

# Unified approach to addressing tax challenges in digital economy (2/7/20)

Following up on the topic of digitalisation discussed in our [Flash News article “Taxing permanent establishments in digital economy” on 23 August 2018](#), we have prepared a series of articles summarising the key points of Pillar One and Pillar Two, documents recently issued by the OECD.

## Background

The taxation of multinational enterprises (MNEs) has been one of the most popular topics over the past few decades. Companies operating in more than one country have found ways of optimising their tax burden by shifting profits from a hightax jurisdiction to one with little or no tax.

Many governments and businesses around the world are faced with complex issues relating to the taxation of business profits. To help find solutions, the Organisation for Economic Cooperation and Development (OECD) and the G20 launched the Base Erosion and Profit Shifting (BEPS) project in 2013.

After a new issue arose in 2018, the OECD published another analysis addressing the tax challenges of the digital economy. This was a starting point for the development of solutions to the emerging issues, leading to the release of the OECD/G20 Inclusive Framework’s “Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy.”

## Challenges of the digital economy

The digital economy is a result of integrating IT innovations into MNE business activities. The types of business models of digital economy include varieties of e-commerce, app stores, online advertising, cloud computing, participative networked platforms, high speed trading, and online payment services.

The biggest challenge for fair taxation of the digital economy on the one hand and the wide scope for MNE tax planning on the other hand lies in the fact that digital economy allows MNEs to do business and gain high revenues all over the world without being actually present in the countries where the business is taking place. A few good examples are companies such as Amazon and Google having faced headline-making tax disputes on the high revenues from online sales and not paying taxes in the countries where the most revenues are generated. At the same time, the current global tax system and provisions of double tax treaties, which mostly regulate the taxation of MNEs all over the world, do not have any instruments to address the new challenge of the digital economy, as the main taxation rules were established long before the victorious march of the digital economy into MNE business activities.

The Work Programme is a big step towards changing the world’s taxation system, aimed at fair taxation of revenues gained as a result of digital business activities.

## The Work Programme

The Work Programme entails the most significant reforms of the international tax system in decades, i.e. a reallocation of taxing rights and the introduction of a global minimum tax. The Work Programme has been

prepared to develop a consensus solution to the tax challenges arising from the digitalisation of the economy:

- the allocation of taxing rights between jurisdictions;
- fundamental features of the international tax system, such as the traditional notions of permanent establishment and applicability of the arm's length principle;
- the future of multilateral tax cooperation;
- the prevention of aggressive unilateral measures; and
- the intense political pressure to tax highly digitalised MNEs.

The Work Programme's proposals for reform are organised into two pillars. Pillar One focuses on the allocation of taxing rights and seeks to undertake a coherent and concurrent review of the profit allocation and nexus rules. Pillar Two calls for the development of a co-ordinated set of rules to address ongoing risks from structures that allow MNEs to shift their profits to jurisdictions where they are subject to little or no tax.

Each pillar also outlines questions the OECD will be working on in order to find solutions. These questions are also open to public comment so that experts can provide their views on technical and administrability issues.

*(to be continued)*