

Taxation of Electronically Supplied Services – all you need to know

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Agenda

- ▶ **Direct Taxation**

- ▶ Domestic Perspective
- ▶ International Perspective

- ▶ **Indirect Taxation**

- ▶ Introduction
- ▶ Relevant Rules
- ▶ 2015 changes

- ▶ **Conclusion**

DIRECT TAXATION

From a Domestic perspective...

- ▶ The Income Tax Act (“ITA”) does not contemplate specific provisions.
- ▶ Generic provisions will apply.
- ▶ Tax treatment will depend on the status of the electronic service provider.

From an International perspective...

- ▶ Given the multi-national characteristics of the transactions involved, income derived from the provision of electronic services could have double tax implications;
- ▶ Application of source basis of taxation could be a challenging affair;
- ▶ The OECD Model Tax Convention and the Commentary (“The Model”) establish a number of important principles;
- ▶ In the absence of domestic tax provisions, local Tax Authorities tend to rely on the Model and its Commentary.

The OECD Model Convention

- ▶ Income derived from the provision of electronic services generally falls within the definition of “*Business profits*”;
 - ▶ If the customer, however, acquires a right to commercially exploit a digital product, income could be characterised as “*royalty income*”.
- ▶ Business profits attributable to a permanent establishment, i.e. a fixed place of business (“FPB”), are taxable in the country where such a FPB is situated;
- ▶ Establishing whether an entity has a FPB in a country is complex but, generally, it is down to the location of the server and the use thereof vis-à-vis the operations pursued by the entity.

The OECD Model Convention (cont'd)

- ▶ The operation of server in a country generally establishes a FPB for the operator thereof if, *inter alia*, the below conditions are met:
 - ▶ It has a degree of permanency;
 - ▶ It is at the disposal of the operator; and
 - ▶ It performs core functions;
- ▶ The presence of personnel for the operation thereof is not required to establish a FPB; and
- ▶ No FPB if the server is solely used for preparatory or auxiliary functions.

The OECD Model Convention (cont'd)

- ▶ Paragraph 42.7 to the Commentary of the Model provides a list of activities which are considered to be of a preparatory or an auxiliary nature:
 - ▶ *“providing a communications link — much like a telephone line between suppliers and customers;*
 - ▶ *advertising of goods or services;*
 - ▶ *relaying information through a mirror server for security and efficiency purposes;*
 - ▶ *gathering market data for the enterprise;*
 - ▶ *supplying information.”*
- If the above activities, however, form an essential part of the activities pursued by the service provider, then, such functions will be considered to be “core”.

The OECD Model Convention (cont'd)

► The future:

On 24 March 2014, the OECD has issued a Public Discussion Draft whose purpose is to *inter alia* identify “the broader tax challenges raised by the digital economy (Section VI) and summarises the potential options to address them that have been presented to, and initially discussed by, the Task Force”.

INDIRECT TAXATION

INTRODUCTION

Electronic Services

‘Electronically supplied services’ as referred to in Directive 2006/112/EC shall include services which are delivered over the Internet or an electronic network and the nature of which renders their supply essentially automated and involving minimal human intervention, and impossible to ensure in the absence of information technology.’

Article 7 of Council Implementing Regulation 282/11

Electronic Services (cont'd)

Examples:

Website supply;

Webhosting;

Distance teaching;

Electronic books;

Downloading of films/music/games.

Electronic Services (cont'd)

Examples of non electronic services

Supply of a service where the supplier and the customer communicate via electronic mail.

Goods where the order and processing is done electronically (example purchasing goods on ebay or amazon).

RELEVANT RULES

Place of Supply Rules

Within EU	Taxable person in same Member State	Location of customer in EU Member State (Local Vat charged by supplier)
Within EU	Taxable person in different Member State	Location of customer in EU Member State (Reverse Charge Mechanism)
Within EU	Non taxable persons within EU	Location of supplier in EU Member State (Local Vat charged by supplier)
Within EU	Taxable person/Non taxable person Outside EU	Location of taxable person/Non taxable person outside the EU
Outside EU	Taxable person in EU Member State	Location of taxable person in EU Member State (Reverse Charge Mechanism)
Outside EU	Non taxable person in EU Member State	Location of non taxable person in EU Member State (Normal/MOSS Registration)

Place of Supply Rules (cont'd)

Examples:

- ▶ Maltese supplier sells electronic book to a non taxable person in the UK;

Place of Supply = Malta with Maltese supplier charging 18% Maltese Vat.

- ▶ A non EU supplier provides webhosting services via internet to a non taxable person in Malta;

Place of Supply = Malta with non EU supplier charging 18% Maltese Vat.

Special Scheme

- ▶ Option for non EU Suppliers supplying electronic services to non-taxable persons in EU Member States to register in a single EU Member State and fulfill all Vat obligations (instead of registering in all Member States);
- ▶ Vat rate charged is the rate applicable in the MS where the non taxable persons reside;
- ▶ Non EU Suppliers submit one electronic Vat Return;
- ▶ Payment of all Vat due is made in the Member State of Registration ,which is afterwards distributed to the different Member States according to the declaration made.

Special Scheme (cont'd)

- ▶ Non EU suppliers may in practice choose to establish their business in a Member State with a low Vat rate (such as Luxembourg) rather than opt for the Special Scheme;
- ▶ Place of Supply will be deemed to be Luxembourg (where the supplier is established) for supplies of electronic services to non taxable persons in EU Member States.

2015 CHANGES

New Place of Supply Rules

- ▶ From 1 January 2015;
- ▶ Applies for supplies of telecommunications, broadcasting and electronic services to non taxable persons;
- ▶ For B2C transactions shift from Location of Supplier to Location of customer;
- ▶ Suppliers need to register in all Member States where they effect B2C transactions (MOSS available);
- ▶ Suppliers need to determine where their customers are established.

New Place of Supply Rules (cont'd)

Within EU	Taxable person in same Member State	Location of customer in EU Member State (Local Vat charged by supplier)
Within EU	Taxable person in different Member State	Location of customer in EU Member State (Reverse Charge Mechanism)
Within EU	Non taxable persons within EU	Location of customer in EU Member State (Normal/MOSS Registration)
Within EU	Taxable person/Non taxable person Outside EU	Location of taxable person/Non taxable person outside the EU
Outside EU	Taxable person in EU Member State	Location of taxable person in EU Member State (Reverse Charge Mechanism)
Outside EU	Non taxable person in EU Member State	Location of non taxable person in EU Member State (Normal/MOSS Registration)

New Place of Supply Rules (cont'd)

Example:

- ▶ Maltese supplier sells electronic book to a non taxable person in the UK;

Place of Supply = UK with Maltese supplier charging UK Vat.

Mini One Stop Shop (MOSS)

- ▶ 2 schemes –
 - ▶ **Union scheme** – for taxable persons established in the EU;
 - ▶ **Non-Union scheme** – for taxable persons not established in the EU.
- ▶ Applies for supplies of telecommunications, broadcasting and electronic services to non taxable persons.
- ▶ Avoid the need for Vat registrations in different Member States where B2C transactions are effected.

Invoicing

- ▶ Rules relevant in the Member State of consumption;
- ▶ In Malta a recent notice was issued stating that there will be no obligation to issue fiscal receipts under MOSS.

CONCLUSION

Summary

- ▶ Non-resident electronic services suppliers establish a FPB in Malta if they make use of a server located in Malta for the performance of core functions with some degree of permanency;
- ▶ Profits attributable to the FPB are taxable in Malta;
- ▶ Change in Place of Supply of B2C transactions;
- ▶ Suppliers of electronic services will potentially charge 28 different vat rates;
- ▶ Vat registrations in different Member States can be avoided by using MOSS.