

# Tax And The Internet - OECD And Singapore Guidelines

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## SYNOPSIS

The purpose of this paper is to examine the challenges facing tax authorities worldwide as a result of the Internet and electronic commerce. Electronic commerce are contracted and delivered in a paperless and faceless format, led by rapid changes in information and communications technologies. These technologies have enabled taxpayers to move their “place of business” from one tax jurisdiction to another - quickly, seamlessly and effortlessly.

New technologies in banking and payment systems, and new software technologies housed in servers in remote locations, have enabled taxpayers to “hide” transactions and to choose whichever low-tax jurisdictions they like to record (electronically) these transactions. These developments have made it necessary to re-examine the traditional tax definitions and concepts based on conventional commerce.

The OECD, the main international body on international taxation issues, is taking the lead to address these issues. Almost all governments based their double-tax treaties on the OECD Model Tax Convention on Income and on Capital. This paper will discuss the reports released by the Committee on Fiscal Affairs (“CFA”) of the OECD on the taxation of electronic commerce.

Electronic commerce is borderless, it deals with cross-border transactions. Which country should be taxing the transaction? Who should be paying the tax? Are the traditional definitions of income, business profits, royalties, and other conventional tax concepts settled and agreed in existing tax treaties still relevant?

*This paper will not specifically address taxation issues as such.* Rather this paper will address the *impact* of the internet and electronic commerce on *some* of the tax issues, in particular the international direct tax issues. In the process, the paper will also discuss the tax guidelines of the Inland Revenue Authority of Singapore on the taxation of electronic commerce.

## THE CHALLENGES FACING TAX AUTHORITIES AND TAXPAYERS

The OECD noted that the Internet enabled new ways for businesses to advertise, sell and deliver products and services to customers. Some examples are :

- (a) the sale of physical and digital goods through web sites;
- (b) services provided through web sites such as onshore and offshore banking, travel bookings, share trading, etc;

- (c) on-line information for sale;
- (d) on-line advertising;
- (e) internet gambling; and
- (f) on-line global trading and dealings.

As the OECD rightly pointed out “the Internet will change the environment within which tax administrations operate”.

For tax authorities, the ability of taxpayers to make untraceable transactions on the internet poses serious problems for tax collection. A country-specific internet address may not necessarily mean the server is located in that country. Tax administrators will have difficulties enforcing withholding taxes if they cannot verify the identity of the payer or the payee.

Tax administrators face tax compliance issues such as :

- (a) establishing the identity and location of potential taxpayers;
- (b) establishing proof of tax evasion when electronic records are maintained offshore;
- (c) taxing points are more difficult to establish when consumers trade electronically offshore; and
- (d) tax evasion becomes easier when tax havens and offshore banking facilities are easily accessible.

The OECD also noted the opportunities to lower the costs of tax collection. Some examples include the electronic filing of tax returns; automated deductions of taxes; electronic exchange of information; faster processing and more productivity through the use of electronic data interchange (EDI) systems for customs processing.

## **CONCLUSION**

Internet technology, electronic payments, electronic contracting and electronic delivery of goods and services – all of these developments have created concern on the part of tax administrators that their tax base will be eroded. The old boundaries and demarcations as to who has the taxing rights are now shifting.

Businesses exporting intellectual and intangible properties want to be taxed only in their home countries, arguing they are carrying on a business and are earning business profits and not royalties. Tax administrators in technology-importing countries say their residents are paying for scientific know-how and these should be classified as royalties, not business profits. Whilst these arguments have gone through the OECD consultation processes, they take on a new urgency as a result of the Internet.

For the first time, businesses can now generate sales, receive payments and make deliveries, without having to have a permanent establishment in the customer’s country. Businesses can now locate digital or electronic “offices” in low-tax jurisdictions, keep only electronic records (with many copies in different locations), assumed digital

identities without disclosing their real addresses and identities, and quickly move or transfer operations in and out of a country and from country to country.

Tax administrators of technology-exporting countries and of technology-importing countries may have to co-operate to deal with the new technological options open to taxpayers to re-arrange their tax affairs.

The OECD is continuing its work on redefining and reviewing the taxation issues of permanent establishment, business profits, royalties and other payments in the context of electronic commerce. Singapore has issued just a few e-tax guidelines. Further guidelines will depend on the consensus that the OECD and other world bodies are able to achieve in their consultation processes.

*This is not the full LLM Paper.*

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