

COMMISSION RECOMMENDATION

of **XXX**

on the corporate taxation of a significant digital presence

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 292 thereof,

Whereas:

- (1) The Commission Communication on "A Fair and Efficient Tax System in the European Union for the Digital Single Market"¹ adopted on 21 September 2017 stated that new international rules specific to the challenges raised by digital economy are needed to determine where the value of businesses is created and how it should be attributed for tax purposes. To advance the approaches considered under the OECD Base Erosion and Project Shifting (BEPS) project Action 1 report on "Addressing the Tax Challenges of the Digital Economy" released in October 2015, this would entail reform of international tax rules on the definition of a permanent establishment, transfer pricing and profit attribution applicable to digital activities.
- (1) The European Council Conclusions of 19 October 2017 "underlined the need for an effective and fair taxation system fit for the digital era" and "looked forward to appropriate Commission proposals by early 2018". The ECOFIN Council in its Conclusions of 5 December 2017 underlined "that a globally accepted definition of permanent establishment and the related transfer pricing and profit attribution rules should also remain pivotal when addressing the challenges of taxation of profits of the digital economy" and encourages "close cooperation between the EU, the OECD and other international partners in responding to the challenges of taxation of profits of the digital economy".
- (2) The ECOFIN Council in its same Conclusions also "urges the OECD to find appropriate solutions for upgrading the global network of double tax conventions, modify its Model Tax Convention and accompanying commentaries, as well as its Transfer Pricing Guidelines and Guidance on Attribution of Profits to Permanent Establishments, in order to address these global challenges".
- (3) The permanent establishment concept as currently set out in Article 5 of the OECD Model Tax Convention should be revised to take into account, for example, revenue and other user-based criteria for determining the "significant digital presence" of a business. The profit attribution rules as currently set out in Articles 7 and 9 of the OECD Model Tax Convention and the OECD Transfer Pricing Guidelines should be revised to take into account, for example, the contribution to value creation of users and data. The international work should include further consideration of the use of the profit split method to ensure a fair allocation of profits to the significant digital presence.

¹ COM/2017/0547 final.

- (4) Double Tax Conventions actually play an important role in encouraging cross-border trade efficiency by improving certainty for taxpayers as regards their international dealings. By entering into a double tax convention the Contracting States agree to attribute the taxing rights between themselves with a view to eliminating double taxation and thereby fostering economic activity and growth. Appropriate revisions and additions to the double tax conventions signed by the Member States of the Union with their non-Union partners should therefore be promoted in order to ensure consistency between the Digital Single Market and the global economy.
- (5) Member States of the Union are invited to use as a source of illustration or interpretation for the changes to their double tax conventions with non-Union jurisdictions the provisions of Directive YY/YY/EU (Council Directive laying down rules for the corporate taxation of a significant digital presence).

HAS ADOPTED THIS RECOMMENDATION:

1. Subject matter and scope

This recommendation puts forward a proposal for adaptations to the double tax conventions of Member States with non-Union jurisdictions to extend the concept of a permanent establishment so as to include a significant digital presence through which the business of an enterprise is wholly or partly carried on in another jurisdiction, and rules for attributing profits to the significant digital presence.

2. Recommendation

Member States are recommended to negotiate the necessary adaptations to their double tax conventions with non-Union jurisdictions so as to bring into effect the following elements:

i) a definition of a significant digital presence as follows:

1. For the purposes of this Convention, the term “permanent establishment” shall include a "significant digital presence" through which the business of an enterprise is wholly or partly carried on.

2. A "significant digital presence" shall be considered to exist in a given jurisdiction in a tax period if the business of an enterprise consists wholly or partly of the supply of digital services through a digital interface and one or more of the following conditions is met with respect to the supply of those services by that enterprise together with its associated enterprises:

a) the total revenues obtained in that tax period and resulting from supplying those digital services to users using a device in a given jurisdiction to access the digital interface exceeds EUR [...]*

b) the number of users of any of those digital services using a device in a given jurisdiction to access the digital interface exceeds [...] * in that tax period;

[c) the number of contracts for supplying a digital service that are concluded by accessing the digital interface in that tax period by the enterprise with users using a device in a given jurisdiction exceeds [...] *.]

* The thresholds for determining when a significant digital presence constitutes a permanent establishment should be defined in the double tax conventions in line with those set by the national rules of the Member States, taking into account Directive YY/YY/EU (Council Directive laying down rules for the corporate taxation of a significant digital presence).

3. For the purposes of these rules the jurisdiction where a user's device is used shall be determined by reference to the Internet Protocol (IP) address of the device or, if more accurate, any other method of geolocation.

ii) rules for attributing profits to a significant digital presence as follows:

1. The profits attributable to the significant digital presence shall be those that such digital presence would have earned if it were a separate and independent enterprise performing the same or similar activities under the same or similar conditions, in particular in its dealings with other parts of the enterprise, taking into account the functions performed, assets used and risks assumed, through a digital interface.

2. The determination of profits attributable to the significant digital presence shall be based on a functional analysis. In order to determine the functions of, and attribute the economic ownership of assets and risks to, the significant digital presence, the economically significant activities performed by such presence through a digital interface shall be taken into account. For this purpose, activities undertaken by the enterprise through a digital interface related to data or users shall be considered economically significant functions of the significant digital presence which attribute risks and the economic ownership of assets to such presence.

3. In determining the attributable profits under paragraph 2, due account shall be taken of the economically significant activities performed by the significant digital presence which are relevant to the development, enhancement, maintenance, protection and exploitation of the enterprise's intangible assets.

4. The economically significant activities performed by the significant digital presence through a digital interface include, inter alia, the following:

- (a) collection, storage, processing, analysis, deployment and sale of user-level data;
- (b) collection, storage, processing and display of user-generated content;
- (c) sale of online advertising space;
- (d) making third-party created content available in a digital marketplace;
- (e) the provision of any other digital service.

5. In determining the attributable profits under paragraphs 1 to 4, taxpayers shall use the profit split method unless a taxpayer proves that an alternative method based on internationally accepted principles is more appropriate having regard to the results of the functional analysis. The splitting factors may include expenses incurred for research, development and marketing as well as the number of users and data collected per Member State.

3. Interaction with other Union acts

It is recommended that provisions in the double tax conventions of Member States with non-Union jurisdictions take into account the definitions, thresholds and other conditions for a significant digital presence and rules for attributing profits to a significant digital presence laid down in the provisions of Directive YY/YY/EU (Council Directive laying down rules for the corporate taxation of a significant digital presence) to ensure consistent application at the international level.

[In accordance with the provisions of Directive YY/YY/EU (Council Directive laying down rules for the corporate taxation of a significant digital presence),, for each Member State, an entity shall only fall within the scope of Directive XX/XX/EU (Digital Services Tax) for the purposes of the charge to DST in that Member State if the following conditions are met:

- (a) the entity is resident for corporate tax purposes in a non-Union jurisdiction;

(b) the Member State has a double tax convention in force with that non-Union jurisdiction;

(c) that convention does not include provisions similar to Articles 4 and 5 of Council Directive YY/YY/EU laying down rules for the corporate taxation of a significant digital presence.']

4. Follow-up

Member States should inform the Commission on the measures taken in order to comply with the present recommendation, as well as on any changes made to such measures.

5. Addressees

This Recommendation is addressed to Member States.

Done at Brussels,

For the Commission

[...]

Member of the Commission