



KPMG Meijburg & Co

Transfer Pricing & E-Commerce/Digital Economy

The International Tax and Transfer
Pricing maze in the Technology Era

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Tax is our business



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Agenda

Profiling E-Commerce

- What's the change

Transfer pricing perspectives

- TP Models / issues with traditional approaches
- Real life case
- Permanent establishment (PE) perspective
- Colin-Collin

OECD and Base Erosion and Profit Shifting (BEPS) and EU Proces and Italian perspective

Key take aways



Profiling E-Commerce

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What's the change?

- E-Commerce – buying and selling of goods/services over the internet or a computer network
- Information and communication technologie underlying E-Commerce are triggering to a paradigm shift in the way businesses operate
- Transfer pricing issues in E-Commerce not necessarily new, but



A critical step is understanding the elements in the virtual supply chain – where is the value created?

Issues: Direct taxes: corporate income tax and transfer prices

Indirect taxes: Value added tax (VAT), customs and withholding taxes

What's the change?

- A truly global organisation is a reality
- Change in competition
- Relevance of intangibles



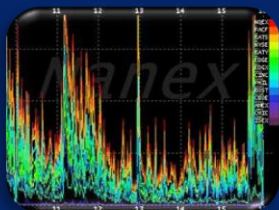
- Changing ways of doing business
- Locus standi of value drivers is a challenge
- Process in order and local “look and feel” of website matters

Transfer pricing perspectives



Various E-Commerce Models

High frequency trading



- Complex algorithms run on servers located remotely from traders and the algorithm developers
- Server = PE?

- ALP trading activities?
- Reward developers and others in the supply chain?
- Value attributed to capital used to financing trading activity?

Cloud computing



- Server space is provided to a third party, who conducts business through the server
- Likely significant issue

- Taxable nexus?
- Location specific factors
- Server location is intrinsic to the cloud user's business model?

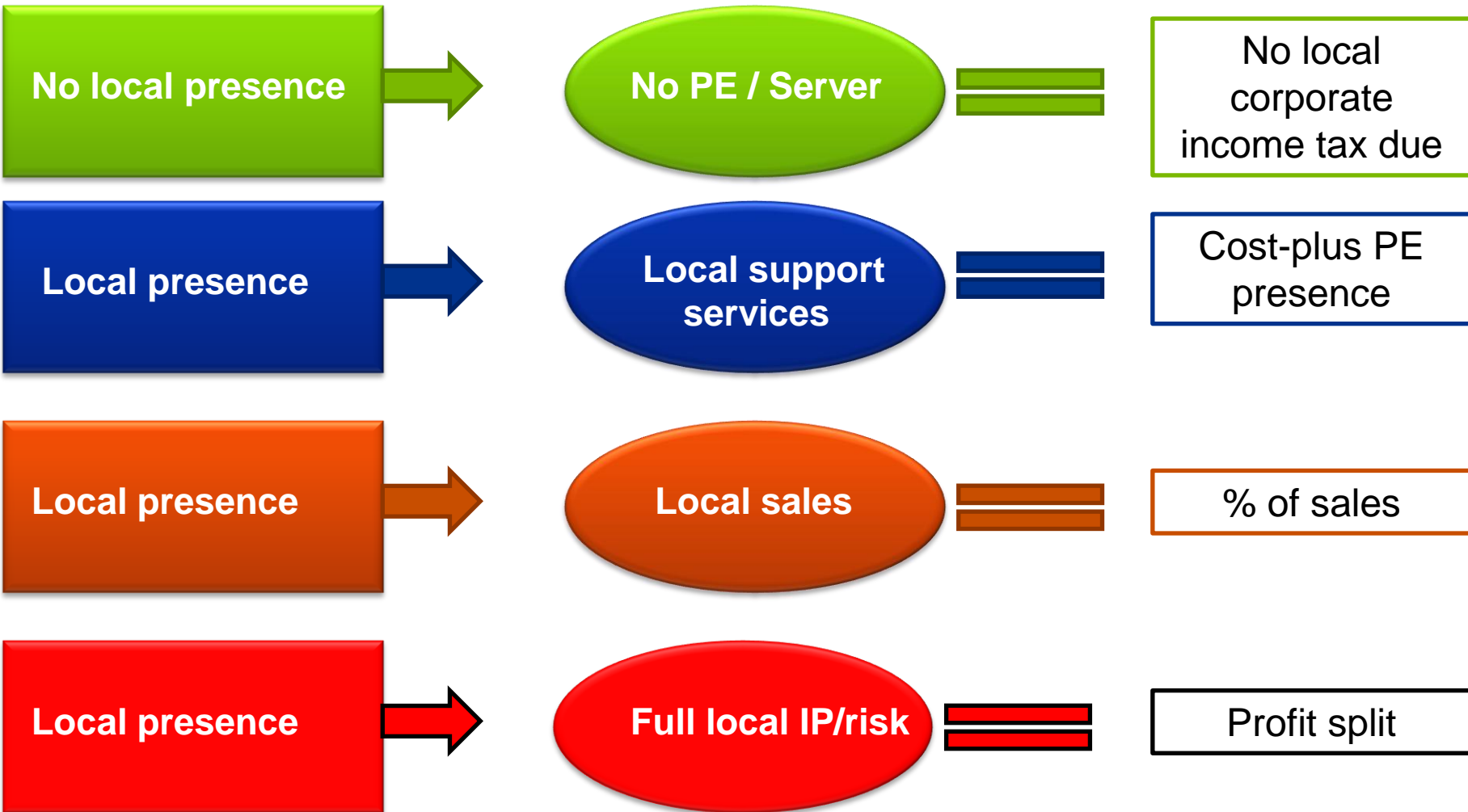
Advertising Models



- Online business rely on advertising income model
- Content provided free of charge, income from third parties via advertisement

- Models are driven by commercial requirements
- Practical considerations as to whether local market sales/activity is required

TP models: 4 potential business models scenario's



Issues in application of traditional transfer pricing

- Do the existing / traditional TP methods suffice and how to apply these in the digital economy
- Applying the separate transaction approach and finding comparables
- Comparability and Comparable Uncontrolled Price analyses
- Functional analyses

Where is the decision maker?

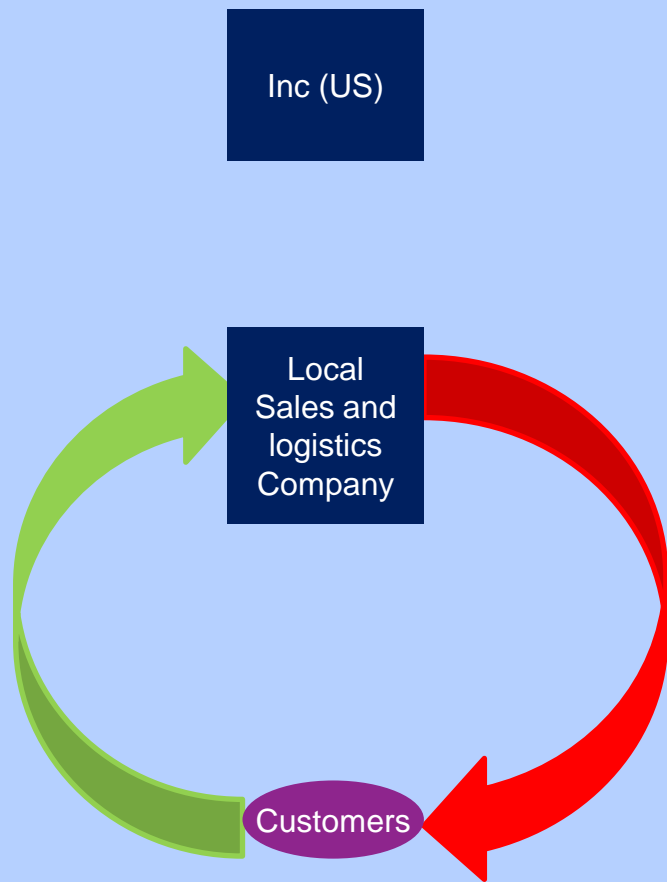


Issues in application of traditional transfer pricing

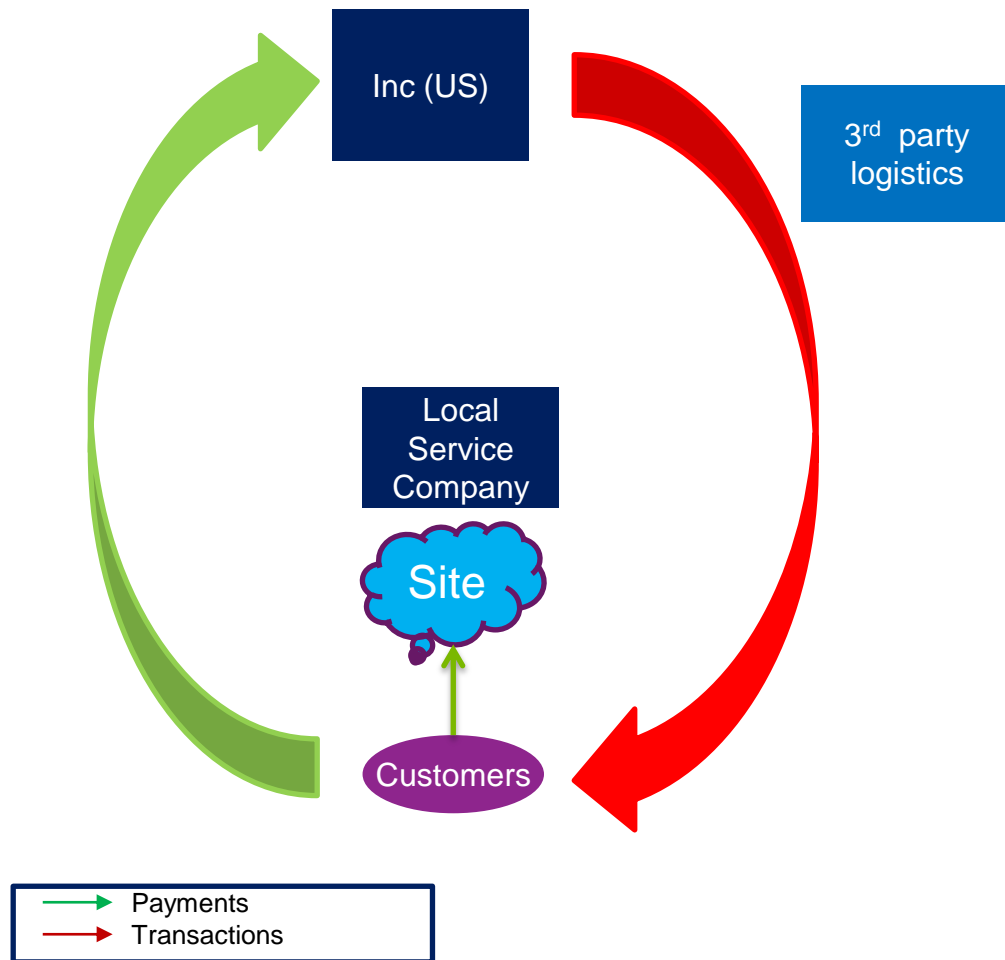
- **Identifying and valuing intangibles**
- **Location savings (in case of outsourcing) and their profit attribution**
- **Global trading: track locations of functions, risks and (in)tangible assets in a virtual world is a challenge**
- **In E-Commerce focus on:**
 - **people/functions**
 - **versus**
 - **(in)tangible assets (e.g servers and local market)**

Case: Potential E-Commerce Operating Structure for Europe

I. Current Operating Structure for Europe



II. Future E-Commerce Operating Structure for Europe



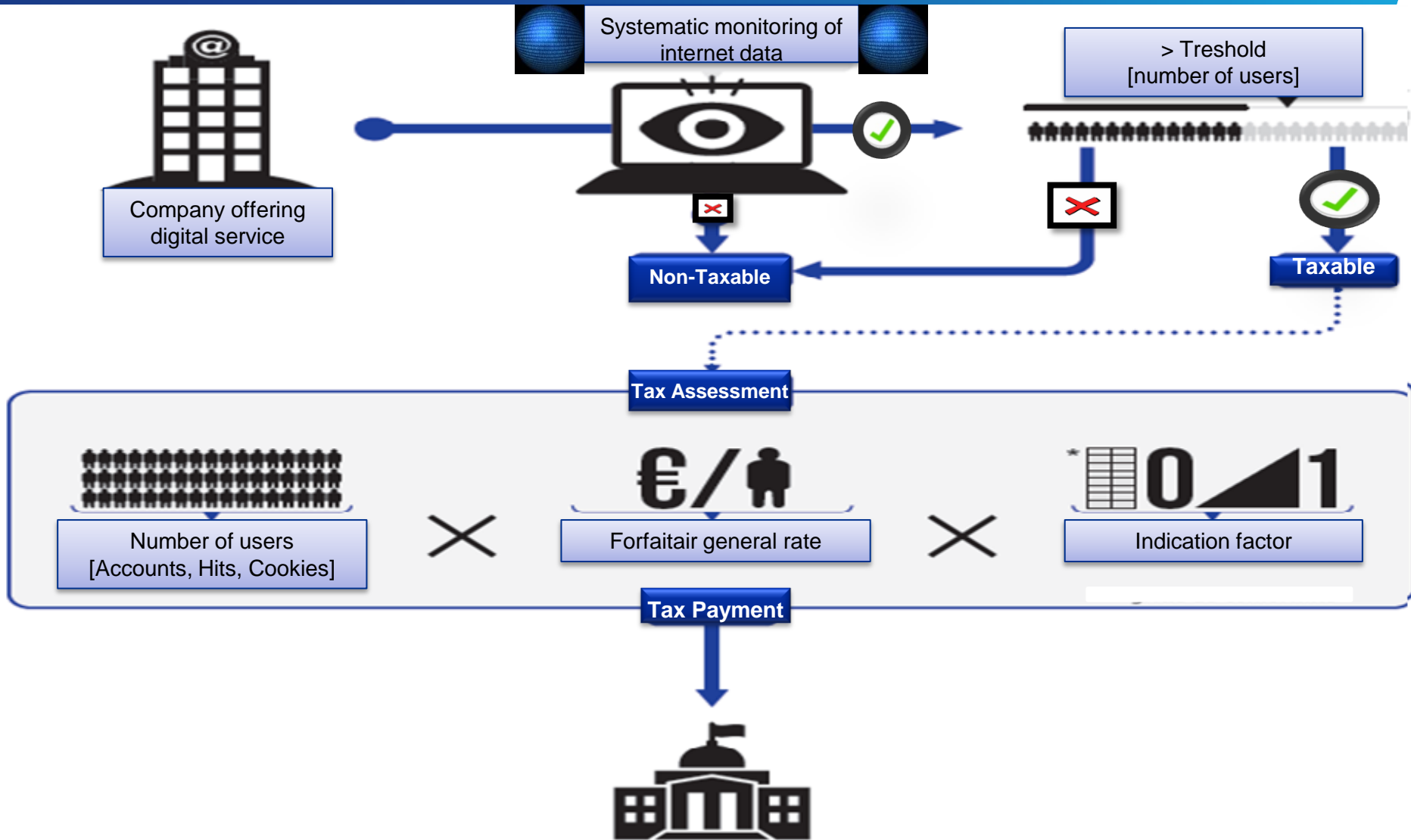
Permanent Establishment / Server PE perspective

- Permanent establishment is a fixed place of business through which the business of an enterprise is wholly or partly carried on:
 - Place of business: physical presence
 - At disposal of the company: owned, leased
 - Fixed: actually being moved?
 - Through which
- No PE is deemed to exist if activities are restricted to preparatory or auxiliary activities
- Smart server may constitute PE if it sells -> advertises, offers, sells, collects and delivers

PE interest by tax authorities

- US IT Multinational Entity (MNE) visited by ‘army’ of French tax inspectors and police officers
- Resulted in the presentation of an 1 Billion French tax bill
- Not the only IT MNE to face such allegations in France
- Milestone court cases such as:
 - Zimmer in France
 - Dell in Norway
 - Dell in Spain
 - Roche Vitamins in Spain
- have increased other countries’ tax authorities’ appetite to raise PE challenges

Colin-Collin Model - proposed tax measure on the collection and use of Data



**OECD and BEPS
EU Proces and
Italian perspective**



OECD and BEPS and EU Proces

- First meeting of the OECD Task Force in October 2013:
 - Analysis of business models and identification of special features of digital economy players
 - Effects of these features on BEPS strategies
 - Actions to tackle BEPS in the digital economy
 - Broader, systemic issues raised by the digital economy and options to address them
- Second meeting in February 2014
- Discussion Draft out for comments on March 24, 2014
- Public Consultation by April 23, 2014
- OECD Report to be finalized by September 2014?
- The European Commission has set up a special working group to devise a new taxation framework appropriate for digital economy - Pressure from France (and Italy) to impose new digital tax – and the current focus is on VAT

Article 1 Law no 147 of 27 December 2013

Introduced three provisions regulating VAT, TP and traceability of payments for on-line advertising services

VAT - Paragraph 33

➤ Italian companies shall purchase:

- advertising services and online sponsored links only from Italian registered companies;
- Internet ads and sponsored links appearing on the results pages of the search engines viewable on the Italian territory (i.e. search advertising services), only from Italian registered publishers, advertising agencies, search engines or other advertising companies

After postponement of entry into force of this rule until July 1st 2014, it has been repealed by Decree Law no 16 of 6 March 2014, in view of a coordination with EU regulations

VAT rule



Potential breach of EU principles:

- ✓ Freedom of establishment
- ✓ Freedom to provide services



Risk of incurring in **infringement procedures and consequent penalties** from EU institutions

- Directive 2006/112/EC and Regulation (EU) No 282/2011 on the common system of value added tax
- Directive 2000/31/CE on electronic commerce
- Directive 2006/123/EC on services in the internal market

Article 1 Law no 147 of 27 December 2013

Transfer pricing - Paragraph 177

Companies which carry out an activity aimed at the collection of on-line advertising and auxiliary services, for the determination of business income attributable to intercompany transactions, are required to use profit indexes other than those applicable to costs incurred for the performance of their business

- ! *Companies can use the profit indicators based on the costs incurred only if authorized by the Tax Authority within the International Standard Ruling (APA) procedure*

Traceability of payments - Paragraph 178

Payments for the purchase of online advertising services must be made exclusively by bank or post transfer reporting the identification data of the beneficiary or by other means of payment that are traceable and able to convey the VAT number of the beneficiary



Key take aways

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Key take aways

- **Specific corporate tax and VAT implications in Italy**
- **Digital Economy/E-Commerce is integrated in conventional businesses**
- **One digital business model for all does not exist**
- **Potential permanent establishment risk for corporate tax**
- **Digital economy is now on the agenda of the OECD and EU**
- **EU Digital Economy Group: next tax meeting on March 13/14, 2014**
- **OECD response expected on March 24, 2014**
- **OECD to maintain traditional transfer pricing methods?**



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**Thank you for
your time!**

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