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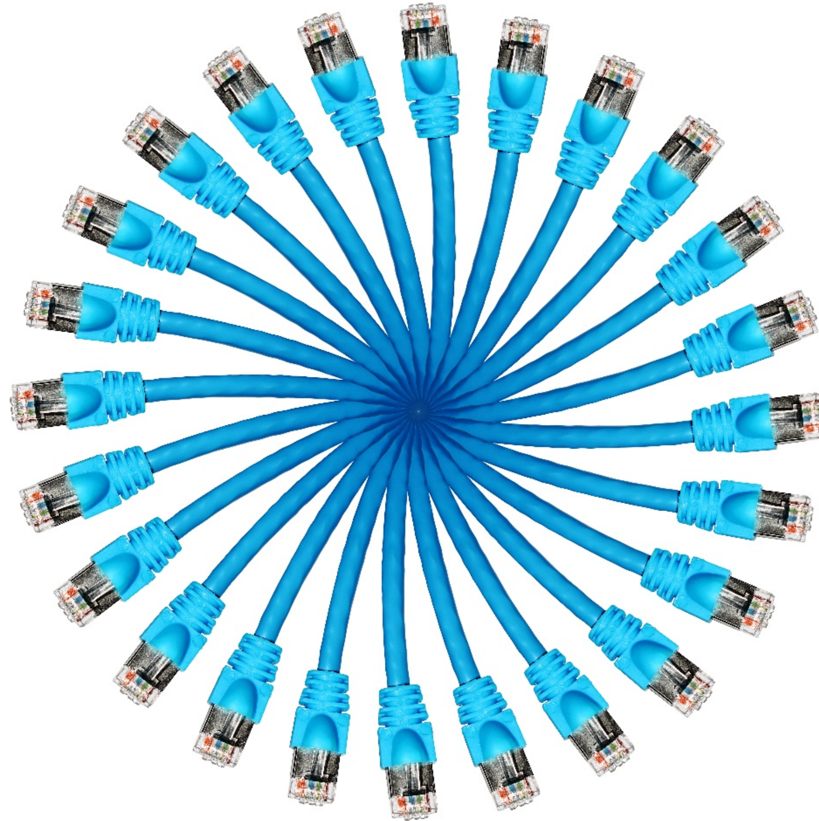

Video-on-demand streaming services and value added tax

A rapidly evolving legislative environment

July 2016

Video-on-demand ("VoD") and other online streaming services are growing exponentially. A 2015 report from Juniper Research projected that on-demand services could see their global subscriber base nearly quadruple from 92 million subscribers in 2014 to over 333 million in 2019[1]. Historically, consumers have only been able to download content through platforms and intermediaries. Now, though, VoD providers are moving to sell content directly to consumers—capitalizing on strong brands built through high-profile TV series, many of which are produced in house.

Commercially, this makes sense. While intermediaries have been—and still are—an important route to market, their commissions and margins can be significant. However, as VoD providers expand sales across multiple jurisdictions to reach a global audience, they face a complex and evolving indirect-tax landscape—one that intends a healthy dose of caution. This article provides an overview of the tax challenges involved, as well as some considerations for doing business in this environment.

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[1] "OTT – A Threat Networks Can't Shake Off", Juniper Research, 2015

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Understanding the tax landscape

The Organisation for Economic Co-operation and Development ("OECD") looks to local tax authorities to collect tax on services, including those provided digitally such as video streaming and on-demand services, at the place of consumption—in short, where consumers purchase and view the content. The OECD emphasized this intention in Action 1 of its base erosion and profit shifting ("BEPS") initiative, which focused on taxation challenges of the digital economy. The OECD's international VAT/GST guidelines on the place of taxation for business-to-consumer supplies of services and intangibles offer further detail on this specific point.

The OECD's actions have had significant impact. Prior to the September 2014 release of the OECD's paper, "Addressing the Tax Challenges of the Digital Economy," only a handful of countries sought to tax nonresident providers of electronic services—and many of those failed to implement legislation effectively. As a result, US multinationals had no requirement to register and account for VAT/sales tax on content supplied to private consumers outside of Switzerland, Norway, Iceland, South Africa, and the 28 European Union member states. Even within the European Union, there were no known / enforced penalties prior to January 1, 2015, for failure to register, principally because, due to the lack of a clear, practical legal framework, the authorities were unable or unwilling to enforce these rules.

Today, many more countries are looking to bring nonresident businesses within the scope of their local indirect tax regimes. A specific challenge is that each of these countries seeks to tax suppliers in a slightly different way. For example:

• South Africa requires companies to account for VAT on sales to both businesses and consumers.

• Japan, in contrast, only requires payment of Japanese Consumption Tax on business-to-consumer sales; however, it defines "consumer" not by the nature of the recipient but by whether or not the service supplied is contractually designated for business purposes. If it is, no tax is due even when the purchaser of the service is not a "business" customer.

• The European Union member states have no threshold below which businesses can avoid the requirement to register. In Switzerland, however, the threshold is 100,000 CHF (approximately $100,000 at today's exchange rates).

This lack of uniformity requires businesses to confirm the exact requirements, including what is within and outside of the scope of the tax net, on a country-by-country basis.

In practice, tax authorities still rely heavily on self-policing by affected businesses and on voluntary registration to pay tax. This self-policing is benefiting from the overall increased awareness of these "new indirect taxation principles" of the digital economy. Additionally, although tax authorities still struggle to enforce the rules on a consistent basis, the framework that was created by the OECD, the EU Commission and other organizations has not only allowed many more countries to introduce rules to tax digital services, it has also changed the mindset of taxpayers impacted by new legislation in this area.

While many businesses historically have taken the position that they are outside the reach of a European or African tax authority, the risks of not registering today can be significant. And this is not just a matter of potential penalties and interest. In an environment that shines the spotlight on businesses' tax affairs and where the general public expects compliance, failure to register in a jurisdiction that requires it could produce lasting reputational damage.Furthermore, to enhance enforcement, the European Union has confirmed that it intends to invest additional funding and resources to identify suppliers that have failed to register. It is likely other countries will follow suit soon.

Implications for VoD providers

Beyond sales through intermediaries, many VoD providers are unlikely to make many business-to-business transactions; thus, the question of whether your sales are within or outside the scope of a tax regime such as that in Japan is likely of limited relevance. While sales may fall below the registration threshold in certain countries, where there is no such threshold and where the jurisdiction has introduced local legislation to tax these services, expect to be within the country's local tax net if your business has customers there. This is the case whether or not you have a (physical) presence in that country.

Being in the tax purview of countries from Australia to Albania can have considerable implications, many of which may fall outside the traditional tax department remit. Even where this does fall within the tax department remit, as businesses continue to evolve so quickly, tax departments too often only find out "after the fact".

Implication	Background	Key Questions
Keeping up with evolving registration requirements	It is imperative to stay abreast of changes in countries where registrations are already required (and in place), it is equally important to understand 1) where future registration may be required and 2) how to determine compliance by the date from which rule changes are introduced. This can be particularly challenging given the short timeframes within which some countries have sought to introduce legislative change.	How will you keep up to date as new jurisdictions introduce registration requirements?
Pricing	The rates of tax payable can be as high as 27 percent (in Hungary). Outside of the United States, prices are almost normally presented to consumers as being "tax inclusive"; therefore, the impact on subscription pricing is a vital consideration.	How, if at all, will you update pricing to account for tax on sales? And how will you communicate that change to your customers?
Customer Interactions	Businesses must have sufficient information to demonstrate the country(s) in which their customers are located and, thus, where they should consider account for tax. In order to obtain this information, it may be required to ask customers for additional information and to develop a practical strategy for managing these interactions.	What customer information do you currently have, and is this information sufficient evidence (in the event of audit) of your customers' locations? If not, how will you obtain [Eliminate the use of this term or contact risk management.] additional required information?
Business structuring and contractual considerations	Some businesses have incorporated local entities in countries where they may likely otherwise be required to register as a nonresident, while others have set up regional contracting entities that are responsible for sales to customers in a given region. A VoD provider that operates through a number of intermediaries may have differing VAT accounting responsibilities that are dictated by the contractual position between the parties and the country into which it is supplying services.	Through which entity or entities should you sell, and in what capacity will you provide services (e.g., as an agent or principal for VAT purposes)? How can contracts be structured to protect the business in the event of VAT increases or the introduction of a VAT regime?
Compliance / IT / Systems	Given the local nuances in legislation and the differences in tax rates, compliance can be challenging—particularly for organizations with unsophisticated accounting systems or tax engines. In addition, configuring ERP and other systems correctly to manage these changes will be important to ensure that VAT is being accounted for and reported correctly. In some instances, developing technology and testing this can take considerable time.	How will you handle the volume of returns required and the local language requirements in many jurisdictions? Additionally, how will you make sure your systems are set up correctly and that these systems pull through the data and information required to prepare and submit indirect tax returns? What information and lead-in time will your IT function need to do this?
Resourcing	While the tax returns may not be overly complex (in many cases), registration for indirect taxes can result in often-lengthy audits and tax authority challenges—straining existing professionals and resources.	Who within your organization will be responsible for managing compliance requirements?

What should you do next?

First and foremost, recognize that the growing attention to this area by local tax authorities, the increasing pace of legislative change and enforcement capabilities, and the ever-increasing expectations and debate around tax and morality requires attention—and action. In today's environment, doing nothing could be costly.

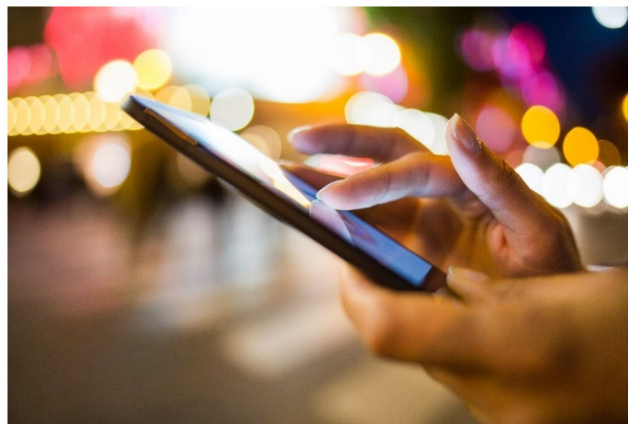
Next, consider the nature of the services you are supplying and determine whether these services fall within the scope of the taxation rules outlined above.

Subsequently, identify the specific business processes within your organization that are directly impacted or need to be changed in order for the company to be able to meet these indirect tax requirements. The schedule on the previous page outlines those processes that are most commonly affected when dealing with these requirements for the first time.

While this article focuses on VoD providers, the issues described above potentially apply to suppliers of all types of digital content—from software providers and app developers to those delivering remote online learning or providing access to online databases of information.

Finally, take the steps necessary to understand the location(s) of your customers and the volume of sales in those jurisdictions. This will be critical to understanding your global indirect tax footprint and profile. Depending on your business, this may be relatively easy, or it could be quite difficult. But without this information, it will be difficult to make decisions about where and how to manage your organization's indirect tax position. In some cases, you may be required to report retrospective liabilities. In others, you may be able to make a sound case for managing the position prospectively.

Either way, up-to-date information about your customers and sales will be critical to effective compliance and proactive tax management.



Video-on-demand and online streaming services are growing exponentially. As providers expand sales across a global audience, they may encounter a complex and evolving indirect-tax landscape.

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