CHANGING THE UK TAX VIEW ON DIGITAL BUSINESS MODELS AND DIGITAL TAX ADMINISTRATION

As it is apparent throughout this publication, Brexit is naturally a primary issue of concern among business leaders concerned with British-German trade relations. From a tax perspective, however, further areas of UK tax law should receive attention due to their substantial consequences. Last year, substantial changes were made to the UK tax code. This year, there was an increased focus on digital tax matters – on both the taxation and the administrative side.

TAXING THE DIGITAL ECONOMY

In 2015, the UK was the first European country to implement a tax aimed at an "unfair" reduction in UK tax revenues in relation to business (and, thus, profits) made by a group in the UK. This "diverted profits tax" aimed to constitute formerly deliberately avoided permanent establishments in the UK, and allows the UK tax authority (HMRC) to tax profits earned by such PEs.

Now, the UK has again taken the lead in the initiative to modify long-established taxation principles in order for them to remain relevant and applicable to digital business models. In a position paper update published on 13 March alongside spring budget proposals, the UK government states that users themselves may generate a significant share of the value that should be a relevant basis for taxation, but that such value is not yet captured by current rules. In particular, users add value through their individual contribution and participation (for example when putting pictures on Instagram, adding comments to discussions on Facebook, and the like). Widely in line with similar proposals published by the EU as well as the OECD some time later, the UK aims to integrate the taxation of such businesses into the existing framework (e.g. through modification of the relevant rules of double taxation agreements). However, short-term solutions may be required as well, such as revenue taxation. Revenue taxation would be a fundamental change of corporate income tax principles: No longer would taxable profit be the computation base for the tax but gross revenue. Accordingly, consequences could be significant, particularly if such measures are implemented unilaterally, as occurred with the DPT in 2015. They could also be significant in the sense that business models based on mass volumes and comparably low relative profits may lose substantial portions – if not all – of their net profits.

MAKING TAX DIGITAL

Starting with a roadmap published in December 2015, the process towards digitalising tax processes at the HMRC has been gaining speed significantly in the recent months. According to HMRC, "making tax digital" is based on four pillars:

1. **Better use of information**
   The intention here is for the tax authority to electronically gather information relevant tax filings by individuals or entities from other sources, where available. This could be from employers, banks, or other departments of the public authorities. While the HMRC views this as an effort to make tax filings less complicated and time-consuming, others claim that it will end self-assessment, as information will be gathered elsewhere.
2. **Tax in real time**
   Based on available information, the HMRC plans to make tax information concerning tax liabilities, outstanding payments etc. available to taxpayer in real time.
3. **A single financial account**
   The HMRC intends to align various tax databases so that taxpayers can see their obligations in a manner similar to "surfing" through their online-banking records.
4. **Interacting digitally with customers**
   Here, the intention is to interact with taxpayers and tax service providers in a more digital way, in particular with respect to deadlines and by facilitating communication via web chat.

From early 2019, businesses will need to use the interface for their quarterly VAT filings. From 2020, all other taxes shall be fully integrated into the system.

With respect to VAT, it is now time to ensure that digital systems are working by 2019. Since both the VAT-related consequences from Brexit and the changes to UK tax filings will coincide, particular care will need to be taken. With respect to corporate income taxes, a formal consultation is expected in 2018 to discuss the details and scope of the new digital regime. One way or another, this will be a valuable source of information for monitoring upcoming developments.

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