/ECommerce-Recommendation-2016.pdf> (accessed 6th March 2019).

⁸⁶ OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report.* Page 122.

⁸⁷ *Ibid.*

⁸⁸ OECD [2019]. *The Role of Digital Platforms in the Collection of VAT/GST on Online Sales.* Page 26.

⁸⁹ *Ibid.*

⁹⁰ *Ibid.*

⁹¹ *Ibid.*

The OECD also proposed that jurisdictions implement better systems of tracking VAT hence the attempted effort to simplify the existing methods of collecting VAT. The traditional way of collecting VAT at the border could be improved if the systems are up to date with technological developments and electronic methods are introduced.⁹² This method could be considered to be a reliable solution if a number of thresholds are removed on low-value goods.⁹³ Jurisdictions are not keen on imposing VAT/GST on low-value goods as the administrative burden thereof outweighs the amount of revenue collected from them.⁹⁴ In Africa, the Kingdom of eSwatini takes note of low-value goods which are constantly delivered to an individual by post and demands payment on imports from the consumer.

The collection of VAT/GST on low-value import goods has also been a subject of interest within the broader indirect challenges of the digital economy. The TFDE notes that the exemptions and lowered thresholds imposed on low-value goods were justified before the digital economy became popular.⁹⁵ In the present digital era, low-value goods (imports) have the capacity to generate a high amount of revenue which is being lost to tax authorities through exemptions.⁹⁶ The OECD has proposed VAT collection methods in low-value import goods which include the *purchaser collection model* where the OECD proposed that the buyer self-accesses themselves and remit the VAT due to the revenue authority.⁹⁷ The *vendor collection model* was also proposed where the non-resident supplier was expected to remit VAT to the market jurisdiction upon registration via the simplified method that the OECD is still to recommend in 2020.⁹⁸ Lastly, the OECD proposed that intermediary VAT collectors may be used for VAT collection. These intermediaries would include postal services, express carriers (who already use digital platforms to record their activities) and the creation of transparent e-commerce platforms

⁹² OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 124.

⁹³ *Ibid.*

⁹⁴ OECD [2019]. *The Role of Digital Platforms in the Collection of VAT/GST on Online Sales*. Page 31.

⁹⁵ OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 123.

⁹⁶ *Ibid.*

⁹⁷ *Ibid.* Page 124.

⁹⁸ *Ibid.*

that would allow parties to the transaction to assess the VAT due to the jurisdiction that they are party to.⁹⁹ The idea of e-commerce platforms could be a well-intended solution if tax administrations worldwide implemented such bodies for the benefit of their tax systems as well as data sharing platforms to enable transparency.

The OECD indicated that there are number of business models where the VAT/GST guidelines would apply. These include the business-to-business (B2B) model under which the payment of VAT/GST is better monitored, and the business-to-consumer (B2C) model which is more difficult to track. The B2C model involves the direct sale of commodities to an individual, and from a supplier that can be based at the far end of the consumer's location.¹⁰⁰ This describes all international digital transactions between suppliers and individuals worldwide. Revenue from the B2C model business through the digital platform has increased whilst the ability to impose tax on such revenues has not been implemented.¹⁰¹ The OECD has indicated that the best way to solve B2C related challenges was to ensure an effective method of VAT collection.¹⁰² It therefore proposed in B2C transactions that:

- i) the right to levy VAT/GST in digital transactions must be retained by the customer's jurisdiction of residence¹⁰³;
- ii) market jurisdictions must make their VAT vendor registration simpler for foreign digital businesses;¹⁰⁴ and
- iii) in the interest of upholding the principle of fairness in taxation, the foreign suppliers will charge VAT at the same rate as that of local suppliers so as to avoid artificial shifting of PE status by local suppliers.¹⁰⁵

⁹⁹*ibid.* Page 125.

¹⁰⁰*ibid.* Page 125.

¹⁰¹OECD [2019]. *The Role of Digital Platforms in the Collection of VAT/GST on Online Sales.* Page 13.

¹⁰²OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report.* Page 129.

¹⁰³This is regardless of the supplier's headquarters and/or place of business.

¹⁰⁴Through a simplified online method.

¹⁰⁵OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report.* Page 129.

The OECD's VAT/GST guidelines are evolutionary¹⁰⁶ in nature and as such, authorities must be prepared for further developments and how to address them in order to keep up with digital technology.¹⁰⁷ Some of the above VAT solutions were refined from the OECD's earlier proposals regarding VAT remittance in international trade. Although these proposals did not directly address issues in the digital economy, the proposed draft principles act as a guideline for the above stated proposed solutions to the digital tax problems.¹⁰⁸ The EU responded to the issues associated with VAT (indirect challenges raised by the digital economy) by endorsing the OECD international VAT guidelines.¹⁰⁹ In its Interim Report,¹¹⁰ the OECD noted the success of the guidelines that were applied by the EU states in their increased VAT revenue collections.¹¹¹ This proves that the VAT recommendations/proposed solutions have made a significant impact on the EU community and are likely to yield the same results should they be adopted by the international community at large.¹¹² From the above, it is apparent that the VAT solutions led to a successful implementation in its initial application due to the guidelines that were published after the proposed solutions contained in Action 1.

2.5 CONCLUSION

The OECD has not finalised the proposed solutions discussed above, neither has it made any recommendations relating to the proposed solutions. Because of the ongoing process, the OECD has in turn, requested input to address those solutions before any final consensus can be reached in 2020.¹¹³ The EU appreciates the importance of implementing effective uniform digital tax solutions on an international level. In the absence of an international consensus, the different EU countries have implemented interim digital solutions in an effort to retain revenues that are due to them from digital

¹⁰⁶It is reviewed as per the developments of technology and in accordance with the recommendations of the TFDE.

¹⁰⁷OECD [2017]. *International VAT/GST Guidelines*.

¹⁰⁸<http://www.oecd.org/tax/consumption/34422650.PDF> (accessed on 27th February 2019).

¹⁰⁹OECD [2017]. *International VAT/GST Guidelines*.

¹¹⁰OECD/G20 [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018*.

¹¹¹*Ibid* at 104.

¹¹²*Ibid* at 108.

¹¹³OECD [2019]. *Addressing the Tax Challenges of the Digitalisation of the Economy – Public Consultation Document*.

transactions. In this regard, it is important for the EU to table its opinions regarding the proposed solutions and revisit their tax-related agreements. The OECD must ensure that it issues guidelines that countries are capable of following when implementing the solutions highlighted above.

CHAPTER THREE – APPLICATION OF THE OECD’S PROPOSED SOLUTIONS TO SADC

3.1 INTRODUCTION

The OECD is in the process of devising solutions to the problems raised by digital economics in tax matters with the final solutions being expected to be published by 2020. This process involves inviting the public to comment on its initial publication of digital tax solutions, which some countries have implemented or are in the process of implementing. A number of tax entities, such as the African Tax Administration Forum (ATAF) and the UN Conference on Trade and Development (UNCTD), realise that African tax authorities struggle to implement existing tax measures to avoid double non-taxation and lose large amounts of tax revenue in the process. Binder Dijker Otte (BDO) opines that these new solutions will place a heavier burden on African countries, financially.¹¹⁴ From an objective view of African tax systems, the proposed solutions and the public consultations are not enough to solve African digital tax problems. In its technical report, the ATAF¹¹⁵ noted that the rules that were to be implemented in the digital tax project have to be simpler for both African tax administrations and their taxpayers.¹¹⁶ This chapter explores a number of solutions the OECD proposed and developed from consultations with different jurisdictions, including developing countries.¹¹⁷

The UN,¹¹⁸ considered the proposed solutions by the OECD to be helpful to developing countries. This chapter analyses the solutions proposed by the OECD in relation to the African tax context, paying particular attention to South Africa and the SADC.

¹¹⁴<https://www.bdo.co.za/en-za/insights/2019/tax/taxing-the-digital-economy-why-is-africa-not-getting-its-fair-share>. (accessed 21st May 2019).

¹¹⁵This is an African tax forum that provides a platform for Africa tax authorities to share ideas on how to address current tax problems.

¹¹⁶Africa Tax Administration Forum, *Technical Note: CBT/TN/01/19*. (accessed 25th April 2019).

¹¹⁷OECD/G20 [2015]. *Base Erosion and Profit Shifting Project. Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*. Page 3.

¹¹⁸Fifteenth Session held on 11th October 2017.

3.2 TAXATION OF THE DIGITAL ECONOMY IN DEVELOPING COUNTRIES – BROADER DIRECT TAX CHALLENGES

A commentary published by the International Monetary Fund (IMF) recognised that some of the proposed digital tax solutions contained in the BEPS project were challenging to implement by developing countries.¹¹⁹ This is contrary to the Committee of Experts' view on the same matter. The IMF and BDO's views suggest that the OECD should be cognisant of the challenges of developing countries and tailor its solutions to suit them. After the publication of the OECD's Action 1 on digital taxation, many countries responded by publishing content relating to digital economics. This content contained a number of digital tax related solutions for their specific jurisdictions. South Africa was one of the countries that published a report relating to digital taxation through the DTC.¹²⁰

It is important to note that all organisations that contributed to the proposed solutions surrounding digital taxation recognised that the digital economy is a fluid concept that needs to be constantly revised to keep up to date with its developments.¹²¹ The same organisations also recognised that the digital economy is not an easy tax subject for policymakers due to its fluidity.¹²² This challenge can be worse in developing economies as these are not financially equipped to handle constantly changing tax policies.¹²³

3.2.1 Change in the definition of PE status and new source rules

The DTC, on the basis of the OECD's BEPS project, recommended that South Africa adopt the international tax community's digital tax solutions as outlined by the OECD.¹²⁴ In this regard, the DTC focused on the measures that were recommended to revise the definition of PEs in order to encompass income that would result in it being declared as

¹¹⁹<https://www.imf.org/external/np/exr/consult/2018/corptaxation/pdf/2018commentscorptaxation.pdf>. (accessed 27th April 2019).

¹²⁰This Committee was established in 2013 for a 5-year tenure within the Republic of South Africa.

¹²¹ADB Institute [2017]. *ADB Policy Brief No. 2017-5: Fair Taxation in the Digital Economy*. Asian Development Bank Institute.

¹²²*Ibid.*

¹²³OECD [2013]. *Action Plan on Base Erosion and Profit Shifting*.

¹²⁴Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

stateless income.¹²⁵ Stateless income is described as income that is neither derived within its domicile country nor is it liable for taxation within its country of source but may be moved to a low tax jurisdiction.¹²⁶ This stateless income will be a predominant feature in the operation of the digital economy. The revision of the definition of PEs could be achieved through ensuring that tax planning is done by breaking down activities and classifying them as auxiliary or preparatory work for a particular corporation.¹²⁷ The DTC states that such methods of tax planning can be minimised through a more inclusive definition of PE status. Currently, the definition of PE provides that:

*...a permanent establishment as defined from time to time in Article 5 of the Model Tax Convention on Income and on Capital of the Organisation for Economic Co-operation and Development: Provided that in determining whether a qualifying investor in relation to a partnership, trust or foreign partnership has a permanent establishment in the Republic, any act of that partnership, trust or foreign partnership in respect of any financial instrument must not be ascribed to that qualifying investor.*¹²⁸

From the OECD and DTC's discussions of PE concepts within the digital economy, another component encompassing digital tax should be included in the above-quoted definition of PE in South Africa.

It is also possible that a more inclusive definition of PE status could also lead to the emergence of new "source rules". The new source rules that have been proposed by the DTC would allow for the source of income to be where the South African recipient of the goods or services pays for them, thus allowing South Africa to retain taxing rights in such a transaction.¹²⁹ The DTC proposes that the new source rules should be implemented to enable South Africa to tax proceeds from digital goods and services that are supplied

¹²⁵*Ibid.*

¹²⁶E.D. Kleinbard. "Stateless Income" [2011] Vol.11 No.9 Florida Tax Review. Page 700 at 702.

¹²⁷A.W. Oguttu. "Tax Base Erosion and Profit Shifting in Africa – Part 2: A Critique of Some Priority OECD Actions from an African Perspective".[2017] ICTD Working Paper 64.

¹²⁸Income Tax Act 58 of 1962, section 1.

¹²⁹Davis Tax Committee, *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

within the Republic, and also those that are consumed within the Republic.¹³⁰ These new source rules as recommended by the DTC attempt to create a source of funds on digital transactions that impute tax benefits on South Africa. This is an effective recommendation which is likely to benefit South Africa if it is properly implemented as it manages to bring back revenue that would be lost to it in digital transactions. The DTC, therefore, recommended that the government amend section 9 of the Income Tax Act¹³¹ in order to incorporate taxation of digitally supplied services by non-residents as a “source of income”.¹³² Section 9 of the current Income Tax Act does not contain any provisions that are directly linked to the provision of digital services and goods by a non-resident.¹³³ This is not to say that the recommendations have been overlooked by the government. Some of these have been implemented as recommended.

The “source” issue can be approached by considering the case of *CIR v Lever Brothers*.¹³⁴ A South African registered company Overseas Holdings (Pty)¹³⁵ Ltd (Overseas Ltd) was indebted to Lever Brothers and Unilever for an amount it inherited through its purchase of a Dutch company, as well as interests on that amount. Overseas Ltd paid the amounts due out of dividends received from an American branch of the Lever Brothers and Unilever holdings from 1940 to 1942. The Commissioner sought to assess Lever Brothers on the interest received as income tax. On appeal, the court held that South Africa was not the source of the income it sought to tax and therefore had no right to issue the income tax assessment. The court considered the meaning of the word “source” to indicate the origin of the money and not its location when it was received and paid back. In this case, the origin of the funds was in the transaction that was concluded between the companies, where the originating cause arose to require such a transaction to be born. This decision was based on the reasoning that the source of the income could not be established to be South Africa, as no business or contracts were concluded in

¹³⁰ *Ibid.* Page 26.

¹³¹ Act 58 of 1962.

¹³² Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1. Page 28.

¹³³ *Ibid.*

¹³⁴ Commissioner of Inland Revenue v Lever Brothers and Another [1946] AD 441.

¹³⁵ This company was also a subsidiary of Unilever.

South Africa; neither were there any obligations to be carried out in South Africa. The only obligation arose from a purchase price which was to be paid over time, whilst interests had to be paid on that amount to a company situated in the UK.

This case set a basis for the source principle. However, its application to the digital economy could prove to be a challenge. Deloitte avers that if the issue of the source could be addressed by applying the originating cause principle from the lever Brothers case, a loophole for digital service suppliers would be created.¹³⁶ This loophole could allow these suppliers to argue that their servers are not situated in South Africa, therefore the source is not South Africa thus defeating the BEPS initiative and purpose.¹³⁷

3.2.2 Administration of unregistered companies

South Africa hosts a number of international companies that maintain a PE, making them liable to submit tax returns in South Africa. The problem with a permanent establishment is clear in a digital economy where a PE does not need to be established for business to be concluded. A transaction is capable of being concluded without the need for physical presence or physical contact between parties. In this regard, the DTC recommended that the government implement rules that require companies that have business that flows through South Africa to submit tax returns.¹³⁸ To achieve this, the DTC has suggested that the South African Revenue Service (SARS) modify the IT14 return to include information based on facts, not just mere tax law.¹³⁹ The DTC does not view administration of these tax returns to be a burden to SARS.

3.2.3 The DTC's proposed solutions to the administrative challenges of the digital economy in South Africa

The DTC recognised the above challenges of tax administration and proposed a number of solutions that would enable SARS to effectively execute its duty. This included the

¹³⁶Deloitte. *Navigating the Digital Age: Tackling the Evolving Digital Economy with Direct Tax Laws*. <https://www2.deloitte.com › content › dam › Deloitte › Documents › tax.> (accessed 15th April 2019).

¹³⁷*Ibid.*

¹³⁸Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

¹³⁹*Ibid.*

DTC's recommendation to SARS to make use of the OECD Mutual Administrative Assistance in Tax Matters Convention (the Administrative Assistance Convention) which came into force in 2011. This Administrative Assistance Convention was adopted by the OECD and the EU and is described as a mutually beneficial arrangement for signatories. It covers an extensive form of co-operation on all taxes and ensures that there is a uniform application of the convention by the signatories that have ratified it.¹⁴⁰ The DTC's reason for this recommendation is that South Africa should not be overburdened by the application of new tax rules when there is an Administrative Assistance Convention that can be invoked should the need arise. This is in line with the understanding that digital tax is an international concept which can be successfully implemented if there is mutual assistance and uniformity.¹⁴¹ Nonetheless, the DTC has cautioned SARS that when executing its administrative duties, the expenses incurred should not outweigh the benefit that is expected to be derived from the collected taxes.¹⁴² In addition, the DTC has encouraged SARS to make use of the information-sharing provisions contained in double tax agreements (DTA), which South Africa is party to.¹⁴³

3.2.4 Davies Tax Committee legislative recommendations

In accordance with the OECD's BEPS action plan, the DTC made recommendations regarding income tax. These recommendations include amending section 6 *quin* of the Income Tax Act and reviewing 10(1)(o)(ii). Section 6 *quin* "provided that foreign tax credits would be allowed against tax payable in respect of withholding taxes imposed on service fees from a South African source".¹⁴⁴ This section has since been repealed by the Taxation Laws Amendment Act 2015¹⁴⁵ in order to avoid profit shifting to another source where that source is within the digital sector.

¹⁴⁰https://www.oecd.org/ctp/exchange-of-tax-information/ENG_Convention_Flyer.pdf (accessed 3rd May 2019).

¹⁴¹Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1. Page 64

¹⁴²*Ibid.*

¹⁴³ *Ibid.*

¹⁴⁴<https://www.rsm.global/southafrica/news/section-6quin-amendment-foreign-tax-credits-no-longer-deductible> (accessed 12th February 2019).

¹⁴⁵Amendment 7 thereof.

In turn, the recommended review of section 10(1)(o)(ii) of the Income Tax Act pertains to exempt foreign income by a South African tax resident. The DTC also recommended that the Income Tax Act be considered together with the Electronic Communications and Transactions Act¹⁴⁶ when dealing with matters relating to the digital economy.¹⁴⁷ This consideration is to allow for easy access to digital-based services without increasing the government's administrative burden.¹⁴⁸ The above legislative changes are an indication of South Africa's efforts to ensure that it keeps important tax income within its borders thus attempting to follow the proposed BEPS solutions. These amendments do not adequately address the BEPS digital concerns and more additions to tax legislations need to be made to correct that shortfall within the amendments.

The South African courts have also followed the international tax developments and have attempted to adjudicate matters accordingly. In the case of *AB LLC and BD Holdings LLC v Commissioner of the South African Revenue Service*,¹⁴⁹ the Appellants provided services to a South African tax resident during 2007 and left the country in 2008 after completing the services. During the year 2011, the Appellants learned that they owed SARS taxes and fines for unpaid taxes during their years of operation in South Africa, which they disputed. The court based its decision on the provisions of the DTA that was concluded between South Africa and the United States of America (the US) particularly articles 5 (1) and 5(2)(k). Article 5 (1) of the DTA between the US and South Africa states that "(f)or the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on". Additionally, Article 5 (2) (k) states that:

(t)he term "permanent establishment" includes especially: (k) the furnishing of services, including consultancy services, within a Contracting State by an enterprise through employees or other personnel engaged by the enterprise for such purposes, but only if activities of that nature continue (for the same or a connected project) within that State for a period or periods aggregating more than

¹⁴⁶Act 25 of 2002.

¹⁴⁷Davis Tax Committee [2016]. *Second and Final Report on Base Erosion and profit Shifting*. Page 12.

¹⁴⁸ *Ibid.*55

¹⁴⁹(13276) [2015] ZATC 2 (15 May 2015).

183 days in any twelve-month period commencing or ending in the taxable year concerned.

The court held that the articles cannot be read separately. The words “include especially” in article 5(2)(k) mean that they should be understood to mean that there are “specific activities” which create an establishment in South Africa. This being the case, the court applied the 183-day rule and found that the Appellants had established a permanent establishment in the form of Boardroom X. In this regard, both Appellants were found to be liable for tax in South Africa by virtue of their PE and the provisions of the DTA. Although this judgment has been subject to a number of criticisms, it is clear that South Africa has attempted to ensure that the term PE is broadly interpreted to allow for a number of activities to be subject to tax in South Africa.

Although South Africa is making strides to meet the digital economy’s PE requirements, the DTC has indicated that this may not be what some of the developed countries prefer. The DTC gave examples of prominent companies with a digital presence that may be expected to shift some of their revenues in order to remit tax in countries where they are present digitally.¹⁵⁰ This includes companies like Google and Amazon which are headquartered in the United States.¹⁵¹ Presently, the contributions of different companies to the OECD’s requests for input indicate that developed countries are willing to implement the OECD’s proposed solutions.

3.3 TAXATION OF THE DIGITAL ECONOMY IN DEVELOPING COUNTRIES – INDIRECT TAX CHALLENGES

The challenges raised in indirect tax in the digital economy are largely VAT related challenges. The OECD, as indicated in the previous chapter, developed a number of VAT guidelines, which some countries have already adopted.

¹⁵⁰ Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1. Page 29.

¹⁵¹ *Ibid.*

South Africa has a number of provisions in its VAT Act¹⁵² that shows its move towards integrating the digital economy within its legislation. This includes the definition of “electronic services” in section 1 of the VAT Act and the addition of “electronic services” within the definition of “enterprise”. The DTC suggested that South Africa should include a clear definition of “telecommunication services” and also set out a well-defined “place of supply” of any such telecommunication services within any tax legislation.¹⁵³ While there are potentially lesser problems expected in the VAT section, as most of the OECD recommendations were implemented by South Africa, the DTC has identified a few issues with the OECD’s VAT/GST guidelines that should be addressed. It has been identified that penalising foreign suppliers for the non-verification of a VAT vendor status of its customer is impractical and places a large administrative burden on the taxpayer.¹⁵⁴ The South African government also indicated that reliance could not be placed on the common practice of “reverse charge mechanisms” on imported services, as there was difficulty in enforcing compliance.¹⁵⁵ As such, the DTC has recommended that South Africa adopt the OECD’s guidelines as a protective measure to the foreign supplier; foreign suppliers of electronic services will be required to register as vendors should their supply exceed R50 000.¹⁵⁶

The DTC has recognised that the VAT guidelines¹⁵⁷ are mainly concerned with monitoring vendor registration by the concerned tax authorities and/or the foreign supplier. This raises concerns of the administrative burden on (especially) SARS, as it does not have the resources to follow-up on all electronic transactions conducted with South African residents, neither does it have the ability to verify any tax information received from non-

¹⁵²89 of 1991.

¹⁵³Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

¹⁵⁴*Ibid.*

¹⁵⁵Department of National Treasury of the Republic of South Africa [2019]. *Explanatory Memorandum: Regulations Prescribing Electronic Services for the Purpose of the Definition of “Electronic Services” in Section 1(1) of the Value Added Tax Act, 1991.*

¹⁵⁶Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

¹⁵⁷As issued by the OECD and the EU.

resident digital entities.¹⁵⁸ The DTC recommends that South Africa follow international tax developments and implement them to promote development and uniformity, albeit not blindly.¹⁵⁹ South Africa must also ensure that the administrative burden does not overburden the government and its residents but must be minimised as much as possible through the foreign electronic supplier.¹⁶⁰

3.4 RECOMMENDATIONS FOR SADC AND DEVELOPING COUNTRIES

In order for developing countries¹⁶¹ to successfully apply the recommendations of the OECD to their tax administration system, it has been noted that they must follow the modified fundamental tax principles which also include principles of efficiency and neutrality in the digital economy.¹⁶² It is important that the principles of tax are clearly defined, especially within the digital tax context, as these can easily be distorted in an effort to retain taxing rights between jurisdictions. In this regard, ATAF proposed that rules be implemented to ensure that a balance is struck when apportioning taxing rights between jurisdictions (with special focus being paid to Africa).¹⁶³ In its technical note, ATAF published a detailed digital tax solution for African countries that is similar to the DTC's proposals for South Africa and OECD's proposals for the international community.

As the UN Committee of Experts on International Cooperation in Tax Matters (the UN Tax Committee) recognised that the solutions proposed by the OECD were largely beneficial to developed countries, it issued recommendations for developing countries.¹⁶⁴ The UN Tax Committee realised that many developed countries¹⁶⁵ were introducing unilateral

¹⁵⁸Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

¹⁵⁹*Ibid*

¹⁶⁰*Ibid*

¹⁶¹Particularly in the SADC region in this case.

¹⁶²<https://irp-cdn.multiscreensite.com/a521d626/files/uploaded/Report-of-Committee-on-Taxation-of-e-Commerce-Feb-2016.pdf> (accessed 25th November 2018).

¹⁶³*Ibid*.

¹⁶⁴https://www.un.org/esa/ffd/wp-content/uploads/2017/10/15STM_CRP22_-_Digital-Economy.pdf (accessed 27th April 2019).

¹⁶⁵Italy, Netherlands, the UK and France.

measures in their tax legislations successfully.¹⁶⁶ It therefore suggested, contrary to the OECD's views in the same matter, that developing countries unilaterally adopt digital tax measures in order to retain tax revenue that could be lost during the period leading up to the finalisation of the BEPS project in 2020.¹⁶⁷ The most challenging issue for African countries is likely to be a lack of resources to follow-up on online presences and enforce compliance. However, this can be resolved by signing a mutual agreement.¹⁶⁸ In this respect, the UN states that in order for there to be effective changes to the PE statuses, the DTAs between developed and developing countries must be revised.¹⁶⁹ ATAF has proposed that the current OECD proposals be simpler than the past international tax rules in order to protect the African countries' tax base and allow for more tax certainty.¹⁷⁰

3.5 CONCLUSION

ATAF has suggested that African countries consider the OECD's proposed solutions (such as the revised profit allocation and nexus rules).¹⁷¹ These are designed to ensure that profits are allocated to the user jurisdiction rather than from the source of business or transaction.¹⁷² The DTC recognises that source rules may be easier to determine and modify to the advantage of South Africa¹⁷³ and other SADC countries if developed countries would be willing to cooperate; this would lead to less tax being owed to them.¹⁷⁴

¹⁶⁶https://www.un.org/esa/ffd/wp-content/uploads/2017/10/15STM_CRP22_-_Digital-Economy.pdf (accessed 27th April 2019).

¹⁶⁷*Ibid.*

¹⁶⁸As is the case with South Africa.

¹⁶⁹https://www.un.org/esa/ffd/wp-content/uploads/2017/10/15STM_CRP22_-_Digital-Economy.pdf (accessed 27th April 2019). These and other recommendations will be discussed further in Chapter Five as few developing countries in the SADC region have implemented them.

¹⁷⁰African Tax Administration Forum [2019]. *The Place of Africa in the Shift Towards Global Tax Governance: Can the taxation of the digitalised economy be an opportunity for more inclusiveness?* Page 28.

¹⁷¹African Tax Administration Forum, *Technical Note: Inclusive Framework Proposals to Address the Tax Challenges Arising in Africa from the Digitalisation of the Economy*. CBT/TN/02/19. (accessed 23rd April 2019)

¹⁷²*Ibid.*

¹⁷³In this case the SADC as the least developed jurisdictions.

¹⁷⁴Davis Tax Committee. *Second Interim Report on Base Erosion and Profit Shifting (BEPS) in South Africa* [2016] Annexure 1.

The DTC has issued a warning to South Africa that should be heeded by all developing countries - it is not enough to simply follow the lead of the developed countries, instead, countries should endeavour to conduct their own research before implementing international tax developments.¹⁷⁵ Currently, the SADC tax database does not contain any information regarding tax modifications by SADC countries, neither does it contain any BEPS digital tax recommendations for SADC countries. However, South Africa has been the most active SADC member country in the OECD, as it is described as a key participant within the OECD. This raises concerns about Africa's dedication to its tax developments. Following this observation, it is important to note that none of the SADC countries have thus far implemented the OECD's digital tax recommendations.

¹⁷⁵ *Ibid.*

CHAPTER FOUR – DISPUTE RESOLUTION IN THE DIGITAL ECONOMY

4.1 INTRODUCTION

The OECD has suggested a number of solutions to the problems relating to the taxation of the digital economy, as highlighted in the previous chapters. Implementing these solutions could result in a number of problems, including interpretation and profit allocation related disputes.¹⁷⁶

The digital economy requires effective tax regulations to be implemented in order to address the issues associated with BEPS challenges. The interpretation of these regulations may differ from country to country and as such, more effective methods of dispute resolution must be implemented on an international level.¹⁷⁷ Treaty rules traditionally required that profits be taxed in the country of residence or in a country hosting a permanent establishment.¹⁷⁸ However, any current PE rules will change drastically with digital taxation and a transparent approach to any disputes that may arise must be clearly outlined for the benefit of all parties concerned.¹⁷⁹

Incidentally, making dispute resolution mechanisms more effective was identified to be one of the solutions in the BEPS project by the OECD as Action 14. The objective of Action 14 is to prevent tax-related disputes or alternatively to ensure efficiency, reliability and transparency should a dispute arise.¹⁸⁰ In this chapter, dispute resolution is discussed in relation to how it directly and indirectly affects digital taxation. This chapter focuses on the relationship between the solutions suggested for Action 1 and the need to implement those solutions through dispute resolution, should the need arise.

¹⁷⁶PwC [2019]. *Public Consultation Document on Addressing the Tax Challenges of the Digitalisation of the Economy (PCD) as per the invitation for public input dated 13 February 2019.*

¹⁷⁷<https://www.oecd.org/tax/beps/tax-challenges-digitalisation-part-2-comments-on-request-for-input-2017.pdf> (accessed 29th November 2018).

¹⁷⁸OECD/G20 [2015]. *Base Erosion and Profit Shifting Project. Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report.* Page 26.

¹⁷⁹

¹⁸⁰OECD/G20. *Inclusive Framework on BEPS Progress Report.* July 2017 – June 2018.

4.2 DISPUTE RESOLUTION – THE OECD’S POSITION

The OECD has issued regulation guidelines, which are currently followed by member countries, while the UN attempts to establish its tax guidelines, which are also optionally followed by some countries. The OECD member countries are mostly first world countries and very rarely developing countries. This results in a lack of uniformity when implementing tax regulations in each country, giving rise to different interpretations of tax regulations. In turn, this gives rise to conflicts.¹⁸¹ The possibility of different interpretations of regulations due to uncertainty is most likely to be unprecedented in the digital economy.¹⁸² The OECD anticipated this and also published Action 14¹⁸³ and Action 15, titled OECD’s Mandate for the Development of a Multilateral Instrument on Tax Treaty Measures to Tackle BEPS (the Mandate).¹⁸⁴

In its policy notes, the OECD indicated that countries understood the importance of having effective dispute prevention measures and in failure of that, of having effective dispute resolution tools.¹⁸⁵ The OECD, in its pursuit to make dispute resolution more effective, suggested that countries respect their counterparts’ taxing rights and in utmost good faith follow the provisions of Article 25 of the OECD Model Tax Convention (the OECD Convention).¹⁸⁶ Article 25 of the OECD Model Tax Conventions provides for the application of the Mutual Agreement Procedure (MAP). This MAP essentially requires that a contracting state ensures that a taxpayer is awarded relief timeously and in accordance with the provisions of the OECD Convention in any tax dispute.¹⁸⁷ The MAP is an important provision of the OECD Convention and it provides for the “proper application

¹⁸¹<https://www.oecd.org/tax/beps/tax-challenges-digitalisation-part-2-comments-on-request-for-input-2017.pdf> (accessed 29th November 2018).

¹⁸²Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

¹⁸³OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*.

¹⁸⁴OECD/G20 [2015]. *Action 15: A Mandate for the Development of a Multilateral Instrument on Tax Treaty Measures to Tackle BEPS*.

¹⁸⁵OECD/G20 [2019]. *Addressing the Tax Challenges of the Digital Economy – Policy Note. As approved by the Inclusive Framework on BEPS on 23 January 2019*. Page 3.

¹⁸⁶OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*. Page 13.

¹⁸⁷OECD [2015], “Article 25 Mutual Agreement Procedure,” in *Model Tax Convention Income and on Capital 2014 (Full Version)*.

and interpretation” of the OECD Convention.¹⁸⁸The MAP also provides for further relief for the taxpayer should the dispute remain unresolved for two years.¹⁸⁹ This MAP seems to be an answer to many tax entities’ concerns of the interpretation of the proposed digital tax solutions.

The OECD has attempted to address issues related to lack of uniformity through the establishment of the Forum on Tax Administration (FTA) in 2002. The purpose of the FTA is to suggest a uniform approach to different tax administrative problems for member and participating countries.¹⁹⁰ In Action 15, the FTA was expanded to include an FTA MAP Forum, in which the OECD urges countries to become member countries so as to ensure that there are uniform applications of MAP provisions within the FTA’s affiliated countries.¹⁹¹ The OECD further explored the issue of uniformity within the application of the MAP and tax treaties. The OECD encouraged states to be wary of inconsistent interpretations of the tax treaties, which can be solved by the application of paragraph 3 of Article 25.¹⁹² Paragraph 3 of Article 25 states that:

(t)he competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention.¹⁹³ They may also consult together for the elimination of double taxation in cases not provided for in the Convention.¹⁹⁴

The MAP provisions require that countries should undertake to make their MAP process transparent through the publication of their MAP guidelines on a publicly accessible platform.¹⁹⁵ The OECD has requested that countries endeavour to ensure that taxpayer

¹⁸⁸OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*. Page 13

¹⁸⁹*Ibid.*

¹⁹⁰*Idem.* Page 16.

¹⁹¹*Ibid.*

¹⁹²*Idem.* Page 29.

¹⁹³OECD [2017]. *Articles of the Model Convention with Respect to Taxes on Income and on Capital*. Article 25 Paragraph 3.

¹⁹⁴This mutual agreement is meant to work as a way of helping tax authorities to come together and resolve matters that can otherwise lead to different results if they are resolved individually.

¹⁹⁵OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*. Page 20.

disputes are resolved timeously and in other circumstances proactively avoided in order to prevent disabling the taxpayer's ability to meet his tax obligations in another jurisdiction.¹⁹⁶ The MAP is especially beneficial to the taxpayer as it is meant to provide rapid relief to the taxpayer and it is meant to be structured in a manner that it is easily accessible.¹⁹⁷

The OECD has stressed the importance of the OECD Convention.¹⁹⁸ Although some treaties between individual countries are not based on it, a number of countries are signatories thereof. In this regard, the OECD has appealed to the tax administrations to ensure that their domestic tax provisions are not in conflict with those of Article 25 of the OECD Convention, especially where disputes are resolved outside the time limits of domestic laws.¹⁹⁹ The FTA MAP Forum drafted and published a "Strategic Plan" that outlines the importance of raising tax regulation awareness between jurisdictions to the benefit of both the taxpayer and the tax officials within others jurisdictions.²⁰⁰

The OECD also recommended that countries implement what it terms an advance pricing arrangement (APA) within their DTAs. APAs are arrangements where a taxpayer can enter into an agreement with taxing authorities in advance in order to establish ways of carrying out transfer pricing mechanisms over a long period of time.²⁰¹ APAs are seen as a means of avoiding the rise of disputes through an established agreement of taxation as well as avoiding double taxation for the taxpayer.²⁰² In digital tax, however, APAs are viewed as agreements that may quickly become invalid due to the ever-changing market conditions.²⁰³ Grant Thornton is of the opinion that APAs could be more operational in the

¹⁹⁶*Ibid.* Page 19

¹⁹⁷*Ibid.*

¹⁹⁸OECD [2017]. Articles of the Model Convention with Respect to Taxes on Income and on Capital.

¹⁹⁹OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*. Page 26.

²⁰⁰*Idem.* Page 29

²⁰¹ OECD [2007]. *Manual on Effective Mutual Agreement Procedures*. Page 43.

²⁰²OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*. Page 29.

²⁰³Grant Thornton International Ltd. *Addressing the Tax Challenges of the Digital Economy*. (Letter to the TFDE dated 6 March 2019).

digital economy if there is an allowance for modification of the agreements to match technological developments.

4.3 DISPUTE RESOLUTION AND DIGITAL TAXATION

Digital tax is a new concept under which many disputes are likely to arise given the ability of a digital platform to form an economic presence in more than one jurisdiction. The solutions discussed²⁰⁴ above concerning digital taxation brings with them new concepts of rights to tax profits. The International Bureau of Fiscal Documentation (IBFD) recognised that the changes that came about as a result of the digital economy could potentially result in changes in relationships between countries.²⁰⁵ The effect of such a change in relations will most likely be brought about by the allocation of taxing rights within the digital economy.²⁰⁶ An unprecedented number of disputes may arise between the taxpayer and the relevant taxing jurisdictions. The OECD's Action 14 has placed particular importance on the remedies available to the taxpayer and has not fully explored dispute resolution mechanisms between taxing jurisdictions.

The issue of possible disputes arising between jurisdictions has been of particular concern to one entity within the OECD, namely BIAC. In its public consultation document²⁰⁷, BIAC has welcomed the OECD's attempt to ensure effective and timely dispute resolution mechanisms through the MAP and the adoption the Mandate. The Mandate is a Multilateral Instrument on Tax Treaty Measures to Tackle BEPS. The purpose of the Mandate is to allow member signatories thereof to modify their tax treaties without having to re-negotiate them individually in order to incorporate BEPS measures.²⁰⁸ BIAC has proposed that instead of having the OECD focus on ensuring

²⁰⁴ In Chapter Two and Three of this dissertation.

²⁰⁵ <https://www.ibfd.org/sites/ibfd.org/files/content/pdf/Taxsutra-Digital-Economy-Dispute-Resolution-Blockchain-technology-dominate-12th-edition-of-IFA-Mauritius-Conference.pdf> (accessed 23 February 2019).

²⁰⁶ *Ibid.*

²⁰⁷ Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²⁰⁸ OECD/G20 [2015]. *Action 15: A Mandate for the Development of a Multilateral Instrument on Tax Treaty Measures to Tackle BEPS*.

effective dispute resolution measures, the OECD must also find solutions to dispute preventive measure as well as binding dispute resolution measures between jurisdictions for the good of businesses.²⁰⁹

4.4 DISPUTE RESOLUTION BETWEEN JURISDICTIONS

The Asian Development Bank Institute (ADBI) recognised that in order to effectively address the challenges of the digital economy, countries had moved on from traditional jurisdictional tax approaches.²¹⁰ This will definitely give rise to a number of tax-related disputes between jurisdictions. In 2007, the OECD published a report that issued guidelines on improving tax treaty disputes.²¹¹ This report established tax dispute mechanisms within the MAP. The OECD has now attempted to perfect these mechanisms in its Action 14.²¹² The attempt by the OECD to perfect the Action 14 mechanisms amounts to further contributions to the provisions of a DTA, which provides for dispute resolution mechanisms between states (mostly ADR). Many different tax organisations have not made an effort to establish an international tax resolution body because there are no set rules that form “public international tax law”.²¹³ There is instead, a general consensus that there cannot be an international way of looking at tax treaties due to their inflexibility and the way they are incorporated into law optionally by different jurisdictions.²¹⁴ This has been identified as an issue in the past and the OECD has addressed it in its BEPS action plans.

Updates to the OECD Convention and the UN Model Tax Convention (UN Convention) were published in 2017 in line with the BEPS action plan²¹⁵ These conventions are not

²⁰⁹Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²¹⁰ADBI Institute [2017]. *ADBI Policy Brief No. 2017-5: Fair Taxation in the Digital Economy*. Asian Development Bank Institute.

²¹¹<https://www.oecd.org/ctp/dispute/38055311.pdf> (accessed 21 March 2019).

²¹²OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*.

²¹³Olivier L, *et al.* [2011]. *International Tax: A South African Perspective*. 2011. Page 288.

²¹⁴Rohatgi R. [2005]. *Basic International Taxation*. Vol. 1 2nd ed. United Kingdom, Richmond Law & Tax Ltd. Page 37.

²¹⁵UN [2013]. *United Nations Model Double Taxation Convention between Developed and Developing Countries*. UN, New York. <https://doi.org/10.18356/a545408b-en>. (accessed 21 November 2018).

the law but guiding principles to the tax treaties that are signed between countries. These two models are very similar and only differ in a few provisions. The differences between the two conventions are indicative of the works of the UN and the OECD. The UN's provisions favour an inclusive approach which attempts to attract investments to developing countries through controlling discrimination of international taxpayers.²¹⁶ The UN published a guide to Article 25 wherein it outlined the recommended application of the MAP that is contained in the UN Convention. The UN indicated that the MAP was not a measure for inter-jurisdictional²¹⁷ disputes alone but that these could also be resolved through diplomatic means as outlined in tax treaties.²¹⁸ One of these measures, as they were in the updated OECD Convention commentary, stipulates that should states fail to reach a consensus in any matters before them a person can submit such dispute for arbitration. The outcome of the arbitration would then be binding on all the jurisdictions concerned as well as the taxpayer.²¹⁹

The OECD made a few updates to the OECD Convention, which could likely cater to territorial tax disputes. The OECD Convention's introductory paragraphs state that countries should consider entering into tax treaties that would allow for the *possibility* of arbitration in the event of cross border tax disputes.²²⁰ Article 25 of both the OECD Convention and the UN Convention deal with MAP and attempt to establish a means of communication between tax authorities and the taxpayer in an amicable manner. Articles 25 of both conventions²²¹ provide that Contracting States may communicate with one another through a joint commission consisting of their representatives with the purpose of reaching a resolution under the terms of a mutual agreement that would have been

²¹⁶*Ibid.*

²¹⁷Disputes between countries.

²¹⁸https://www.un.org/.../16STM_Chapter5_Dispute-Handbook_Mutual-Agreement.pdf (accessed 4th March 2019).

²¹⁹ www.oecd.org/ctp/treaties/2017-update-model-tax-convention.pdf (accessed 22nd June 2018).

²²⁰OECD [2017]. "Introduction" in *Model Tax Convention on Income and on Capital: Condensed Version 2017*.

²²¹The UN Convention has alternative A and B wherein A does not include provisions for arbitration whilst alternative B does. The OECD Convention does not have alternative A or B, it is simply one Article with 5 paragraphs.

concluded, should there be difficulties in resolving a tax dispute.²²² Contracting States may also institute arbitration proceedings should there be any difficulties in resolving tax disputes, with the UN Convention making a requirement for a competent authority to institute these proceedings whilst the OECD Convention allows for an interested party in the dispute to institute arbitration proceedings.²²³

In a public commentary on dispute resolution,²²⁴ the OECD realised that the lack of open communication channels between tax authorities makes it difficult for them to resolve disputes through the MAP procedure.²²⁵ In an attempt to address this, the OECD has encouraged the exchange of information between jurisdictions. Paragraph 3 of Article 25 states that countries should be willing to resolve any tax disputes arising between one Contracting State and a taxpayer with the counsel of the other Contracting State, should the intended outcome of that matter have a direct effect on either Contracting State.²²⁶ This provision clearly supports exchange of information in the manner that the OECD expects for effective dispute resolution mechanisms.

The OECD's positive move towards a system of open exchange of information in tax-related matters is of great assistance in digital taxation. Exchange of information could be encouraged through the conclusion of a DTA that allows for it. In order to conclude an effective DTA between countries, the OECD has also recommended that countries consider the "ability and willingness of a state to provide assistance in the collection of taxes".²²⁷ Digital tax is largely reliant on digital information collected and shared between states as the transactions are concluded online. This provision, should the countries be

²²²www.oecd.org/ctp/treaties/2017-update-model-tax-convention.pdf (accessed 22nd June 2018), Article 25 Paragraph 4. https://www.un.org/.../16STM_Chapter5_Dispute-Handbook_Mutual-Agreement.pdf (accessed 4th March 2019). Article 25 Alternative A Paragraph 4 and Alternative B Paragraph 4.

²²³*Ibid.* OECD Convention Article 25 Paragraph 5, UN Convention Alternative B Paragraph 5.

²²⁴OECD [2015]. "BEPS Action 14: Making Dispute Resolution Mechanisms More Effective." Comments Received on Public Discussion Draft 2015.

²²⁵*Ibid.*

²²⁶OECD [2017]. *Model Convention with Respect to Taxes on Income and Capital: Condensed Version 2017*.

²²⁷OECD [2017]. "Introduction" in *Model Tax Convention on Income and on Capital: Condensed Version 2017*.

open to it, would prove to be beneficial to the contracting states and signatories of both the UN Convention and the OECD Convention.

Article 7 of the OECD Convention states that no state can tax profits of an enterprise of another state unless that enterprise has a PE in that state.²²⁸ With the advent of the digital economy, the provisions of Article 7 are likely to lead to a number of disputes between jurisdictions. It is expected that the OECD realises the restrictiveness of Article 7 and will therefore attempt to expand it in order to allow for digital tax transactions. Article 5 of the OECD Convention relating to PEs was updated but did not specifically mention digital transactions.²²⁹ Chapter Two of this dissertation indicated that the capacity to tax profits in the digital economy would arise from where a contract was signed by the purchaser of the goods but the OECD did not make provisions for such contracts in Article 5 paragraph 5. Article 5 paragraph 5 of the OECD Convention makes provisions for establishing PE status where an individual concludes contracts on behalf of an enterprise, when contracts effectively transfer property rights owned by that enterprise or renders services on behalf of that enterprise.²³⁰ Paragraph 6 contains an exclusion to paragraph 5, if such an individual was acting as an independent agent of the concerned enterprise.

It is important for the OECD to make relevant allowances in the Convention for many tax models that arise within the digital economy. These tax models are most likely to lead to numerous disputes between contracting states as well as third party states from which the taxing rights would have been acquired.²³¹ The currently proposed digital tax solutions are of concern to ActionAid International. ActionAid International realises that there is a real possibility of countries losing the income that they were previously entitled to and has therefore taken to advising developing countries not to be party to binding arbitration agreements.²³² ActionAid International has however promised to review its stance on

²²⁸OECD [2017]. "Commentary of Article 5" in *Model Tax Convention on Income and on Capital: Condensed Version 2017*.

²²⁹*Ibid*.

²³⁰www.oecd.org/ctp/treaties/2017-update-model-tax-convention.pdf (accessed 22nd June 2018). Article 5 Paragraph 5.

²³¹Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²³²IMF/ActionAid [2018]. *Analysis of International Corporate Taxation*. (accessed 9 April 2019).

binding arbitration procedures only if the OECD takes into account developing countries' struggle with the current "skewed" international tax rules.²³³

Although the MAP may be the focus-point for the OECD, the question is whether it will be the same with digital taxation. The OECD made its position clear regarding dispute resolution between states, yet it is still to propose more developments regarding dispute resolution in digital taxation where lines of taxation have been blurred, especially between states. BIAC recognises the need to have a well-defined and strong dispute resolution mechanism in order to create a balance between the states and the taxpayer.²³⁴

4.4.1 Dispute resolution for the taxpayer (individuals and businesses)

The digital economy has led to the rise of a number of business models that are not typically catered for tax legislation.²³⁵ With the implementation of the BEPS project, more particularly Action 1, a number of disputes will most likely arise between the taxpayer and the tax authority. A number of dispute resolution mechanisms for individuals and tax authorities have been highlighted above. Dispute resolution mechanisms for the unintended taxation or double taxation of the taxpayer has been largely addressed by Action 14 of the BEPS project.

Due to the shift in the concept of a PE in the digital economy, it is probable that the taxpayer could be subject to possible double taxation or double non-taxation. In order to control the effects of double taxation, the OECD has attempted to ensure fairness for the taxpayer through the MAP procedure, which is more beneficial to the taxpayer and easier to follow-up in the event of a dispute with a tax authority.²³⁶ The OECD also indicated in Action 14 that countries are required to publish guidelines on how to access their

²³³ *Ibid.*

²³⁴Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²³⁵OECD/G20 [2015]. *Base Erosion and Profit Shifting Project: Addressing the Tax Challenges of the Digital Economy. Action 1: 2015 Final Report*.

²³⁶OECD/G20 [2015]. *Action 14: Making Dispute Resolution Mechanisms More Effective Final Report*. OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

respective MAPs on a publicly accessible platform.²³⁷ This is meant to alert (especially) non-resident taxpayers on how to attain relief in the event of a dispute.

An important update to dispute resolution is the update to Article 25, which is an outline of the MAP. Paragraphs 14 to 19 have allowed the taxpayer to initiate proceedings under the MAP without waiting for tax to be charged to him.²³⁸ These proceedings may be initiated when such taxation is not in accordance with the OECD Convention and is an actual possibility.²³⁹ A situation where taxes are erroneously assessed could be easy to anticipate in the digital economy since taxation will ideally occur at the destination state. The taxpayer has been accorded three years to launch an appeal on his taxation in the event of such being done in a manner that is not in accordance with the OECD Convention.²⁴⁰

BIAC states that the importance of dispute resolution in digital tax is such that it should be included as one of the pillars of proposed solutions within the next updates to Action 1.²⁴¹ Although many tax related organisations are quick to indicate the expenses involved in long litigation for the governments, it is important to note that it will be more expensive for the taxpayer *vis a vis* litigation costs and taxes that will still have to be paid to that particular jurisdiction. BIAC therefore proposes that taxpayers must be alerted to dispute prevention measure such as the APA for their benefit in order to reduce pressures and delays that may be associated with the actual dispute resolution process.²⁴²

4.5 CONCLUSION

BIAC openly advocates for an agreement containing tax thresholds, APA's and other dispute preventative measures to be put in place in order to avoid the dispute resolution

²³⁷ *Ibid.*

²³⁸ www.oecd.org/ctp/treaties/2017-update-model-tax-convention.pdf (accessed 22nd June 2018).

²³⁹ *Ibid.*

²⁴⁰ *Ibid.*

²⁴¹ Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²⁴² *Ibid.*

itself.²⁴³ In view of the operation of the digital economy, it is important for tax authorities that the provisions for dispute resolution proposed by the OECD are clearly explained to the public. BIAC has noted with concern that dispute resolution was considered to be merely incidental to the challenges surrounding the digital economy instead of forming an integral part thereof.²⁴⁴ It is clear that the introduction of tax regimes in the digital economy will therefore most certainly lead to misunderstandings between the taxpayer and the taxing authority and between two contracting authorities. It is also important for the OECD to take into account the views of ATAF, UNCTD and ActionAid International regarding developing countries.

The OECD to find a way to create a platform that publishes international tax precedents in order to attempt to adhere with the Ottawa tax principles of certainty and uniformity.

²⁴³ *Ibid.*

²⁴⁴ *Ibid.*

CHAPTER FIVE –THE PUBLIC’S RESPONSE TO THE OECD’S PROPOSED SOLUTIONS

5.1 INTRODUCTION

Digital tax is a new concept. It has been difficult to tackle, with attempted solutions originally coming from the Ottawa Framework²⁴⁵ and more significantly from the OECD in 2015. Although the OECD proposed a number of solutions relating to digital taxation in its Action 1 of the BEPS project, commentaries submitted thereafter reflected that more solutions could be suggested or improvements could be made to the proposed solutions. In its 2018 Interim Report, the OECD indicated that the 2015 Action 1 report is not final with the final report expected in 2020.²⁴⁶

5.2 GENERAL RESPONSES TO THE OECD’S ACTION 1 PROJECT

Although the Action 1 BEPS project is to be finalised in 2020, many countries have reacted favourably to the first report that was published in 2015. Several companies, including KPMG, have shown appreciation for the OECD’s Action 1 Report but have cautioned against applying these tax measures in an uncoordinated unilateral manner if they are to be implemented with certainty and in uniformity in line with important tax principles.²⁴⁷ Companies and enterprises are however of the view that some of the OECD’s proposed solutions would be difficult to execute for both the taxpayers and the administrators. These companies have recommended easier ways to implement the OECD’s proposed solutions.

In its 2017 commentary to the TFDE, KPMG indicated that for a more sufficient solution to be reached, a thorough and inclusive process had to be employed which would take

²⁴⁵OECD Committee on Fiscal Affairs [1998]. *Electronic Commerce: Taxation Framework Conditions*.

²⁴⁶OECD/G20 [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*.

²⁴⁷KPMG International [2019]. *Comments on OECD Public Consultation Document on Addressing the Tax Challenges of the Digitalized Economy*. With reference to the Ottawa tax principles.

time and further research to achieve.²⁴⁸ This indicates an ongoing process which would take years to complete. In turn, this shows that even though the OECD proposed a number of solutions both in its Action 1 report and the further 2018 Interim Report, more is still expected in digital taxation. The OECD issued another publication calling organisations to comment on the issues raised in its 2019 request for input.²⁴⁹ These comments are what this chapter is based on, as many of these organisations either came up with new solutions for digital taxation or made further contributions to the proposals put forward by the OECD in its public consultation document. This chapter will therefore outline the views of a number of companies that specialise in tax.

BIAC is responsible for business advisory services to the OECD. In its comments to the OECD's request for input, BIAC cautioned the OECD on a number of comments that were submitted by other companies to the OECD in response to its request for comments on Action 1 and the 2018 Interim Report. Its responses will be outlined below in response to some of the suggestions made by other entities.

Importantly, BIAC suggested that any solutions proposed on digital taxation must be consistent with economic reality and should address the concerned problems.²⁵⁰ BIAC also stated that the digital economy will bring with it many changes to the current taxing rights. This change will mean some countries will lose taxing rights whilst others will gain them.²⁵¹ Due to the potential for disputes in that scenario, BIAC has proposed that dispute resolution must be made mandatory instead of merely binding, as it currently stands.²⁵²

²⁴⁸KPMG International [2017]. *Comments with respect to the request for input with respect to the series of questions related to the BEPS Action 1 report on Addressing the Tax Challenges of the Digital Economy (the 2015 report) and the Draft Outline of the Interim Report for the G20 Finance Ministers.*

²⁴⁹OECD [2019]. *Addressing the Tax Challenges of the Digitalisation of the Economy: Public Consultation Document.*

²⁵⁰Business at OECD [2019]. *Business at OECD Feedback on Addressing the Tax Challenges of the Digitalization of the Economy Public Consultation Document.*

²⁵¹*Ibid.*

²⁵²*Ibid.*

5.2.1 BEPS Monitoring Group – Comments submitted to the OECD

The BEPS Monitoring Group requested that the OECD improve the proposed solutions by requiring clarity on the taxes suggested. Their main concerns were based on the multinational enterprise (MNE) based solutions. MNE are enterprises that are based in multiple jurisdictions and are capable of shifting their tax obligations to low-cost jurisdictions.²⁵³ The proposed MNE solutions are meant to ensure transparency within large MNEs in their tax filings in different jurisdictions.²⁵⁴ The UK has introduced legislation in order to monitor MNEs called the Diverted Profits Tax, where a rate of 25% is fined on any profits derived from an attempt to artificially avoid tax liability in the UK.²⁵⁵ This type of legislation has been successfully implemented within the UK with the OECD predicting its success should more countries intend to implement it.²⁵⁶ This however contradicts the OECD's concerns of unilateral application of BEPS measures in favour of a unitary approach.

The MNE-based solutions are akin to formulating new transfer pricing requirements. In order to eliminate the additional administrative burden that will be associated with the newly proposed transfer pricing regulations in digital economics, the BEPS Monitoring Group proposed that the OECD should attempt to formulate a standard key. This key can be used as a guideline to profit allocation that the international community can follow in order to avoid double application of the same taxes, and profit shifting within the MNE's to a lower tax cost jurisdiction.²⁵⁷ This would involve a fixed set of rules that guide the international tax community's method of application of the profit allocation to the new digital tax system.²⁵⁸ This approach was rejected by BIAC. BIAC indicated that this approach would be unfair to the concerned taxpayers because no businesses are the same and the individual integrity of each business could be compromised by assuming

²⁵³OECD/G20 [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 106.

²⁵⁴ *Ibid.* Page 147.

²⁵⁵This is considered to be a punitive form of tax for those MNE's that artificially avoid their UK tax liability.

²⁵⁶OECD/G20 [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. Page 151.

²⁵⁷The BEPS Monitoring Group [2019]. *Submission to the Inclusive Framework Public Consultation on Addressing the Tax Challenges of the Digitalisation of the Economy*.

²⁵⁸ <https://www.ey.com/...tax.../EY-tax-technology-and-transformation.pdf>. (accessed 29th July 2019).

that they are the same.²⁵⁹ However, the BEPS Monitoring Group believes that its proposed approach could lead to a better way of avoiding disputes that could arise as a result of new transfer pricing guidelines issued for digital taxation, thus making it easier on both the taxpayer and the tax authority.²⁶⁰

The BEPS Monitoring Group has also strongly encouraged the OECD to reconsider its intention to allocate MNE profits singularly, and instead focus on the “unitary firms they are” in order to do away with possible double taxation.²⁶¹ ATAF does not share this view. ATAF requested that the current profit allocation rules be modified to show the flow of MNE profits that are due to their market jurisdiction to avoid under-taxing that jurisdiction.²⁶² The BEPS Monitoring Group also proposed that a balance of factors should be done before the allocation of profits can be made in MNEs. These factors include considering labour and capital vs sales rather than simply focusing on the sales at the market jurisdiction alone.²⁶³ Value creation is largely based on the outcome of all factors considered, thus creating a risk of uncertainty should there be too much focus on one factor over another for allocation of profits consideration. BIAC suggested that attention be paid to MNEs as singular entities, as this would avoid double taxation whilst also pointing out the dangers of profitable MNEs in competition law related matters.²⁶⁴

5.3.2 Deloitte Touche Tohmatsu Limited (Deloitte) – Comments submitted to the OECD

Deloitte’s concerns were concerned with ensuring that the objects of the Ottawa Framework are adhered to. Deloitte is of the view that Action 1 is not entirely concerned with BEPS, instead, Action 1 will change the current taxation framework in order to make

²⁵⁹Business at OECD [2019]. *Business at OECD Feedback on Addressing the Tax Challenges of the Digitalization of the Economy Public Consultation Document*.

²⁶⁰The BEPS Monitoring Group [2019]. *Submission to the Inclusive Framework Public Consultation on Addressing the Tax Challenges of the Digitalisation of the Economy*.

²⁶¹*Ibid*.

²⁶²The African Tax Administration Forum [2019]. *The Place of Africa in the Shift Towards Global Tax Governance: Can the Taxation of the Digitalised Economy be an Opportunity for more Inclusiveness?*

²⁶³The BEPS Monitoring Group [2019]. *Submission to the Inclusive Framework Public Consultation on Addressing the Tax Challenges of the Digitalisation of the Economy*.

²⁶⁴Business at OECD [2019]. *Business at OECD Feedback on Addressing the Tax Challenges of the Digitalization of the Economy Public Consultation Document*.

allowances for the digital era.²⁶⁵ Deloitte indicated the need for consistency in order to minimise the emergence of tax-related disputes in the application of the newly proposed rules.²⁶⁶ This view was supported by BIAC, which indicated the importance of consistency through the application of the Ottawa Framework tax principles in order to ensure effective dispute resolution mechanisms and ensure global agreement in digital tax-related solutions.²⁶⁷

Deloitte has proposed a residual profit split method between more than two multinational levels instead of the usual split between two jurisdictions.²⁶⁸ Deloitte, in this instance, recognises that digitalisation will make it possible for revenue derived therefrom to be attributed to more than two jurisdictions. This comes after the realisation that the digital economy will spread profits to more than one jurisdiction, therefore, a fairer approach to that consequence must be anticipated. Deloitte also notes that there is a high potential for increased tax disputes and has proposed that where profits are split between more than one jurisdiction, the jurisdictions be involved in auditing and further arbitration to ensure a binding decision.²⁶⁹

5.3.3 Ernst and Young (EY) – Comments submitted to the OECD.

Ernst and Young (EY) shared the same sentiments with its counterparts on a number of issues that are related especially to a unitary approach, which sees a single application and interpretation of the proposed digital tax solutions. EY has urged the OECD to monitor the implementation process in order to educate country officials on the newly proposed rules and indicate that these rules have no retrospective application, neither do they interpret rules that are already in existence.²⁷⁰ EY has also proposed a fair application of

²⁶⁵Deloitte [2019]. *Public Consultation Document: Addressing the Tax Challenges of the Digitalisation of the Economy*.

²⁶⁶*Ibid.*

²⁶⁷Business at OECD [2019]. *Business at OECD Feedback on Addressing the Tax Challenges of the Digitalization of the Economy Public Consultation Document*.

²⁶⁸Deloitte [2019]. *Public Consultation Document: Addressing the Tax Challenges of the Digitalisation of the Economy*.

²⁶⁹*Ibid.*

²⁷⁰Ernst & Young [2019]. *Comments on Public Consultation Document: Addressing the Tax Challenges of the Digitalisation of the Economy*.

the new rules. This would involve a taxpayer being able to invoke the MAP between its home country and the country that requires taxes where it would not have been required to pay such taxes in the past.²⁷¹ This also means that the MAP should be allowed even in countries where a DTA does not exist between the two jurisdictions, important focus being on the needs of the taxpayer.

BIAC notes that the proposed solutions should not be too complicated for developing countries to incorporate, neither should they be too complicated to be explained to interested parties.²⁷²

5.3.4 Klynveld Peat Marwick Goerdeler (KPMG) – Comments submitted to the OECD 2017 & 2019).

KPMG notes that there is a general unwillingness by tax authorities to adopt measures to assist administratively, where there are divergent perspectives/a difficulty encountered in the application of tax profit attributions.²⁷³ This is a call for global contribution to a more effective tax system that distributes taxing rights fairly such that global consensus is reached eventually through the new age digital tax rules.²⁷⁴ The OECD published new VAT/GST guidelines that have been qualified as a success thus far by the many jurisdictions that have adopted them, due to the global consensus reached in applying them. However, the issue as KPMG has noted, remains the administrative burden that has been placed upon different companies and administrations with the introduction of these guidelines.²⁷⁵

²⁷¹ *Ibid.*

²⁷² Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²⁷³ KPMG International [2017]. *Comments with respect to the request for input with respect to the series of questions related to the BEPS Action 1 report on Addressing the Tax Challenges of the Digital Economy (the 2015 report) and the Draft Outline of the Interim Report for the G20 Finance Ministers*.

²⁷⁴ OECD/G20 [2018]. *Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS*. OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

²⁷⁵ KPMG International [2017]. *Comments with respect to the request for input with respect to the series of questions related to the BEPS Action 1 report on Addressing the Tax Challenges of the Digital Economy (the 2015 report) and the Draft Outline of the Interim Report for the G20 Finance Ministers*.

In March 2019, with the OECD's request for comments, KPMG furnished more of its views on the matter. KPMG noted the importance of providing effective dispute resolution mechanisms. It requested that there be equality between developing countries and developed countries in arbitration proceedings.²⁷⁶ This equality can be achieved through providing adequate training, support and resources to the developing economies.²⁷⁷ The UN and ATAF also support KPMG's view of including solutions that are beneficial to developing countries to a larger extent, as they lobby for a fairer tax representation for African economies. BIAC is of the view that should there be any policy reviews incorporating dispute resolution, such reviews should take place on a global scale in order to avoid the numerous disputes that will arise from unilateral diverging policies in a sensitive tax environment.²⁷⁸

5.3.5 Pricewaterhouse Coopers International (PwC) – Comments submitted to the OECD

PwC did not offer any further solutions to digital taxation but instead sought to indicate the effect of the OECD's proposed solutions. PwC cautioned against an increased administrative burden as this has a negative effect on the taxpayer's investment capacity as well as a negative impact on the tax authority's ability to acquire more revenue.²⁷⁹ PwC also expressed concern over the proposed profit allocation principle. It predicts that this principle can potentially give rise to double taxation in an economy where dispute resolution mechanisms have not been modified to deal with this.²⁸⁰ Yet, this can be solved by allocating taxing rights in a consistent, coherent and agreed manner preferably through the APA method.²⁸¹

²⁷⁶KPMG International [2019]. *Comments on OECD Public Consultation Document on Addressing the Tax Challenges of the Digitalized Economy*.

²⁷⁷*Ibid.*

²⁷⁸Business at OECD [2019]. *Feedback on Addressing the Tax Challenges of the Digitalisation of the economy Public Consultation Document*. (Letter addressed to the OECD).

²⁷⁹PwC [2019]. *Public Consultation Document on Addressing the Tax Challenges of the Digitalisation of the Economy (PCD) as per the invitation for public input dated 13 February 2019*.

²⁸⁰*Ibid.*

²⁸¹Business at OECD [2019]. *Business at OECD Feedback on Addressing the Tax Challenges of the Digitalization of the Economy Public Consultation Document*.

BIAC recommended that in order for the profit allocation principle to be successfully implemented, it should be done by all tax authorities to avoid proposing a voidable tax solution.²⁸² The idea behind this request is that it would not be fair to expect one jurisdiction to adhere to a principle that is most likely to result in it losing profits through a digital transaction whilst another jurisdiction is not willing to adhere to the same principle. This could give rise to uncertainty and unwillingness to cooperate, even in dispute resolution mechanisms.²⁸³

5.3.6 The United Nations (the UN)

The UN did not submit any comments in response to the request by the OECD but it has constantly kept itself up-to-date with the advances made by the OECD through its Committee of Experts on International Cooperation in Tax Matters (the UN Tax Committee). This UN Tax Committee meets on a yearly basis to discuss any significant tax developments. In 2017, the UN Tax Committee noted that the OECD's proposed nexus status could potentially ring-fence the digital economy.²⁸⁴ Ring-fencing the digital economy is a proposed solution that the OECD has rejected due to its impracticality of focusing on just the digital economy and not the rest of the BEPS causing issues.²⁸⁵

The UN is largely concerned about developing countries and mostly makes propositions that will be simpler for developing countries to implement. The UN proposed that when considering allocating taxing rights to the market, many factors could be considered in order to avoid detrimental taxing effects to developing countries.²⁸⁶ These factors included a combination of factors such as determining users, sales and digital presence as opposed to simply considering the market and sales.²⁸⁷ Tax Justice Network Africa noted with concern that Africa, as a developing economy, already loses a large amount

²⁸² *Ibid.*

²⁸³ OECD/G20. *Inclusive Framework on BEPS Progress Report*. July 2017 – June 2018.

²⁸⁴ <https://www.un.org/esa/ffd/events/event/fifteenth-session-tax.html> (Committee of Experts on International Cooperation in Tax Matters [2017]. (accessed 27 April 2019)

²⁸⁵ OECD [2019]. *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy*. OECD/G20 Inclusive Framework on BEPS, OECD, Paris. Page 28.

²⁸⁶ https://www.un.org/esa/.../18STM_CRP12-Work-on-taxation-issues-digitalization.pdf. (accessed 24th June 2019).

²⁸⁷ *Ibid.*

of money through illicit financial flows (IFFs); the proposed digital tax solutions could lead to an even greater burden and loss through its administrative system.²⁸⁸ This view has also been supported by IMF, ActionAid International and ATAF. Joy Ndubai, an ActionAid International Global Tax advisor stated that although some African countries²⁸⁹ already have legislation in place for digital transactions like VAT, there is still challenges in corporate taxation. She highlighted with concern that African countries are not utilising resources available to them in order to be fully capacitated to implement digital tax solutions.²⁹⁰ Ms Ndubai also noted that African countries will face challenges even when they elect to use the same available resources (like data sharing and country to country reporting) due to a general lack of resources to mobilise the jurisdictions in the first place.²⁹¹

Although there are a number of tax specialist organisations internationally, they are not as pro-active in dealing with major tax issues as are the World Trade Organisation (WTO) in trade disputes, International Labour Organisation (ILO) in labour matters and the World Intellectual Property Organisation (WIPO) in intellectual property matters. These organisations offer extensive services in their respective fields, which include dispute resolution (ADR) services. The tax field has the OECD but it does not have an internationally sanctioned dispute resolution entity.

5.4 CONCLUSION

KPMG showed particular concerns with the unilateral application of digital tax solutions and encouraged countries to await an international solution.²⁹² It seems that the lack of international certainty, from a dispute resolution point of view, will stunt economic development. It is not only KPMG that is concerned about the lack of international tax

²⁸⁸The Tax Justice Network Africa [2019]. *Joint Submission to the OECD Public Consultation on the "Tax Challenges of Digitalisation"*.

²⁸⁹Notably South Africa.

²⁹⁰<https://www.youtube.com/watch?v=166PArkJ2tg&feature=youtu.be> (accessed 11 October 2019).

²⁹¹*Ibid.*

²⁹²KPMG International [2019]. *Comments on OECD Public Consultation Document on Addressing the Tax Challenges of the Digitalized Economy*.

solutions but also the BEPS Monitoring Group that has expressed concern over the lack of set “international tax law”. The BEPS Monitoring Group has recognised that there is a need to ensure uniformity between its recommendations relating to digital tax and the MAP and also advocated for a tax dispute resolution and an adjudicating body.²⁹³

The UN and the World Bank Group have indicated that developing countries do not have the same freedoms and resources to implement the proposed solutions to digital tax and that the OECD must consider them in its proposals.²⁹⁴ The OECD has indeed proposed solutions to the taxation of the digital economy and for the management of disputes that may arise therefrom. The proposed solutions which have thus far been made into law, such as DPT, have seen companies attempting to avoid the liability that comes from contravening it. There is a measure of success in some of the proposed solutions, yet it is still to be seen how far-reaching that success will be internationally, as there has not been any response from SADC. The proposed solutions will allow for the digital economy to be taxed in a way that grants countries fair taxing rights whilst avoiding disputes that may arise.

²⁹³The BEPS Monitoring Group [2019]. *Submission to the Inclusive Framework Public Consultation on Addressing the Tax Challenges of the Digitalisation of the Economy*.

²⁹⁴World Bank Group [2016]. “South Africa: Sector Study of Effective Tax Burden and Effectiveness of Investment Incentives in South Africa – Firm Level Analysis”.

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