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electronic marketplaces for international business

TAXES AND DUTIES

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Thank
YOU

Direct company income taxes

Companies are liable for tax on the profits of the business. A number of countries tax companies depending on where they are legally domiciled.

Others, in contrast, charge tax where the company is permanently located. As with individuals, the Government will seek to tax the company on the profits it obtains, irrespective of the fact that they may be international in origin. It may of course be the case that more than one country claims that the business is permanently resident in its territory, a conflict that leads to the phenomenon of "double taxation".

These situations are resolved by recourse to the treaties entered into by the countries involved. The legal framework summarised in this expression has particular implications in relation to electronic commerce. Whilst with traditional commerce a company inevitably has some physical referent (offices, employees, warehouses, means of delivery, etc.) which can constitute such "permanent establishment", this is not usually so on the Internet, where neither the web pages nor the servers can be described as such (although it is true that the issue is certainly complex as regards the latter; the OECD has even set up a study committee to look for a satisfactory solution).

Governments, which until recently have not participated directly in electronic commerce, are now trying to formulate legal policies which would enable them to tax these electronic commercial activities, where it is difficult to measure the actual volume of transactions and to establish an appropriate tax rate.

Value Added Tax (VAT)

There are major considerations to bear in mind in this context, above all in relation to Value Added Tax (VAT). This tax is charged in the EU, and all OECD Member States (except three) have also introduced it. The following analysis is made from the perspective of the EU, where application of the tax is much more sophisticated.

The application of VAT is addressed in Directive 2002/38, which provides for equality between electronic and conventional media. The normal VAT rate is applied to most content supplied by conventional means – music, software, videos, etc. There will be no reason to differentiate in the case of electronic commerce, which according to the Directive is subject to the same VAT rate depending on the Member State, as we shall now see.

Current VAT legislation allows lower rates (including a zero rate) to be charged for printed matter (books, newspapers, publications, etc.), although digital information services give rise to fundamentally different products. The Commission will shortly produce a proposal to review the reduced VAT rates in order to simplify and ensure more uniform application of VAT.

For the purposes of applying this tax, we must consider whether:

- The transaction concerns goods or services
- The transaction is business-to-business (B2B), or business-to-consumer (B2C).
- The consumer is established inside or outside the EU.

Sale of goods

B2C transactions

If both parties to the transaction are established in the same EU country, the VAT rate applicable will be that of that country.

Where the parties are established in different EU countries, a complex system of tax thresholds will apply, varying in the different Member States from 35,000 to 100,000 euros. In this case, the VAT applicable is that payable in the country in which the business is established, if annual sales to other Member States are not above the relevant threshold.

Otherwise, the VAT applicable is that chargeable in the consumer's home country (where it is sometimes compulsory to be registered in certain tax registers).

B2B transactions

If both parties are established in the same Member State, the rate of VAT applicable is, obviously, that established in the country in question. If the businesses are established in different countries, the VAT payable is that set in the country from which the goods are supplied.

Supply of services

In the provision of services, the VAT of the country that supplies them is applicable, irrespective of the country to which those services are destined. There are, nevertheless, a number of exceptions depending on the type of service and on whether their recipient is a business or an individual customer.

The most relevant exceptions in the context of electronic commerce are:

- On the provision of cultural, scientific, sporting or educational services, VAT will be paid according to the rates of the country in which those services are provided.
- VAT on services relating to real property is paid according to the country in which the property is located.
- Lastly, consulting, engineering, telecommunications, legal advice, accounting, data processing and financial or insurance services shall have provisions similar to those already described for products.

There is a marked lack of harmonisation of the rates applicable in the various EU Member States, which vary between 15% and 25%. It is also important to point out that certain individuals (charities, government organisations, certain social associations, etc.) are not subject to this indirect taxation, or enjoy specific provisions.

On occasions, the business may recover the amount paid. A fundamental principle of the European VAT system under the Sixth VAT Directive (77/388) is that each business in the supply chain passes on the VAT on the service it provides, and deducts it from the service it receives. Since special circumstances are envisaged for businesses not physically located in the EU, this issue does not arise.

However, if the business has to pay VAT on goods or services acquired for its business activities in the EU, the Thirteenth Directive (86/560) on arrangements for the refund of value added tax to taxable persons not established in Community territory will apply, with the effect of ensuring that the tax will be recovered by the Member State affected.