



Allocation of the Right to Tax Income  
from Digital Intermediary Platforms  
– Challenges and Possibilities for Taxation in  
the Jurisdiction of the User

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## ABSTRACT

The authors analyse the current (lack of) possibilities for user-jurisdictions to tax the value generated by the increased use of digital intermediary platforms. Focus is on analysing the possibilities for user-jurisdictions to tax the remuneration received by a foreign enterprise owning a digital intermediary platform and on discussing whether the users' provision of personal data in exchange for access to the platform could be considered a barter transaction for tax purposes in the user-jurisdiction. Among other things, it is concluded that user-jurisdictions, pursuant to current international tax treaties, will normally be precluded from taxing the income of foreign platform enterprises, as the platform enterprises are often able to deliver their digital services remotely. Against this background, a number of tax policy challenges and options of relevance for taxing platform enterprises are discussed, in particular the proposed directive on significant digital presence recently put forward by the European Commission. It is concluded that the proposal may prove to be an adequate step towards taxation in the user-jurisdictions, even though the proposal needs further work in order to become sufficiently clear and targeted and the scope may be limited.

## 1. INTERNATIONAL TAX LAW AND THE DIGITAL CHALLENGE

In recent years, it has become clear that the increasing digitalisation of the economy poses challenges with respect to international taxation, as current international tax law and its underlying principles have not kept pace with the changes in global business practices, including practices based on the intensified use of information and communications technology.<sup>1</sup> Accordingly, as the current international tax framework was originally designed to deal with "brick and mortar" businesses, it may be argued that the framework is not sufficiently equipped to address modern, digitalised business practices, where physical presence in the market jurisdictions is no longer necessary.<sup>2</sup>

Policymakers have discussed these challenges at least since the late 1990s,<sup>3</sup> but the attention has dramatically increased in later years. In particular, the OECD/G20 project aimed at mitigating base erosion and

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<sup>1</sup> Marcel Olbert and Christoph Spengel, 'International Taxation in the Digital Economy: Challenge Accepted?' (2017) 9 *World Tax Journal* 1.

<sup>2</sup> Georg Kofler et al., 'Taxation of the Digital Economy: Quick Fixes or Long-Term Solution?' (2017) 57 *European Taxation* 12. See also the same authors, 'Taxation of the Digital Economy; A Pragmatic Approach to Short Term Measures', (2018) 58 *European Taxation* 4.

<sup>3</sup> See e.g. OECD, *Taxation and Electronic Commerce – Implementing the Ottawa Taxation Framework Conditions* (OECD Publishing 2001). For more on the earlier policy initiatives see e.g. Peter Koerver Schmidt, 'Den digitale økonomi som skatteretlig udfordring' in Borge Dahl et al. (eds), *Liber Amicorum Peter Møgelvang Hansen* (Extuto 2016).

profit shifting (BEPS) has attracted interest.<sup>4</sup> The project focuses on aggressive tax planning carried out by multinational enterprises,<sup>5</sup> and one of the deliveries consisted of a report specifically dealing with the tax challenges of the digital economy.<sup>6</sup> Among other things, the report highlighted some key features of the digital economy that was seen as particularly relevant from a tax law perspective. These features for example included increased mobility, reliance on data, network effects and the spread of multisided business models. As such, the features of the digital economy were not considered to generate unique BEPS risks, but it was acknowledged that these features could exacerbate the risks.<sup>7</sup>

The report also addressed a number of broader tax challenges raised by the digital economy, and a number of policy options were considered, however, without reaching an agreement on whether any of the options should be adopted.<sup>8</sup> After the release of the report, the OECD/G20 has continued its work, and in March 2018 a new interim report was made publicly available.<sup>9</sup> The new report further elaborates on the tax issues raised by digitalisation and concludes that, overall, there is support for undertaking a coherent and concurrent review of two key aspects of the existing tax framework, namely nexus rules and profit allocation rules.<sup>10</sup>

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<sup>4</sup> OECD, *Addressing Base Erosion and Profit Shifting* (OECD Publishing 2013) and OECD, *Action Plan on Base Erosion and Profit Shifting* (OECD Publishing 2013).

<sup>5</sup> For more on the background of the BEPS project see Yariv Brauner, 'BEPS: An Interim Evaluation' (2014) 6 *World Tax Journal* 1.

<sup>6</sup> OECD/G20, *Addressing the Tax Challenges of the Digital Economy – Action 1 Final Report* (OECD Publishing 2015).

<sup>7</sup> *Ibid.* p. 11-12.

<sup>8</sup> *Ibid.* p. 99 and p. 136-139.

<sup>9</sup> OECD/G20, *Tax Challenges Arising from Digitalisation – Interim Report* (OECD Publishing 2018). Also academia has showed a massive interest in the tax challenges raised by the digital economy. Hence, several contributions in the academic literature have recently addressed the broader issues. Besides the contributions already mentioned see for example Ina Kerschner and Maryte Somare (eds.), *Taxation in a Global Digital Economy* (Linde Verlag 2017), Yariv Brauner and Pasquale Pistone, 'Adapting Current International Taxation to the New Business Models: Two Proposals for the European Union' (2017) 71 *Bulletin for International Taxation* 12, Joachim Englisch, 'BEPS Action 1: Digital Economy – EU Law Implications' [2015] *British Tax Review* 280, Maarten de Wilde, 'Tax Jurisdiction in a Digitalizing Economy; Why Online Profits Are So Hard to Pin Down' (2015) 43 *Intertax* 12, Miranda Stewart, 'Abuse and Economic Substance in a Digital BEPS World' (2015) 69 *Bulletin for International Taxation* 6/7, Aleksandra Bal and Carlos Gutiérrez, 'Taxation of the Digital Economy' in Madalina Cotrut (ed), *International Tax Structures in the BEPS Era: An Analysis of Anti-Abuse Measures* (IBFD 2015), Walter Hellerstein 'Jurisdiction to Tax in the Digital Economy: Permanent and Other Establishments' (2014) 68 *Bulletin for International Taxation* 6/7, and Arthur Cockfield et al., *Taxing Global Digital Commerce* (Wolters Kluwer 2013).

<sup>10</sup> OECD/G20 (2018) [footnote 9], p. 212-213. It is contemplated that a final report should be published in 2020.

In light of the topic of this article, it is particularly interesting that the interim report further elaborates on the significance of user-participation in the value creation process of certain highly digitalised business models, including business models relying on digital intermediary platforms. Thus, even though consensus was not reached, the interim report reflects that a number of countries are of the opinion that the current international tax regime fails to recognise the contribution and importance of user participation in the value creation process of these highly digitalised businesses, as the existing nexus rules and profit allocation rules do not result in an appropriate alignment between the location in which profits are taxed and the location in which value is created.<sup>11</sup>

Against this background, the authors of this article analyse the current (lack of) possibilities for user-jurisdictions to tax the value generated by the increased use of digital intermediary platforms.<sup>12</sup> In this regard, it should be acknowledged that applicable domestic tax laws often will provide sufficient legal basis for taxing the payment received by a user providing a service to another user through a digital intermediary platform, even though it might be difficult to enforce the tax in practise. For example legal basis often exists for taxing the proceeds received by an Uber-driver or the proceeds received by the letter of an apartment through Airbnb but enforcement may be difficult. However, these issues will not be addressed in this article.<sup>13</sup> Instead, focus will be on analysing the possibilities for user-jurisdictions to tax the remuneration received by the enterprises owning the digital intermediary platform (hereinafter: the platform enterprises), and on discussing whether the users' provision of personal data in exchange for access to the platform could be considered a barter transaction for tax purposes in the user-jurisdiction.

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<sup>11</sup> Ibid p. 171-172. It is not the purpose of this article to discuss whether the view of these countries is actually appropriate or not. For a critical discussion see for example Eric C.C.M. Kemmeren, 'Should the Taxation of the Digital Economy Really be Different' (2018) 27 EC Tax Review 2 and Werner Haslehner, *Taxing where value is created in a post BEPS (digitalized) World*, Kluwer International Tax Blog <<http://kluwertaxblog.com/2018/05/30/taxing-value-created-post-beps-digitalized-world/>> (24 August 2018).

<sup>12</sup> Only issues concerning direct taxation will be dealt with.

<sup>13</sup> Instead, see for example Giorgio Beretta, 'Taxation of Individuals in the Sharing Economy' (2017) 45 Intertax 1, and same author 'The Taxation of the Sharing Economy' (2016) 70 Bulletin for International Taxation 11, Nangel Kwong, 'The Taxation of Sharing Economy Activities' in Ina Kerschner and Maryte Somare (eds.), *Taxation in a Global Digital Economy* (Linde Verlag 2017), p. 61 et seq., Shu-Yi Oei and Diane M. Ring, 'Can Sharing be Taxed?' (2016) 93 Washington University Law Review 4, Roberta A. Kaplan and Michael L. Nadler, 'Airbnb: A Case Study in Occupancy Regulation and Taxation', (2017) 82 University of Chicago Law Review Online 1, and Jane Bolander, 'Deleøkonomi og skat' in Børge Dahl et al. (eds.), *Liber Amicorum Peter Møgehang Hansen* (Extuto 2016), p. 29 et seq.

The analysis is divided in two main parts. The first main part contains an analysis and discussion of the possibilities for taxing the value creation in the user-jurisdiction under current tax regimes (section 2). The second main part discusses a number of tax policy challenges and options of relevance for taxing platform enterprises, in particular the proposed directive on significant digital presence recently put forward, as part of the European Commission's Digital Tax Package (section 3).<sup>14</sup> Finally, the article contains a section which recaptures the main conclusions (section 4).

## 2. DIGITAL INTERMEDIARY PLATFORMS AND CURRENT TAX PRINCIPLES

### 2.1. LACK OF TAXATION IN THE JURISDICTION OF THE USER

In short, increased digitalisation – including the widespread use of the internet and mobile devices – has expanded the possibility of sharing goods and services beyond individuals' social networks and immediate surroundings.<sup>15</sup> In this context, digital intermediary platforms such as Uber and Airbnb have been able to turn the collaborative model into profitable, global businesses.<sup>16</sup> Thus, the fact that digital intermediary platforms have significantly widened the possibilities for sharing property and services, including across national borders, has created new opportunities for both consumers and entrepreneurs and has raised issues with regard to the application of existing legal frameworks, including the tax framework.<sup>17</sup>

From a tax perspective, sharing economy transactions may be divided into different kinds of transactions, one of which is cash transactions, where users of the network share personal goods or provide services on a peer-to-peer basis via digital intermediary platforms for a fee.<sup>18</sup> In short, the business model of such digital intermediary

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<sup>14</sup> Proposal for a Council Directive laying down rules relating to the corporate taxation of a significant digital presence, COM(2018) 147 final, and Proposal for a Council Directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services, COM(2018) 148 final.

<sup>15</sup> Vassilis Hatzopoulos and Sofia Roma, 'Caring for sharing? The Collaborative Economy under EU Law' (2017) 54 *Common Market Law Review*, p. 81-128.

<sup>16</sup> For more on the business models of Uber and Airbnb including related private law issues see Marie Jull Sørensen, 'Private Law Perspectives on Platform Services: Uber – a business model in search of a new contractual legal frame?' (2016) 5 *Journal of European Consumer and Market Law* 1, and Vanessa Mak, 'Private Law Perspectives on Platform Services: Airbnb – Home Rentals between AYOR and NIMBY' (2016) 5 *Journal of European Consumer and Market Law* 1.

<sup>17</sup> Communication from the Commission on a European agenda for the collaborative economy, COM(2016) 356 final. and Giorgio Beretta, 'The European Agenda for the Collaborative Economy and Taxation' (2016) 56 *European Taxation* 9.

<sup>18</sup> For more on the different transaction types see Beretta (2017) [footnote 13].

platforms relies on a three-party relationship between the platform, the providing users and the buying users. Accordingly, the platform creates value by matching end-users for example drivers and passengers so that they can complete a ride on a pay-as-you-go basis. Consequently, such business models rely on a mediation technology which creates value by linking users of the network, as well as organise and facilitate the exchange between users, and ensure transaction quality using a review system whereby users have the option of rating the quality of the interaction.

The activities performed by the platform enterprise thus generally include: 1) network promotion and contract management activities, for example related to inviting potential users to join the network, 2) service provisioning activities, for example related to matching the users, facilitating the supply of goods or services and the payment, and 3) network infrastructure operation activities related to maintaining and running a physical and information infrastructure.<sup>19</sup>

In exchange for providing the mediation technology (typically in the form of an app-based market place), the platform enterprise takes a fee. For example, Uber takes a portion of the gross fares generated by partners (usually up to 20%, depending on the market), and Airbnb charges the hosts a fee of 3% on every booking plus an additional service fee paid by the guests up to 20%.<sup>20</sup>

It is publicly known that some of the larger platform enterprises enjoy low effective taxation of their worldwide income, due to their tax-efficient and often rather complex corporate structures that include entities in low tax jurisdictions.<sup>21</sup> One element in this tax planning is to avoid establishing a taxable presence (nexus) in the jurisdictions where the users are located (hereinafter: the user-jurisdiction).<sup>22</sup> For example, in the case of Uber, a subsidiary in the Netherlands processes the worldwide payments for all rides.<sup>23</sup> Moreover, even though Uber has established subsidiaries in a number of countries where it operates, these subsidiaries do normally not attract a lot of taxable income, as they only

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<sup>19</sup> OECD/G20 (2018) [footnote 9], p. 38-40 and p. 66-73. Please see the report itself for a more elaborate description of such business models.

<sup>20</sup> <<https://www.airbnb.dk/help/article/1857/what-are-airbnb-service-fees>> (24 August 2018), and Oei and Ring (2017) [footnote 13], p. 1002.

<sup>21</sup> Carrie Brandon Elliot, 'Taxation of the Sharing Economy: Recurring Issues' (2018) 72 *Bulletin for International Taxation* 4a.

<sup>22</sup> *Ibid.* For more on the lack of a taxable nexus in the user-jurisdiction in the form of a permanent establishment see section 2.2.2 below.

<sup>23</sup> Even though the fees received are taxable, the effective taxation is low, among other things because the subsidiary in the Netherlands can deduct intra-group royalty payments.

provide low-risk support services that generally are remunerated on a cost plus-basis.<sup>24</sup>

The fact that highly digitalised enterprises can provide their services without obtaining a taxable nexus in the user-jurisdictions has caused intense debate. Thus, it has been argued that even though data may be collected from the users without monetary consideration, these data constitute a key resource of highly digitalised businesses.<sup>25</sup> Accordingly, it may be argued that the users become a kind of “virtual workers” for these digital enterprises and that it is troubling if these enterprises do not contribute with tax revenues to the jurisdictions where their users live and “work” for them.<sup>26</sup> As the collaborative business models are characterised by high user participation intensity, this argument may also be made with respect to the contributions provided by users of digital intermediary platforms.<sup>27</sup>

Against this background, section 2.2 takes a closer look at the interaction between the platform enterprise and its users. In this regard, it is discussed whether it is correct to consider the interaction between the platform enterprises and the users as one pure cash transaction, which is the payment of a service fee that can generally only be taxed in the user-jurisdiction if a taxable nexus is established there, or whether the interaction in addition contains some kind of barter transaction (section 2.2.1). Subsequently, issues concerning classification and allocation of the right to tax are analysed (section 2.2.2).

## 2.2. THE INTERACTION BETWEEN PLATFORM ENTERPRISES AND USERS

### 2.2.1. TRANSACTIONS RELEVANT FOR TAX PURPOSES

Before it is relevant to classify payments and allocate the taxing right for tax treaty purposes, it must be analysed whether and how the interaction between the platform enterprise and the users should be recognised for domestic tax purposes. Nevertheless, as it is outside the scope of this article to undertake a comprehensive comparative study of various domestic tax regimes, the analysis below is limited to outlining

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<sup>24</sup> Elliot (2018) [footnote 21], who states that Airbnb uses a setup similar to Uber’s. See also Brian O’Keefe ‘How Uber plays the tax shell game’ (2015) *Fortune Magazine* (22 October).

<sup>25</sup> HM Treasury, *Corporate tax and the digital economy: position paper update* (2018), p. 7 et seq.

<sup>26</sup> Nicolas Colin and Pierre Collin, *Task Force on Taxation of the Digital Economy* (2013), p. 2. See also Raffaele Petruzzi and Svitlana Buriak ‘Addressing the Tax Challenges of the Digitalization of the Economy – A possible Answer in the Proper Application of the Transfer Pricing Rules?’ 72 *Bulletin for International Taxation* 4a, who argue that users who generate valuable data serve as “unconscious” contributors and/or employees.

<sup>27</sup> OECD/G20 (2018) [footnote 9], p. 56-59. Users must often disclose their preferences to access the services. Moreover, the users of digital platforms may be seen to bear the burden of verifying the product quality, e.g. by giving a rating or writing a review.

the basic features of the interaction, based on the fact that no income tax systems appear to focus exclusively on cash compensation.<sup>28</sup> In other words, in most income tax systems at least some non-cash barter transactions are considered to possess a taxable component.<sup>29</sup>

As an example, the main principles in Danish tax law could briefly be considered. According to section 4 of the Danish State Tax Act, the main rule is that all income is taxable whether in money or in kind, unless the income consists of a gain from the disposal of private property, pursuant to section 5 of the Danish State Tax Act. In the case of provision of services, the provider will be taxable, if a payment is received in return for the service. In this respect, not only cash payments must be included but also payments in kind that objectively have economic value. This also applies if one service is traded in exchange for another service. For instance, if Person A paints Person B's living room in exchange for Person B repairing Person A's car, both services should in principle be valued and taxed. However, services may be so insignificant and the connection between them so weak that no taxation takes place.<sup>30</sup> Yet, the borderline between a non-taxable interaction and a taxable barter transaction is not clear.<sup>31</sup>

Even though national tax regimes are diverse, the following analysis and discussion of interactions between the platform enterprise and its users will be based on the working hypothesis that the general features of many tax systems are somewhat similar to the Danish tax regime when considering barter transactions for tax purposes.<sup>32</sup>

In addition, it is assumed that the underlying rationale for treating (some) barter transactions as taxable events is often founded in (explicit

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<sup>28</sup> Beretta (2016) [footnote 13], who argues that this is the case no matter whether the domestic tax regime in question is a so-called global system or a scheduler system.

<sup>29</sup> Kwong (2017) [footnote 13], p. 66.

<sup>30</sup> Bolander (2016) [footnote 13], pp. 30-31. See also the report from the Danish Ministry of Taxation, *Rapport om vennetjenester/sort arbejde, eget arbejde, forbrug af egne varer, produkter og ydelser samt personalegoder* (2002), in which it was stated that so-called tax-exempt acts of friendship could be defined as customary non-commercial services between family, friends and the like caused by ordinary helpfulness, generosity or social involvement.

<sup>31</sup> In 2012, the Danish legislator tried to elucidate when favours between friends and family are not taxable by introducing section 7 Å of the Danish Tax Assessment Act. For more on the traditional perception of the income concept in Danish tax law see Jan Pedersen et al., *Skatteretten 1* (Karnov Group 2015), p. 208 et seq., Aage Michelsen et al., *Lærebog om Indkomstskat* (Jurist- og Økonomforbundets Folag 2017), p. 147 et seq., and Thøger Nielsen, *Indkomst beskatning I* (Juristforbundets Forlag 1965), p. 172.

<sup>32</sup> It is recognised that for example jurisdictions relying on old UK doctrines may be different as the judicial concept of income under those doctrines excludes benefits in kind that cannot be converted to cash. See Lee Burns and Richard Krever 'Individual Income Tax' in Victor Thuronyi (ed), *Tax Law Design and Drafting* (Kluwer Law 2000), pp. 507-508.

or implicit) neutrality considerations,<sup>33</sup> broadly understood as the aim that taxes should not affect economic behaviour.<sup>34</sup> Accordingly, based on these assumptions, the economic substance of the interaction between the users and the platform enterprise will now be analysed and compared to how interactions similar in economic substance are normally treated for domestic tax purposes.

It seems straightforward that the cash payment made by the user to the platform enterprise for the provision of various digital services shall be recognised for tax purposes. Accordingly, the cash payment will normally constitute taxable income in the hands of the recipient platform enterprise in the jurisdiction where the platform enterprise is resident according to domestic tax rules (unless the recipient enterprise is located in a tax haven). Moreover, the provisions on limited tax liability in the tax code of the user-jurisdiction may prescribe that tax, for example a withholding tax, shall be levied on the payment in the user jurisdiction (however, as explained in section 2.2.2. below the applicable tax treaty will typically preclude taxation in the user-jurisdiction of payments from a user to a foreign platform enterprise).<sup>35</sup>

In contrast to cash payments, there seems to be no consensus between countries on whether data collection from users as well as their participation and provision of content (for example trust generating reviews of other users of the platforms, user profile data, user locations in real time, credit card data and bank information) in return for access to the digital intermediary platform should be recognised as barter transactions between the users and the platform enterprise.<sup>36</sup>

In the tax literature, barter transactions have recently experienced renewed topicality in relation to the raise of virtual currencies and cryptocurrencies in respect to whether these new currencies constitute means of payment or means of exchange.<sup>37</sup> However, up until now, no

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<sup>33</sup> Ibid, pp. 507-508. See also Robert I. Keller 'Taxation of Barter Transaction' (1982) 67 *Minnesota Law Review* 411, where the author argues that '[a]ll taxpayers who engage in barter transactions are in the same economic position they would have been had they received cash for their goods or services in an amount equal to the value of the goods or services actually received and used that cash to purchase goods or services from the other party to the exchange.'

<sup>34</sup> The broad definition of neutrality used in Simon James and Christopher Nobes *The Economics of Taxation* (Prentice Hall 1998), p. 306.

<sup>35</sup> According to Chang Hee Lee and Ji-Hyun Yoon, 'General Report' in International Fiscal Association (eds), *Cahiers de droit fiscal international* volume 103 B: Withholding tax in the era of BEPS, CIVs and the digital economy (Sdu 2018), p. 236, every country covered in the branch reports rely on a withholding system to collect a number of taxes concerning non-residents.

<sup>36</sup> OECD/G20 (2018) [footnote. 9], p. 38-40.

<sup>37</sup> See for example Aleksandra Bal 'Stateless Virtual Money in the Tax System' (2013) 53 *European Taxation* 7 and the same author 'Blockchain, Initial Coin Offerings and Other Developments in the Virtual Currency Market' (2018) 20 *Derivatives & Financial*

relevant analysis of the distinction between barter transactions and other interactions, which neither constitute a money transaction nor a taxable barter transaction, seems to have been conducted for direct tax purposes.<sup>38</sup>

No generally accepted definition of a barter transaction exists but one could be: *‘Transactions whereby products or services are directly exchanged between two suppliers without using money as a medium of exchange’*.<sup>39</sup> Four cumulative conditions in order for a transaction to be regarded a barter transaction can be derived from this definition.

First, the articles exchanged should be regarded as products or services. This should most likely be broadly interpreted as to include almost anything that may be controlled and offered for attention, acquisition, use or consumption etc. In this context, it seems difficult to argue that the supply of data by users of a platform, as well as the access to the platform provided by the platform enterprise, cannot be considered within the scope.<sup>40</sup>

Second, the products or services should be exchanged, which in respect of barter transactions may be defined as: *‘the barter of the comparatively superfluous for the comparatively necessary’*.<sup>41</sup> This only seems to require that some right, for example to own or use a product, is given or some service is provided. That will likely include a platform enterprise’s right to collect user data, as well as the right for the users to access the platform.<sup>42</sup> In respect of the term comparatively, this is a subjective measure and, consequently, it is challenging to determine whether the data and access to the platform are comparatively superfluous and necessary to the users and the platform enterprise. However, as the users

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Instruments 2 and Louise Fjord Kjærsgaard and Katja Dyppele Weber ‘Skattemæssig behandling af virtuelle valutaer’ [2018] *Tidskrift for skatter og afgifter*, 2.

<sup>38</sup> Piergiorgio Valente ‘Digital Revolution – Tax Revolution?’ (2018) 72 *Bulletin for International Taxation* 4a, lists the following question as one of the questions that are still pending: *‘Should consumers/users be taxed in respect of the deemed benefits derived from the transition of data owned?’* However, the author does not provide an answer. In the literature on VAT Sebastian Pfeiffer ‘VAT on Free Electronic Services?’ (2016) 27 *International VAT Monitor* 3, has discussed whether electronic services are subject to VAT where the consideration consists of personal data provided by the users.

<sup>39</sup> Julie Rogers-Glabush, *IBFD International Tax Glossary* (IBFD 2009), p. 35.

<sup>40</sup> It has been debated how to classify personal user data collected by enterprises. For example, Colin and Collin (2013) [footnote 26] discuss how to qualify data collected from users given that such data are not per se an intangible asset owned by the collecting enterprise.

<sup>41</sup> W. Stanley Jevons ‘Money and the Mechanism of Exchange’ [1896] *The International Scientific Series*, p. 8

<sup>42</sup> For example in respect of Uber, both the driver and the passenger must sign an agreement which entails that a wide spectrum of driver and passenger data may be collected and used by Uber.

and the platform enterprise are generally unrelated, it seems reasonable to assume that this is the case.<sup>43</sup>

Third, it has to be an exchange between two suppliers. Again, this seems to be a broad concept that may include most situations where a person provides products or services that people want or need, especially over a long period of time.<sup>44</sup> In direct tax law, it is rarely necessary to discuss whether a given taxpayer should be seen as a “supplier”, as this is normally not decisive for the taxation. However, within other legal disciplines, it is a central question to answer. Accordingly, interpretive aid may perhaps be found in other fields such as indirect tax law and private international law.

For VAT purposes, it has been discussed in the literature whether a highly digitalised business such as a platform enterprise is the only supplier of a service, or whether both the platform enterprise *and* the users should be considered taxable suppliers. The strongest arguments seem to support that the users of a platform should not be considered suppliers in a VAT context. This is based on the fact that users allegedly cannot be viewed as carrying out economic activities (economic exploitation with the purpose of obtaining income) *and* that the provision of personal data in order to gain access to the platform could constitute a mere form of payment similar to crypto currencies, which is accepted as a mean of payment for VAT purposes. However, uncertainty exists, as it could also be argued that the link between the service (access to the platform) and the consideration (provision of user data) is too weak to cause that the consideration could constitute a mere payment.<sup>45</sup> As crypto currencies are typically regarded as properties and not a mean of payment for direct tax purposes, it could be argued that the principles from VAT cannot be directly relied on in the analysis of whether the interaction between the users and the platform enterprise should be recognised as a barter transaction.<sup>46</sup>

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<sup>43</sup> See Keller (1982) [footnote 33], where it is stated ‘[...] *that in most taxable exchanges the same basis figure would result whether the taxpayer used the value received or the value given up theory of cost, since generally the value of two exchanged in an arms length transaction are either equal in fact, or are presumed to be equal.*’

<sup>44</sup> See for example the general definition of supplier in Cambridge Dictionary <<https://dictionary.cambridge.org/>>.

<sup>45</sup> Pfeiffer (2016) [footnote 38]. Even though VAT law may provide some inspiration, it should be kept in mind that there are fundamental differences between the underlying principles of direct tax law and indirect tax law. See Karina Kim Egholm Elgaard, *Interaktion mellem momsretten og indkomstskatteretten* (Jurist- & Økonomforbundets Folag 2016), p. 131 et seq.

<sup>46</sup> Bal (2013) [footnote 37], Kjærsgaard and Weber (2018) [footnote 37] and administrative practice from the Danish Tax Council, decision of 9 March 2018, SKM2018.104.SR, decision of 3 April 2018, SKM2018.130.SR, decision of 31 August 2017, SKM2017.520.SR, and decision of 1 April 2014, SKM2014.226.SR.

In private international law, emphasis is often put on who provides the characteristic performance of the transaction with respect to determining the applicable law in the absence of choice. In this regard, where a party enters into a contract in the course of his trade or profession, it is rebuttably presumed that this is the party that provides the characteristic performance which again means that the other party is considered a buyer and not a supplier.<sup>47</sup> Nevertheless, if it is not possible to identify a *single* party that provides the characteristic performance of a transaction, the presumption does not apply.<sup>48</sup> Accordingly, if relying on these principles from international private law, the interaction between the platform enterprise and the users could only be viewed as a barter transaction if none of the parties can be seen as the party providing the characteristic performance.

Fourth, money cannot be used as a means of payment in the transaction; hence, barter transactions should be distinguished from sale and purchase of products and services in which money is exchanged. Even though a fee is typically paid by the user for acquiring a service through a digital intermediary platform, it should be noted that the recipient of the fee will not necessarily be the same group entity as the entity collecting the user data, and that it may be possible to split the overall interaction into a monetary transaction, as well as a non-monetary transaction.<sup>49</sup> Moreover, it is typically possible to access the platform without actually acquiring anything, and even in that case, user data is collected and used. Correspondingly, in a number of situations, personal data seems to be exchanged for access to the platform. Although, no generally accepted definition of money exists for tax purposes, neither of the articles exchanged between the users and the platform enterprise have the general characteristics of money known from economic theory, that is something which can be used as a medium of exchange, a measure of value, a standard value, and storage of value.<sup>50</sup>

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<sup>47</sup> Article 4 (2) of the Convention on the Law Applicable to Contractual Obligations (adopted 19 June 1980, entry into force 1991) (hereinafter: The Rome Convention). See Richard Plender and Michael Wilderspin, *The European Private International Law of Obligations* (Sweet & Maxwell 2009), p. 169.

<sup>48</sup> *Ibid.*

<sup>49</sup> As mentioned in section 2.1. above, in the case of Uber a subsidiary in the Netherlands processes the worldwide payments for all rides, whereas the data seems to be collected and used by the headquarter entity, see OECD/G20 (2018) [footnote 9], p. 67.

<sup>50</sup> Jevons (1896) [footnote 41], pp. 13-18. In Danish administrative practice, the Danish Tax Council has stated that from a Danish domestic tax law perspective for an article to be regarded as money it must be: (1) regulated by the global currency market, (2) subject to regulation by a central bank, (3) redeemable, and (4) affiliated with a jurisdiction or currency area. See decision of 25 March 2014, SKM2014.226.SR, regarding the qualification of Bitcoins, and decision of 22 August 2017, SKM2017.520.SR regarding the qualification of Bookcoins.

If the interaction can be viewed as a barter transaction, the interaction could potentially give rise to income taxation on both sides of the transaction, depending on the applicable domestic tax law. The underlying reason is that splitting the interaction in two separate supplies in consideration for money does not change the economic substance of the transaction.<sup>51</sup>

However, generally, tax systems accept that various kinds of interactions are not relevant for tax purposes. An example could be the social interaction between two colleagues discussing an issue. This discussion may be of mutual benefit if both colleagues thereby gain new insights. Nevertheless, typically, such interactions are viewed as social, everyday interactions where the link between the interaction and the creation of economic value are considered too weak to be recognised for tax purposes. Accordingly, if the interaction between the users and the platform enterprise can be considered similar to such social, everyday interactions, it normally implies that the interaction is not relevant for tax purposes for any of the parties.

Altogether, there does not seem to be a clear and general answer to how the interaction between the users and the platform enterprise shall be viewed, among other things because all interactions between users and the various platforms are not completely alike and since the existing tax regulations have not been drafted with such digital transactions in mind.<sup>52</sup> However, it seems far-fetched to compare the interactions between the users and the platform enterprise to social, everyday interactions, as at least the platform enterprise has a clear commercial rather than social motive. Further, there seems to be a clear link between the collection and use of data and the creation of economic value for the platform enterprise.<sup>53</sup> In addition, as most users would probably not allow the collection of user data or would not spend time on writing reviews etc. without getting something in return, it seems reasonable to presume that the users' access to the platform provides some kind of (economic) value for the users, for which the users might otherwise would have been willing to pay for in cash.

Consequently, for direct tax purposes, it could be argued that the non-monetary part of the interactions between the platform enterprise and the users appear to have quite strong similarities with a recognisable

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<sup>51</sup> Keller (1982) [footnote 33] 67 *Minnesota Law Review* 411, where the author argues that '[a]ll taxpayers who engage in barter transactions are in the same economic position they would have been had they received cash for their goods or services in an amount equal to the value of the goods or services actually received and used that cash to purchase goods or services from the other party to the exchange.'

<sup>52</sup> Apart from viewing the interaction as either a barter transaction or a social, everyday event some intermediary outcomes could also be considered. For example, it could be considered whether the platform should be seen as the only part providing a service, and the users as a "pure" buyer paying in kind, or vice versa.

<sup>53</sup> OECD/G20 (2018) [footnote 9], p. 29.

barter transaction. This may, at least in theory, give rise to income taxation on both sides of the transaction, if the applicable domestic tax legislation has similarities with the main principles of the Danish regime and an applicable tax treaty allocates the right to tax the user of such income to the user-jurisdiction, for example as ‘business income’ or ‘other income’.

Nevertheless, even though it may be possible for the user-jurisdiction to find legal basis in current tax regulations for taxing resident users of the receipt of a payment in kind (in the form of access to the platform), no jurisdictions are, to our knowledge, currently enforcing such taxation.<sup>54</sup> One reason for this could obviously be that taxpayers, tax authorities, and courts do not agree or are not (yet) aware that such legal basis may be found in the applicable domestic tax legislation. However, in practice, it may also play a role that enforcing such taxation would entail severe practical challenges, inter alia, because of difficulties with valuation of the payments in kind.<sup>55</sup> Further, there seems to be a risk that the costs associated with controlling and collecting such taxes will be significant compared to the tax revenue collected, as the value of each barter transaction is likely to be low, whereas the volume of barter transactions could be massive.<sup>56</sup> Finally, the taxation of users on the access to digital intermediary platforms would conflict with a number of other principles underpinning most tax systems. For example, it must be expected that individual taxpayers will have a hard time understanding and accepting being taxed, just because they obtain access to a platform.<sup>57</sup>

As a consequence of the fact that user-jurisdictions in practice are not levying tax on users receiving a payment in kind in the form of access to a platform, the following section on classification for tax treaty purposes will only address issues related to the payment from users to a foreign platform enterprise. In other words, the section below will only

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<sup>54</sup> It is generally recognised that income tax systems struggle to capture transactions where money is not used as a medium of payment on either side of the transaction see OECD/G20, (2018) [footnote 9].

<sup>55</sup> OECD, *Exploring the Economics of Personal Data: A Survey of Methodologies for Measuring Monetary Value* (OECD Publishing 2013). Further, it seems impossible to distinguish how much value is associated with the data of a specific user, as this depends on inter alia the scale and quality as well as the specific business model adopted by the enterprise, see also Olbert and Spengel (2017) [footnote 1]. Less debated, though equally challenging, is the valuation of the access provided to the users.

<sup>56</sup> OECD/G20, (2015) [footnote 6], p. 100.

<sup>57</sup> Carrying out such taxation of a potentially very high number of low value user transactions could in practice conflict with underlying objectives such as simplicity, administrability, fairness and efficiency. For a general and critical discussion of the various objectives see Louis Kaplow, *The Theory of Taxation and Public Economics* (Princeton Press 2008), p. 37 et seq.

consider the allocation of taxing rights with respect to the income received by the platform enterprises (not by the users).

### 2.2.2. CLASSIFICATION FOR TAX TREATY PURPOSES

The development and wide spread use of the OECD Model Tax Convention on Income and on Capital (hereinafter: the OECD Model) has supported the so-called ‘classification and assignment of sources method’ which means that income is classified under a number of categories and taxing powers are assigned to each state for each category of income.<sup>58</sup> However, as described and analysed above, the digitalisation has enabled monetisation in new ways that raise questions regarding both the rationale behind the existing classifications of income and the consistency of the treatment of similar types of transactions.<sup>59</sup>

In regard to the classification of payments in digital transactions, the Technical Advisory Group concluded in its report from 2001 (hereinafter: The TAG Report)<sup>60</sup> that one of the most important classification issues were the distinction between business income and royalties corresponding to Article 7 and 12 of the OECD Model, assuming that all payments are received in the course of carrying on a business.<sup>61</sup> This distinction is also of importance with respect to the classification of payments from the users to the platform enterprise, as it potentially affects the allocation of the right to tax. The reason is that numerous bilateral tax treaties allow the source state (the user-jurisdiction) to withhold a tax on royalty payments, whereas the right to tax business income is exclusively granted to the domicile state unless the income should be allocated to a taxable permanent establishment (hereinafter: PE), located in the source state, pursuant to Article 7 of the OECD Model (2017).<sup>62</sup> In other words, so-called nexus is needed in the user-jurisdiction, in order for the user-jurisdiction to be able to tax the income of a foreign platform enterprise.

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<sup>58</sup> Chang Hee Lee, ‘Impact of E-Commerce on Allocation of Tax Revenue between Developed and Developing Countries’ in Reuven Avi-Yonah (ed), *International Tax Law Vol. 1* (Edward Elgar Publ. 2016) and Michael J. Graetz and Michael M.O’Hear ‘The Original Intent of U.S. International Taxation’ in Reuven Avi-Yonah (ed), *International Tax Law Vol. 1* (Edward Elgar Publ. 2016), with reference to David Rosenbloom and Stanley I. Langbein ‘United States Tax Treaty Policy: An Overview’ (1981) 19 *Columbia Journal of Transnational Law* 359, who view the choice of classification and assignment as the basic structure for virtually all current bilateral tax treaties.

<sup>59</sup> OECD/G20 (2015) [footnote 6], p. 98 et seq.

<sup>60</sup> OECD Technical Advisory Group on Treaty Characterisation of Electronic Commerce Payments, *Tax Treaty Characterisation Issues Arising from E-commerce* (1 February 2001 and adopted by the OECD Council in July 2002).

<sup>61</sup> *Ibid.*, p. 4.

<sup>62</sup> Lee and Yoon (2018) [footnote 35], p. 238. See also Hanna Litwinczuk ‘Poland: Payments for Copyrights of Computer Software as Royalties’ in Michael Lang et al. (eds) *Tax Treaty Case Law around the Globe* (IBFD 2011), pp. 288-299.

According to the main rule in Article 5(1) of the OECD Model (2017), a PE means a fixed place of business through which the business of an enterprise is wholly or partly carried on. However, as physical presence is required in order to create a PE, digital enterprises have the possibility of providing their services in the user-jurisdiction remotely without establishing a PE. For example, platform enterprises provide their services remotely through digital intermediary platforms and thereby generally avoid establishing a PE in the user-jurisdiction. Moreover, as the number of matches made by the platform between end-users are only limited by computer power, the scale and geographical scope of the platform enterprises' activities may be comprehensive, even though no taxable nexus is established.<sup>63</sup>

Recently, amendments have been made to the PE-definition in the OECD Model (2017) and its commentaries.<sup>64</sup> However, as physical presence is still used as the nexus-defining criterium, many digital business models, including platform enterprises, will still be able to provide their digital services without establishing a PE in the user-jurisdictions.<sup>65</sup>

Nevertheless, it should be recalled that Article 7 is secondary to Article 12 of the OECD Model (2017) if an enterprise does not carry on its business through a PE in the source state (the user-jurisdiction). Accordingly, it must initially be considered whether the payment

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<sup>63</sup> OECD/G20 (2018) [footnote n. 9], p. 70-71.

<sup>64</sup> The amendments were prescribed in OECD/G20, *Preventing the Artificial Avoidance of Permanent Establishment Status – Action 7 Final Report* (OECD Publishing 2015). A number of bilateral tax treaties will incorporate these changes through the adoption of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, (signed on 7 June 2017, entry into force on 1 July 2018).

<sup>65</sup> Peter Hongler and Pasquale Pistone, *Blueprints for a New PE Nexus to Tax Business Income in the Era of the Digital Economy*, IBDF Working Paper 20 January 2015, and Kofler et al. (2017) [footnote 2]. The 2017-amendments to Article 5 of the OECD Model with Commentary included an expansion of the dependent agent-test, a tightening of the independent agent criteria, and a narrowing of the PE-exemptions for preparatory and auxiliary activities. However, several countries that have signed the Multilateral Instrument have chosen not to apply the amended PE definition. No analysis of the (amended) PE definition will be conducted in this article, as several other contributions in the literature have already done this. See for example Vishesh Dhuldhoya, 'The Future of the Permanent Establishment Concept' (2018) 72 Bulletin for International Taxation 4a, Peter Blessing, 'Preventing the Artificial Avoidance of PE in Base Erosion and Profit Shifting (BEPS) – Impact for European and International Tax Policy' in Robert Danon (ed.), *Base Erosion and Profit Shifting (BEPS) – Impact for European and International Tax Policy* (Schulthess, 2016), Daniel W. Blum 'Permanent Establishments and Action 1 on the Digital Economy of the OECD Base Erosion and Profit Shifting Initiative – The Nexus Criterion Redefined' 69 Bulletin for International Taxation 6/7, and Anders Norgaard Laursen, 'Ændringer af fast driftssteddefinitionen afledt af BEPS-projektet', [2018] SR-Skat, p. 111 et seq.

received by the platform enterprise constitutes a royalty. In this respect, it should be noted that the definition of royalties varies in bilateral tax treaties, though it is often inspired by the definition of royalties included in Article 12 (2) of the OECD Model (2017):

The term ‘royalties’ as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.

The word ‘payment’, as used in the definition, should be interpreted broadly and only requires the fulfilment of an obligation to put funds at the disposal of the creditor in the manner required by contract or by custom.<sup>66</sup> Consequently, a payment does not need to be in cash to be within the scope of the definition.<sup>67</sup> Hence, the cash fee as well as the data provided by the users of a platform (if presumed that the data also forms part of the taxable part of the remuneration to the platform), could potentially be classified as royalties. However, the classification of payments between the users and the platform enterprise shall be based on a thorough analysis of the facts on a case-by-case basis. Nonetheless, it must be expected that the payment, as a starting point, could often be considered a payment related to a mixed contract.<sup>68</sup>

According to The TAG Report and the commentaries to Article 12(2) of OECD Model (2017), a payment in consideration for know-how and copyrights concerning software shall only in relatively rare cases be classified as royalties. This is based on the understanding that such payments are generally for the provision of services using underlying copyrights or know-how and not for *the right to use* or be *imparted* in the copyrights or knowhow.<sup>69</sup> This also seems to be the case with respect to

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<sup>66</sup> Para. 8.3 of the commentaries to Article 12 of the OECD Model (2017).

<sup>67</sup> Matthias Valta, ‘Income from Royalties’ in Ekkehart Reimer and Alexander Rust (eds), *Klaus Vogel on Double Taxation Conventions* (Wolters Kluwer 2015), p. 993.

<sup>68</sup> Such mixed contracts should be broken down, on the basis of the information contained in the contract or by means of a reasonable apportionment and classified separately except if; (i) one part of what is being provided constitutes by far the principal purpose of the contract, *and* (ii) the other parts are only of an ancillary and largely unimportant character. In such cases, the classification of the principal part should generally be applied to the whole amount of the consideration, according to para. 11.6 (know-how) and 17 (software) of the Commentaries to Article 12 of the OECD Model (2017).

<sup>69</sup> OECD Technical Advisory Group on Treaty Characterisation of Electronic Commerce Payments (2001) [footnote 60], p. 5 and 7. See also para. 11-11.6 (know-how) and 12-17.4 (software) of the commentaries to Article 12 of the OECD Model (2017).

the payment made to a platform enterprise, as the users are not given information on the ideas and principles underlying the platform, such as the logic, algorithms, programming languages or techniques.<sup>70</sup> Consequently, the payment should typically be classified as business income, according to Article 7 of the OECD Model (2017) which entails that the user-jurisdiction will not be entitled to tax the income, if the platform enterprise does not have a PE in the user-jurisdiction.

It should be mentioned that some bilateral tax treaties contain an expanded royalty definition which also includes payments for the provision of technical services and that the scope of ‘technical’ is disputed. The prevailing understanding, however, seems to be that making data and software, or functionality of that data or software, available for a fee does not constitute a service of a technical nature.<sup>71</sup> On this basis, it could be argued that even with an expanded definition of royalties, the payments from the users to the platform enterprise (whether in cash or in personal data) shall typically be classified as business income and shall therefore not be taxable in the user-jurisdiction, assuming that no PE of the platform enterprise is established.

Consequently, if the user-jurisdiction cannot tax the income of the platform enterprise and in practice cannot either carry out taxation of the users, the user-jurisdiction will be left with nothing to tax with respect to value generated in the interaction between the platform enterprise and the users.<sup>72</sup> On this basis, it is a fact that some countries wish to explore other opportunities for establishing a taxing right in the user-jurisdiction. Some of these initiatives will be discussed further in section 3.

### 3. POLICY CHALLENGES AND OPTIONS

#### 3.1. UNILATERAL AND OECD REACTIONS

Currently, and as explained above, user-jurisdictions are normally not entitled to tax the income of a foreign platform enterprise, if the enterprise does not have physical presence in the user-jurisdiction in the form of a PE. Moreover, even though it may be possible for the user-jurisdiction to find legal basis for taxing resident users of the receipt of a

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<sup>70</sup> For illustrative examples see para. 11.5 and 14.3 in the commentaries to Article 12 of the OECD Model (2017).

<sup>71</sup> OECD Technical Advisory Group on Treaty Characterisation of Electronic Commerce Payments (2001) [footnote 60], p. 15. Whether ‘technical’ should be understood strictly in the context of know-how, industrial IP and secrets, or as to having a wider meaning is debated in international tax literature, see for example Matthias Valta (2015) [footnote 67], p. 1019-1021, where the author summarises and discusses the various views.

<sup>72</sup> Obviously, the providing user of a platform will typically be taxable in the user-jurisdiction depending on the applicable domestic tax law. However, this is outside the scope of this article, as explained in section 1.

payment in kind (in the form of access to the platform), no jurisdictions are, to our knowledge, currently enforcing such taxation.

Against this background, and because similar challenges occur in relation to other digital business models, it is not surprising that some countries have made an effort to explore new opportunities for establishing a taxing right in the user-jurisdiction.

A part of these efforts has been made under the auspices of the OECD. Thus, besides the targeted initiatives that were agreed upon in the course of the BEPS project,<sup>73</sup> a number of broader tax policy options, enabling (some) taxation in the user-jurisdiction, have been discussed, including; 1) a new nexus in the form of a significant economic presence, 2) a withholding tax on certain types of digital transactions, and 3) an equalisation levy. However, for various reasons, none of the options were agreed upon and recommended.<sup>74</sup>

Even though no agreement was reached with respect to the broader tax challenges, the BEPS Report on Action 1 stated that countries could introduce any of these three options in their domestic laws or tax treaties as additional safeguards against BEPS (provided they respect existing treaty obligations).<sup>75</sup> Perhaps as a consequence of this, a number of countries have taken such unilateral action.<sup>76</sup> India, Hungary, and Italy have for example adopted rules that (will) impose equalisation levies on certain kind of digital services, and both the UK and Australia have introduced a so-called diverted profits tax. Moreover, Israel has introduced rules that create a taxable nexus in Israel if the foreign enterprise has a digital PE there. Finally, and of particular interest for the topic of this article, it should be mentioned that Slovakia has introduced a new broad PE concept to encompass ride and room-sharing intermediation services.<sup>77</sup>

As already mentioned, it is understandable that some countries feel a need to take action in order to protect their tax bases from the challenges caused by highly digitalised business models. However, the proliferation of unilateral approaches may have severe adverse impacts

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<sup>73</sup> Including the amendments to the PE definition mentioned in section 2.2.2.

<sup>74</sup> OECD/G20 (2015) [footnote 6], p. 13 and p. 97 et seq. For elaborate proposals on how the PE concept could be extended and how to use withholding taxes to address the challenges raised by the digital economy see Peter Hongler and Pasquale Pistone, (2015) [footnote 65] and Yariv Brauner and Andrés Baez, *Withholding Taxes in the Service of BEPS Action 1: Address the Tax Challenges of the Digital Economy*, Working paper of 2 February 2015 (IBFD 2015) .

<sup>75</sup> OECD/G20 (2015) [footnote 6], p. 13 and p. 97 et seq.

<sup>76</sup> The lack of consensus is also reflected in the interim 2018-report, even though the report states that continued work is undertaken in order to reach a consensus-based solution by 2020. See OECD/G20 (2018) [footnote 9], p. 212-213.

<sup>77</sup> For a recent overview of the various unilateral initiatives see Lee Sheppard, 'Digital Permanent Establishment and Digital Equalization Taxes' (2018) 72 *Bulletin for International Taxation* 4a.

on investment and growth, inter alia, due to the increased risk of double taxation, as well as increased interpretational complexity. This concern is also shared by the European Commission which is of the opinion that the adoption of unilateral and divergent approaches by Member States could be ineffective and fragment the single market by creating national policy clashes, distortions and tax obstacles for businesses in the EU. Accordingly, the European Commission finds that coordinated initiatives are needed.<sup>78</sup>

### 3.2. THE EU PROPOSAL ON SIGNIFICANT DIGITAL PRESENCE

For quite some time, the EU has been engaged in discussions and initiatives addressing the tax challenges raised by highly digitalised businesses, including the challenges caused by the increased use of digital intermediary platforms.<sup>79</sup> In continuation of these efforts, the European Commission has recently proposed two new directives. The first directive proposal is laying down rules that should enable member states to tax income generated in their territory if the taxpayer is considered to have a significant digital presence in the member state (even without having physical presence).<sup>80</sup> Moreover, the second directive introduces an interim solution enabling member states to levy a tax of 3% on revenues from certain types of digital services (digital services tax), where the main value is created through user participation.<sup>81</sup>

Below, the proposal laying down rules relating to a significant digital presence is analysed in further detail. Particular focus will be on the elements of relevance for platform enterprises, despite the fact that the directive has a broader scope. The proposal on a digital services tax is not addressed. The reasons for focusing on the first proposal are, among other things, that the digital service tax is only proposed as an interim measure, it is not a tax on income (but on turnover), the digital services tax has already received severe criticism by academic scholars,<sup>82</sup> and the whole idea seems to lack substantial support from member states.<sup>83</sup>

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<sup>78</sup> Directive Proposal COM(2018) 147 final [footnote 14], p. 5.

<sup>79</sup> European Commission, *Commission Expert Group on Taxation of the Digital Economy – Report* (2014). See also Bjørn Westberg, ‘Taxation of the Digital Economy – An EU Perspective’ (2014) 54 *European Taxation* 12, and Paolo Centore and Maria Teresa Sutich, ‘Taxation and the Digital Economy: Europe is Ready’ (2014) 42 *Intertax* 12.

<sup>80</sup> Directive Proposal COM(2018) 147 final [footnote 14].

<sup>81</sup> Directive Proposal COM(2018) 148 final [footnote 14].

<sup>82</sup> Johannes Becker and Joachim English, *EU Digital Services Tax: A Populist and Flawed Proposal*, Kluwer International Tax Blog <<http://kluwertaxblog.com/2018/03/16/eu-digital-services-tax-populist-flawed-proposal/>> (24 August 2018), and Eric C.C.M. Kemmeren (2018) [footnote 11].

<sup>83</sup> In a questionnaire sent to the Member State’s tax authorities, only 9 respondents answered that they believe that a digital services tax would solve the current problems. See Commission Staff Working Document, SWD(2018) 81 final/2, p. 94.

The basic idea behind the first proposal is to extend the currently applied PE-concept in order to include a significant digital presence<sup>84</sup> and to set out new principles for attributing income to such significant digital presence, as new attribution rules are needed in order to better capture the value creation of highly digitalised business models.<sup>85</sup>

According to Article 2, the proposed directive shall apply only for purposes of corporate tax in each Member State and should apply to entities irrespective of where they are resident for tax purposes.<sup>86</sup> However, in order to not violate the Member States' tax treaties with third countries, it follows that the directive should not apply to entities resident in third countries if the Member State has concluded a tax treaty with that third state and the treaty does not include provisions similar to the proposed provisions on significant digital presence.<sup>87</sup> This exception is obviously necessary in order to not cause treaty override, but it may entail a significant reduction of the scope of the new rules if the Member States are not successful or sufficiently interested in re-negotiating their tax treaties with third countries.

According to Article 4(1), a PE will be considered to exist if a significant digital presence exists through which a business is wholly or partly carried on. The phrase '*through which a business is wholly or partly carried on*' is also used with respect to the existing PE-rule set out in Article 5(1) of the OECD Model (2017). However, in that context, the phrase is usually meant to indicate that persons who, in one way or another, are dependent on the enterprise (personnel) conduct the business of the enterprise in the State in which the fixed place is situated.<sup>88</sup> Given that a significant digital presence of for example a platform enterprise may exist, even if no personnel is carrying on

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<sup>84</sup> Accordingly, it follows from Article 4(2) of the proposed directive that the new concept must be viewed as an addition that does not affect or limit the application of any other test under EU law or national law for determining a PE.

<sup>85</sup> As a consequence of the scope and focus of this article (allocation of the right to tax), the profit allocation rules proposed in Article 5 are not further analysed. For more on how profits could be attributed to a digital PE see Yariv Brauner and Pasquale Pistone, 'Some Comments on the Attribution of Profits to the Digital Permanent Establishment' (2018) 72 Bulletin for International Taxation 4a.

<sup>86</sup> The encompassed corporate taxes are listed in Annex I to the directive proposal.

<sup>87</sup> However, the Commission has adopted a recommendation which recommends that Member States negotiate the necessary adaptations to their tax treaties with third countries, so as to bring provisions on significant digital presence into effect. See Commission Recommendation of 21 March 2018 relating to the corporate taxation of a significant digital presence, C(2018) 1650 final. Moreover, as set out in the Directive Proposal COM(2018) 147 final [footnote 14], p. 1-4, the intention is that the proposal should contribute to the ongoing efforts of the OECD and that similar provisions eventually should become part of the OECD model, as well as the Commission's preferred overall solution; the common consolidated corporate tax base (CCCTB).

<sup>88</sup> Para. 6 in the commentaries to article 5(1) of the OECD Model (2017).

business in the user-jurisdictions, because no or limited human intervention is needed, it makes little sense to interpret the phrase in line with its traditional understanding. Despite this, the proposal does not contain any material guidance on how to interpret this phrase.

Pursuant to Article 4(3), a significant digital presence shall be considered to exist in a Member State if the business carried on through it consists wholly or partly of the supply of digital services through a digital interface and one or more of three conditions is met.<sup>89</sup> Before dealing with the three conditions, it is worth taking a closer look at the concepts of digital services and digital interface.

Starting with the last concept, digital interface is briefly defined in the proposal's Article 3(2) as any software, including a website or a part thereof and applications, including mobile applications accessible by users. This definition is very broad and seems to cover most, if not all, digital interfaces currently used for digital intermediary platforms.

A more elaborate definition is provided in Article 3(5) with respect to the concept of digital services.<sup>90</sup> Accordingly, digital services should be understood as services delivered over the internet or an electronic network and the nature of which renders their supply essentially automated and involving minimal human intervention and impossible to ensure in the absence of information technology. It should be noted that 'minimal human intervention' means that the services involve minimal human intervention on the side of the platform enterprise without any regard to the level of human intervention on the side of the users (which may be substantial). In this regard, a digital intermediary platform must also be regarded as requiring minimal human intervention in situations where the platform enterprise initially sets up the system, regularly maintains and updates the system, or repairs it in cases of problems linked with its functioning.<sup>91</sup> However, it is important to note that the mere sale of services facilitated by using a digital intermediary platform is not regarded as a digital service for the providing user (for example the Uber-driver or the lettor of an apartment on Airbnb). In other words, it is the platform enterprise that gives access to the digital intermediary

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<sup>89</sup> Whether the conditions are met should be evaluated with respect to the entity carrying on that business, taken together with the supply by each of that entity's associated enterprises in aggregate. The term "associate enterprise" is defined in art. 3(9).

<sup>90</sup> Article 3(5) includes a list of services which in particular are considered *digital services*. These examples further underline the broad scope of the concept and makes it even clearer that also the services supplied by a digital intermediary platform in a Member State may constitute a significant digital presence. These examples are complemented by a list of encompassed digital services in Annex II to the directive proposal. Annex III provides a list of services that are not included.

<sup>91</sup> Directive Proposal COM(2018) 147 final [footnote 14], p. 6-9. The definition corresponds to the definition of "electronically supplied services" in article 7 of the Council Implementing Regulation (EU) No 282/2011 of 15 March 2011.

platform for remuneration (for example Uber or Airbnb) which is considered to provide digital services.<sup>92</sup>

As mentioned above, a significant digital presence of a platform enterprise should only be considered to exist if one or more of the following three conditions are met; (a) the proportion of total revenues obtained in that tax period and resulting from the supply of digital services to users located in that Member State in that tax period exceeds EUR 7,000,000; (b) the number of users of one or more of digital services who are located in that Member State in that tax period exceeds 100,000; or (c) the number of business contracts for the supply of any such digital service that are concluded in that tax period by users located in that Member State exceeds 3,000.

With respect to condition (a) Article 3(6) prescribes that ‘revenues’ basically means all proceeds of sale and of other transactions net of VAT and other taxes and duties, whether of a monetary or non-monetary nature. The proportion of total revenues in a Member State shall, pursuant to Article 4(7), be determined in proportion to the number of times that devices are used in a tax period by users located anywhere in the world to access the digital intermediary platform.

With regard to both condition (a) and (b), a user shall, according to Article 4(4), be deemed to be located in a Member State in a tax period, if the user uses a device in that Member State in that tax period to access the digital intermediary platform. Moreover, the Member State where a user’s device is used shall be determined by reference to the Internet Protocol (IP) address of the devices or, if more accurately, any other method of geolocation.

Even though condition (a) and (b) might seem relatively simple to apply, practical and interpretive difficulties must be expected to arise. For example, in practice, it might be difficult to delineate revenues obtained from the supply of digital services from other (related) kinds of revenue. In addition, it might not be particularly easy to keep sufficient track of the often vast numbers of users and their locations and at the same time preserve the privacy of the users.<sup>93</sup>

Finally, with respect to condition (c), it is stipulated that a contract shall count as a business contract if the user concludes the contract in the course of carrying on business. It seems that this could include contracts concluded by “providing users” acting sufficiently frequently and professionally. However, it may be difficult for the platform

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<sup>92</sup> Directive Proposal COM(2018) 147 final [footnote 14], p. 6-9.

<sup>93</sup> Article 8 of the proposed directive states that the data collected shall be limited to data indicating the Member State in which the users are located, without allowing for identification of the user. Anyway, concern has been raised about the compatibility with EU privacy rules. See Cristiano Garbarini, *Six questions plus one about the EU Directive on the taxation of a significant digital presence*, Kluwer International Tax Blog <<http://kluwertaxblog.com/2018/04/20/six-questions-plus-one-proposed-eu-directive-taxation-significant-digital-presence/>> (24 August 2018).

enterprise to know and control whether this is in fact the case. In addition, it is stated in Article 4(5) that such users shall be deemed to be located in a Member State in a tax period if the user is resident for tax purposes in that Member State in that tax period or the user is resident for corporate tax purposes in a third country but has a PE in that Member State in that tax period. As the domestic tax rules for determining residence vary between Member States, this link to domestic tax legislation may cause additional complexity.

Overall, the proposed directive on significant digital presence is not without some merit. It addresses a legislative and political need to preserve Member States' tax bases in a time where the new digital business models, including digital intermediary platforms, challenge the existing international tax regime. Correspondingly, the new concept enables the user-jurisdictions to tax (parts of) the profits generated by the interaction between the users and a foreign platform enterprise.<sup>94</sup> Furthermore, a uniform EU approach seems preferable to the proliferation of Member States' unilateral approaches.

However, some limitations of the proposal have to be emphasised. For example, and as identified above, a number of the terms used in the directive contain interpretive uncertainties, and in general the current proposal appears to need further work in order to become sufficiently clear and targeted. In addition, it may be questioned whether the thresholds are set at appropriate levels and whether the criteria are at risk of ring-fencing certain digital activities (too much). Further, it does not seem clear how enterprises relying on both a digital and a physical presence would be affected.<sup>95</sup> Finally, and from a more political perspective, it should be factored in that it may not be easy to persuade non-EU treaty partners to alter the tax treaties in order to introduce a provision on significant digital presence.<sup>96</sup> Should this be the case, it might cause a flow of digital business from the EU to other non-EU jurisdictions.<sup>97</sup>

#### 4. CONCLUSIONS

As physical presence is still used as the nexus-defining criterium, platform enterprises are often able to provide their digital services without establishing a PE in the user-jurisdiction. This entails that user-jurisdictions will normally be precluded from taxing the income of

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<sup>94</sup> However, if the new concept should be able to address the challenges it is crucial that appropriate attribution rules are adopted, in order to capture the value creation of the digital business models.

<sup>95</sup> This concern has also been raised with respect to the significant economic presence concept contemplated by the OECD. See Olbert and Spengel (2017) [footnote 1].

<sup>96</sup> See also Kofler et al. (2017) [footnote 2], who argues that the appropriateness of different standards within and outside the EU is highly questionable.

<sup>97</sup> Garbarini (2018) [footnote 93].

foreign platform enterprises, as the income should typically be classified as business income, pursuant to Article 7 of the OECD Model (2017), and since the platform enterprises are often able to deliver their digital services remotely.

Taking a closer look at the interaction between the platform enterprises and the users, it may be possible to argue that some kind of barter transaction takes place, as the users of the digital intermediary platform provide vital data to the platform enterprise in exchange for getting “free” access to the platform. However, even though it may be possible for some user-jurisdictions to find legal basis in existing tax legislation for taxing resident users of the receipt of a payment in kind (in the form of access to the platform), this does not seem to be a viable option in practice.

As a consequence of the current lack of possibility for taxation in the user-jurisdictions, the European Commission’s recent proposal for a directive laying down rules relating to a significant digital presence seems to be particularly interesting, as it will enable user-jurisdictions within the EU to tax (parts of) the profits generated by foreign platform enterprises. Accordingly, even though the proposal needs further work in order to become sufficiently clear and targeted, and the scope may be limited in order not to cause treaty override, it may prove to be a step in the right direction, if adopted.