

# Taxation and E-commerce

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A D V O C A T E S

# Overview

- E-commerce and taxation - a global challenge
- Direct tax aspects
- Indirect tax aspects



# A Global Challenge

- New aspect of the global economy
- E-commerce gives rise to cross-border transactions
- Which country has the right to tax the income generated through e-commerce?



# Essential Questions

- Is e-commerce a new type of commerce or merely a more efficient method of conducting existing business?
- Should tax authorities apply the general rules to e-commerce transactions or is there need for new tax principles specifically designed for e-commerce?



# Direct Taxation



# Direct Taxation

- Companies ordinarily resident and domiciled in Malta are subject to tax in Malta on their world wide income
- E-commerce gives rise to cross-border transactions
- Malta has 50 plus double tax treaties based on the OECD Model Convention



# Double tax treaties

## Article 7 - Business Profits

*The profits of an enterprise of a contracting state shall be taxable only in that State unless the enterprise carries on business in the other Contracting state through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.*



# What is a Permanent Establishment (PE)?

*A fixed place of business through which the business of an enterprise is wholly or partly carried on.*



# Permanent Establishment

## Article 5 of the OECD Model Convention

A 'permanent establishment' shall include especially:\_

- a place of management
- a branch
- an office
- a dependent agent

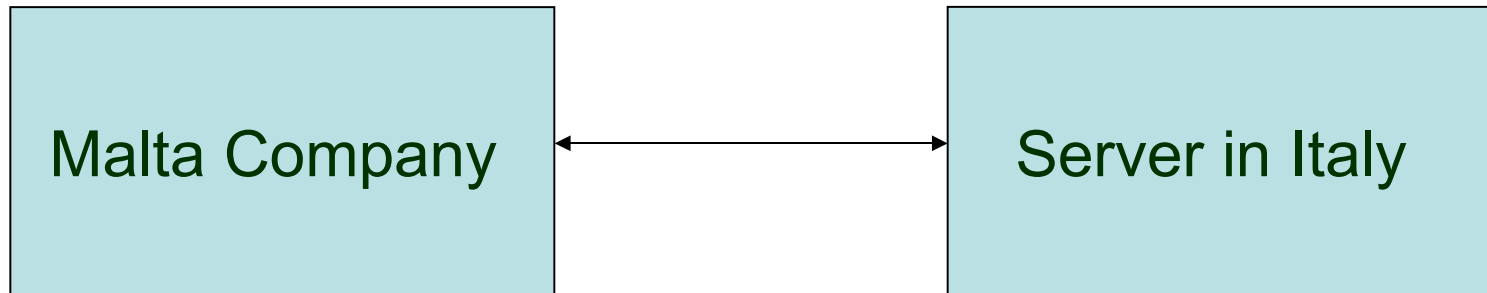


# PE and E-commerce

*‘A location where automated equipment is operated by an enterprise may constitute a permanent establishment in the country where it is situated’ – OECD Commentary Article 5 42.1 2008*



# Permanent Establishment



# Permanent Establishment

Therefore:

- A server may constitute a fixed place of establishment.
- A distinction must be made between the server and the data/software stored on that server.
- A server made available in terms of a hosting arrangement does not necessarily constitute a permanent establishment: BUT it may if the server is at the disposal of the enterprise.



# Is it a permanent establishment?

Some questions to ask yourself:

- Does the server constitute a 'fixed place'?
- Is the business of the enterprise wholly or partly carried on through the server used by the enterprise?
- Are the operations carried on through the server auxiliary or preparatory in nature vis-à-vis the enterprise's business?



# PE Elements

- Server must be in a 'fixed place' for a sufficient period of time.
- Enterprise's business must be wholly or partly carried on through the server.
- An enterprise with a server at a particular location may have a permanent establishment there even though no personnel is required at that location to maintain it.

BUT not if what is hosted / transacted through the server is auxiliary or preparatory to the enterprise's business.



# Indirect Tax



# VAT

- A general consumption tax assessed on the value added to goods and services
- Applies to all goods and services imported and sold for use or consumption in the EU
- Ultimately borne by the final consumer and generally not a cost to business
- An indirect tax paid by purchaser as part of the price



# Cross-border transactions

- Underlying principle in cross border transactions: only 1 Member State may levy VAT on a particular supply
- This right is determined by the Place of Supply Rules
- Besides determining the jurisdiction to tax, the Place of Supply Rules may determine whether a taxable person has an obligation to register in a particular jurisdiction



# Applying the Place of Supply Rules

- First Step – is it a supply of a good or a supply of a service?
- It is not always easy to determine whether a supply is a supply of a good or a supply of a service, particularly in e-commerce



# Is it a supply of a good or a supply of a service?

Example:

- A gaming company registered in Malta purchases a software package from a company established in the UK
- Is this supply of software a supply of a good or a supply of a service?



# Is it a supply of a good or a supply of a service?

*‘The supply of software and the updating thereof’ is an electronically supplied service – 3<sup>rd</sup> Schedule Item 10 VAT Act*



# ECJ case law

- The supply of standard software on a CD is considered to be a supply of a good
- The supply of standard software previously developed, put on the market and recorded on a carrier (e.g. CD) and subsequently customised to that purchaser's specific requirements would be considered as a supply of a service
- BUT – it is a supply of a service only if the customisation is neither minor nor ancillary



# Place of Supply of Services

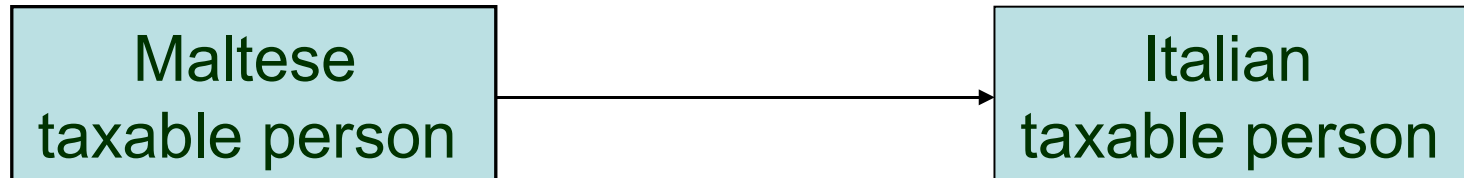


# General Rule: B2B

- Supply of a service to a taxable person acting as such – place of supply: where that person has established his business
- Supply of a service to a fixed establishment of the taxable person located elsewhere – place of supply: where that fixed establishment is located
- If no place of establishment or fixed establishment - place of supply: where he has his permanent address or usually residence



# General Rule: B2B



Assuming Italian taxable person is established in Italy VAT would be chargeable in Italy

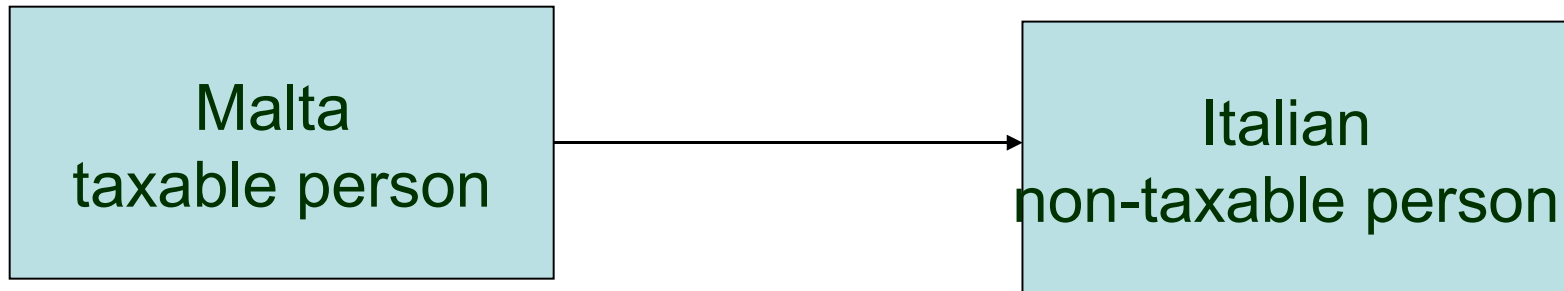


# General Rule: B2C

- Place of supply of services to a non-taxable person: where the supplier has established his business
- If the supplier makes the supply from a fixed establishment located in a place other than the place where he has established his business - place of supply: the place where the fixed establishment is located
- In the absence of a place of establishment or fixed establishment – place of supply where supplier has his permanent address or usually resides



# General Rule: B2C



Assuming that the Malta taxable person is established in Malta, place of supply would be deemed to be Malta and Maltese VAT would be charged thereon



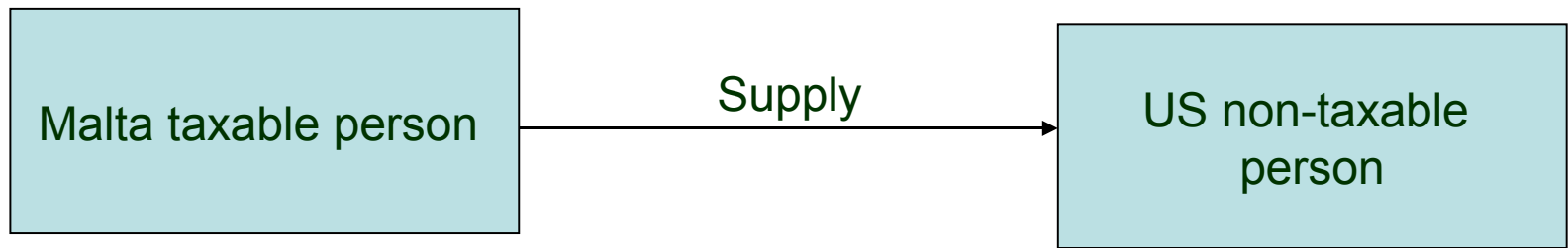
# Exceptions – ‘ESS’

“Electronically supplied services” includes services relating to:

- website supply and web-hosting
- distance maintenance of programmes and equipment,
- supply of software and updating thereof,
- supply of images, text and information,
- supply of music, films and games including games of chance and gambling games



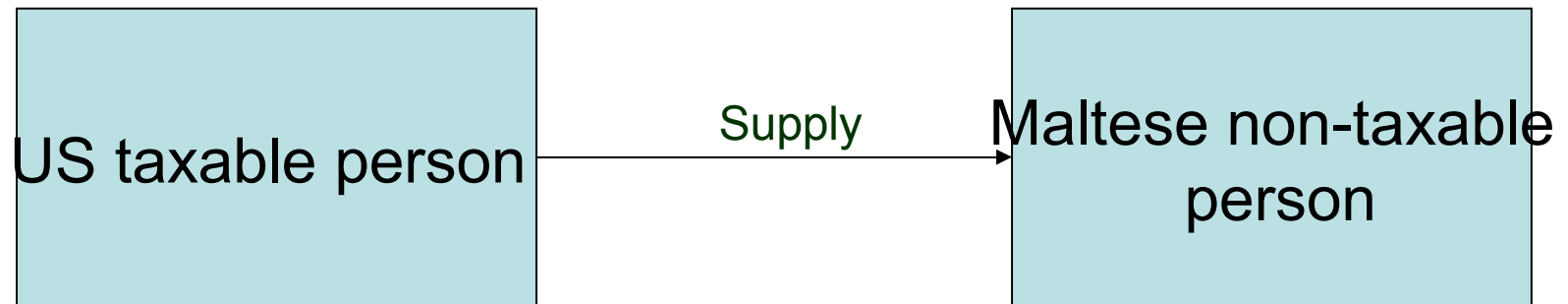
# Exception One



Place of supply is deemed to be the US - the place where the customer is established /permanently / usually resides. No VAT



# Exception Two



Assuming effective use and enjoyment is in Malta, place of supply is Malta and Malta VAT is due



# Exception Two: Obligation to Register?

A taxable person established outside the Community and providing electronically supplied services to a non-taxable person within the EU may choose the Member State in which to register, rather than having to register in each Member State in which the electronically supplied services are effectively used and enjoyed.



# Exception Two

BUT:

Said taxable person established outside the EU has the obligation to charge VAT on the services provided at the VAT rate applicable in the country of consumption, not the VAT rate of the Member State of registration



# Place of Supply of Goods\_



# Supply of a Good

- A supply of goods without transport – place of supply: where the goods are placed at the disposal of person acquiring those goods
- A supply of goods with transport – place of supply: where the goods are at the time when the transport of those goods begins



# Supply of a Good

- When the transport of goods begins outside the Community and ends in a Member State - the supply of those goods by the importer and any subsequent supply takes place in the Member State where it is imported
- Distance Sales Rules apply in the case of an intra-community supply of goods:



# Conclusion

It may be simple to do business through the internet but not to tax it .....





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