



The UK Digital Services Tax: an Overview (2020)

1st June 2020

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The UK Digital Services Tax: an Overview (2020)

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up to date as of **26th May 2020**



Introduction



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An Introduction

- This webinar will cover the UK's new Digital Services Tax (the "DST"). The DST will apply to revenues earned from 1 April 2020.
- The DST reflects a general international movement towards an updated structure of taxation for digital businesses, and a response to the steady digitalisation of the global economy. A key intention is to tax profits in the location where value is generated.
- The Organisation for Economic Co-operation and Development (the "OECD") continues to work to establish a global consensus on how digital taxation should be developed. However, the UK follows countries such as France and Italy in establishing provisions to tackle the issues in the meantime.
- This webinar assumes that the DST will be enacted in its current form when the Finance Bill 2020 receives Royal Assent.

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The Basics

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The Basics

- The DST is a 2% tax on the revenues of large businesses that provide certain digital services. The in-scope revenues must be derived from UK users.
- The services within the scope of the DST are:
 1. Social media services;
 2. Internet search engines; and
 3. Online marketplaces.
- A business is considered to be a “large” business if it has annual global (on a consolidated group analysis) revenues of over £500m, more than £25m of which are attributed to UK sales. All revenues must be “in-scope” revenues to be relevant for the test.
- The first £25m of revenues attributable to UK services is excluded from the calculation.

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The Basics

- Certain businesses can utilise an alternative basis of charge. According to the alternative basis, the applicable DST rate is based on the UK operating margin of the relevant activities of the business (or group). Essentially, where the business (or group) has an operating margin of zero (or a negative operating margin), calculation of DST should be reduced accordingly.
- DST must be paid within nine months of the end of the relevant accounting period. The DST return must be submitted within one year.

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The Scope

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The Scope

- The service provided must be an “online service”.
- HMRC guidance suggests that an in-scope online service should be a substantive business service by itself (i.e., not just ancillary or incidental to another service).

An example:

- The comments section of the online version of a newspaper would generally be considered to be ancillary to the provision of digital journalistic content. In many cases, the comments facility has no distinct purpose and the business may have no plans to develop or monetise this facility independently from its broader plan to expand the newspaper (see HMRC guidance at **DST12500**).
- Where most users visit the website to consume the journalistic content and the opportunity to comment on articles is clearly a secondary driver, HMRC guidance considers that the comments facility is unlikely to be a separate service to the wider provision of the online newspaper. However, it is noted that the group should consider whether the online newspaper meets any of the relevant conditions.

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The Scope

- The online service must fall within one of the following three categories:

1. Social media services

This category includes two conditions:

- (a) That the service has a main purpose of promoting interaction between users;
and
- (b) That the service enables the sharing of user-generated content, where this is “a significant feature of the service”.

2. Internet search engines

No specific definition is provided, but this concept does exclude ‘embedded’ search engines. Where the website contains a search box using third party technology to display results, the third party provider is generally considered to be undertaking the relevant activity (although this will depend on the facts of each case).

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The Scope

3. Online marketplaces

The marketplace must have a main purpose to facilitate the sale or hire of goods or services offered by users, and will enable users to sell or advertise (even if the sale is concluded on another platform). HMRC guidance provides a list of considerations to assist in determining whether there is an online marketplace.

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The Scope

- An exclusion applies for online financial marketplaces, including the trading of commodities, financial instruments or foreign exchange.
- “Trading” includes the creation of instruments.
- The provider of such online marketplaces need not be a regulated entity.

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The Scope

- Revenues falling within scope are taxable if they:
 - Are attributable to one of the three ‘in-scope’ categories outlined above (see slide 5); and
 - Are linked to UK user participation.
- Revenues from ancillary activities are also included (e.g., payment fees for online marketplace sales).
- Where advertising services are included within other in-scope activities, such services are also included in the calculation of the tax (if the advertising services obtain a significant benefit from the digital service).

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The Scope

An example:

- A group operates a search engine, and generates revenue by allowing businesses to pay it to display advertising against users' search results. It also enters into agreements with third party websites to take control of their advertising space and auction this to other customers looking to display advertising across a range of websites. This activity would be considered an online advertising service.
- The search engine provider tracks user behaviour across its own search website and other third party websites, and also offers businesses seeking to advertise a similar set of products to use to target adverts at users. In this case, the advertising service does derive significant benefit from the search engine (see HMRC's guidance at **DST19500**).

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The Scope

- Revenues must be *attributable* to *UK users* to be within the scope of the DST.
- A "UK user" is a user that can be reasonably assumed to be normally located or established in the UK (either an individual or company). Note, however, that the scope is not limited to UK-incorporated companies or UK permanent establishments.
- Each determination is considered to be a pragmatic test, based on available information (such as UK physical address details, or UK payment details. In some circumstances, a user's IP address may also be helpful information). Businesses should consider how to analyse and assess their user data to meet the relevant requirements, but are only expected to use the evidence available to them to determine if it is reasonable to assume the relevant user is a UK user.
- Revenues are generally considered to be "attributable" to UK users if they arise in connection with UK users. There are some specific rules that relate to online marketplaces but, in general, a 'just and reasonable' apportionment is to be made.

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The Mechanics

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The Mechanics

- The DST applies to relevant revenues where:
 - total group digital services revenues exceed £500m, and
 - total UK digital services revenues exceed £25m.
- A £25m allowance applies to each accounting period, for the first £25m of UK taxable revenues.
- In theory, double taxation relief should be available to prevent double taxation from the application of an equivalent DST in another jurisdiction. However, this is subject to conditions and limitations to certain circumstances.

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The Mechanics

- An alternative basis of charge may apply to loss-making or low-margin companies (this is sometimes referred to as the “safe harbour”).
- Eligible businesses may elect (on an accounting period basis) for the rate of charge to be calculated according to their UK operating margin. It is possible for the election to be made against certain categories of revenue (and not against others).
- DST will generally be deductible as an allowable expense against UK Corporation Tax, subject to the applicable rules for deductibility of expenses (incurred wholly and exclusively for the purposes of the trade). HMRC’s guidance acknowledges that a company’s DST expense is directly related to the earning of its revenues and is a legal obligation of performing that trade. In most cases (according to HMRC guidance), it is likely the expense will have been incurred wholly and exclusively for the purposes of the trade.
- There is no credit relief for DST against any other tax.

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The Mechanics

- DST is payable annually, nine months after the end of the relevant accounting period.
- DST liability is calculated at the level of the group but chargeable on the companies within the group that recognise the relevant revenues.
- Groups can nominate a group company to deal with some administrative aspects of the DST (including notifying HMRC when the revenue threshold conditions are first met, calculating liability and submitting annual returns). If no such nomination is made, these responsibilities fall to the ultimate group parent.
- The amount and timing of relevant revenues is determined from the consolidated group accounts, as per the relevant accounting framework.

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The Mechanics

- A targeted anti-avoidance rule (the “TAAR”) applies in order to counteract arrangements with a main purpose of achieving a DST tax advantage.
- The TAAR applies to relevant anti-avoidance arrangements (see HMRC’s guidance at **DST46000**). In order to fall within scope:
 - There must be an arrangement;
 - A main purpose of the arrangement must be to enable a person to obtain a DST tax advantage; and
 - The TAAR will not apply when the obtaining of the tax advantage can reasonably be regarded as consistent with the principles, and policy objectives, of the DST legislation.
- When the TAAR applies, HMRC must counteract the arrangement by making such adjustments that are just and reasonable.

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The Future

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The Future

- The UK Government has stated that the DST will be disapplied when an appropriate global solution is enacted.
- The relevant legislation contains the requirement that the DST is reviewed before the end of 2025.
- The OECD intends to reach a multinational solution by the end of 2020.
- The US has so far resisted digital services taxes as applied in France, leading to a trade dispute. At present, both France and Italy have delayed collection of their digital services taxes. The EU's digital tax proposal also faces future challenges.

What next?

What Next?

- Businesses should assess whether they are likely to fall within the scope of the DST.
- If businesses are likely to fall within the scope of the DST, they should consider procedures and systems to assist with assessment, analysis of data and calculation.
- Group companies should consider if it will be appropriate to nominate an entity to handle the administration of the DST.
- International developments should be monitored (including at a global level, as well as the proposals introduced by the OECD and the EU).

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