



Implementation of the Ottawa Taxation Framework Conditions

THE 2003 REPORT



OECD 

ORGANISATION FOR ECONOMIC CO- OPERATION AND DEVELOPMENT

Pursuant to Article 1 of the Convention signed in Paris on 14th December 1960, and which came into force on 30th September 1961, the Organisation for Economic Co-operation and Development (OECD) shall promote policies designed:

- to achieve the highest sustainable economic growth and employment and a rising standard of living in Member countries, while maintaining financial stability, and thus to contribute to the development of the world economy;
- to contribute to sound economic expansion in Member as well as non-member countries in the process of economic development; and
- to contribute to the expansion of world trade on a multilateral, nondiscriminatory basis in accordance with international obligations.

The original Member countries of the OECD are Austria, Belgium, Canada, Denmark, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom and the United States. The following countries became Members subsequently through accession at the dates indicated hereafter: Japan (28th April 1964), Finland (28th January 1969), Australia (7th June 1971), New Zealand (29th May 1973), Mexico (18th May 1994), the Czech Republic (21st December 1995), Hungary (7th May 1996), Poland (22nd November 1996), Korea (12th December 1996) and the Slovak Republic (14th December 2000). The Commission of the European Communities takes part in the work of the OECD (Article 13 of the OECD Convention).

Publié en français sous le titre :

Mise en œuvre des conditions cadres d'Ottawa sur la fiscalité
RAPPORT 2003

© OECD 2003

Permission to reproduce a portion of this work for non-commercial purposes or classroom use should be obtained through the Centre français d'exploitation du droit de copie (CFC), 20, rue des

Grands-Augustins, 75006 Paris, France, tel. (33-1) 44 07 47 70, fax (33-1) 46 34 67 19, for every country except the United States. In the United States permission should be obtained through the Copyright Clearance Center, Customer Service, (508)750-8400, 222 Rosewood Drive, Danvers, MA 01923 USA, or CCC Online: *www.copyright.com*. All other applications for permission to reproduce or translate all or part of this book should be made to OECD Publications, 2, rue André-Pascal, 75775 Paris Cedex 16, France.

INTRODUCTION

The development of electronic commerce in the 1990s posed a number of taxation questions for all governments. The OECD, with its long and successful history of developing practical solutions to international tax issues, reacted quickly and by 1998 had agreed the Ottawa Taxation Framework Conditions. These set out a number of principles that governments should adopt in their approach to taxation of the emerging sector. Since 1998 the work of the OECD's Committee on Fiscal Affairs has continued to develop these principles into practical guidance for international application.

This report provides an overview and brings the Committee's work up to date and highlights the further work still to be done. For more specific information on aspects of the Committee's work on tax and electronic commerce readers are encouraged to refer to the OECD's web site at www.oecd.org/taxation.

TABLE OF CONTENTS

Electronic Commerce	9
The Challenges to Individual Governments.....	11
The OECD Response	11
2001 Progress Report	13
Direct Taxes	14
Consumption Taxes	14
Tax Administration.....	15

IMPLEMENTING THE OTTAWA TAXATION FRAMEWORK CONDITIONS: PROGRESS SINCE 2001

Direct Taxes	18
Consumption Taxes.....	19
Electronic Commerce – Verification of Customer Status and Jurisdiction ...	20
Electronic Commerce – Commentary on Place of Consumption for Business- to-Business Supplies (Business Presence)	21
Electronic Commerce – Commentary to the Recommended Approaches to the Practical Application of the Guidelines on the Place of Consumption – Simplified Registration Systems	21
Other Consumption Tax Issues	22
Registration Thresholds.....	22
Using Technology for the Collection of Consumption Taxes	23
Simplification	23
Implementing the Ottawa Framework Conditions – a view from the Consumption Tax TAG	24
Tax Administration	25
Business Identification	26
Transaction Information.....	28
Record Keeping.....	29
Electronic Payment System Accountability.....	31
Input into Standard-setting bodies	32

FUTURE WORK

Direct Taxes	34
Completion of existing work programme	35
Monitoring.....	35
Consumption Taxes.....	36
Tax Administration	36

Overview of work on e-commerce

The 1998 Post-Ottawa Agenda highlighted a number of items for further work. This box lists some of the achievements since 1998:

Taxpayer Service

Member countries are encouraged to develop systems for accepting tax returns through new technologies and for receiving automated payments of social security, payroll taxes and similar deductions;

Member countries are encouraged to develop interactive telephone answering systems for standard enquiries.

Development of simplified registration procedures and processes for non-resident suppliers required to account for VAT/GST.

Creation of a dedicated OECD group to take forward, through exchange of experiences and information, successful practices in developing taxpayer service.

Tax Administration, Identification and Information Needs

International consensus reached and Guidance issued on

- requirements for Internet business identification
- transaction information, record-keeping and accountability of electronic payment systems.
- verification requirements for customer status and jurisdiction

Tax Collection and Control

Voluntary compliance encouraged through development of simplified registration for non-resident suppliers required to collect VAT/GST.

Work on automated collection of cross-border VAT/GST well advanced

Consumption Taxes

Place of taxation issues including definitions of place of consumption for B2B and B2C agreed and published.

Guidance issued on methods for verifying jurisdiction and status of customer.

Recommended approaches to effective administration and collection of tax published

International Tax Arrangements and Co-operation

Clarification in the OECD Model Tax Convention of the application of the permanent establishment definition in e-commerce.

Clarification in the OECD Model Tax Convention of the treaty characterisation of various types of e-commerce payments

Proposals on refining the concept of place of effective management as a tie-breaker rule

Work well advanced on examining how the current treaty rules for the taxation of business profits apply in the context of e-commerce and on examining proposals for alternative rules.

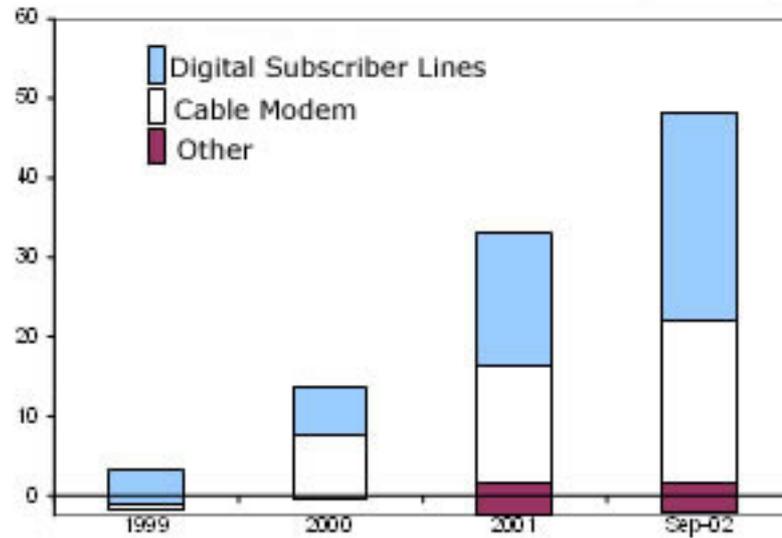
Electronic Commerce

1. As the digital revolution of the 1990s developed so governments around the world became aware of the potential for electronic commerce to transform the way businesses and citizens operate. New ways of doing business emerged creating a new commercial environment in which, amongst other things, businesses suddenly found themselves with access to markets around the globe. For large and small firms the physical constraints of bricks and mortar were less important, start up costs were significantly reduced, and a new entrepreneurial environment blossomed. As both businesses and consumers acquired the hardware necessary to access the Internet so e-commerce grew rapidly.

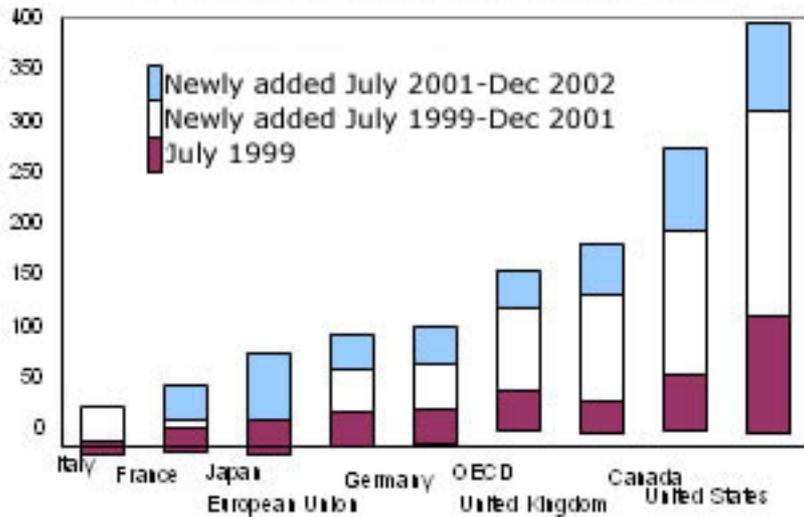
2. But at the turn of the millennium the dot.com bubble burst and a new economic structure of the Internet emerged. Although many small vendors exist, the market is now dominated by a comparatively small number of larger well-recognised companies with established international names and brands that, in the main, existed before the Internet or were built up very rapidly from the early stages of the Internet boom. The e-commerce landscape has evolved, with the majority of businesses integrating e-commerce into their mainstream activities. Larger firms are more likely to use e-commerce for end-to-end advertising procurement, ordering, payment, selling and even delivery of digitised products as they develop integrated internal and external “e-business” strategies, while most smaller firms restrict their e-commerce activities to advertising and e-mail. Business-to-consumer transactions in the main are less well-developed than business-to-business and all firms are more likely to buy and procure than sell over the Internet¹. All these activities are encompassed under the umbrella of “electronic commerce”. But in many cases the use of the Internet and other networks are another extension of “normal” business activity – with major transforming power, but within established market and firm structures. Figure 1 illustrates that growth in the general Information and Communications Technologies (ICT) sector is still comparatively strong.

¹ B2C has been much slower to take off than optimists predicted due, in part, to vendor-side costs and brand establishment, and consumer-side worries about security of transactions, fraud, delivery problems and privacy issues

Broadband connections in the OECD area (millions)



Secure servers per million inhabitants



Source: Broadband connections in the OECD area, OECD (2003), Communications Outlook, Paris
 Secure Servers per million inhabitants, OECD (www.oecd.org/sti/telecom) based on Netcraft
 (www.netcraft.com)

The Challenges to Individual Governments

3. As the Internet moved from its origins as primarily a means of communicating across networks to a medium supporting commercial activities tensions emerged between those who saw the Internet as a new commercial frontier and those who saw a need for governments to provide a regulatory framework within which commerce on the Internet could operate. The opportunities provided by the technology to sell products in circumstances that would formerly have required a degree of physical presence appeared to challenge the application of tax concepts developed for a physical, rather than virtual, world. Some commentators called for the Internet to become a tax-free zone in order to encourage its development. Other commentators saw the Internet offering governments a new source of revenue and advocated a "bit tax" as a means of raising such revenues

4. Governments also saw ICTs as an opportunity to improve the business of government. The potential for enabling the interface between government and citizens to develop was clear. One of the key areas identified in this respect was that of tax and, specifically, the use of the technology as a means of simplifying the interface between tax administrations and taxpayers. On-line tax returns were inevitably highlighted as an area for development that could reduce administrative burdens on both sides. Many governments use tax administration to lead the e-government revolution.

The OECD Response

5. In November 1997 the OECD organised a joint government and business conference in Turku, Finland entitled "Dismantling the Barriers to Global Electronic Commerce", the title of which underscored the OECD's overall approach. A key principle overlaying all the OECD's work on electronic commerce is the creation of an environment in which electronic commerce can develop its full potential. For tax this has required a fiscal environment that strikes a balance between development of electronic commerce and the need to secure the revenue base on which so much government expenditure is based. The Ottawa OECD Ministerial Conference in 1998 "A Borderless World – Realising the Potential of Electronic Commerce", which brought together OECD and non-OECD governments and the business community, furthered this through the adoption of the Ottawa Taxation Framework Conditions, which included a set of broad taxation principles that should apply to e-commerce (see Box 1).

Box 1: Ottawa Taxation Framework Conditions – Principles

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.

Efficiency

- ii) Compliance costs for taxpayers and administrative costs for the tax authorities should be minimised as far as possible.

Certainty and simplicity

- iii) The tax rules should be clear and simple to understand so that taxpayers can anticipate the tax consequences in advance of a transaction, including knowing when, where and how the tax is to be accounted.

Effectiveness and fairness

- iv) Taxation should produce the right amount of tax at the right time. The potential for tax evasion and avoidance should be minimised while keeping counter-acting measures proportionate to the risks involved.

Flexibility

- v) The systems for taxation should be flexible and dynamic to ensure that they keep pace with technological and commercial developments.

6. The links with business that had been established at the Turku conference remained one of the keys to the OECD's approach to e-commerce work. The Committee on Fiscal Affairs (CFA), from the inception of its work, required that business and non-OECD economies must continue to be involved in the implementation of the Ottawa Taxation Framework Conditions. Business had both the knowledge of the technology, and its commercial application, and was more acutely aware of the rapidly changing environment. The global reach of e-

commerce also dictated that the Committee should include key non-OECD economies in its post-Ottawa work.

7. The Committee therefore established an inclusive process through the formation of a number of Technical Advisory Groups (TAGs) comprising representatives from member governments, non-member governments and business. Box 2 sets out the post-Ottawa work structure.

<i>Box 2: Post-Ottawa Work Structure</i>	
<i>Direct Taxes:</i>	<i>Treaty Characterisation TAG Business Profits TAG</i>
<i>Consumption Taxes:</i>	<i>Consumption Tax TAG</i>
<i>Tax Administration:</i>	<i>Professional Data Assessment TAG</i>
<i>A Technology TAG was also created to provide expert technological input into the work of the other TAGs</i>	

2001 Progress Report

8. Following the adoption of the Ottawa Taxation Framework Conditions work progressed on their implementation and in 2001 the Committee on Fiscal Affairs (CFA) published a report, “Taxation and Electronic Commerce – Implementing the Ottawa Taxation Framework Conditions”. The report summarised the considerable progress on aspects of direct taxes, consumption taxes and tax administration and went on to identify further work.

9. The report covered the full range of taxation issues noting that work since Ottawa had shown that neither of the two extremes – a tax-free environment for e-commerce nor special e-commerce taxes (such as a Bit Tax) – were acceptable to governments. The 2001 Report confirmed that the principles that apply to taxation of conventional commerce should equally apply to e-commerce.

Direct Taxes

10. The 2001 Report covered four issues related to direct taxes. The first was the clarification of the application of the permanent establishment (PE) definition in e-commerce. The Committee issued two drafts for public comments and on 22 December 2000, approved the proposed changes to the OECD Model Tax Convention. These changes clarify in what circumstances computer equipment at a given location can constitute a permanent establishment. The second issue was related to the first one: a discussion draft was produced by the Business Profits TAG on the attribution of profits to a permanent establishment constituted by a server at a given location. The third issue was dealt with in the report by the Treaty Characterisation TAG which made recommendations on the characterisation of various types of e-commerce payments under the OECD Model Tax Convention and suggested some clarifications to the OECD Model Tax Convention. The fourth issue concerned the impact of e-commerce on the application of the place of effective management as a tie breaker rule. This was the subject of a Discussion Draft by the Business Profits TAG.

Consumption Taxes

11. Following the publication of the Ottawa Taxation Framework Conditions the Committee on Fiscal Affairs agreed a work programme on consumption taxes. Key issues in that programme included the development of Guidelines on the definition of the place of consumption. The Guidelines affirmed that for business-to-business (B2B) supplies tax should accrue in the jurisdiction in which the recipient has located its business presence. For business-to-consumer (B2C) supplies the place of consumption should be the jurisdiction in which the recipient has his or her usual residence.

12. The 2001 Report went on to set out a number of Recommended Approaches to tax collection mechanisms for cross-border supplies (“Recommended Approaches to the Practical Application of the Guidelines on the Definition of the Place of Consumption”). For B2B supplies the recommended approach underscored the Ottawa conclusion that reverse charge (or self-assessment) was the most appropriate. For B2C supplies the report recognised that there was no one simple solution, but suggested, in the interim, and where this fitted national systems, a simplified registration system that reduced the compliance burdens that full registration would impose.

Tax Administration

13. The Ottawa Framework Conditions recognised the opportunities the technology provided for improving taxpayer service, identification and information needs, and tax collection and control.

14. In the field of tax administration, the Ottawa taxation principles were developed into the following Taxation Framework elements:

Taxpayer service

- Revenue authorities should make use of the available technology and harness commercial developments in administering their tax system to continuously improve taxpayer service.

Tax administration, identification and information needs

- Revenue authorities should maintain their ability to secure access to reliable and verifiable information in order to identify taxpayers and obtain the information necessary to administer their tax system.

Tax collection and control

- Countries should ensure that appropriate systems are in place to control and collect taxes.
- International mechanisms for assistance in the collection of tax should be developed, including proposals for an insert of language in the OECD Model Tax Convention.

15. The process of implementing these principles involved an intensified dialogue with business and with non-member economies through the Professional Data Assessment TAG and the Technology TAG.

16. A range of “implementation options” had been identified at Ottawa and were expanded upon in the 2001 Report, which also identified the importance of exchanging practices and knowledge between tax administrations.

17. The proposed implementation options relating to tax administration were:

- Revenue authorities may consider requiring that businesses engaged in electronic commerce identify themselves to revenue authorities in a manner

that is comparable to the prevailing requirements for businesses engaged in conventional commerce in a country.

- Revenue authorities may consider encouraging business practices that identify businesses engaged in electronic commerce.
- Revenue authorities may consider mechanisms facilitating tracing, for tax purposes, of inadequately identified web sites and other electronic places of business.
- Revenue authorities may consider making their views on user identity known to other bodies with a role in determining the identity of parties engaged in electronic commerce.
- Revenue authorities should express their views to the appropriate bodies to ensure that features of electronic payment systems do not exacerbate the challenges associated with the cash economy.
- Revenue authorities should co-operate with businesses developing codes of practice or other instruments which would encourage the widespread application of appropriate technologies, such as message digests and digital notarisation, to ensure the integrity of electronic records.
- Revenue authorities may consider expressing their views on information requirements to appropriate bodies developing standards or protocols for electronic commerce.
- Revenue authorities may consider encouraging taxpayers that utilise encryption or security technology to also consider key recovery, trusted third party or other arrangements to guard against the inadvertent loss of encryption keys.

18. These “implementation options” were reviewed by the Forum on Strategic Management (now called the Forum on Tax Administration) in the 2001 Report and further work on a range of issues was identified, including:

- Jurisdictional verification (how is a business trading through the Internet satisfactorily identified?)
- Transaction data elements (what elements should software developers incorporate into systems?)
- Co-ordinating input into standard-setting bodies

19. The report also acknowledged that future work should focus specific attention on compliance issues for small and medium-sized enterprises. By

taking forward the work within a framework of international co-operation, implementation of the tax compliance and administration options was likely to be more effective than through individual domestic development. This was particularly true in areas such as input into global standard bodies, where an OECD-wide approach was likely to have greater impact than one from individual administrations.

IMPLEMENTING THE OTTAWA TAXATION FRAMEWORK CONDITIONS: PROGRESS SINCE 2001

20. Since the 2001 Report work has continued on the issues identified within each of the three strands:

- Direct taxes;
- Consumption taxes; and
- Tax administration.

21. Again, valuable input from business and non-OECD economies has provided a comprehensive perspective on all of these issues. The TAG structure was streamlined into three – Business Profits, Consumption Taxes and Compliance, Information and Documentation, this latter focusing on the tax administration issues.

Box 3: Post-2001 Report Work Structure

Direct Taxes: Business Profits TAG

Consumption Taxes: Consumption Tax TAG

Tax Administration: Compliance, Information and Documentation TAG

A Technology Panel was also created to provide expert technological input into the work of the TAGs

22. The e-commerce environment has changed significantly over the last three years but many of the issues identified in both 1998 and 2001 continue to preoccupy governments and business. And the twin OECD approach of providing a fiscal environment that enables e-commerce to grow whilst ensuring integrity in revenue policies and collection is as appropriate today as it was in 1998.

Direct Taxes

23. Work has continued in a number of areas. The report from the Treaty Characterisation TAG led to clarifications to the Model Commentary being published in the 2003 Update to the OECD Model Tax Convention. That update also included the changes to the Commentary on Article 5 in relation to the circumstances in which a location where computer equipment is used might constitute a permanent establishment (PE). The Business Profit TAG released in June 2003 a revised version of its draft on place of effective management including proposed amendments to the Model Commentary. This draft and the public comments on it will be considered with a view to deciding what, if any, amendments to the OECD Model Tax Convention are needed.

24. The Business Profits TAG is in the process of finalising a discussion draft on whether the current treaty rules for taxing business profits are appropriate for e-commerce for release for public comment later in 2003. The BP TAG draft on the attribution of profit to a server PE and the public comments thereon were made available to the Committee to assist in the revision of its discussion draft on attributing profits to PEs in general. Once this has been revised the BP TAG will consider whether it is necessary to revise its own draft.

25. On transfer pricing, the Committee concluded that having monitored developments in the area of e-commerce since 1998, no new or pressing issues have been identified in relation to transfer pricing aspects of e-commerce. Further, the analysis of fact patterns of different e-commerce business models showed that the existing guidance of the Transfer Pricing Guidelines appears capable of dealing with the issues. The Committee may return to this in case the normal monitoring procedures identify developments in electronic commerce. It is intended to publish the report on the impact of e-commerce on the application of the Transfer Pricing Guidelines in the OECD Tax Policy Studies series.

Consumption Taxes

26. Under consumption taxes such as Value Added Tax (VAT) – referred to by some jurisdictions as Goods and Services Tax (GST) - the supplier is responsible for the correct application of tax on each transaction. In an e-commerce environment this means that systems must be able to apply the correct rate of tax, and in the correct jurisdiction, automatically and at the time the transaction is being made. From a business perspective it is essential to ensure that VAT/GST is applied correctly at the time the transaction takes place as there is little chance to correct errors later, especially in the B2C environment. Most e-commerce operates with the minimum of human intervention in processes so it is important that accurate information on the application of these taxes is provided so that systems operators can operate in a fiscal environment that provides certainty.

27. The 2001 Report recognised that there was further work to be undertaken to develop fully the Ottawa Taxation Framework Conditions as augmented by the Guidelines and Recommended Approaches. This work included:

- Verification of the jurisdiction and the status of the customer
- Analysis of registration thresholds in the context of simplification
- Review of technology-based and technology-facilitated collection mechanisms
- Development of international administrative co-operation
- Simplification options and initiatives.

28. In developing the post-2001 report work the Committee on Fiscal Affairs decided to create a “Consumption Tax Guidance Series”. Unlike some aspects of the Committee’s work on direct taxes there is no obvious OECD publication in which to present a comprehensive and coherent set of papers on consumption taxes. Whilst initially the new Guidance Series will focus on electronic commerce issues, over time it will develop into a more comprehensive series on a range of consumption tax issues. In recognition that all countries have different environments in which they operate a caveat that has been agreed by member countries features on all the papers in the Series (see Box 4).

Box 4: Consumption Tax Guidance Series Caveat

Consumption Tax Guidance is a means of developing greater awareness of both policy and administrative issues. On policy issues the Guidance contains recommendations to member governments that are aimed at removing conflicts, distortions and disincentives to international trade. The section on administrative issues has been developed as a result of sharing experiences between member countries. The OECD's Committee on Fiscal Affairs has approved the contents and countries are encouraged to apply the guidance wherever possible. Nothing contained herein binds member countries, although where there is clear consensus amongst the member countries, administrations should consider the guidance in the light of their existing taxation systems and their legislative approaches.

The first papers in that Series are, therefore, the outputs from the Committee's work on electronic commerce. These papers are summarised in the following paragraphs but the complete papers can be found on the OECD's web site (www.oecd.org/taxation).

Electronic Commerce – Verification of Customer Status and Jurisdiction

29. The guidance paper on this issue provides practical guidance on mechanisms that may be used to establish the status (business or private) and jurisdiction of the customer for low value electronic commerce transactions where the vendor does not have an established relationship with the customer. The intangible nature of many e-commerce transactions (such as a supply of a digitised product) means that in order to deliver the product it is not essential for the supplier to have the customer's physical address. So the question arises as to how a supplier can be sure of the customer's location in order to apply the correct tax decision. At the same time the supplier will need to know whether or not the customer is registered for VAT/GST (a VAT/GST-registered customer will account for tax under reverse charge/self-assessment). The guidance concludes that the status and jurisdiction of a customer should be based on customer self-identification, supported by a range of other criteria including payment information, tracking/geolocation software, nature of the supply and digital certificates. It will be important to monitor the application of these recommendations as technology develops and the means of determining customer location improve.

Electronic Commerce – Commentary on Place of Consumption for Business-to-Business Supplies (Business Presence)

30. The Guideline on the Definition of the Place of Consumption for the Taxation of Cross Border Services and Intangible Property in the Context of E-commerce provides that for cross border business-to-business supplies of services and intangibles:

- The main criterion for determining the place of consumption (and therefore the place of taxation) for the supply is the jurisdiction in which the recipient has located its business presence.
- Countries may use a different criterion where the application of the main criterion results in a distortion of competition or avoidance of tax, (e.g. resulting from the routing of services through establishments in non-tax or low-tax jurisdictions)

31. The commentary builds on the main criterion by stating that in cases where a customer has multiple locations, the terms of the contract (e.g. invoicing, terms of payment, use of intellectual property) should normally provide sufficient indicative evidence to assist both business and revenue administrations in determining the jurisdiction of consumption. It then develops an override to this by suggesting that where supplies are routed through low-tax or no-tax jurisdictions in order to avoid or minimise taxation of consumption, a country may choose to require a business presence in its jurisdiction to account for tax to the extent – but only to the extent - that consumption takes place in that jurisdiction. In addition, and in order to avoid double taxation, the host country of the business location may choose to provide a correction proportionately equivalent to the tax collected by the country under the application of this test.

Electronic Commerce – Commentary to the Recommended Approaches to the Practical Application of the Guidelines on the Place of Consumption – Simplified Registration Systems

32. This guidance explores registration and declaration procedures and record keeping requirements in the context of simplified registration systems for e-commerce B2C cross border transactions. It suggests that governments that implement simplified registration systems consider using electronic registration and declaration and encourages tax administrations to review and develop a legal basis to allow for the use of electronic record keeping systems.

Other Consumption Tax Issues

Registration Thresholds

33. The 2001 Report highlighted the role that registration thresholds might have to play in minimising compliance requirements for non-resident suppliers and identified that this was an area for further clarification. As can be seen from the full version of the report (available at www.oecd.org/taxation) a number of complex issues have arisen, partly from the fact that there is a variety of thresholds across OECD countries.

34. Variations on the theme of thresholds can be seen in the relevant tables published in the OECD's "Consumption Tax Trends"². Countries approach the issue of thresholds from a number of different perspectives:

- Equivalent registration and collection threshold
- No registration threshold but a separate collection threshold
- Separate thresholds for suppliers of services
- Separate thresholds for the charitable sector
- Differing thresholds for non-resident suppliers as opposed to domestic suppliers
- Absence of thresholds

35. In addition to these variations in approach there is also a wide range of annual turnover limits from nil up to a top value of over €200,000. The report acknowledges that against this background developing a consistent approach across all countries was not feasible. The discussion was focused on the application of thresholds to non-resident e-commerce suppliers utilising the simplified interim approach. However, the fact that many countries do not currently grant thresholds to non-resident suppliers has raised issues over neutrality, compliance burdens and practical application. The report concludes that countries should carefully consider these features as part of the development of simplified registration systems. This is an issue that the Committee will keep under review.

² see also Table 8 at <http://www.oecd.org/EN/document/0,,EN-document-22-nodirectorate-no-1-32519-22,00.html>

Using Technology for the Collection of Consumption Taxes

36. There is also a report available at www.oecd.org/taxation on how technology might better be used in collecting tax on cross-border B2C transactions. There is little doubt that the most difficult issue for the application of consumption taxes to electronic commerce is the collection of tax on digitised products sold from a vendor in one country to a consumer in another. As noted above the 2001 Report recommended an interim approach of simplified registration that would allow a relatively easy registration and reporting system. But the reality is that as sales of these products develop (as they are forecast to) no matter how simple a registration and reporting system may be, the potential requirement for a business to deal with a large number of countries in which it has no physical presence is unlikely to be a sustainable solution. As work has progressed on this subject it has emerged that technology could play the key role, and tax administrations should consider the steps to create the legal and administrative environment which will enable the development of business driven technological solutions. Section VI of the report sets out the issues to be addressed.

Simplification

37. The technology that supports electronic commerce also has potential for simplifying the application of consumption tax systems. The new Consumption Tax Guidance Series includes Commentary to the Recommended Approaches to the Practical Application of the Guidelines on the Place of Consumption – Simplified Registration Systems. This addresses a number of issues in this area, including documentation and record-keeping in the context of the interim simplified registration process. Work on tax administration issues has also identified a number of options for simplifying requirements such as record-keeping and transaction information. But it is clear that simplification is a thread that runs through much, if not all, of the work on consumption taxes.

38. Business has made it clear that, in terms of compliance costs, they regard administrative processes as important issues for simplification. As they noted in the 2001 Report the more that processes can be simplified and aligned between countries the greater the scope for easing burdens and encouraging compliance. The Committee recognises that, in some areas at least, these will be longer-term objectives. Nevertheless, implementing the guidance contained in the Consumption Tax Guidance Series on suggested procedures for verification of status and jurisdiction and the streamlined processes for simplified registration

will ease business concerns. Any moves towards greater consistency in application of procedures should result in reduced compliance burdens.

Implementing the Ottawa Framework Conditions – a view from the Consumption Tax TAG

39. Business members of the Consumption Tax TAG have raised some issues that, they feel, are in need of further work in order for the Ottawa Taxation Framework Conditions to be satisfactorily implemented. They have produced a report, in conjunction with Committee's Working Party on Consumption Taxes, although not necessarily endorsed by the Working Party. The full version of the report is on the OECD web site. A major concern expressed by business is double taxation and the report identifies several causes, including:

- Conflicting place of supply rules;
- Conflicting definitions;
- Conflicting tax results arising from different verification requirements for either jurisdictional determination or taxpayer status; and
- Incompatible approaches to treating bundled supplies.

40. In working through this issue it became clear that different jurisdictions have taken different approaches to the taxation of cross-border services and intangibles under their national VAT/GST systems. Emerging from this debate is an understanding that these different approaches have potential for double taxation and unintentional non-taxation, not only for e-commerce but for a wider range of internationally traded services. As a result the Committee will be undertaking further work later in 2003 to ascertain the extent and the nature of the problems arising from the application of consumption taxes to international services.

41. Business members are also keen to see the development of exchange of information between countries especially where this might lead to a satisfactory resolution of double taxation disputes. International agreements are suggested as one means of facilitating this. This issue may well emerge in the Committee's further work on the application of consumption taxes to international services.

42. Some businesses remain concerned that by defining digitised products as "not goods" (as was confirmed in the Ottawa Taxation Framework Conditions) differing channels of delivery can result in different tax rates. The most quoted

example of this is the on-line newspaper that may, as a result of its classification as a service, be liable at a standard rate of VAT/GST, whilst the conventional version will often benefit from a reduced rate. Governments largely take the view that the different functionality inherent in the on-line version means that, typically, the electronic product is significantly different from its hard copy version. But it remains the case that for those businesses with an interest in supplying such on-line products this will remain problematic.

Tax Administration

43. Post 2001 work focused on:

- Jurisdictional verification (how is a business trading through the Internet satisfactorily identified?)
- Transaction data elements (what elements should software developers incorporate into systems?)
- Record keeping requirements (how should records be maintained to ensure their integrity and authenticity over time?)
- Co-ordinating input into standard-setting bodies

Box 5: Revenue Administration Guidance Series

The work of the Forum on Tax Administration forms the first papers in the Series. All the papers bear a standard caveat:

Each Revenue authority faces a varied environment within which they administer their taxation system. Jurisdictions differ in respect of their policy and legislative environment and their administrative practices and culture. As such, a standard approach to tax administration may be neither practical nor desirable in a particular instance.

The documents forming the OECD Tax guidance series need to be interpreted with this in mind. Care should always be taken when considering a Country's practices to fully appreciate the complex factors that have shaped a particular approach.

44. The work has continued to benefit from the input of business and non-OECD government representatives through the Compliance, Information and Documentation Technical Advisory Group (CID TAG).

45. As a means of making the outcomes of this work available to a wider audience the Committee created a Revenue Administration Guidance Series (see Box 5). The papers in the Series have been agreed with the CID TAG.

46. What follows is a summary of the relevant papers in the Revenue Administrations Guidance Series. The full papers are available at www.oecd.org/taxation.

Business Identification

47. This Guidance examines the issues associated with the identification of on-line businesses and encourages appropriate standards of identification of businesses offering services or products via the Internet.

48. The development of global electronic commerce introduces a new element into the accurate identification of businesses for both consumers and regulatory authorities – the physical business is no longer directly observable. In an electronic commerce environment a business may only be identifiable by its domain name (*e.g.* www.businessname.com) and the correspondence between a domain name and the location of where the business activity is undertaken is generally weak.

49. The Guidance identifies two self-identification mechanisms that, if complied with, would ease the concerns of revenue authorities. These mechanisms are:

- The provision of appropriate contact information on the business web site.
- The completion and maintenance of relevant web site ownership information in the gTLD and ccTLD WHOIS databases.

50. The following guidance is identified for revenue authorities:

- Revenue authorities are encouraged to derive and promulgate a common position on the issue of Business Identification in an electronic commerce environment.

- Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organisations to ensure that businesses engaged in eCommerce provide, and accurately maintain, the following contact information on their web site:
 - The business’s legal name and the jurisdiction in which it is registered together with any applicable business and tax registration numbers.
 - The trading name under which it conducts business.
 - The principal physical addresses of the business, including jurisdiction, sufficient to ensure the Revenue authority can locate the business offline.
 - An online method of contact such as e-mail.
 - The name of a point of contact within the business, and
 - The telephone number of that point of contact.
- Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organisations to ensure businesses engaged in e-commerce provide and maintain complete and accurate information to the Internet registrar with which they register.
- Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organisations to ensure that country code Top Level Domain registrars for their geographic jurisdictions abide by internationally recognised registrar requirements in respect to the collection, verification and global availability of WHOIS data for business registrations.
- Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organisations to ensure that the Internet Corporation for Assigned Names and Numbers (ICANN) considers on a periodic basis whether regular pre or post verification of WHOIS data by registrars is warranted in certain circumstances.
- Revenue authorities should closely monitor developments in business identification.

Transaction Information

51. This guidance paper provides appropriate guidance on transaction information for businesses offering services or products via the Internet. The paper is written from an audit perspective, to ensure that an appropriate amount of information exists on the transaction so as to enable verification of the tax results arising from the transaction or aggregated series of transactions. While written for the emerging electronic commerce environment it applies equally to traditional business transactions using electronic systems.

52. To the extent that transaction information requirements and their format and mode of storage can be more consistently agreed between jurisdictions the costs of compliance and of administering the system are likely to be reduced. It should be recognised that most of the transaction information data elements are already in place in most businesses as part of their existing accounting systems and processes, either for internal control reasons or to comply with domestic legal requirements.

53. The approach of the guidance paper is a minimalist one that aims to provide a pragmatic balance between the costs and burdens placed on business and the need for revenue authorities to establish that the correct tax has been declared. Additional data to that required for normal business practices should only be required where it is essential for good governance of tax systems.

54. The following guidance is identified for revenue authorities:

- Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organizations, such as developers of accounting software and private auditors, to promulgate the common position, set out in the guidance paper, as a basis for:
 - ensuring that businesses engaged in e-commerce create, record and maintain appropriate transaction information,
 - developing specifications for a standard international audit data file that meets the requirements of all parties, and
 - developing common specifications for technology based and non-technology based techniques providing sufficient assurance for all parties with respect to the authenticity and integrity of transaction information,

in an electronic commerce environment (including where records are created, recorded and/or maintained electronically).

- Revenue authorities should closely monitor developments in transaction information.

Record Keeping

55. This paper provides guidance on the appropriate standards for record keeping by businesses offering services or products via the Internet. It is equally applicable to transaction-based taxes (VAT/GST) and direct taxes that make use of aggregated transaction information. It is aimed specifically at record keeping requirements for e-commerce, although its principles apply equally to all computerised record keeping.

56. Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organisations, such as accountancy bodies, developers of accounting software and private auditors, to develop:

- Record keeping requirements in support of the OECD Taxation Framework conditions to facilitate the creation and maintenance of reliable and verifiable records that can be trusted to contain a full and accurate representation of electronic commerce transactions.
- Record keeping requirements that allow, to the fullest extent possible, the use of commercial records to meet statutory requirements.
- Common specifications for technology based and non technology based techniques providing sufficient assurance for all parties with respect to the authenticity and integrity of transaction information that is created, transmitted, recorded and maintained.
- A specification for a standard audit file that meets the requirements of all parties operating e-businesses or using a computerized accounting system.
- More consistent approaches to access and retention periods for electronic records that take account of technological developments, commercial practice, and the minimum requirements commensurate with good governance of the tax system in such an environment.

57. Revenue authorities are encouraged to work with relevant government regulatory agencies, business associations and other organisations, such as accountancy bodies, developers of accounting software and private auditors, to ensure that:

- An appropriate regulatory framework exists to allow the creation, transmission, retention and access to electronic records and for their use for evidentiary purposes.
- An appropriate level of access is available to Revenue authorities and private auditors that includes:
 - A range of access options to computer systems and supporting documentation for revenue auditors
 - Timely access to electronic records in a readable format
 - Access to electronic records held in other jurisdictions. These records should be maintained to the same standard as in the jurisdiction where the business is located.
 - Access to electronic records held by 3rd parties.
- Appropriate assistance from anyone concerned with the operation of the system is available to auditors.
- Records should be produced for examination within a reasonable time, and in a readable format.
- Adequate storage and procedures for retrieval of electronic records exists. In particular they should ensure that:
 - All material data is stored including (where held) electronic signatures and certificates and related keys for signature verifications. If data is encrypted, keys and recovery procedures should also be appropriately maintained to ensure revenue authorities are provided with decrypted data in a readable format.
 - Transaction data received in electronic format should be stored as received; or if converted to another format then documentation relating to the conversion process should be maintained. The authenticity and integrity of the content of source documents must be preserved throughout the required period of storage through the use of electronic or other controls.

- The usability and readability of data must be preserved through the required retention period, in particular when data is transferred from one storage system to another.
- An audit trail for tax relevant electronic records is maintained throughout the required period of storage.
- The burdens, including those related to retention periods, placed on businesses storing data are reasonable.

Revenue authorities should closely monitor developments in record keeping methods and technologies.

Electronic Payment System Accountability

58. The Guidance encourages an appropriate level of accountability in electronic payment systems in a manner consistent with conventional systems so that taxpayers can continue to rely on data from these systems to substantiate their tax position. Revenue authorities also often use these systems to verify the taxes and charges due to Governments by a business. The inclusion of an appropriate level of accountability in electronic payment systems can reduce the need for costly ‘after-market’ adjustments to the systems of taxpayers including businesses, customers and payment system providers.

59. The paper identifies three levels of accountability in electronic payment systems:

- Fully accounted;
- Semi-accounted; and
- Unaccounted.

60. A payment system that, in addition to the component amounts of the transaction, identifies **both** parties to the transaction is referred to in this paper as a ‘**fully accounted**’ payment system. A payment system that identifies **only the business** undertaking the transaction is known in this paper as a ‘**semi-accounted**’ payment system.

61. With an ‘**unaccounted**’ payment system **neither the customer nor the business** is necessarily identifiable to the payment system provider. The business receiving the tokens representing electronic money can on-spend these without redeeming them through the payment system provider, leaving no third

party audit trail. These payment systems are thus designed or configured so that significant transactions can be carried out with full anonymity of both parties. As both the Customer and the Business can remain anonymous this payment mechanism is most analogous to physical money – but at the same time its unique advantages over physical cash raise special concerns for law enforcement agencies, including revenue authorities.

62. The issues that arise from the potential differences in levels of payment system accountability are analysed in the paper and the following guidance is suggested for Revenue authorities:

- Revenue authorities should derive and promulgate a common position on the issue of electronic payment system accountability.
- Revenue authorities are encouraged to raise the issue of electronic payment system accountability with relevant Government regulatory agencies.
- Revenue authorities may consider suggesting to relevant government regulatory agencies that electronic payment systems should be at least semi-accounted in nature and/or that load limits for unaccounted systems should be adopted.
- Revenue authorities may consider suggesting to electronic payment system developer's or other relevant parties that such payment systems should be at least semi-accounted in nature and/or that load limits for unaccounted systems should be adopted.
- Revenue authorities should closely monitor developments in new electronic payment systems.

Input into Standard-setting bodies

63. In its work on standard-setting bodies the Committee has ensured input regarding the importance of the accuracy of commercial web site information in the WHOIS registrar databases. This work, done in co-operation with other parts of the OECD, was for the long term successful administration of taxes in a global e-commerce environment, and was provided to ICANN by the Committee. The input emphasised the need for strengthened integrity and reliability of those databases and is reflected in the Business Identification guidance referred to above.

FUTURE WORK

64. Certain types of on-line business activity are genuinely new and have required careful analysis of the taxation position. Tax implications for telecommunications services, the on-line supply of digitised products, Internet auction databases and the supply of rights have been covered in the Committee's work since 1998. One of the key (and certainly the most frequently quoted) principles of the Ottawa Framework Conditions is that of neutrality. Ottawa recognised that "taxation should seek to be neutral and equitable between forms of electronic commerce and between conventional and electronic forms of commerce". By and large the work that has been carried out has achieved this. But during the scope of its work, the Committee has found increasing dangers in treating e-commerce in isolation. If e-commerce receives specific treatment, without that treatment being applied equally to conventional commerce, the risks of breaching neutrality increase.

65. As noted above, electronic commerce is now part of mainstream activities for most businesses, with the majority of businesses extending activities onto the Internet that they were undertaking before its advent. They are using the Internet's potential to complement existing sales channels, enhance existing goods and services, and expand geographical reach. A recent OECD paper contained the following comment: "e-government is more about government than "e"³. Equally it is said that **e-commerce is now more about commerce than "e"**. As such the Committee recognises that ICT has created radical change across much of the business environment. But the growth in trade, and especially the significant growth in cross-border services, has been driven not only by e-commerce, but by a host of factors. Increasing globalisation, improved access to markets, deregulation and privatisation initiatives along with evolving firm strategies have all contributed to these changes. Focusing on only one component of these changes may well invoke risks for future work on taxation. To address this new environment, the Committee will integrate its continuing work on electronic commerce into its mainstream core work and maintain adherence to its ground-breaking work on defining the place of consumption for consumption taxes, tax treatment of digitised products and characterisation of payments and the location of on-line vendors in the Internet world.

³ OECD Policy Brief "The e-government imperative: main findings"

66. By so doing the Committee will be better positioned to adopt a holistic approach to taxation, rather than on specific aspects (such as e-commerce). To illustrate this, the report from the Consumption Tax TAG notes the application of differing bases for place of taxation rules to the international trade in services, leading to potential for double or unintentional non-taxation. This conclusion came about as a result of analysing how these rules affect e-commerce, but if, in addressing these issues, the focus is retained solely on e-commerce, the issues affecting the wider set of international services will be missed. In order to address these concerns the Committee has included in its current work programme issues related to the application of consumption taxes to international services⁴. Moreover, it follows that by working on services more generally, rather than on e-commerce specifically, the risk of breaking the neutrality principle is much reduced.

67. There do, however, remain some specific issues for e-commerce that require further work.

Direct Taxes

68. The BP TAG's future work programme will be divided into 2 parts. The first part will involve the completion of the parts of the original work programme that it is felt still merit attention. The second part will be to continue to monitor developments and take appropriate action where necessary in the light of any developments that occur. This is in line with the mandate given to the TAG, which provided that

“The work of the TAG will involve looking at how the current treaty rules for the taxation of business profits apply in the context of electronic commerce and examining the feasibility and desirability of proposals for alternative rules. Thus it is envisaged that a large part of that work will be to monitor developments. For that reason, the Group might be in existence for some time and may produce a number of reports.”

69. It is proposed that the new work programme will be reviewed by the Committee in June 2004.

⁴ For some countries the notion of ‘services’ includes supplies of intangible personal property.

Completion of existing work programme

70. Looking at the existing work programme it is not proposed to start any new topics but instead to complete the areas where substantial progress has already been made:

Whether the current treaty rules are appropriate for e-commerce

71. It is proposed that the TAG completes its discussion draft on this issue and releases it for public comment by 31 December 2003, with a view to presenting a final report to the Committee in June 2004.

Place of effective management

72. The TAG final report on this issue was placed on the OECD website in early June 2003 with a deadline for public comments of 1 September 2003. The draft together with the public comments will subsequently be considered by the Committee

Attribution of profit to a server PE

73. The Committee will wait until the OECD has revised Part I of the Discussion Draft on Attributing Profits to a PE in general (that revision would take into account the TAG's draft and the public comments on it). The TAG will then review the revised Part I to ensure that it adequately dealt with e-commerce issues.

Monitoring

74. The task of the TAG will be to monitor developments in e-commerce as regards the application of direct taxes, especially where those developments challenge the international consensus reflected in tax treaties and conclusions reached at the Ottawa meeting in 1998. The type of developments that would be monitored would include, for example, any significant proposal for special e-commerce direct taxes or e-commerce treaty rules or any substantial effect on direct tax revenues attributable to business models based on new information technologies. This monitoring process will consist in identifying such developments and carrying work on them if is appropriate to do so.

Consumption Taxes

75. The outstanding issue is that of facilitating tax collection procedures for cross-border B2C e-commerce transactions. Issues that the Committee has identified for further work here include:

- The legal implications of using of intermediaries
- The role of certified software
- Identification of costs of implementing technology, who might be responsible for them and how to minimise the costs to both government and business
- Evaluation of on-line remote auditing in terms of system interface, accessibility and standards
- Development of a consumption tax environment that will allow market driven technological tax collection solutions to flourish

76. Further detail on this work can be found in Section VI of the Report on Automating Consumption Tax Collection Mechanisms.

77. In addition the Committee will be monitoring the implementation by member countries of the *Recommended Approaches to the Practical Application of the Guidelines on the Definition of the Place of Consumption* with specific attention being paid to developments in technology that might allow for:

- Improved verification of customer status and jurisdiction.
- New models for the effective collection of consumption taxes on cross-border B2C e-commerce.

78. In taking this work forward the Committee looks forward to continued co-operation with representatives from both business and non-OECD governments.

Tax Administration

79. The Committee will continue its work on improving the application of technology to a wide range of tax administration applications. Features such as tax business architecture, call centres and Tax XML, in addition to the further development of on-line reporting by taxpayers, will be examined. Much of this work will provide member countries with the ability to learn of successful practices, thereby adding to the efficient application of technology to successful tax administration.

80. Work will also continue, in close co-operation with business representatives, on the development of the Standard Audit File. This is the recording of key business information (transactions and ledger postings) into a file in a specified common format. This greatly facilitates the auditing of such businesses by allowing the tax auditor to utilise computerised audit techniques via standard routines or modules. Most of the audit can be carried out independently of the business's accounting software and significant time and resource savings result for both business and tax administrations.

81. Work will also be initiated on the development of an Internet Search Tool that will provide tax administrations with a tool to improve their efficient use of the Internet as a resource.