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Tax Justice Network Australia Submission on the digital economy and Australia's corporate tax system

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The Tax Justice Network Australia (TJN-Aus) welcomes this opportunity to make submission on the digital economy and Australia's corporate tax system Treasury discussion paper.

The Tax Justice Network globally has been concerned that for the last decade, some of the worst offenders in the world of corporate tax cheating have been the digital giants, corporations like Google, Facebook, Amazon and Apple. These corporations present a particular problem for governments, in that so much of their business takes place online, making it easier for them to locate their profits offshore. There have been many well publicised cases demonstrating how some of these technology corporations have used accounting tricks to get their tax rate down to close to zero.

1. Is user participation appropriately recognised by the current international corporate tax system? If not, how should value created by users be quantified and how should it be taxed?

User participation is not adequately captured in the existing international corporate tax system. However, TJN-Aus recognises the balance that needs to be struck between being able to tax the extra profit a corporation gains from user participation through the calculation of that value and the need for simplicity. To have a complex system that attempts to calculate the exact value added in each circumstance will open up the system to be contested by the corporations and require much higher regulatory costs to implement and in resolving disputes with the corporations. Therefore it would make sense instead to have a simple tax applied to corporations where user participation adds to the corporation's profits.

2. Is the value of intangible assets including 'marketing intangibles' appropriately recognised by the current international corporate tax system? If not, how should value associated with intangibles be quantified and how should it be taxed?

The Tax Justice Network globally supports the transition from the OECD arms' length principle for all transfer pricing to a formulary apportionment and unitary taxation.¹ This has also been the view adopted by the Independent Commission for the Reform of International Corporate Taxation (ICRICT) in its 'roadmap' for taxing multinational corporations:²

The fairest and most effective version of unitary taxation is multi-factor global formulary apportionment with a minimum corporate tax rate. We urge global leaders to adopt a roadmap towards this goal, including more short-term measures which would be more effective, easier to administer, and provide greater certainty, than the current defective methods.

After consideration of worldwide residence taxation, destination-based cash-flow tax and formulary apportionment, the Commission concluded:

¹ <https://www.taxjustice.net/topics/corporate-tax/transfer-pricing/>

² <https://www.taxjustice.net/2018/02/07/icrict-roadmap-taxing-multinationals/>

It is the Commission view that global formulary apportionment is the only method that allocates profits in a balanced way using factors reflecting both supply (e.g., assets, employees, resources used) and demand (sales). Neither can create value without the other.

3. Are the current profit attribution rules ‘fit for purpose’? If not, how should profits be attributed?

The TJN is of the view that the current profit attribution rules are not fit for purpose and in the longer term there should be a move to formulary apportionment and unitary taxation.

4. What are your views on allocation taxing rights over residual profits associated with: (i) user contribution to ‘user’ countries, or (ii) ‘marketing intangibles’ to market countries?

5. Should existing nexus rules for determining which countries have the right to tax foreign resident companies be changed? If so, how?

6. From a tax perspective, do you consider that the digitalised economy distinguishable from the traditional economy? If yes, are there economic features of the digitalised economy that present special challenges in the context of taxation? How are these features relevant for assessing the costs and benefits of various models of taxation?

The TJN-Aus takes the view that fundamental reforms are needed to the global tax framework. Digitalisation affects the whole economy, and many corporations use multi-channel models, so there should not be a special regime for digital businesses. For example, retailers which now sell through the web platforms backed by large warehouses also in many cases combine these with local outlets acting as showrooms and delivery points. Also, firms which have a physical presence in many countries, such as retailers like Ikea or Starbucks, link them together through digitally controlled complex supply chains. We support the view of the BEPS Monitoring Group that reforms of the international tax rules should be based on the following principles:

- (i) Neutrality between business models, both digital and non-digital, but also regardless of the extent or form of digitalisation, including multi-channel models;
- (ii) Ending the advantages enjoyed by multinational enterprises (MNEs) of amassing large untaxed earnings which can be used to fund their growth and so reinforce their dominant monopoly positions;
- (iii) Adopting a new approach to taxation of MNEs which would treat them in accordance with the business reality that they operate as global firms, and applying clear, simple and preferably standardised criteria for allocating their worldwide profits to countries where they have a real business presence and away from countries where few or no activities take place.

7. Can and should any changes to the international nexus and profit attribution rules be ring-fenced to apply only to highly digitalised businesses? If so, how?

No, changes to the international nexus and profit attribution rules should apply more broadly to achieve the principle of taxing profits in the places where a corporation is actually creating value and doing business. This does not just apply to digital corporations. In the case of commodities, it would still mean the taxing right would primarily rest in the country where the commodity is produced, not where it is sold.

To ring-fence digital businesses would be going against the principled approach agreed in the G20/OECD BEPS project and in other international studies of the issue. For example, the primary conclusion of the European Commission’s Expert Group on Taxation of the Digital Economy in its report of 2014 was that:

There should not be a special tax regime for digital companies. Rather, the general rules should be applied or adapted so that “digital” companies are treated the same way as others.

8. Are there changes other than to nexus and profit attribution rules that should be made to the existing international corporate tax framework and/or Australia’s tax mix to address the challenges presented by globalisation and digitalisation?

As stated above, TJN supports a long term shift to formulary apportionment and unitary taxation. We support the view of the ICRICT that a transition in this direction is the use of the profit-split method, which the OECD has accepted since 1995.³ This method apportions the combined profits of relevant related affiliates of the multinational enterprise, based on “allocation keys” which reflect each entity’s contribution to the generation of profit, albeit at a transaction-level rather than at an entity-level.

9. What does the experience of other countries that have introduced interim measures or that are contemplating them mean for Australia?

10. Should Australia pursue interim options ahead of an OECD-led, consensus-based solution to address the impacts of the digitalisation of the economy on the international tax system?

The Australian Government should put in place interim measures to address the impacts of the digitalisation of the economy as such changes by multinational corporations are not waiting for consensus to be achieved by governments. If governments wait for consensus to be achieved, then it will be in the interests of some multinational corporations to seek to derail consensus from ever being achieved, if they benefit from being able to avoid paying the taxes they should be paying under the existing global taxation framework. By governments taking interim actions, it will motivate multinational corporations to support governments to reach consensus and change the global framework to reflect the shifts digitalisation of the economy is causing.

Such interim measures should:

- (i) Be in line with the principle stated in the G20 Declaration on International Tax in 2013 of taxing MNEs ‘where economic activities occur and value is created’;
- (ii) Do not damage developing countries revenues and emerging economies; and
- (iii) Where possible are taken in concert with other countries.

As an additional comment, the TJN-Aus believes governments should be free to require that tax records which are stored on the cloud need to be stored on a local server. Local server requirements ensure the tax authority can access records to check for tax evasion, without having to rely on a mutual legal assistance treaty to get them from a server in another country. For example, the New Zealand government requires tax records stored on the cloud to be stored on a server in New Zealand and failure to do so is an offence punishable by a fine. (<https://www.ird.govt.nz/technical-tax/revenue-alerts/revenue-alert-ra1002.html>)

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³ Independent Commission for the Reform of International Corporate Taxation, ‘A Roadmap to improve rules for taxing Multinationals. A Fairer Future for Global Taxation’, February 2018, 10.

Background on the Tax Justice Network Australia

The Tax Justice Network Australia (TJN-Aus) is the Australian branch of the Tax Justice Network (TJN) and the Global Alliance for Tax Justice. TJN is an independent organisation launched in the British Houses of Parliament in March 2003. It is dedicated to high-level research, analysis and advocacy in the field of tax and regulation. TJN works to map, analyse and explain the role of taxation and the harmful impacts of tax evasion, tax avoidance, tax competition and tax havens. TJN's objective is to encourage reform at the global and national levels. The Tax Justice Network aims to:

- (a) promote sustainable finance for development;
- (b) promote international co-operation on tax regulation and tax related crimes;
- (c) oppose tax havens;
- (d) promote progressive and equitable taxation;
- (e) promote corporate responsibility and accountability; and
- (f) promote tax compliance and a culture of responsibility.

In Australia the current members of TJN-Aus are:

- ActionAid Australia
- Aid/Watch
- Anglican Overseas Aid
- Australian Council for International Development (ACFID)
- Australian Council of Social Service (ACOSS)
- Australian Council of Trade Unions (ACTU)
- Australian Education Union
- Australian Manufacturing Workers Union
- Australian Nursing & Midwifery Federation
- Australian Services Union
- Australian Workers Union, Victorian Branch
- Baptist World Aid
- Caritas Australia
- Centre for International Corporate Tax Accountability and Research
- Community and Public Service Union
- Electrical Trades Union, Victorian Branch
- Evatt Foundation
- Friends of the Earth
- GetUp!
- Greenpeace Australia Pacific
- International Transport Workers Federation
- Jubilee Australia
- Maritime Union of Australia
- National Tertiary Education Union
- New South Wales Nurses and Midwives' Association
- Oaktree Foundation
- Oxfam Australia
- Save the Children Australia
- Save Our Schools
- SEARCH Foundation
- SJ around the Bay
- Social Policy Connections
- TEAR Australia
- The Australia Institute
- Union Aid Abroad – APHEDA
- UnitedVoice
- Uniting Church in Australia, Synod of Victoria and Tasmania
- UnitingWorld

- Victorian Trades Hall Council
- World Vision Australia