Global indirect tax obligations in the digital economy

Over 170 countries employ a value-added tax (VAT), also known in certain countries as goods and services tax (GST). As a result, many U.S.-headquartered multinational companies operate in countries that impose a VAT/GST regime. An increasing number of these VAT/GST jurisdictions have introduced, or are in the process of introducing, VAT/GST rules aimed at the digital economy, creating global tax obligations for U.S.-based companies.

These rules focus on three main aspects of the digital economy:

1. Remote sales of digital services
2. Remote sales of so-called low-value consignments
3. Tax obligations of digital intermediaries such as online platforms or marketplaces.

Any business, even a traditional business not operating in the digital economy or a nonprofit, that falls within any of these categories may thus have foreign VAT/GST obligations even in the absence of any physical nexus abroad.

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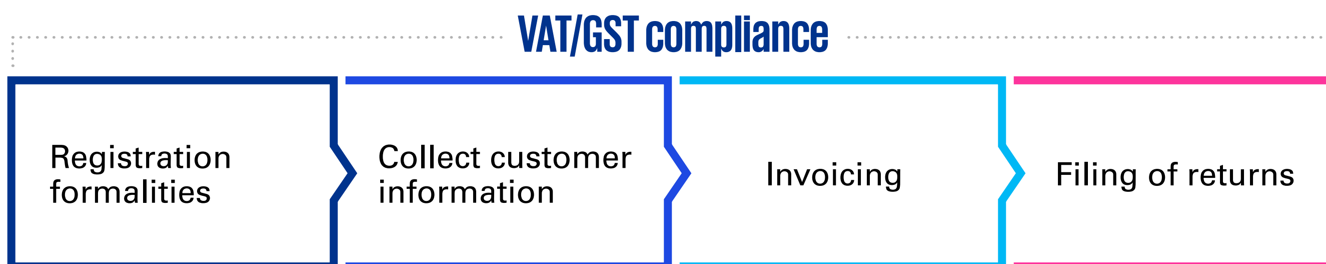
The VAT/GST iterative process

Determining a company's foreign VAT/GST obligations under the digital economy rules is an iterative process that requires taxpayers to identify the following:

- **Where:** More than 100 jurisdictions with specific digital economy VAT/GST rules
- **Liability to collect VAT/GST:** Direct sales versus intermediary (e.g., online platforms)
- **Scope of taxable transactions:** Varies greatly among jurisdictions: limited to digital services (e.g., Korea) or all services (e.g., New Zealand); certain products may be subject to a reduced rate or exemption (e.g., e-books in some European Union countries); recently some countries are broadening their rules to require including all remotely provided services
- **Customer:** In principle, only business-to-consumer (B2C) sales; however, some jurisdictions apply the rules to business-to-business sales and the definition of B2C is not always straightforward (e.g., it could include public bodies and nonprofits)

Registration thresholds vary generally from nothing (e.g., Saudi Arabia) to $100,000 (e.g., Switzerland based on worldwide income), depending on the jurisdiction.



The four corners of VAT/GST compliance

Once a foreign VAT/GST obligation is identified, a business will have to meet the following compliance requirements:

- **Register for VAT/GST:** Simplified versus full VAT/GST registration; in addition, several jurisdictions require the appointment of a local fiscal representative and/or may require specific documents to register for VAT/GST.
- **Collect customer information**: Several jurisdictions require nonresident businesses to collect certain data elements in order to determine the customer location or the final destination of goods sold. Some countries also impose additional data collection and reporting obligations on digital intermediaries.
- **Invoicing**: Some countries require nonresident businesses to comply with local, often burdensome, VAT/GST invoicing requirements.
- **Filing of returns**: The filing frequency of returns as well as the content of the returns varies greatly between jurisdictions.

Impact beyond tax

VAT/GST rules aimed at the digital economy have an impact beyond the tax:

- **Record keeping:** The location, language, and length of record keeping varies greatly between jurisdictions (e.g., up to 10 years in the European Union)
- **Legal:** Contracts and general terms and conditions need to reflect the tax obligations
- **Pricing:** VAT/GST inclusive versus VAT/GST exclusive
- **Customer experience**: Businesses must determine when and how the customer should provide his/her information without impeding the customer experience
- **Systems**: Businesses must customize their enterprise resource planning (ERP) systems and/or tax engines in order to meet these global requirements.

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Noncompliance with the VAT/GST rules aimed at the digital economy may lead to:

- US financial reporting requirements under ASC 450 and liability provisions
- Penalties and interest imposed by authorities that can be up to 200 percent of the tax due if not mitigated
- Potential criminal charges, including directors and employees being held personally liable
- Potential regulatory prohibitions by a jurisdiction resulting in business operations being terminated (e.g., Mexico blacklisting access to websites of noncompliant taxpayers)
- Closer future scrutiny of processes by the tax authorities, including sharing of information between tax authorities and tax authorities assisting with actual enforcement, either via accommodating requests or application of international agreements
- Potential damage to business relationships and reputation.

How are foreign electronic service/digital economy providers identified?

Tax authorities are increasing the enforcement of these rules to ensure that all taxpayers are compliant. In this respect, tax authorities may identify noncompliant taxpayers using a wide array of approaches, including:

- Identifying suppliers via VAT/GST registered customers and the VAT/GST deduction claims made by the customer
- Identifying suppliers via customers' expense details (i.e., not limited to VAT/GST but may be identified via income tax calculations as well)
- Customers may be encouraged to report noncompliant suppliers to the tax authorities
- Some tax authorities have formed teams/units to "surf" the internet to identify companies making supplies to local customers (individuals or VAT/GST registered businesses)
- Exchange of information with local authorities (e.g., anti-money-laundering authorities, etc.)
- Exchange of information agreements with other jurisdictions
- Information obtained by one tax authority through application of international treaties may be dispersed to other tax authorities
- To the extent a customer utilizes a credit card for payment, some tax authorities may obtain financial details from the financial institution regarding purchases made by local customers, thereby identifying foreign digital service providers.

How KPMG can assist U.S.-based companies with their global VAT/GST digital economy obligations:

- Assess their global VAT/GST footprint
- Provide recommendations for VAT/GST-efficient processes and procedures, including confirming VAT/GST requirements (e.g., invoicing, data collection, record keeping, etc.) and assisting clients with technology solutions to manage said requirements, etc.
- Provide continuous news updates on new jurisdictions implementing specific VAT/GST rules and how these rules impact particular businesses
- Assist with voluntary disclosures to foreign tax authorities
- Assist with global VAT/GST compliance, tailored to the client's specific needs
- Implementation support of VAT/GST requirements in ERP systems.

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The KPMG International Indirect Tax team

The KPMG LLP (KPMG) US-based International Indirect Tax team, which is part of the KPMG State and Local Tax practice, includes over 60 US-based professionals who have real, hands-on experience assisting clients with VAT/GST-related matters, across more than 20 jurisdictions. They have worked with companies in all sectors and in all stages of their development.

We use this significant experience to help companies identify and address their VAT/GST risks and compliance costs, plus we help them identify ways to mitigate both their absolute VAT/GST costs as well as the cash flow impact that VAT/GST has on them.

Our approach to VAT/GST services combines local resources using technology as both an enabler for VAT compliance as well as a means to help US-based companies gain visibility into their international VAT affairs.

The US team works closely with global Indirect Tax professionals from other KPMG member firms across the globe on a regular basis, enabling member firm professionals to quickly respond to and provide consistent services related to complex global VAT/GST-related issues.

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