The attached document is submitted FOR INFORMATION under Item V of the Draft Agenda of the Sixth Meeting of the Working Party No. 9 Sub-group on Electronic Commerce, to be held on 21-22 September 2000.

Delegates will note that an annex to this document will be available on OLIS under the code DAFFE/CFA/WP9/EC(2000)2/ANN1. It will include the initial comments and responses from the credit card companies to the attached document.

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VERIFICATION OF THE PLACE OF CONSUMPTION FOR ELECTRONIC COMMERCE TRANSACTIONS:
POSSIBLE USE OF CREDIT CARD INDICIA

1. This note has been prepared by Working Party No. 9 Sub-group on Electronic Commerce (in consultation with representatives of the Consumption Tax TAG and the Technology TAG) as the basis for a more detailed dialogue with representatives of the major credit card companies.

Introduction

2. In 1998, OECD Ministers welcomed a number of Taxation Framework Conditions relating to the consumption taxation of cross-border trade.

3. Most importantly, it was agreed that 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.

Issue

4. One of the key issues now facing the OECD Working Party No. 9 on Consumption Taxes is how to determine and verify the jurisdiction where consumption takes place in respect of cross-border digitised supplies.

5. We are particularly interested in business-to-consumer (B2C) transactions as we anticipate that most jurisdictions will rely on a system of self-assessment (or reverse charge) for business-to-business (B2B) transactions.

Background

6. Determining the place of consumption for the traditional cross border supply of goods and services is based on the recipient’s address for delivery. Due diligence by the supplier and verification by revenue authorities is relatively simple.

7. Where a transaction is digitally downloaded or electronically delivered via the Internet, however, there is no physical delivery address for the supplier to rely upon. This creates difficulties for suppliers as well as for revenue authorities.

8. In fact, common VAT design dictates that exported supplies be relieved of tax. Generally, this means that suppliers must determine when a product or a service is leaving the country and then maintain acceptable documentary evidence.
9. From a practical perspective, therefore, exporters of digitised products have a strong vested interest in obtaining proof of export so that they do not find themselves assessed for uncollected domestic VAT.

10. Ideally, taxation of digitised supplies would be based on a “pure consumption test” whereby supplies would be defined as consumed in the place where the recipient actually uses the good or service irrespective of:
   - Where the provider or customer is located at the time the service is provided.
   - The contract.
   - Payment; or
   - Beneficial interest.

11. Under a “pure consumption test” the tax should, in principle, accrue to the country in which the actual consumption takes place for all transactions.

12. However, applying the pure definition gives rise to a number of difficulties, including:
   - Actual use of the service by a recipient in a jurisdiction other than where the provider is established would mean that the provider might have to account for the tax in that jurisdiction.
   - In many cases the supplier could not determine where the recipient actually uses or consumes the good or service.
   - It could lead to difficult attribution rules where the supply is consumed in multiple jurisdictions; and
   - Revenue authorities might be unable to identify and verify that a taxable transaction had occurred.

13. Consequently, an approach is required which will take account of the consumption principle, and ensure certainty for business and revenue authorities, while also preventing competitive distortions through double taxation or unintentional non-taxation.

14. It is extremely important that the compliance burden for business be minimised in order to encourage compliance and facilitate commerce.

15. For B2C transactions the Working Party is considering an approach under which the place of consumption is deemed to be where the consumer has a permanent address, or alternatively, their usual place of residence.

16. Almost certainly the first step in determining the recipient’s jurisdiction will be a request by the supplier for the recipient to self-identify their country of residence (most probably via a pull-down menu).

17. Not surprisingly, however, revenue authorities are reluctant to rely on self-declaration in the absence of some form of secondary verification.

18. Therefore, the Working Party is exploring a range of indicia and proxies, including credit cards, that may be used to verify self-identification by the recipient.
Credit cards

19. In our view, the dominant (if not exclusive) form of payment for consumer transactions over the Internet in the near future will be the credit card. Ostensibly, the user’s billing address would be an obvious method to verify a recipient’s declaration of country of residence.

20. That said, we appreciate that a credit card user’s billing address is held by the issuer and is not publicly available for various privacy and legal reasons.

21. One alternative may be to use the jurisdiction of the financial institution issuing the credit card as a proxy for the country of residence of the recipient.

22. Our preliminary understanding is that the International Standards Organisation (ISO) has central control over the “ISO Register of Card Issuer Identification Numbers”. This register records each number range issued against the identity of the financial institution. The recorded information includes the name, address, city, state, postal code, and most importantly, the country of the bank.

23. The issuer identification number on a credit card may be compared against the ISO register/database to identify the issuing bank’s jurisdiction. The issuing bank’s jurisdiction could then be used as a proxy to verify the recipient’s self-declaration.

24. We also understand that in North America, suppliers can avail themselves of an Address Verification System to verify a credit-card billing address.

25. Using the issuing financial institution’s jurisdiction as a proxy to verify the recipient’s jurisdiction is not flawless. For example:
   - It relies on the hypothesis that the credit-card user and issuer reside in the same jurisdiction. Of course, a recipient may maintain a credit card from a financial institution in a jurisdiction other than their usual place of residence (however, these situations will represent a minority of the cases).
   - It has the potential to slow the speed of transactions, depending on how quickly the customer verification could be accomplished.
   - It is potentially open to abuse/distortion (through the deliberate use of a credit-card issuer located in a “tax haven”).

26. Nonetheless, we view this option with guarded optimism and would like to examine in more detail some of the issues with the aid of the credit-card industry.
Questions

1. Is the information available from a credit card or the issuer to determine a cardholder’s address (or, at least, to the state or city level)?
   - Could this information be matched against the declared residency of the customer in real time?

2. Is the information available for a supplier to verify the country of the issuing financial institution \( e.g. \) via the ISO?
   - Is this information an appropriate proxy of the recipient’s jurisdiction (\( i.e. \) to be matched against the declared residency of the recipient)?
   - Credit-card companies recently added a range of indicators of “transaction type” for “card not present” transactions which include codes for Internet-facilitated transactions. Has this change achieved the desired results? Does this bode well for the verification option/hypothesis that the issuing bank’s jurisdiction “matches” the customer’s jurisdiction?
   - Is jurisdictional information about the issuing financial institution also available for debit cards?

3. How does the Address Verification System work? Would it provide jurisdictional verification information at the country level?
   - We understand this system is currently available in North America and a similar system will soon be available in the United Kingdom. Are similar systems available outside of North America or will they be in the future?
   - How could e-payment software facilitate this process? Is such software currently available?

4. Are there privacy or commercial difficulties in releasing the information discussed in questions 1 and 2?
   - In terms of question 2 and the ISO register – is this not publicly available information?

5. Are there limitations on the ability of consumers to obtain credit cards in jurisdictions outside of their permanent country of residence (\( e.g. \) franchise arrangements with issuing banks)?

6. How many financial institutions issue credit cards from jurisdictions that might be considered to be a “tax haven”?
   - Are there significantly more credit-card holders proportionate to the number of residents in such jurisdictions?