All Working Party No. 9 Delegates are invited to review the attached "Third Draft of Possible Guidelines on the Place of Consumption for Services Traded Internationally", and provide the Secretariat with written answers to the specific questions posed in paragraph 4 of the Introduction by no later than 4 August 2000.

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INTRODUCTION TO THE THIRD DRAFT OF POSSIBLE “GUIDELINES”
ON THE PLACE OF CONSUMPTION FOR SERVICES TRADED INTERNATIONALLY

Background

1. This note concerns the third draft of possible “guidelines” on the principle of taxation in the place of consumption.

2. The fundamental issue which Delegates must now address is the scope of application of the proposed guidelines, and how that scope should be expressed. At the meeting of Working Party No. 9 on 9 June 2000, a difference of approach re-emerged on this point, with several Delegations arguing in favour of a “narrower” definition rather than the “broader” definition the majority had supported in the WP9 Sub-group on Electronic Commerce (“Sub-group”) on 7-8 June.

3. To help resolve this problem, it was agreed that the Secretariat would circulate a further revised draft of the guidelines with both the “narrow” and “broad” approaches illustrated (see paragraphs 3-6 of the attached draft).

4. All Working Party No. 9 Delegates are invited to review this draft and provide the Secretariat with written answers to the specific questions set out below by no later than 4 August 2000.

Questions

1. Which approach to the definition (Option A or Option B) do you favour?

2. Why? Please explain your choice by reference to specific examples, especially to illustrate why you do not favour the alternative option. If, for example, you prefer Option A, please explain why you think Option B does not achieve the correct result. Likewise, if you prefer Option B, explain why Option A is inappropriate.

This process is particularly important for those arguing in favour of the narrow definition (Option B). Please be as clear as possible about the instances in which you believe Option A would achieve an incorrect result (by, for example, including certain services that you feel should be excluded for the application of the guidelines). To help expose the salient differences between the two Options, some “key observations” have been included under each Option in the draft. (Such observations would, of course, not feature in the final version of any guidelines.)
Context

5. To help set this exercise in context, the Secretariat strongly recommends that Delegations address the above questions having referred back to the following key documents:

- **The Ottawa Taxation Framework Conditions**
  [ref. DAFFE/CFA(98)38/REV3]

  Note here, not only the specific conclusions in respect of consumption taxes [Box 3, points (v) - (viii)] – as reflected already in the introduction to the guidelines – but also the terms of the Post-Ottawa Agenda [Box 4, points (vi) and (vii)]:

  **Consumption taxes**

  (vi) Reaching agreement on, inter alia, defining place of consumption, on place of taxation rules and on internationally compatible definitions of services and intangible property.

  (vii) Developing options for ensuring the continued effective administration and collection of consumption taxes as electronic commerce develops.

  Note, too, the key commitment to neutrality [Box 2, point (i)]:

  **Neutrality**

  (i) Taxation should seek to be neutral and equitable between forms of electronic commerce and between conventional and electronic forms of commerce. Business decisions should be motivated by economic rather than tax considerations. Taxpayers in similar situations carrying out similar transactions should be subject to similar levels of taxation.

- **The Work Programme of the Working Party No. 9 Sub-group on Electronic Commerce**
  [ref. DAFFE/CFA/WP9(99)2]

  Note here the terms of the Sub-group’s mandate and the supporting material in Annex A on place of consumption.

- **The Sub-group’s own key Policy Paper on Place of Consumption**
  [ref. DAFFE/CFA/WP9/EC/WD(99)3/REV1]

  This paper was the subject of intensive work in the Sub-group and was presented to Working Party No. 9 in December 1999. Note here the terms of paragraph 4, in particular, and the conclusion (paragraph 11.1):

  *In summary, it is suggested that the most practical place of consumption for intangible services might be the customer’s location and that member countries could then tax or relieve services within their jurisdiction, according to their local practice.*...
Next steps

6. Having received replies from Delegates to these two questions, the Secretariat, together with the Chairs of Working Party No. 9 and the Sub-group, will consider how best to resolve any outstanding differences. This may be through bilateral dialogue with Delegations and/or through further debate in the Sub-group (at its next meeting in September 2000).

7. If, thereafter, matters remain fundamentally unresolved, it may be necessary for Working Party No. 9 itself to meet exceptionally during October 2000 in order to resolve this issue.

8. Your replies to the questions in paragraph 4 should be sent by no later than 4 August 2000 to Simon Woodside [E-mail: simon.woodside@oecd.org and/or Fax: (33 1) 44 30 61 36] who will also be happy to address any queries you may have in the meantime about this process and/or these papers.
THIRD DRAFT OF POSSIBLE “GUIDELINES”
ON THE PLACE OF CONSUMPTION FOR SERVICES TRADED INTERNATIONALLY

Introduction

1. In 1998, OECD Ministers welcomed a number of Taxation Framework Conditions relating to the consumption taxation of cross-border trade, including:
   i) In order to prevent double taxation, or unintentional non-taxation, rules for the consumption taxation of cross-border trade should result in taxation in the jurisdiction where consumption takes place.
   ii) For the purpose of consumption taxes, the supply of digitised products should not be treated as a supply of goods.
   iii) Where businesses acquire services and intangible property from a non-resident vendor, consideration should be given to the use of reverse charge, self-assessment or other equivalent mechanism.

2. The guidelines below are intended to achieve the practical application of the Taxation Framework Conditions, particularly in the context of electronic commerce. Member countries are encouraged to introduce the mechanisms necessary to implement the guidelines.

Application

[Option A]

3. In the context of national value-added (consumption) tax systems, these guidelines are intended to define the place of consumption (and so the place of taxation) for the cross-border supply of services and intangible products by non-resident vendors/suppliers that are not otherwise required to register in the destination jurisdiction under existing mechanisms.\[1\]

4. These guidelines apply to the cross-border supply of services and intangible products that are capable of delivery from a remote location.

5. The guidelines do not, therefore, apply in circumstances where the place of consumption may be readily ascertained, as is the case where a service is performed in the presence of both the service provider and the customer (e.g. hairdressing, hospitality and recreational services such as live concerts). Nor are the guidelines intended to apply in the case of services or intangible property where the place of consumption can more appropriately be said to occur at a location identifiable by reference to a particular criterion, for example, services related to particular real property or goods. Finally, it is recognised that specific types of services, for example, telecommunications services, may require more specific approaches to determine their place of consumption.

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1. The objective is to ensure certainty and simplicity for businesses and tax administrations, as well as neutrality via equivalent tax implications for the same products in the same market (i.e. avoiding competitive distortions through unintentional non-taxation).
Key observations

- The broad scope of this Option, outlined in paragraph 4 (i.e. including services and intangible products), is significantly limited by the qualifications that follow in paragraph 5.

- Services that require both the physical presence of the vendor and the customer are excluded.

- Where a particular criterion more appropriately determines the place of consumption (for example, the location of land where the service relates to real property), then such services are also excluded. This exclusion is also broad enough to remove many professional services from the guideline. Thus, for example, the place of taxation of legal services in relation to litigation would be where the litigation takes place.

- Additionally, this approach envisages that in certain circumstances, even where there is no specific criterion, revenue authorities may take the view that the general guidelines should not apply (e.g. telecommunication services).

- A key feature of this approach is its neutrality. Where the principle of taxation in the place of consumption applies, it will apply equally notwithstanding different modes of delivery.

[Option B]

6. In the context of national value-added (consumption) tax systems, these guidelines are intended to define the place of consumption (and so the place of taxation) for the cross-border supply of digitised services and products.

Key observations

- By definition, this approach applies only to the supply of digitised products and services. In principle, therefore, it is “narrower” in application.

- The definition, however, does not exclude digitised services that relate to, for example, land or goods located in a particular jurisdiction. Thus, while it applies only to a limited range of services and products (i.e. those that are digitised) it can be said to be broader in application than Option A in many respects.

- One alternative would be to specifically define what constitutes a digitised product or service through a narrow, but inclusive list of all such supplies. However, difficulties associated with creating and maintaining such a definitive list would seem to make this an impractical idea.

- This approach also suggests a difference in treatment depending on whether the service or intangible property is delivered in a digitised form or otherwise (e.g. via telephone). It is important to consider the likely reaction (particularly from the business community) to a guideline that appeared to treat digital and non-digital services and products in a non-neutral fashion.
Guidelines

“Business to business”

7. The place of consumption for supplies of services and intangible products made to a non-resident business recipient should be:

   a) The jurisdiction in which the recipient has located its business presence; or
   b) Where the primary use or enjoyment is in a jurisdiction other than that described in paragraph (a), the jurisdiction where the intangible service is primarily used or enjoyed.

“Business to private consumer”

8. The place of consumption for supplies of services and intangible products made to a non-resident private recipient is the country where the recipient has a permanent address or the recipient’s usual country of residence.

2. A “business presence” is an establishment with the human and technical resources required to receive and utilise the supply. This may include the headquarters, registered office or seat of economic activity, the branch of a business, or a separate legal entity that effectively acts as a branch. Where a product is used in multiple locations the place of consumption is deemed to be the main location (e.g. headquarters).

3. Countries are encouraged to implement a “use or enjoyment” provision to ensure that the mobility of communications is not used to avoid tax by routing services through temporary establishments in non- or low-tax countries.

4. The “usual country of residence” denotes an address other than a permanent address at which a private individual regularly resides. While some consumers may have more than one country of residence they should be expected to declare the country in which they spend the majority of their time.

5. It is recognised that implementing this guideline will not always result in taxation in the actual place of consumption. Under a “pure” place of consumption test, intangible services are consumed in the place where the customer actually uses the services. However, the mobility of communications is such that to apply a pure place of consumption test would lead to a significant compliance burden for vendors.
Recommended approaches to the practical application of the guidelines

“Business to business”

1. Member countries should consider the use of a reverse charge, self-assessment or other equivalent mechanism in respect of these transactions.6

“Business to private consumer”

2. [“Recommended” collection mechanism(s)?]

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6. As per the Framework Conditions, countries are encouraged to collect tax on business to business transactions through a “reverse charge” or equivalent system. Under such a system the business recipient declares the tax due as if it were a supply (sale) by the business recipient itself. At the same time the recipient is entitled to a credit in the same way as if it had made the purchase from a supplier within its own jurisdiction (countries may wish to waive the reverse charge where an input tax credit or deduction of input tax would otherwise be available). Such a system would protect revenues while ensuring the competitiveness of domestic suppliers.