

# WTS Tax Update for the Digital Economy

United Kingdom Digital Services Tax



## 1. Introduction

In the 2018 UK Budget, the UK Government announced the intended introduction of a Digital Services Tax "DST". The 2020 UK Budget reconfirmed this intention and despite continued pressure from the US, the law to introduce this tax was included in the Finance Act 2020. Consequently, with effect from 1 April 2020 this new tax will apply.

Furthermore, despite the UK Government applying a raft of tax fiscal measures to combat the Covid-19 outbreak there has been no announcement of any delay to this tax.

The UK Government has calculated that DST could raise approximately £1.5bn over the four years following its introduction.

## 2. Tax rate

The DST tax rate of 2% will apply to revenues from a "digital services activity" derived from UK users by taxable persons.

## 3. Taxable persons

Companies that carry on a "digital services activity" and provide those services to UK users where:

- Worldwide "digital services revenues" exceeds £500 million; and
- More than £25 million of those revenues are derived from UK users;

are taxable persons for the purposes of DST.

Digital services revenues are those revenues that arise in connection with a digital services activity.

In order to determine the figures above and, therefore, the liability to the UK DST, the thresholds must be calculated at a group level. The group consists of all entities that are included in the group consolidated accounts. Therefore, digital services revenue of all group entities counts towards the DST thresholds even where they do not have a UK taxable presence for corporation tax purposes.

## 4. Scope

The scope of UK DST is limited to revenues from the following "digital services activities":

- 1) **Providing a social media platform** – this is an online platform where the main purpose, or one of the main purposes of which is to promote interaction between users and enables content to be shared with other groups of users;
- 2) **Providing an internet search engine;** and
- 3) **Providing an online marketplace** – this is an online platform where the main purpose, or one of the main purposes of which is to facilitate the sale of goods or services by users, or to advertise or otherwise offer to other users particular goods or services for sale.

Digital services revenues will include all revenues earned by the group and connected with the above digital service activities regardless of how the business or group monetises the service.

Regulated financial and payments service providers are exempt from DST and DST is not accountable on the underlying value of the goods and services provided between users selling through an online marketplace.

## 5. Nexus rule & taxable basis

The DST is charged on UK digital services revenue obtained by taxable persons. The first £25m of a group's revenues derived from UK users will not be subject to DST.

Revenues are usually derived from UK users where a UK user uses the services. However, the following special rules apply:

- 1) In relation to a transaction on an online marketplace, where one party to that transaction is a UK user or the advertising is paid for by a UK user, all of the revenues from that transaction will be treated as derived from UK users;
- 2) Advertising revenues will be deemed UK derived when the advertising is intended to be viewed by a UK user;

- 3) Revenues arising from an on-line platform in connection with the sale or provision of UK accommodation/real estate is also expected to be UK revenue. Otherwise, for land or buildings not in the UK, the revenue will only come within the scope of DST where the recipient of the service is a UK user.

Where the revenue is deemed to be UK revenue, but the user is normally located in a country outside the UK, the guidance indicates that the revenue charged will be reduced by 50% if the user is in a country operating a similar tax to DST.

While the administrative aspects of DST will be dealt with by the "responsible member" of the group, the DST liability will be allocated based on each entities UK digital services.

In order to calculate the charge, first the "group amount" is determined by totaling the UK digital services revenues for each member of the group, deducting £25million from this amount and then applying 2% to the remainder. The relevant entity's liability is the appropriate proportion of the group amount.

However, groups will be able to opt for an alternative method of calculating the DST liability. This different calculation should be beneficial for businesses with low profit margins and should ensure that DST cannot create a loss for the business.

## 6. Formalities

The DST in respect of an accounting period is payable nine months following the end of the accounting period. In addition, the following must be complied with:

- A "responsible member" of the group must be appointed. This is the person who is nominated to fulfill the reporting obligations on behalf of the group. At this moment no general requirement to appoint a fiscal representative in the UK for non-UK resident taxpayers is installed.
- The responsible member must notify the tax authority where the threshold conditions were met in an accounting period. That notification must be made within 90 days of the end of the accounting period;
- The responsible member must submit a DST return for the relevant accounting period. The return is due within one year of the end of the accounting period.
- The responsible member must keep all records in relation to the DST return.

## 7. Penalties

Taxable persons who fail to submit their DST returns are subject to the following penalties:

- £100 if the return is filed within 3 months of the deadline or £200 in any other case;
- Where the failure to submit is a third successive failure or more, the penalties above are increased to £500 and £1,000 respectively;
- Where a person fails to submit a DST return within 18 months of the deadline, then a further penalty of 10% of the unpaid tax if the return is filed within 2 years or 20% of the unpaid tax in any other case, is due;
- Interest is due on DST which remains unpaid.

## 8. WTS Global: Next Steps

Even though the thresholds have been set such that only the largest businesses should either fall within the scope of the tax or have an actual tax liability, many businesses operating in the digital arena will need to consider the application of DST.

While for some businesses, it may be easy to identify revenue that is within the scope of the tax, for others this will represent a challenge. Therefore, changes to systems and processes may be necessary.

As with all DSTs either implemented or proposed, the intention is for it to be a temporary measure to address issues the OECD has been considering with regards to the digital economy. In fact, the UK is legislating that before the end of 2025, the UK Government must conduct a review of DST. Therefore, once a global agreement is reached on the taxation in the digital arena, the expectation is that DST will be revoked.

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