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International tax rules do not fulfill their purpose

European Commission has introduced the strategy for a fair and efficient tax system in the European Union for the digital single market (1). The aim is to tax the companies in jurisdiction where their profits are generated and value added. The purpose of the principle is to ensure that the digital economy is fairly taxed.

Digitalization has fundamentally changed the evolution of business models and blurring the lines between goods and services, transforming products to their digital representation and vice versa. Within last 10 years, e-commerce enterprises have increased their revenues on average 32% per year. Market capitalization of technology companies was 7% in 2016 and 54% respectively in 2017.

The main challenge is to tax the profits where the value is created. However this is not as simple in every case. There are two main policy challenges today that need to be addressed:

Where to tax i.e. how to establish and protect the taxing right in the country where digital services are provided without physical presence, despite having a commercial presence? In other words, it is necessary to amend permanent establishment principles.

What to tax i.e. how to attribute profit in digitalized business models based on intangible assets, data and knowledge. In other words, it is necessary for transfer pricing rules to in compliance with sharing the profits according to value added in different countries.

At EU level, the Common Consolidated Corporate Tax Base proposal has been introduced as one of the possible solutions. European Commission believes that CCCTB (2) creates fair framework to determine permanent establishment as well as

distributing profit according to enterprise assets, employees and turnover. The general idea is, that multinational corporations could submit one

corporate income tax return, based on what the profit is distributed between related member states and referred member state could tax it's part according to domestic legislation. Also, it is possible to take into account incurred losses.

The Commission envisages a legislative proposal for spring 2018, ideally to implement solutions suggested by the OECD.

(1) <http://data.consilium.europa.eu/doc/document/ST-12429-2017-INIT/en/pdf>

(2) [http://www.europarl.europa.eu/RegData/etudes/BRI E/2017/599395/EPRS_BRI\(2017\)599395_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRI E/2017/599395/EPRS_BRI(2017)599395_EN.pdf)