



AFRICAN TAX
ADMINISTRATION FORUM

FORUM SUR
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FISCALE AFRICAINE

POLICY BRIEF

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Domestic Resource Mobilisation *Digital Services Taxation in Africa*

INTRODUCTION

This policy brief is designed to assist ATAF members in their tax policy considerations of the taxation of highly digitalised businesses operating in African countries.

Many ATAF members have reported difficulties in taxing such businesses. Their economies are rapidly becoming more and more digitalised and that digitalisation often enables multinational enterprises (MNEs) to carry out business in African countries with no or very limited physical presence in those countries. This makes it difficult for African countries to establish taxing rights over the profits the MNE is making from those business activities.

This is due to the current international tax rules only allocating taxing rights to a country where a non-resident enterprise creates sufficient physical presence in that country i.e. creating a “nexus” in that country. Business models that enable an MNE to carry out business in an African country with no or very limited physical presence in that country therefore represent a significant tax risk. The examples cited by commentators of such business models are usually those such as social media platforms, search engines and online marketplaces.

The OECD Inclusive Framework has for some time been discussing trying to find a global consensus based solution to the tax challenges arising from the digitalisation of the economy. ATAF has been providing technical analysis and support to our members who are also Inclusive Framework members to ensure that if there is a global solution it is fit for purpose in Africa (see the [series of ATAF Technical Notes](#)).

However there is a significant risk for African countries in simply waiting to see whether the OECD Inclusive Framework can achieve an international solution. Doing so could significantly delay enacting and implementing legislation to ensure countries obtain the appropriate taxing rights on the profits of highly digitalised businesses. Such delays may cost African countries millions of dollars of tax with many such business seeing significant increases in their profits during the COVID 19 pandemic. Meanwhile that pandemic has decimated many African economies and the need to ensure that tax revenues bolster national budgets has become critical to sustain even the most essential national requirements in the pandemic.



2. ADDRESSING THE TAX CHALLENGES FROM DIGITALISATION

To assist members in their consideration of whether to introduce new rules to tax highly digitalised businesses ATAF is developing a *Suggested Approach to Drafting Digital Services Tax Legislation* that will set out a series of options for drafting such legislation.

The paper, which will be prepared by the ATAF Cross Border Taxation Technical Committee and ATAF Secretariat, will provide African countries that are considering introducing a Digital Sales Tax (DST) with a suggested structure and content for their legislation. It will provide a framework based on DST legislation enacted in other jurisdictions but adapted to meet the specific challenges faced by African countries. Explanatory notes will be provided describing in greater detail some of the reasoning underlying the draft legislation.

Digital Service taxes are less likely to be an income tax where they are:

- levied on the supply of a certain defined category or categories of e-services and imposed on the parties to the supply without reference to the particular economic or tax position of the supplier.
- charged at a fixed rate, calculated by reference to the consideration paid for those services (without reference to the net income of the supplier or the income from the supply); and
- not creditable or eligible for any other type of relief against income tax.

The Suggested Approach will be designed not to be an income tax as it proposed the tax is levied on the supply of narrowly defined services (being those provided by in-scope business activities), and charged at a fixed rate by reference to the consideration paid (that is, the gross turnover attributable to the in-scope business activities) and not the net profit of the recipient, and it would not be creditable against the country's income tax. In particular, the DST would be paid in addition to a country's income tax charge, so it is not in any way in lieu of income tax.

If the DST is not an income tax for Double Tax Agreement purposes countries can introduce the DST unilaterally, without the need for international agreement. It also cannot be credited against the country's income tax, but it might be considered a business expense, and so would be deductible in accordance with the country's ordinary income tax deduction rules.

If a country's Double Tax Agreements are consistent with Article 2 of the ATAF Model Tax Convention the DST would be payable by a non-resident even if it did not have a physical presence in the country. The ATAF Model Tax Convention requires a non-resident to have a physical presence before a contracting State can impose income tax on their sales income. However, Article 2 states that they only apply to income taxes or taxes substantially similar to an income tax. This means that a DST would not conflict with the ATAF Model Tax Convention provided the DST is not an income tax or substantially similar to an income tax

3. BENEFITS OF ADOPTING A DST

A DST is a way of collecting tax from those types of businesses that present the greatest challenge to the current international tax framework, and which have to date been paying little tax in Africa.

Further, a DST should be relatively simple to calculate and administer compared to income tax. In addition, the size of the digital economy is growing as a proportion of the total economy of Africa. Consequently, it will become increasingly important for African countries to ensure that the digital economy is taxed appropriately.

While the revenue raised would not be large for most African countries, a DST could have other benefits. Much of the recent public concern about the under-taxation of multinationals has focussed on high-profile digital companies that do not have a physical presence in countries so are not subject to income tax. By taxing these companies, a DST could improve public confidence in the fairness of the tax system, which is an important factor underlying voluntary compliance.

4. ISSUES AND POTENTIAL DRAWBACKS OF A DST

The DST applies in addition to income tax. This could result in both DST and income tax applying to the same income of some firms (including possibly some domestic firms). This will mainly be an issue for domestic businesses, as they are already taxed in the country on all their income. Non-resident digital businesses pay low rates of income tax generally and are not currently subject to income tax on any income attributable to users in most African countries.

Another issue is that, as a tax on gross turnover, the DST would apply to firms in loss, or with low margins. This is something that can be partially mitigated with de minimis thresholds, as the larger firms tend to be more profitable. A lower DST rate also helps to mitigate this issue. However, these features cannot eliminate the issue altogether.

It is important that any DST does not reduce the growth of the digital sector in African countries, particularly start-ups and small and medium enterprises (SMEs). For this reason, any DST would need robust de minimis thresholds, to ensure it only targets established and profitable digital businesses.

Members should also note that the Office of the United States Trade Representative has just initiated investigations with respect to Digital Services Tax (DSTs) adopted or under consideration by Australia, Brazil, the Czech Republic, the European Union, India, Indonesia, Italy, Spain, Turkey and the United Kingdom. The U.S. Trade Representative has requested consultations with the governments of these jurisdictions. The investigations could lead to tariffs being imposed on the countries' exports to the U.S. It is possible the US might initiate similar investigations with respect to DSTs adopted or under consideration in ATAF member countries.