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TAXING THE FUTURE: DIGITAL STATELESS INCOME, BUSINESS ORGANISATION, AND THE SEARCH FOR A NEW REGULATORY PARADIGM

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At a time when "stateless income" is the main tax imperative, this article analyses the challenges of internationalising taxation of multinational enterprises in the digital economy and traversing the normative solutions provided so far (and still to be provided) by both coordinated and unilateral rules and policies. In such a way, this article is therefore firmly entrenched at an important intersection of comparative and business law. Considering that the main problem for tax authorities might be that they have remained national—and landlocked—whereas multinational enterprises operate globally—and virtually, this article also brings into the analysis the connected issues of free trade, globalization, and State sovereignty. The article demonstrates the necessity for international and multilateral solutions such as the Organization for Economic Cooperation and Development's Base Erosion and Profit Shifting project's "Two-Pillar" solution and explains how this solution can be supplemented by other multilateral reforms.

I. Introduction

This article explores the complex challenges of taxing the digital economy (including the rise in stateless income that can be attributed to the digital economy) considering that the international tax system vis-à-vis multinational enterprises ("MNEs") was developed (over several decades) long before the emergence of the digital economy. In addition, although these challenges have "surged" in recent years (since the growth in digital trade has been matched by taxation concerns), the international tax system has not yet evolved as expected.[1] Furthermore, in view of the fact that the digital economy is also no longer a "new economy", since it can be traced back to

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[1] See World Economic Forum, *Digital Trade in Services and Taxation* (White Paper, October 2021) <http://www3.weforum.org/docs/WEF_Digital_Trade_in_Services_and_Taxation_2021.pdf> at 5–9; see also Wolfgang Schön, "Is There Finally an International Tax System?" (2021) 13(3) World Tax Journal 357.

around 1995,[2] this article also examines why the evolving international tax system for MNEs still struggles to cope with the challenges of regulating the digital economy and why the Group of 20 ("G20") and the Organization for Economic Cooperation and Development ("OECD") found it necessary to jointly launch their Base Erosion and Profit Shifting ("BEPS") project, which culminated in their "Two-Pillar" solution, which was recently finalised and agreed to by 136 countries on 8 October 2021.[3]

Prior to the Two-Pillar solution (and maybe after), several countries had been implementing various unilateral or bilateral mechanisms to address the challenges of taxation in the digital economy (such as relying on bilateral tax treaties, which are arguably no longer fit for purpose and launching various Digital Service Taxes ("DSTs")).[4] Through consideration of such measures and a particular focus also on the regulation of "stateless income", which has been described as "the main tax imperative of the day", this article reconsiders the challenges of internationalising the rules on the digital economy (both "old" challenges and "new" challenges) and discusses the efficacy of the various measures and proposals that have been launched to tackle these challenges (including the G20/OECD projects mentioned above).[5] Specifically, the article presents a view as to whether the BEPS projects' recently endorsed Two-Pillar solution is heading in the right direction vis-à-vis the challenges of regulating the digital economy—and not crumbling before our eyes—and suggests additional methods to supplement the BEPS project's Two-Pillar solution.[6]

Additionally, since the responses to these challenges demonstrate that taxation is both a multilevel governance problem and a rightful exhibition of a State's sovereignty in regulating tax matters, the question is also considered of whether we are on track to solve the problems, or whether there is damage to the World Trade Organization ("WTO")-led system of free trade for only partial gains (if any).[7] In this regard it is noted that the BEPS projects' Two-Pillar solution agreed to on

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2 See Martin Peitz & Joel Waldfogel, *The Oxford Handbook of the Digital Economy* (New York: Oxford University Press, 2012).

3 See OECD, "Statement on a Two-Pillar Solution to Address the Tax Challenges Arising From the Digitalisation of the Economy" (8 October 2021) <https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.pdf>; see also "International community strikes a ground-breaking tax deal for the digital age", *OECD*, 8 October 2021 <https://www.oecd.org/tax/international-community-strikes-a-ground-breaking-tax-deal-for-the-digital-age.htm>**;** Jeffrey M Kadet, "BEPS – A Primer on Where it Came from and Where It's Going" (2016) 150 Tax Notes 793; Ulrich Schreiber, "Remarks on the Future Prospects of the OECD/G20 Programme of Work – Profit Allocation (Pillar One) and Minimum Taxation (Pillar Two)" (2020) 74(6) Bulletin for International Taxation 338; Reuven S Avi-Yonah, "The International Tax Regime at 100: Reflections on the OECD's BEPS Project" (2021) 75(11/12) Bulletin for International Taxation.

4 See WEF, *Digital Trade*, *supra* note 1 at 13–14; see also Brian J Arnold, "The Interpretation of Tax Treaties: Looking to the Future" (2021) 75(11/12) Bulletin for International Taxation 665; Philip Baker, "Multilateral Tax Treaties" (2021) 75(11/12) Bulletin for International Taxation; Stef van Weeghel, "Have the OECD Model and the UN Model Served Their Purpose? Are They Still Fit for Purpose?" (2021) 75(11/12) Bulletin for International Taxation 588.

5 See Itai Grinberg & Joost Pauwelyn, "The Emergence of a New International Tax Regime: The OECD's Package on Base Erosion and Profit Shifting (BEPS)", 19(24) *ASIL Insights* (28 October 2015).

6 See Graeme S Cooper, "Building on the Rubble of Pillar One" (2021) 75(11/12) Bulletin for International Taxation.

7 See Thomas Rixen & Brigitte Unger, "Taxation: A Regulatory Multilevel Governance Perspective" [2021] *Regulation & Governance*; see also Antony Ting & Sidney J Gray, "The Rise of the Digital

8 October 2021 includes the commitment "*to remove all Digital Services Taxes and […] not to introduce such measures in the future*".[8] In this regard the removal of DSTs may ease trade tensions, given for example the US' Section 301 investigations into various countries' DST measures.[9]

Firstly, in part II this article explains why internationalising taxation rules in the digital economy is a systemic problem that keeps on growing and which the BEPS project (and the Two-Pillar solution) may struggle to solve. In this part, there is also identification and consideration of both the so-called "old" and the "new" challenges posed when internationalising the rules on the digital economy. The old challenges are the preponderance of intangible assets, the challenges in regulating big data ("Big Data"), the increasing adoption of multi-sided business models and the difficulty of determining the jurisdiction in which value creation occurs. The new challenges relate to the even newer technologies still emerging in the digital space (like virtual currencies and other crypto-assets). In part III of this article, there is consideration of the solutions and the proposals launched as regards the problems of internationalising taxation in the digital economy. First, the coordinated solutions and proposals provided *eg*, by the United Nations ("UN") and the OECD (including the BEPS project and its Two-Pillar solution) are considered. Second, some of the unilateral solutions and proposals launched are discussed, including looking at the various DSTs already introduced (also including the Diverted Profits Tax ("DPT"), and solutions to tax Significant Digital Presence ("SDP")). Thirdly, suggestions of other new taxation solutions are provided, such as the concept of a Digital Permanent Establishment ("PE"), methods to tax Big Data, equalization taxes and the taxing of sales instead of profits, taxation based on "value creation" rather than "value consumption" and taxing the shareholders of MNEs that predominantly operate digitally. In part IV there is an analysis of the regulation of trade in the digital economy, where this article argues both that "too much" unilateral interference with the digital economy should be avoided, and also that any attempt to ringfence the digital economy from the remainder of the economy is bound to fail. In part V, this article revisits the lingering concept of State sovereignty in the context of the disruption caused by regulating the digital economy as regards taxation and the solutions and proposals addressed in part III of this article. Part VI concludes.

II. Taxation in the Digital Economy: A Regulatory Challenge That Keeps On Growing

In this part, stateless income is defined and its link with the regulatory challenges in the digital economy is demonstrated.[10] Thereafter the regulatory challenges, which

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Economy: Rethinking the Taxation of Multinational Enterprises" (2019) 50(9) Journal of International Business Studies 1656.

8 See OECD, "Statement on a Two-Pillar Solution", *supra* note 3 at 3 [emphasis added].

9 See Jinyan Li, "The Legal Challenges of Creating a Global Tax Regime with the OECD Pillar One Blueprint" (2021) 75(2) Bulletin for International Taxation 84 at 92.

10 See Edward D Kleinbard, "The Lessons of Stateless Income" (2011) 65 Tax Law Review 99; Edward D Kleinbard, "Stateless Income's Challenge to Tax Policy" (2011) 132 Tax Notes 1021; Edward D Kleinbard, "Stateless Income's Challenge to Tax Policy, Part 2" (2012) 136 Tax Notes 1431.

the digital economy has brought (and continues to bring) are identified. This part shows that each of the regulatory challenges provides a link (to a greater or lesser extent) with the regulation of stateless income and that the digital economy has greatly increased the complexity of responding to the regulatory challenges. For instance, in many situations "real operations" have already been replaced by "virtual intra-group transactions" and the source of the factors of production through which MNE income is derived do not even physically exist.[11]

There is also a clear consensus that the existing international tax laws exacerbate the governance problems. For instance, Petruzzi and Buriak state that "outdated tax regulations and principles could result in situations of non-taxation or tax avoidance and, ultimately, the loss of revenue on the part of the treasuries of countries".[12] Consequently, it is said that one of the most discussed issues among all stakeholders regarding taxation of MNEs is "how to tax the digitalised part of a business, especially when this creates substantive value without any physical presence in a state".[13] It was largely due to these regulatory challenges that the G20 and OECD jointly launched the BEPS project in 2013, the G20 specifically established a "Digital Economy Task Force" in 2017, and the BEPS project finalised its Two-Pillar solution on 8 October 2021 (which was agreed to by 136 countries).[14]

A. *The Precipitation of Stateless Income*

Stateless income concerns are not a particular response to digital tax challenges. Instead, stateless income concerns focus on tax avoidance by profit shifting to lower tax jurisdictions. Indeed, stateless income is defined as income generated in a jurisdiction that is "neither the source of the factors of production through which the income was derived nor the domicile" of the parent company of the MNE.[15] Stateless income is income derived for tax purposes by a multinational group from business activities in a country other than the group's ultimate parent company's domicile but taxed only in a jurisdiction that is neither the source of the income's factors of production nor the group's parent company's domicile.[16] In other words, profits are not sufficiently allocated to jurisdictions where MNE's operate, *ie*, there is no physical presence because of current PE rules. Google Inc.'s "Double Irish

[11] See Fleming Jr J Clifton, Robert J Peroni & Stephen E Shay, "Getting Serious about Cross-Border Earnings Stripping: Establishing an Analytical Framework" (2015) 93(3) North Carolina Law Review 673; Ting & Gray, "The Rise of the Digital Economy", *supra* note 7 at 1657.

[12] Raffaele Petruzzi & Svitlana Buriak, "Addressing the Tax Challenges of the Digitalization of the Economy – A Possible Answer in the Proper Application of the Transfer Pricing Rules?" (2018) 72(4a/Special Issue) Bulletin for International Taxation 1.

[13] *Ibid*.

[14] See OECD, "Statement on a Two-Pillar Solution", *supra* note 3; see also OECD, "International community strikes a ground-breaking tax deal", *supra* note 3; Kadet, "BEPS – A Primer", *supra* note 3; Schreiber, "Remarks on the Future Prospects", *supra* note 3; Avi-Yonah, "The International Tax Regime at 100", *supra* note 3.

[15] See Edward D Kleinbard, "Stateless Income and Its Remedies" in Thomas Pogge & Krishen Mehta, eds, *Global Tax Fairness* (Oxford: Oxford University Press, 2016) at 129.

[16] See Kleinbard, "The Lessons of Stateless Income", *supra* note 10.

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Dutch Sandwich"[17] structure is one example of stateless income tax planning in operation. Nevertheless, a link with the regulation of taxation in the digital economy can be formulated, since digital business models provide further means for MNE managers "to locate profits in low-tax jurisdictions without affecting the locations of their real operations" (*ie*, to generate stateless income).[18]

The G20/OECD BEPS project was a first step to tackle these growing regulatory problems.[19] Although Action 1 of the BEPS project stated that "the digitalization and the resulting business models do not generate unique BEPS issues", it did however state that "some of the key features of [digitalization] exacerbate BEPS risks".[20] Further, the BEPS project continues to evolve in an attempt to catch up with the old and new challenges posed by the regulation of taxation in the digital economy (as can be seen with the Two-Pillar solution). In this regard, section II.B. identifies the old challenges posed by the regulation of taxation in the digital economy and section II.C. identifies some of the new challenges that the regulation of taxation in the digital economy poses (and will pose). The two sections also show that the BEPS project was inevitably always a few steps behind the MNEs in the digital economy. This is largely due to the information asymmetries between the MNE who knows and understands its business model (and how it internally allocates value) and the tax authorities who struggle to comprehend the business models they see from the outside (and are often bedazzled by the value propositions presented by the MNEs). This was in fact the purpose of BEPS Action 12, *ie*, to "require taxpayers to disclose their aggressive tax planning arrangements".[21]

B. *The "Old" Regulatory Challenges Posed by the Digital Economy*

The OECD described its four main areas of concern with the regulation of taxation in the digital economy when the BEPS project was launched; first, an unparalleled reliance on intangible assets; second, the growing use of Big Data; third, the increasing adoption of multi-sided business models; fourth, the difficulty of determining the jurisdiction in which value creation occurs.[22] Below there is an analysis of each challenge.

1. *Whose (intangible) asset is it anyway?*

The premise for taxation of intangible assets is simple. Specific classes of intangible assets (such as relating to Intellectual Property) are treated as property by many tax

17 See "Google shifted $23 billion to tax haven Bermuda in 2017: filing", *Reuters* (4 January 2019) <http://www.reuters.com/article/us-google-taxes-netherlands/google-shifted-23-billion-to-tax-haven-bermuda-in-2017-filing-idUSKCN1OX1G9>.

18 See Ting & Gray, "The Rise of the Digital Economy", *supra* note 7 at 1656.

19 In the OECD, *BEPS Project Explanatory Statement: 2015 Final Reports* (2016), it is stated that that the G20 Leaders endorsed the Action Plan on BEPS in September 2013.

20 See OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 – 2015 Final Report* (2015) at para 368.

21 See OECD, *Action Plan on Base Erosion and Profit Shifting* (2013) at 22–23.

22 *Ibid* at 10.

authorities and, consequently, the tax claim against MNEs is that "the owner of an intangible asset is subject to the same responsibilities as any other property owner", *eg*, such as being subject to taxation and other governmental powers.[23] The taxation challenge rests in identifying and capturing these intangible assets (from a taxation perspective), which are easily transferable and flow simultaneously and endlessly across borders. Moreover, in today's digital economy (practically all) MNEs develop intangible assets in their business models (and often at every stage of their business models), *eg*, in research and development, in the manufacturing process and marketing and distribution to their customers. Then, after the MNE has developed an intangible asset, it acquires full legal rights to protect and monetise its property (including the sale or transfer of the assets)—provided of course the assets are identifiable, *ie*, that there is "tangible evidence of the existence of an intangible asset".[24]

However, the intrinsic characteristic of intangible assets means they are highly mobile and have become a boon for MNEs to engage in tax avoidance structures. Whilst the primary purposes of MNEs in developing intangible asset mobility might be to increase operational efficiency and to "future-proof" their business, the consequence from a taxation perspective has presented very specific regulatory challenges. In particular, the consequent ease of transferring intangible assets between jurisdictions and the reduced transaction costs involved in doing so means that the tax collection authorities invariably miss out on capturing a significant amount of tax revenue.

2. *Big data: the regulatory challenges of taxing the new "oil"*

Big Data has a big value and, "from a tax perspective, ignoring the value of data is inconsistent with the data economy paradigm", where "data is the new oil".[25] Nevertheless, although almost five years have passed since it was declared that, "the world's most valuable resource is no longer oil, but data", companies are still "legally avoiding taxes on this resource, both during its collection and on the profits it creates".[26]

This is because the business models of many MNEs are increasingly data-centric, but the data the MNE extracts, processes, and refines is usually not adequately valued in the MNEs accounts. The regulatory challenge for tax authorities is that they consequently struggle to assess the data "owned" by the respective MNE, which also becomes an inherently political question since it is largely impossible to determine who holds taxation rights when the data crosses borders and relates to

[23] Robert F Reilly & Robert P Schweihs, *Valuing Intangible Assets* (United States of America: McGraw-Hill, 1998) at 5; see also Matthias Dischinger & Nadine Riedel, "Corporate taxes and the location of intangible assets within multinational firms" (2011) 95(7/8) Journal of Public Economics 691.

[24] Reilly & Schweihs, *Valuing Intangible Assets*, *ibid* at 6.

[25] See Dirk A Zetzsche & Linn Anker-Sørensen, "Taxing Data-Driven Business: Towards Data Point Pricing" (2021) 13(2) World Tax Journal 217 at 217.

[26] See "Regulating the Internet Giants: The world's most valuable resource is no longer oil, but data", The Economist (6 May 2017) <http://www.economist.com/leaders/2017/05/06/the-worlds-most-valuable-resource-is-no-longer-oil-but-data>; Ziva Rubinstein, "Taxing Big Data: A Proposal to Benefit Society for the Use of Private Information" (2021) 31(4) Fordham Intellectual Property Media & Entertainment Law Journal 1199.

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multiple jurisdictions (see also part V below). Furthermore, the situation is further complicated since the entire data "pipeline"—from data extraction to data analysis and data enhancement, etc.—is considered to have a differing value at each stage, *ie*, that each stage of the data refining process might be assigned a share of the MNEs profits (which could then be taxed).[27]

3. *The camouflage of multi-sided business models*

Multi-sided business models represent a shift from more traditional business models where transactions are primarily undertaken offline to the development of multi-sided platforms that facilitate "networking and intermediation of complementary and interdependent categories of users, implying positive network effects" where transactions are primarily undertaken on the internet.[28] Examples of these are the likes of Uber,[29] YouTube,[30] and Airbnb,[31] who have leveraged the "declining costs of acquiring information and intermediation" and deployed "many resources to implement the platform technologically, attract users rapidly and massively and organise sides by creating several complementary user groups".[32]

The regulatory challenge from a taxation point of view arises because identifying and capturing value is extremely complex since these multi-sided business models pursue "a technological platform where each side has a specific process of value creation, value proposition and value capture".[33]

In other words, the value transactions made on the platform are purposely spread between one or more MNEs and the platform's various user groups. Additionally, the structure of the value proposition and value capture may also include externalities, such as advertising revenue or free products, and also constantly varies according to market conditions.[34] A case has also been built that the algorithms generated in these applications need bespoke regulation.[35]

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[27] See Svitlana Buriak & Mario Riedl, "Global Transfer Pricing Conference 2020: Transfer Pricing Developments around the World" (2020) 27(4) International Transfer Pricing Journal 239 at 245.

[28] See Guy Parmentier & Romain Gandia, "Redesigning the Business Model: from One-Sided to Multi-Sided" (2017) 38(2) Journal of Business Strategy 52; Sylvia de Jong, Willem Neuvel & Ágata Uceda, "Dealing with Data in a Digital Economy" (2018) 25(2) International Transfer Pricing Journal 55 at 61.

[29] See Ryan Calo & Alex Rosenblat, "The Taking Economy: Uber, Information, and Power" (2017) 117(6) Columbia Law Review 1623.

[30] See McKinsey Global Institute, "Digital Globalization: The New Era of Global Flows" (March 2016) <http://www.mckinsey.com/~/media/McKinsey/Business%20Functions/McKinsey%20Digital/Our%20Insights/Digital%20globalization%20The%20new%20era%20of%20global%20flows/MGI-Digital-globalization-Full-report.ashx>.

[31] See Josh Bivens, "The economic costs and benefits of Airbnb" (30 January 2019) <http://www.epi.org/publication/the-economic-costs-and-benefits-of-airbnb-no-reason-for-local-policymakers-to-let-airbnb-bypass-tax-or-regulatory-obligations/>.

[32] See Parmentier & Gandia, "Redesigning the Business Model: from One-Sided to Multi-Sided", *supra* note 28 at 52.

[33] *Ibid* at 55.

[34] See Elena Vėgėlytė, "Deconstructing User Participation: Why in the Digital Era Advertising Income Is Different from Other Business Income" (2020) 27(3) International Transfer Pricing Journal 180 at 186.

[35] See Florian Eyert, Florian Irgmaier & Lena Ulbricht, "Extending the framework of algorithmic regulation. The Uber case" (2022) 16(1) Regulation & Governance 23.

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4. *Internationalising value-creation in the digital economy*

The difficulty of determining the jurisdiction in which value creation occurs is a particular regulatory challenge to tax authorities in the digital economy because MNEs frequently have a presence in several jurisdictions (as well as in cyberspace). In each of the above subsections, II.B.1-3 it was shown that MNEs in the digital economy have been presented with new opportunities and methods to legally avoid taxation.

First, as regards intangible assets, it was shown that even if the values attributable to the assets can be determined, the MNE can quickly and efficiently transfer the ownership of its assets across jurisdictions. Second, as regards Big Data, it could be seen that the MNE is generally free to attribute the value to the data that it determines on its own accord (including choosing any jurisdiction where value is created). Third, as regards the multi-sided business models, it was shown that the platforms developed are designed to spread the value proposition and value capture between the MNE(s) and user group(s) involved (which are also very likely to be cross-border).

The ability of the tax authorities to capture value is also limited by the arguably outdated and insufficient regulatory means at their disposal, prevalent in traditional corporate taxation models, *eg*, the traditional approach to taxation based on physical locations has previously prevented tax authorities capturing taxation which does not rely on physical products.[36] Furthermore, the absence of other provisions may mean that tax authorities are more suited to regulating traditional business models rather than the business models of the digital economy (*eg*, the recognition and regulation of Decentralized Autonomous Organizations ("DAOs")).[37] Part III provides an analysis of the solutions and proposals to tackle each of these regulatory challenges.

C. *The "New" Regulatory Challenges Posed by the Digital Economy*

Tax authorities have not been able to adapt to technology with ease when it comes to the regulation of taxation of the digital enterprise. Moreover, the technology sector has been evolving at a rapid pace, which means that now the authorities find it difficult to even consider the regulatory challenges all together (and at once). This further gives rise to new regulatory challenges that have been coming up in recent times, which proliferation has been boosted by the COVID-19 pandemic.[38]

A significant regulatory challenge presented by the digital economy as regards taxation is because further new challenges continue to emerge, *ie*, as new technologies develop, so do new business models (which constantly creates new regulatory problems for the tax authorities). For instance, the total market capitalization for virtual currencies is reported to have reached USD 2 trillion, which left the OECD

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[36] See, *eg*, Aldo Forgione, "Clicks and Mortar: Taxing Multinational Business Profits in the Digital Age" (2003) 26 Seattle University Law Review 719.

[37] See, *eg*, Noopur Trivedi & Jitesh Golani, "Tax Policy for Stablecoins and DAOs: A Peek Into the Future" (2021) 103(3) Tax Notes International 311.

[38] See WEF, *Digital Trade*, *supra* note 1 at 6–8.

rushing to develop a new tax reporting framework for crypto-assets.[39] In the 2020 OECD report on "Taxing Virtual Currencies", the following specific challenges were identified: How should the income created by crypto-assets be treated for tax purposes? Can crypto-assets be considered as property and be subject to property taxes? How should crypto-assets be valued? How should VAT systems treat the creation, acquiring, holding and transfer of crypto-assets? Are there risks of tax evasion and other financial crimes posed by crypto-assets? Do crypto-assets pose problems for tax transparency, compliance and enforcement?[40] The OECD has now released a public consultation document on "Crypto-Asset Reporting Framework and Amendments to the Common Reporting Standard" for 22 March 2022 to 29 April 2022.

Additionally, other crypto-assets seem to be emerging regularly, which may or may not be included in the above concerns, *eg*, Non-fungible Tokens ("NFTs"), which have also perplexed tax authorities as regards how to regulate taxation.[41] There is also a heated discussion in tax circles of how to tax data hosted in the "cloud".[42] Further, there are even newer technologies with possibly bespoke regulatory challenges relating to taxation, *eg*, "blockchain forks".[43]

Although, as regards blockchain technologies, there is also an argument that such technologies will also help administer and process compliance with taxation regulations.[44]

III. (Partial) Solutions to the Regulatory Challenges

Although in principle, MNEs are subject to local taxation in every jurisdiction where they have operations, since local taxation regulations differ between

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[39] See Andrew B Whitford & Derrick Anderson, "Governance landscapes for emerging technologies: The case of cryptocurrencies" (2020) 15(4) Regulation & Governance 1053; see also OECD, *OECD Secretary-General Tax Report to G20 Finance Ministers and Central Bank Governors* (February 2021) <http://www.oecd.org/tax/oecd-secretary-general-tax-report-g20-finance-ministers-february-2021.pdf>; OECD, "Crypto-Asset Reporting Framework and Amendments to the Common Reporting Standard" (22 March 2022) <https://www.oecd.org/tax/exchange-of-tax-information/public-consultation-document-crypto-asset-reporting-framework-and-amendments-to-the-common-reporting-standard.pdf>.

[40] See OECD, *Taxing Virtual Currencies: An Overview of Tax Treatments and Emerging Tax Policy Issues* (October 2020) <http://www.oecd.org/tax/tax-policy/taxing-virtual-currencies-an-overview-of-tax-treatments-and-emerging-tax-policy-issues.pdf> at 8–9.

[41] See Lisa M Blum & Benjamin P Foster, "The taxation of nonfungible token transactions: Certified public accountant", 91(6) *The CPA Journal* (13 August 2021) at 10–13.

[42] See Piyush Gupta, "'Cloud' – A Technological Odyssey" (2014) 20(5) Asia-Pacific Tax Bulletin 308; "EY Roundtable: Taxing the Cloud" (2014) 25(4) Journal of International Taxation 38 at 38–49; Orly Mazur, "Taxing the Cloud" (2015) 103(1) California Law Review 1; William L Fletcher Jr, "Netflix and Quill: Using Access and Consumption to Create a Plan for Taxing the Cloud" (2017) 58(3) William & Mary Law Review 1029.

[43] Mattia Landoni & Gina C Pieters, "Taxing Blockchain Forks" (2020) 3(2) Stanford Journal of Blockchain Law and Policy 197.

[44] See Akash E Nemade *et al*, "Blockchain Technology used in Taxation" (Paper delivered at the 2019 International Conference on Vision Towards Emerging Trends in Communication and Networking (ViTECoN), Vellore, India, 30 March 2019) 1.

jurisdictions, the international taxation of MNEs has been based on the MNE's "trading setup, and the tax regimes and international tax treaties it is exposed to".[45] Additionally, since jurisdictions have competed to attract MNEs, they do not have coordinated taxation policies, such as anti-avoidance legislation to ensure that they do not lose revenue (*eg*, transfer pricing regulations, thin capitalization regulations and controlled foreign company legislation).[46] This has been the case since the first international tax treaties "originated in the late 19th and early 20th century" via the "friendship, commerce, and navigation" treaties.[47] Furthermore, the taxation of MNEs had become so disjointed, it had even been said that the decision of an MNE to pay taxes had become effectively voluntary.[48] The BEPS project and other tax reforms, *eg*, US tax reform have already removed some opportunities for tax avoidance.

It was against this background that the UN in the late 1960s, and then the OECD in 1976 first began to present recommendations for the regulation of MNEs.[49] However, 'the fundamental problem relating to the taxation of MNEs remained, which is "that taxpayers have become global whereas tax authorities have not".[50] Indeed, tax authorities have remained national and still operate via bilateral treaties. It is noted also that, whilst the WTO governs international trade and the International Monetary Fund ("IMF") governs international finance, "no such institutional counterpart exists in the realm of international production" (*ie,* to control MNEs).[51] It is therefore said that MNEs are regulated instead via Bilateral Investment Treaties and other bilateral measures.[52] The G20/OECD BEPS project and the BEPS projects' Two-Pillar approach, therefore, promise an overdue solution.

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[45] Prafula Fernandez & Jeff Pope, "International Taxation of Multinational Enterprises (MNEs)" (2002) 12(12) Revenue Law Journal 106 at 107.

[46] *Ibid* at 106-107.

[47] Lara Friedlander & Scott Wilkie, "Policy Forum: The History of Tax Treaty Provisions – And Why It Is Important to Know About It" (2006) 54(4) Canadian Tax Journal 907 at 909.

[48] See Fernandez & Pope, "International Taxation of Multinational Enterprises (MNEs)", *supra* note 45 at 110.

[49] See Kenneth A Reinert, Oda T Reinert & Gelaye Debebe, "The new OECD Guidelines for Multinational Enterprises: better but not enough" (2016) 26(6) Development in Practice 816 at 817.

[50] See Fernandez & Pope, "International Taxation of Multinational Enterprises (MNEs)", *supra* note 45 at 109.

[51] See Reinert, Reinert & Debebe, "The new OECD Guidelines for Multinational Enterprises", *supra* note 49 at 817–818.

[52] See Arnold, "The Interpretation of Tax Treaties", *supra* note 4; Baker, "Multilateral Tax Treaties", *supra* note 4; see also Julien Chaisse, *International Investment Law and Taxation: From Coexistence to Cooperation*, Think Piece for E15 Task Force on Investment Policy (Geneva: International Centre for Trade and Sustainable Development & World Economic Forum), <https://e15initiative.org/publications/international-investment-law-taxation-coexistence-cooperation/>; Julien Chaisse & Jamieson Kirkwood, "Foreign Investors vs. National Tax Measures: Assessing the Role of International Investment Agreements" in Irma Johanna Mosquera Valderrama, Dries Lesage & Wouter Lips, eds, *Taxation, International Cooperation and the 2030 Sustainable Development Agenda* (Switzerland: Springer, 2021) 149; Peter Gerbrands, Brigitte Unger & Joras Ferwerda, "Bilateral responsive regulation and international tax competition: An agent-based simulation" [2021] *Regulation & Governance*.

A. *Coordinated Solutions and Proposals*

The UN Model Tax Treaty, the OECD Model Tax Treaty, the OECD guidelines for MNEs, the G20/OECD BEPS project and the G20/OECD BEPS projects' Two-Pillar solution are examples of coordinated solutions (albeit the OECD guidelines for MNEs do not specifically relate to tax—and have only had limited success). The other instruments mentioned are tax specific. Below is a short analysis of these instruments.

1. *UN/OECD model tax treaties*

The United Nations Model Double Taxation Convention between Developed and Developing Countries ("UN Model Tax Treaty") and the OECD Model Tax Convention on Income and Capital ("OECD Model Tax Treaty") are "currently the main source of tax treaty clauses around the world".[53] The treaties aim to coordinate national tax regulation and eliminate double taxation by encouraging the use of tax treaties. The UN Model Tax Treaty was first published in 1980 and the latest revision was in 2017.[54] The OECD Model Tax Treaty was first published in 1963 and the latest revision was in 2017.[55]

2. *OECD guidelines for MNEs*

The guidelines do not specifically address the regulation of taxation and the original 1976 version of the guidelines was particularly toothless.[56] Furthermore, although the scope of the guidelines has often been revised (and the guidelines have become more detailed with each revision), the guidelines are still heavily criticised due to "their overall lack of binding power and less than satisfactory implementation".[57] The latest revision in 2011, expanded the guidelines to 15 chapters and, whilst still non-binding on MNEs, now provide for "countries adhering to them" to make a

[53] M Lang *et al*, *The Impact of the OECD and UN Model Conventions on Bilateral Tax Treaties* (Cambridge: Cambridge University Press, 2012) at 1; see also van Weeghel, "Have the OECD Model and the UN Model Served Their Purpose?", *supra* note 4.

[54] See UN, Department of Economic & Social Affairs, *Model Double Taxation Convention between Developed and Developing Countries 2017* (New York: United Nations, 2017).

[55] See OECD, *Model Tax Convention on Income and on Capital: Condensed Version 2017* (OECD Publishing, 2017).

[56] See OECD, *Declaration by the Governments of OECD Member Countries and Decisions of the OECD Council on Guidelines for Multinational Enterprises, National Treatment, International Investment Incentives and Disincentives, and Consultation Procedures* (OECD, 1976) <http://www.oecd.org/daf/inv/mne/50024800.pdf> at 11-18. The 1976 guidelines only appeared as an annex to the OECD's "Declaration on International Investment and MNEs", and were particularly brief—only nine short chapters—with a very limited scope—*eg*, the guidelines did not apply outside of OECD countries.

[57] See Reinert, Reinert & Debebe, "The new OECD Guidelines for Multinational Enterprises", *supra* note 49 at 817.

"binding commitment to implement them" and, "as such, aspects of the guidelines are binding on countries but not on MNEs".[58]

3. *G20/OECD BEPS project*

The BEPS project specifically targets the regulation of taxation in the digital economy—*eg*, Action 1 of the 15 Actions the OECD identified in the "BEPS Action Plan" in 2013 was "addressing the tax challenges of the digital economy" (Action 1).[59] Most of the other actions related to examining and responding to BEPS techniques used by MNEs (which techniques are amplified in the digital economy), *eg*, "Prevent the artificial avoidance of PE status" (Action 5) and "Assure that transfer pricing outcomes are in line with value creation" (Actions 8, 9 and 10).[60] BEPS techniques can be understood as MNE practices of reducing or avoiding corporate tax in certain countries "by the deduction of sums that erode the tax base or by simply shifting profits into lower tax jurisdictions", resulting in the loss of an estimated USD 100 billion to USD 240 billion in tax revenue annually.[61] However, it is said that the BEPS project will not achieve its purposes, *eg*, whilst some of the recommendations may have "a deterrent effect on some BEPS behavior", the overall environment is expected to "basically remain unchanged".[62]

Additionally, although the BEPS project was intended to work as a coordinated approach globally, *eg*, Action 15 is to "Develop a Multilateral Instrument",[63] the BEPS project has been criticised for its lengthy failure to achieve coordinated output. For instance, it has been said that the project was "flawed from the start because it was impossible to achieve consensus in favour of the radical overhaul that was needed" and that "the result is a patch-up job that offers improvements in certain areas but fails to deal with the core problems".[64] This was despite the fact that more than 140 countries participated in the BEPS project (the 34 OECD countries and an additional 80-plus developing countries and other non-OECD/non-G20 countries).[65]

Furthermore, it can also be said that the BEPS project has a highly political dimension and represents an attempt by the OECD countries to maintain their

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[58] *Ibid* at 818.

[59] See OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* note 21 at 14.

[60] *Ibid* at 18, 20-21.

[61] See Philip Baker, "Is there a Cure for BEPS?" (2013) 5 British Tax Review 605 at 605.

[62] See Kadet, "BEPS – A Primer", *supra* note 3 at 805; Julien Chaisse & Xueliang Ji, "'Soft Law' in International Law-Making — How Soft International Taxation Law is Reshaping International Economic Governance" (2018) 13(2) Asian Journal of WTO & International Health Law and Policy 463; Mindy Herzfeld, "The Case against BEPS – Lessons for Tax Coordination" (2017) 21(1) Florida Tax Review 1; Eva Escribano, "Is the OECD/G20 BEPS Initiative Heading in the Right Direction? Some Forgotten (and Uncomfortable) Questions" (2017) 71(5) Bulletin for International Taxation 250.

[63] *Ibid*.

[64] See "New rules, same old paradigm", *The Economist* (10 October 2015) <http://www.economist.com/business/2015/10/10/new-rules-same-old-paradigm>.

[65] See OECD, "Developing Countries and BEPS" <http://www.oecd.org/tax/developing-countries-and-beps.htm>; see also OECD, "The 141 members of the OECD/G20 Inclusive Framework on BEPS" (2021) <http://www.oecd.org/tax/beps>.

dominant position over the development of rules of international tax law, which position they have held since the late 1950s.

4. *G20/OECD BEPS "Two-Pillar" regulatory solution*

On 8 October 2021, following almost two-years of consultation, the OECD BEPS project finalised a "Two-Pillar" approach to regulate BEPS activities, which plan was endorsed by 136 countries.[66] Pillar One relates to the "Re-allocation of taxing rights" and Pillar Two relates to a "Global anti-base erosion mechanism".[67]

Pillar one is designed to provide a fairer distribution of taxable revenue among countries with respect to the MNEs who operate companies digitally. The expectation is that Pillar One will provide for over USD 100 billion of taxable revenue to be reallocated among countries annually.[68] Pillar One will work by shifting the taxation of MNEs from their place of residence to the place of consumption of services (called "market jurisdictions" in the BEPS statement). Pillar One could be considered as a step towards "taxing sales instead of profits", which would represent a fundamental reform of the international tax system that would likely fail had it not achieved international consensus. Until now, MNEs operate on the basis that they only pay taxes on business profits in the country where they have a PE (Article 7 of the OECD Model Tax Treaty).[69] It is suggested that a MNEs' global sales can be ascertained, and tax allocated per each jurisdiction.[70] It is said that such a tax could be attempted if there is global consensus and would likely be enabled by the introduction of "country-by-country reporting", which was part of BEPS Action 13.[71] It remains to be seen how this will be implemented, and how successful this will be. It is also possible that Pillar One might cause distortions, for instance, perhaps MNEs will target customers in lower tax jurisdictions (to the extent that it is possible to 'shift' users, which, like natural resources are sometimes considered fundamentaly immobile).

Pillar Two operates via Global anti-Base Erosion Rules ("GloBE") which were originally designed to create a 'floor' as regards competition over corporate income tax, via introducing a global minimum corporate tax rate of at least 15%. Although

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66 See OECD, "Statement on a Two-Pillar Solution", *supra* note 3.

67 See KPMG, "BEPS 2.0: Pillar One and Pillar Two: KPMG Insights on the recent OECD 'blueprints'" <https://home.kpmg/xx/en/home/insights/2020/10/beps-2-0-pillar-one-and-pillar-two.html>.

68 See, *eg*, OECD, *Addressing the tax challenges arising from the digitalisation of the economy* (OECD, 2021) <https://www.oecd.org/tax/beps/brochure-addressing-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-july-2021.pdf> at 3

69 MNEs potentially pay a whole range of other taxes depending on where they operate, including payroll taxes, indirect taxes, different kinds of withholding taxes, etc.

70 See Ulrich Schreiber, "Sales-Based Apportionment of Profits" (2018) 72(4/5) Bulletin for International Taxation 259.

71 OECD, *Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 – 2015 Final Report* (2015); see also Arthur J Cockfield *et al*, *Taxing Global Digital Commerce* (The Netherlands: Kluwer Law International, 2013); Walter Hellerstein, "Taxing Remote Sales in the Digital Age: A Global Perspective" (2016) 65(5) American University Law Review 1195; Arthur J Cockfield, "Tax Wars: How to End the Conflict over Taxing Global Digital Commerce" (2020) 17(2) Berkeley Business Law Journal 347.

the plan was scaled back in the version finalised on 8 October—due to push back from some countries *eg*, the Republic of Ireland, it nevertheless represents a move toward this goal. Here the expectation is to 'generate' approximately USD 150 billion in extra global tax revenues each year.[72] Nevertheless, it remains to be seen whether Pillar Two will be implemented smoothly in practice or whether it might cause some countries to modify their tax rules so as to mitigate against lost tax revenues caused by complying with the GLoBE rules.[73]

B. *Unilateral Solutions and Proposals*

There have also been various unilateral solutions and proposals to tackle these regulatory challenges. Already some countries have become frustrated by the absence of a multilateral approach vis-à-vis the taxation of MNEs in the digital economy and have started to implement their own regulations unilaterally.[74] In this section, some of these unilateral regulations are presented.

Specifically, many countries have already introduced taxes to try to capture profits earned from digital activities. Below are some examples where such taxes have already been introduced. Additionally, other countries are implementing and discussing similar measures. Therefore, the examples are intended to only provide an indication of what has been done rather than a comprehensive overview.[75]

1. *Diverted profits tax ("DPT")*

Some countries, *eg*, Australia and the United Kingdom ("UK") have introduced a so-called "diverted profits tax" in order to catch MNEs with a "significant economic presence" in the respective territory but divert their profits to a low-tax jurisdiction. In the UK, the DPT has been set at 25% and in Australia, the DPT is 40%.[76] France tried to introduce a DPT, but France's Constitutional Council struck it down as unconstitutional in December 2016.[77] It should be noted that DPTs are not used

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[72] See OECD, "Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy" (October 2021) < https://www.oecd.org/tax/beps/brochure-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.pdf>.

[73] See Avi-Yonah, "The International Tax Regime at 100", *supra* note 3; Noam Noked, "Potential Response to GloBE: Domestic Minimum Taxes In Countries Affected by the Global Minimum Tax" (2021) 102 Tax Notes International 943.

[74] See Jason Osborn, Michael Lebovitz & Astrid Pieron, "Unilateral Taxation of the Digital Economy" (2020) 72(3) Tax Executive 26.

[75] See Daniel Bunn, Elke Asen & Cristina Enache, *Digital Taxation Around the World* (Tax Foundation, 2020), <https://files.taxfoundation.org/20200527192056/Digital-Taxation-Around-the-World.pdf>; Ben Jones *et al*, "Taxation of the digital economy: unilateral measures", (2018) 1389 Tax Journal 8.

[76] See Karen Hughes *et al*, "The U.K. Diverted Profits Tax" (2015) 123(1) J Intl Taxn 37; Anjana Haines, "More headaches for MNEs as Australia's DPT is enacted", *International Tax Review* (5 April 2017) <https://www.internationaltaxreview.com/article/2a68xz39mvoyz39q1g0lc/more-headaches-for-mnes-as-australias-dpt-is-enacted>.

[77] See EY's Global Tax Desk Network, "French diverted profits law struck down by Constitutional Court" *Tax News Update U.S. Edition* (30 December 2016) <https://taxnews.ey.com/news/2016-2247-french-diverted-profits-law-struck-down-by-constitutional-court>.

solely to deal with digital economy issues and were enacted to target MNEs such as Google, Amazon, or Starbucks who *divert* profits away from the country where the profits were made.[78]

2. *Significant digital presence ("SDP")*

Some countries, *eg*, Israel, India, Indonesia, and Slovakia,[79] have modified their corporate tax rules in order to tax the profits of MNEs who have a "significant digital presence" involving that country's users. This is not a separate tax, but a clarification of how income will be attributed to a PE from the supply of digital services, and the adoption of a SDP concept—in the context of corporate income tax. In the case of Israel, the concern is to tax MNEs who have a SDP as regards Israeli users, even though the MNE may not maintain a physical presence in Israel.[80] In India, tax provisions related to SDP were introduced in 2018 as regards non-residents who create a "business connection" in the country (defined in May 2021 as where an Indian non-resident exceeds a revenue threshold of INR 20 million (USD 280,000) in aggregate sales to Indian residents or has more than 300,000 Indian users). In Indonesia, there is a requirement that foreign sellers and operators of e-commerce platforms appoint a local representative in the country to pay and report taxes. In Slovakia, the definition of PE was expanded in 2018 to include provision of recurring online intermediation services (*eg*, for transport and accommodation).

Saudi Arabia and Kuwait have each introduced a similar concept of a "virtual service" PE, which is defined as the provision of services without physical presence, where those services exceed the tax treaty threshold periods, *eg*, the India-Saudi Arabia Income Tax Treaty (2006), provides for a threshold of 182 days in any 12-month period.[81]

3. *Digital services tax ("DST")*

In India, a DST was introduced in 2016 (in the form of an equalization levy), which provided for a 6% tax on any business-to-business payments made to non-resident service providers, in relation to digital services.[82] Digital services were originally defined to include online advertising, providing digital advertising space and similar activities, although this has now been added to by the Finance Act 2020 and also further clarified in the Finance Act 2021. The Finance Act 2020 introduced a "2% tax" on the gross revenues received by a non-resident "e-commerce operator" from

[78] See, *eg*, H Khiem (Jonathan) Nguyen, "Australia's New Diverted Profits Tax: The Rationale, the Expectations and the Unknowns" (2017) 71(9) Bulletin for International Taxation.

[79] See WEF, *Digital Trade*, *supra* note 1 at 10–11.

[80] See Jones *et al*, "Taxation of the digital economy: unilateral measures", *supra* note 75 at 12.

[81] *Ibid* at 13; see also Vladimir A Gidirim, "Taxation of Foreign Multinational Enterprises Conducting Business in and with Saudi Arabia" (2016) 70(4) Bulletin for International Taxation 230.

[82] See Sayan Basak, "Equalization Levy: A New Perspective of E-Commerce Taxation" (2016) 44(11) Intertax 845; Manoj Kumar Singh, "Taxation of Digital Economy: An Indian Perspective" (2017) 45(6) Intertax 467.

the provision of "e-commerce supply or service" to Indian residents or non-resident companies with an Indian PE. Further, amendments were made in the Finance Act 2021 to clarify and expand the scope.[83] France also introduced a DST in 2019. The tax rate is 3% on certain digital services, namely "digital interface" services and "targeted advertising" services.[84] France is expected to cancel the DST if a consensus solution is reached at the G20/OECD Inclusive Framework negotiations.[85] Italy also introduced a DST in 2020. The tax rate is 3% and applies to annual revenues from digital services such as advertising on a digital interface, provision of a digital interface, and transmission of data collected digitally (excluding "intercompany" transactions).[86]

C. *Proposals for New Taxation Regulations*

Section III.B. above provided examples of unilateral regulations (in the form of taxes) that have already been introduced. This section III.C. provides examples of proposals for new tax regulations, *ie*, proposals to introduce methods of taxation that specifically target MNEs who are active in the digital economy, which tax authorities struggle to tax using the existing taxation regulations. It is suggested that the unilateral regulations identified in section III.B. be avoided and that the proposals identified below be considered and implemented on a strictly multilateral basis.

1. *Introduction of a digital permanent establishment (PE)*

A PE may be said to exist when a MNE has a "fixed place of business in a State other than that of its tax residence", through which its business is wholly or partly carried out.[87] However, a digital PE relates to where an MNE's "digital activities are characterised by the lack of need of physical elements […] to be able to carry out its business activity" which produces a "specific mismatch in the definition of the

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[83] See Salim Vagh & Juan Elias, "Expansion of India's Equalisation Levy to Impact More Tech Companies", *Transfer Pricing Times* (23 April 2021) <https://www.kroll.com/en/insights/publications/transfer-pricing/transfer-pricing-times-first-quarter-2021/expansion-of-indias-equalisation-levy-impact-tech-companies>.

[84] See Office of the United States Trade Representative, *Report on France's Digital Services Tax* (2 December 2019) <https://ustr.gov/sites/default/files/Report_On_France%27s_Digital_Services_Tax.pdf>; see also Bruno Gouthiere, "France-New Digital Services Tax: Potential Tax Treaty and EU Law Issues" (2019) 45(5) International Tax Journal 7.

[85] See William Horobin, "France Pledges to Remove Digital Tax When OECD Deal Implemented", *Bloomberg* (6 July 2021) <www.bloomberg.com/news/articles/2021-07-06/france-pledges-to-remove-digital-tax-when-oecd-deal-implemented>.

[86] See Stefano Pavesi & Nicoletta Mazzitelli, "Italy's Digital Services Tax Enters into Force" (2020) 31(4) Journal of International Taxation 19; Yue Dai & Amedeo Rizzo, "How Will the Italian Digital Services Tax Affect the Trade Relations With the U.S. and China?", *Fiscalità e Commercio Internazionale* (16 July 2020).

[87] See José Ángel Gómez Requena & Satumina Moreno González, "Adapting the Concept of Permanent Establishment to the Context of Digital Commerce: From Fixity to Significant Digital Economic Presence" (2017) 45(11) Intertax 732 at 734; see also the definition provided in OECD, *Model Tax Convention on Income and on Capital: Condensed Version 2017*, *supra* note 55 at art 5.

concept of PE" and it means that the MNE "cannot be taxed, due to the theoretical inexistence of a PE".[88] There has been substantial discussion regarding the introduction of the concept of a digital PE, since as soon as this is introduced then the business profits in the relevant jurisdiction will be taxable (and captured by transfer pricing rules). Consequently, this is very significant from a coordinated approach versus unilateral approach governance perspective, *ie*, if only a few jurisdictions introduce the concept of a digital PE, then the affected MNEs can simply avoid the few jurisdictions where the respective MNEs would get caught. It is therefore widely understood that this governance challenge, "must undoubtedly be solved in the most global and uniform manner possible", *eg*, via redrafting the OECD Model Tax Treaty and/or its commentaries.[89]

2. *Methods to tax big data*

As regards Big Data, there have been multiple suggestions, often based on the suggestion that Big Data can be taxed in the same way as the extractive industries are currently taxed, *ie*, with the data considered as a natural resource belonging to the State from where the data came.[90] A more complicated model is 'Data Point Pricing', which is where the raw material (the 'data') is priced and a financial value (a 'price') is assigned to each data point collected (then its use and transfer can be traced by applying traditional accounting methods).[91] Another innovative method proposed is called sustained user relationships (known as SURE), which refer to any offshore operations which are used for data collection, advertising and platform services.[92] SURE is basically an idea to tax usage of the data rather than the location where the data is held/hosted.

3. *Equalization taxes and/or global sales taxes*

There have been many proposals as regards how to tax the sales of an MNE who is not caught by traditional tax rules. One suggestion by some EU Member States is to introduce an "equalization tax" on turnover, which would raise the taxation of the MNE to the level of the corporate income tax in the country in which the revenue was earned.[93] Another suggestion is to shift MNE taxation from national to

[88] Requena & González, "Adapating the Concept of Permanent Establishment to the Context of Digital Commerce: From Fixity to Significant Digital Economic Presence", *ibid.*

[89] *Ibid* at 736; see also Clinton Alley and Joanne Emery, "Taxation of Cross-Border E-Commerce: Avoidance of Permanent Establishment and Multilateral Modifications of Tax Treaties" (2017) 28(11) Journal International Taxation 38; Lisa Spinosa, "A Long-Term Solution for Taxing Digitalized Business Models: Should the Permanent Establishment Definition Be Modified to Resolve the Issue or Should the Focus Be on a Shared Taxing Rights Mechanism?" (2018) 46(6) Intertax 476.

[90] See Buriak & Riedl, "Global Transfer Pricing Conference 2020", *supra* note 27 at 245.

[91] See Zetzsche & Anker-Sørensen, "Taxing Data-Driven Business", *supra* note 25.

[92] See Johannes Becker and Joachim Englisch, "Taxing Where Value Is Created: What's 'User Involvement' Got to Do with It?" (2019) 47(2) Intertax 161.

[93] See Georg Kofler & Julia Sinnig, "Equalization Taxes and the EU's 'Digital Services Tax'" (2019) 47(2) Intertax 176.

global profits. However, it is not clear whether equalization taxes would always be able to catch the MNE. Additionally, as regards the taxation of global sales, due to Agreements for the Avoidance of Double Taxation, this would probably mean that where one tax authority bites, the remaining tax authorities miss out (and the MNE may try to be taxed in the most tax-friendly jurisdiction—as it is now).

4. *Taxation based on "value creation" rather than "value consumption"*

Taxing profits where value is created is a basic principle and aim of the OECD BEPS Project (*eg*, BEPS Actions 8-10 aim to ensure that transfer pricing outcomes are better aligned with value creation of the MNE group).[94] Additionally, whilst the "value creation principle" has been criticised for generating a good amount of uncertainty on the application and definition of this principle, partly because it is drafted in such a broad and vague way, developing a model to fairly allocate the value created by the MNE can nevertheless be considered as a sustainable approach in the long term.[95] This was previously identified as one of the key challenges of the digital economy recognised by the OECD (see part II section B.4).[96] Several countries advocating for taxing rights towards market jurisdictions were doing so on the basis that value was being created by users in the digital context, because of the data they generated, how they interacted with digital services, etc.[97] First, this is because countries do not want to give up their taxation rights. Second, countries wish to avoid "subsidizing" the activities of digitally active MNEs (via their failure to collect tax). Third, since direct taxes on digital transactions attempt to tax the MNE where the data is used, rather than where the value is created, they do not resolve the issue of fair income allocation.[98]

5. *Taxing shareholders of digital multinational enterprises*

Finally, there is a radical proposal for "taxing shareholders of digital MNEs". This idea is quite opposite to the idea of taxing the location where value is created.

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94 See, *eg*, OECD, "Action 8-10: Transfer Pricing" (2020) <https://www.oecd.org/tax/beps/beps-actions/actions8-10/>.

95 See, *eg*, Vikram Chand & Damiano Canapa, "Pillar I of the Digital Debate: Its consistency with the value creation standard as well as the way forward" (24 November 2020) <http://kluwertaxblog.com/2020/11/24/pillar-i-of-the-digital-debate-its-consistency-with-the-value-creation-standard-as-well-as-the-way-forward/>; Michael Lennard, "Act of Creation: The OECD/G20 Test of 'Value Creation' as a Basis for Taxing Rights and Its Relevance to Developing Countries" (2018) 25(3) Transnational Corporations 55.

96 See International Monetary Fund, *Corporate Taxation in the Global Economy*, Policy Paper No 2019/007 (2019) <http://www.imf.org/en/Publications/Policy-Papers/Issues/2019/03/08/Corporate-Taxation-in-the-Global-Economy-46650> at 18.

97 See Aqib Aslam & Alpa Shah, *Tec(h)tonic Shifts: Taxing the Digital Economy*, Working Paper No 2020/076 (2020) <http://www.imf.org/en/Publications/WP/Issues/2020/05/29/Tec-h-tonic-Shifts-Taxing-the-Digital-Economy-49363>.

98 See Johanna Hey, "Taxation Where Value is Created and the OECD/G20 Base Erosion and Profit Shifting Initiative" (2018) 72(4/5) Bulletin for International Taxation 203.

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Additionally, it can no longer be assumed that shareholders are less mobile than the MNEs since these days share transactions can be conducted with the click of a button. Furthermore, typically only the group's ultimate parent might issue shares (and several local subsidiaries might be missed entirely).[99]

IV. Trade: Moving Towards (Or Away From) Virtual Free Trade

The conundrum on whether to regulate or boost the digital economy has put the regulators in a difficult position. This is due to two reasons. Firstly, too much unilateral interference with the digital economy will hamper innovation. This should be avoided. Secondly, any attempt to ring-fence the digital economy from the remainder of the economy is bound to fail. This is because the overall economy is completely digitised and thus, separation of the same is not feasible and would serve to be a counter-productive measure.[100] Furthermore, when governments enact new tax legislation (whether unilaterally or in a coordinated way) they also need to be conscious that they are rewriting trade law and not just tax law (this is exemplified in IV.B. below).

A. *The Mirage of Ring-Fencing the Digital Economy from the Remainder of the Economy*

Several companies are engaged in both physical and digital activities.[101] Ring-fencing for the purposes of tax would create practicality difficulties and may result in creating more issues than solving the ones at hand. The digital economy itself is now becoming the entire economy of a nation and is ubiquitous.[102]

It is understood that the digital economy is increasingly becoming the economy itself and, therefore, "it would be difficult, if not impossible, to ring-fence the digital economy from the rest of the economy for tax purposes".[103] Quite aside from the difficulty of doing so, this article argues that such ring-fencing is diametrically opposed to the principles of free trade, which the G20 and the OECD have also been working towards (and which is led by the WTO). It is observed that "one of the main

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99 See Martin A Sullivan, *Corporate Tax Reform: Taxing Profits in the 21st Century* (New York: Apress, 2011); Maarten Floris de Wilde, *Sharing the Pie: Taxing Multinationals in a Global Market* (The Netherlands: IBFD, 2017); Michael P Devereux *et al*, *Taxing Profit in a Global Economy* (New York: Oxford University Press, 2021).

100 See KPMG, "Comments on the OECD Discussion Draft on the Tax Challenges of the Digital Economy" (14 April 2014) <https://assets.kpmg/content/dam/kpmg/pdf/2014/06/digital-economy-discussion.pdf>.

101 See Bruno Fajersztajn & Ramon Tomazela Santos, "The challenges of taxing the digital economy", *International Tax Review* (30 March 2020) <http://www.internationaltaxreview.com/article/b1ky5z950v9tl6/the-challenges-of-taxing-the-digital-economy>.

102 See OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 – 2015 Final Report*, *supra* note 20.

103 OECD, *OECD Secretary-General Tax Report to G20 Finance Ministers and Central Bank Governors*, *supra* note 39 at 12.

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objectives of international tax norms should be to ensure neutrality in cross-border trading".[104]

B. *Pitfalls and Shortcomings of Unilateral Interference with the Digital Economy*

International economic law has actively been considered as unilateral economic law due to its entry into a new phase of the reassertion of sovereignty by the States, since States position their economic regimes in a way that is favourable to their own domestic needs.[105] While any act of State can be classified as unilateral in international law, the unilateral economic law discussed here refers to the institutionalization of the values and principles surrounding international economic law through domestic legal means.[106]

The unilateral measures implemented to date are, however, likely to result in substantive uncertainties for MNEs and to contradict the OECD's own principles of neutrality, efficiency, certainty and simplicity, effectiveness and fairness and flexibility.[107] The introduction of additional taxes on similar transactions may give rise to double taxation and become an additional barrier to trade.

In fact, since around the same time as the G20/OECD launched the BEPS project in 2013, certain scholars have started to make noises regarding how the digital economy does not fit into the existing rules of world trade.[108] In particular, it is said that the WTO agreements only "tangentially" provide for digital trade.[109] Two challenges for free trade presented by the digital economy are: firstly, the world is "witnessing several different regimes around data and information", *eg*, US, Europe, and China.[110] Secondly, governments are understood to be "increasingly restricting global data flows and requiring data localization, undermining the economic benefits of digital trade".[111] Unilateral taxation is an item that can also add to both of

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[104] See Petruzzi & Buriak, "Addressing the Tax Challenges of the Digitalization of the Economy?", *supra* note 12 at 4.

[105] See Georgios Dimitropoulos, "National Sovereignty and International Investment Law: Sovereignty Reassertion and Prospects of Reform" (2020) 1 Journal of World Investment & Trade 71 at 90.

[106] See Julien Chaisse & Georgios Dimitropoulos, "Special Economic Zones in International Economic Law: Towards Unilateral Economic Law" (2021) 24(2) Journal of International Economic Law 229.

[107] See, *eg*, OECD, Committee on Fiscal Affairs, *Electronic Commerce: Taxation Framework Conditions* (1998) <http://www.oecd.org/ctp/consumption/1923256.pdf> at 4.

[108] See Hosuk Lee-Makiyama, "Future-Proofing World Trade in Technology: Turning the WTO IT Agreement (ITA) into the International Digital Economy Agreement (IDEA)" (2011) 66(3) Aussenwirtschaft 279; Mira Burri, *Should There Be New Multilateral Rules for Digital Trade?*, Think Piece for E15 Expert Group on Trade and Innovation (Geneva: International Centre for Trade and Sustainable Development & World Economic Forum, 2013); Farrokh Farrokhnia & Cameron Richards, "E-Commerce Products Under the World Trade Organization Agreements: Goods, Services, Both or Neither?" (2016) 50(5) Journal of World Trade 793; Andrew D Mitchell & Neha Mishra, "Data at the Docks: Modernizing International Trade Law for the Digital Economy" (2018) 20 Vanderbilt Journal of Entertainment and Technology Law 1073.

[109] See Merit E Janow & Petros C Mavroidis, "Digital Trade, E-Commerce, the WTO and Regional Frameworks" (2019) 18(S1) World Trade Review s1 at s1.

[110] *Ibid* at s1; see also Henry Gao, "Digital or Trade? The Contrasting Approaches of China and US to Digital Trade" (2018) 21(2) Journal of International Economic Law 297.

[111] See Joshua P Meltzer, "Governing Digital Trade" (2019) 18(1) World Tax Review 23 at 23.

these challenges. It is said that to overcome these two challenges may well require "new digital trade rules" (as has been called for), and it is said that some of these new rules can already be found in the WTO agreements and some new rules are being developed in free trade agreements (that exist bilaterally).[112]

V. Sovereignty: A Fight For Digital Supremacy

Considering that digital presence is everywhere and is ubiquitous, several nations have now involved themselves to address the challenges for regulating the taxation of the same. However, State sovereignty is a very important aspect that needs to be considered when taxing digital enterprises. Part V of this article revisits the lingering concept of State sovereignty with respect to the challenges surrounding the regulation of taxation of the digital economy. This part shall also consider the regulatory solutions and proposals addressed in part III of this article.

A. *State Sovereignty in the Context of the Disruption Caused by the Digital Economy as Regards Taxation*

In recent years a concept of "digital sovereignty" has emerged. This means that States seek the "control of data, software (*eg*, Artificial Intelligence), standards and protocols (*eg*, 5G, domain names), processes (*eg*, cloud computing), hardware (*eg*, mobile phones), services (*eg*, social media and e-commerce), and infrastructure (*eg*, cables, satellites and smart cities)".[113] The primary reason why States pursue digital sovereignty is for technological survival, however, another reason States pursue digital sovereignty is so that they can regulate and tax.[114] Indeed, States take tax sovereignty very seriously and there is no reason to think that States will give up their sovereign right to tax in the digital age (whether because of the BEPS project, the Two-Pillar solution or anything else).[115] This was in fact noted in Chapter 2 of the BEPS Action Plan, where the OECD reaffirmed that "[t]axation is at the core of countries' sovereignty" and highlighted that "the interaction of domestic tax rules in some cases leads to gaps and frictions".[116] The OECD then went on to state that, "[t]he global economy requires countries to collaborate on tax matters in order to be able to protect their tax sovereignty".[117]

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[112] *Ibid* at 23.

[113] See Luciano Floridi, "The Fight for Digital Sovereignty: What It Is, and Why It Matters, Especially for the EU" (2020) 33(3) Philosophy & Technology 369 at 370–371.

[114] *Ibid*.

[115] See Laurens van Apeldoorn, "BEPS, Tax Sovereignty and Global Justice" (2018) 21(4) Critical Review of International Socical and Political Philosophy 478; Jennifer Bird-Pollan, "The Sovereign Right to Tax: How Bilateral Investment Treaties Threaten Sovereignty" (2018) 32(1) Notre Dame Journal of Law, Ethics & Public Policy 107; Sol Picciotto, "Technocracy in the Era of Twitter: Between intergovernmentalism and supranational technocratic politics in global tax governance" [2020] *Taxation as Regulatory Governance: Regulation & Governance*; Nikolay Andreev, "Extending Tax Sovereignty to the Internet Space" (2021) 1 Law & Digital Technologies 37.

[116] OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* note 21 at 9.

[117] *Ibid*.

Consequently, it is to be expected that States will oppose multilateral solutions that limit their sovereignty, and it is hard to see compromises regarding similar questions, such as who will hold taxation rights in a cross-border context. In this regard, although the BEPS projects Two-Pillar solution was finalised on 8 October 2021 (and agreed by 136 countries), it will be interesting to see if the Two-Pillar solution will get the traction that the G20 and the OECD expect.[118]

B. *The Need for the Multilateralization of International Tax Law*

Different tax regimes have led to the uneven regulatory treatment of MNEs for the purposes of taxation in various countries, which needs to be addressed and coordinated accordingly.[119] The coordinated policies such as the UN Model Tax Treaty, the OECD Model Tax Treaty, the OECD guidelines for MNEs, the G20/OECD BEPS project and the G20/OECD BEPS projects Two-Pillar solution are a good way forward to simplify the taxing process of such enterprises. These are some multilateral approaches that could be put to use to tackle the regulatory challenges elaborated in this paper. A unilateral approach by States has also been taken by some Countries. Countries need to find an adequate solution to regulate the taxation of digital activities in their jurisdiction since many digital companies escape taxes by taking advantage of their worldwide presence. There have been several measures taken like the DST, DPT, taxing SDP, and virtual service PE to make sure that the profits of such digital companies are accounted for in the jurisdictions, where they are operating. Such policies further allow the States to exercise their sovereignty over such companies without any involvement from the outside parties in their domestic issues.

This article shows the proposals for new taxation regulations to specifically target the MNEs that make immense gains from their digital presence. These are listed in part III.C., and it is suggested that these proposals be considered and implemented on a strictly multilateral basis. Traditional tax regimes have proven to be insufficient hence, new methods need to be implemented to ensure that the MNEs have paid adequate taxes. Firstly, introducing a digital permanent establishment, can make it easier to tax the intangible presence of the MNEs. Secondly, considering that data is now the most valuable resource, it is high time the tax authorities now utilise it in their own favour by, building on modest solutions being used *eg*, in the US and China,[120] and optimizing Big Data solutions to accurately tax the

[118] See Michel Motala, "Tax Sovereignty and Investor Protection: Why the Proposed Global Minimum Tax Is Not the Final Frontier for Corporate Tax Arbitrage" (2021) 16(2) International Organisations Research Journal 99.

[119] See James Alm, Peter Gerbrands & Erich Kirchler, "Using 'responsive regulation' to reduce tax base erosion" [2021] *Regulation & Governance*.

[120] See Kimberly Houser & Debra Sanders, "The Use of Big Data Analytics by the IRS: What Tax Practitioners Need to Know" (2018) 128(2) Journal of Taxation 6; Yuning Gao, Meng Li & Yufeng Lu, "What Can Be Learned from Billions of Invoices? The Construction and Application of China's Multiregional Input-Output Table Based on Big Data from the Value-Added Tax" (2020) 56(9) Emerging Markets Finance & Trade 1925.

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Big Tech companies.[121] Levying Equalization taxes and/or Global Sales taxes are also a way to move forward. A sustainable approach has also been recommended wherein the MNEs are taxed based on the value they have created rather than on the value that has been consumed. Lastly, a radical solution to tax the shareholders of the digital MNEs has been suggested.

VI. Conclusion

Through considering the (old and new) regulatory challenges of taxation in the digital economy and focusing on "stateless income", this article has been able to identify the consequences of both coordinated and unilateral regulations, solutions, and proposals. Furthermore, this article also brought into the analysis the overarching issues of free trade, globalisation, and State sovereignty and in such a way, became firmly entrenched at an important intersection of comparative and business law.

Taxation in the digital economy was explained to be a regulatory challenge that keeps on growing and the "old" and the "new" regulatory challenges posed by the digital economy were identified. It was shown that some of these new challenges have not yet matured, *eg*, the taxation of "blockchain forks", which means that tax authorities will inevitably trail digital innovation.

As regards the solutions and the proposals launched, the article shows that the coordinated solutions and proposals have a greater chance of success, not least because of the threats to a State's tax sovereignty from any unilateral solutions and proposals launched such as Diverted Profits Tax, taxing Significant Digital Presence, Digital Services Tax, and others. It is however suggested that the concept of the Permanent Establishment be extended to catch digitally focused enterprises that may not have a clear physical presence (in a coordinated way via the OECD).

Whilst the BEPS project and the BEPS projects Two-Pillar solution are likely to prove to be a step in the right direction, the bigger issue is that enterprises have become multinational, but tax authorities have not. This means that it is difficult to affect any coordinated solution and States have invariably done things unilaterally, bilaterally, or regionally. This affects trade where "too much" unilateral interference with the digital economy should be avoided.

Last but not least, the BEPS project also is a strategic move where the G20/OECD seek to maintain authority over global taxation, which may actually be the root of the challenges (*eg*, there are internal disputes between say Europe and the US). However, what is fundamentally needed is to launch a new "World Tax Organization" which will have a proper mandate over tax, such as the WTO does as regard trade. Further research will need to reflect on the structural design and rules of such a "World Tax Organization"; however, the future will certainly analyse the BEPS and the years 2016-2021 as a turning point towards the inevitable internationalisation of tax law.

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[121] See Valentine P Vishnevsky & Viktoriia D Chekina, "Robot vs. tax inspector or how the fourth industrial revolution will change the tax system: a review of problems and solutions" (2018) 4(1) Journal of Tax Reform 6.

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