

**CONSUMPTION TAX COLLECTION MODELS IN ONLINE TRADE IN DIGITAL
GOODS**

by

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DECLARATION

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CONSUMPTION TAX COLLECTION MODELS IN ONLINE TRADE IN DIGITAL GOODS

I declare that the above dissertation/thesis is my own work and that all the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

SIGNATURE

DATE

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SUMMARY

Value-Added Tax (VAT) is an indirect tax levied on the supply of goods and services. Governments raise revenue by collecting VAT in order to facilitate the maintenance of basic services for the general population.

Challenges in VAT collection arise from the supply of digital goods to consumers by means of e-commerce transactions. Moreover, VAT collection mechanisms that do not adequately cater for the collection of VAT on the supply of digital goods results in under-taxation and VAT fraud.

The use of an intermediary is a more effective method of collecting VAT on e-commerce transactions since it shifts the compliance burden away from foreign online businesses.

VAT legislation should be amended to cater for the collection of VAT by intermediaries.

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LIST OF ABBREVIATIONS

ABN	Australian Business Number
Apps	Applications
ARN	ATO Reference Number
ATO	Australian Tax Office
AU	African Union
B2A	Business to Administration
B2B	Business to Business
B2C	Business to Consumer
C2A	Consumer to Administration
C2B	Consumer to Business
C2C	Consumer to Consumer
CA	Certification Authority
CRA	Canadian Revenue Authority
EDP	Electronic Distribution Platform
EU	European Union
GDP	Gross Domestic Product
GST	General Sales Tax
HST	Harmonised Sales Tax
IMSI	International Mobile Subscriber Identity
IRAS	Inland Revenue Authority of Singapore
ISP	Internet Service Provider
ITZ	Indirect Tax Zone

MCC	Mobile Country Code
MOSS	Mini One Stop Shop
NAB	National Australian Bank
OECD	Organisation for Economic Cooperation and Development
PC	Personal Computer
PKI	Public Key Infrastructure
PST	Provincial Sales Tax
SAIT	South African Institute of Tax Practitioners
SADC	Southern African Development Community
SARS	South African Revenue Service
SIM	Subscriber Identity Module
SME	Small or Medium-Sized Enterprises
VAT	Value Added Tax

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CHAPTER 1

INTRODUCTION

1.1 BACKGROUND TO RESEARCH PROPOSAL

The Value Added Tax (VAT) collection models remains one of the most spoken of and highly debated subjects concerning consumption taxes in an electronic commerce (e-commerce)¹ context from tax administrators and businesses standpoint.²

The role of tax administrators is to enforce, collect, and administer VAT.³ And with the continuous increase in digital sales through e-commerce transactions, it is imperative for governments to find appropriate collection mechanisms for the collection of VAT.

The rise of the digital economy⁴ has seen an unprecedented growth in e-commerce transactions and with that comes future developments that will require constant observations so as to determine the impact it will have on tax systems.⁵ The speedy technological advancements attributed to the digital economy has brought about new emerging markets.⁶

Goods and services are taxed either directly or indirectly. When it comes to indirect taxation, VAT is levied on the consumption activities of a taxpayer and value is added to

¹ Wigard, R.T. (1997) *Electronic commerce: definition, theory and context the information society* 13 at 6 defines 'e-commerce' as: 'the seamless application of information and communication technology from its point of origin to its endpoint along the entire value chain of business processes conducted electronically and designed to enable the accomplishment of a business goal. These processes may be partial or complete may encompass business to business as well as business to consumer and consumer to business transactions.'

² Basu, S. (2007) *Global perspectives on e-commerce taxation law* (London: Ashgate) at 288.

³ Bruce, D. Fox, W. Murray, M. (2003) 'To tax or not to tax? The case of electronic commerce' *Contemporary Economic Policy* volume 21(1): 33. See also Basu, S. (2007) *Global perspectives on e-commerce taxation law* (London: Ashgate) at 288.

⁴ The OECD defines the 'digital economy' as: "markets based on digital technologies that facilitate the trade of goods and services through e-commerce." See OECD (2013). *The Digital Economy* at 5. Available at <http://www.oecd.org/daf/competition/The-Digital-Economy-2012.pdf>. Accessed 25 October 2017.

⁵ OECD. (2014). *Addressing the tax challenges of the digital economy* at 12. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

⁶ OECD. (2014). *Addressing the tax challenges of the digital economy* at 12. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

the price of the goods or services sold.⁷ The tax on these goods and services can be categorised into sales tax, import and export duties, excise tax and VAT.⁸

Consumption taxes⁹ can be categorized into VAT and General Sales Tax (GST). The GST system was implemented for the first time in South Africa back in 1978. Under the system, an initial general rate of four per cent tax was charged on the sale to the final consumer.¹⁰

GST was deemed to be defective partly because it could only be collected at a single stage in the collection process.¹¹ This resulted in significant loss of revenue for the government.¹² Consequently, VAT was then introduced in South Africa in 1991.

1.2 PROBLEM STATEMENT

The growth of the digital economy has seen consumers buy digital goods such as electronic books (e-books), games and music effortlessly at the click of a button. Some of the reasons why consumers prefer to purchase digital goods online include the ease at which products are readily available; having a larger online market of digital goods; and being able to purchase digital goods at considerably cheaper prices.¹³

In comparison, tangible goods are more expensive as they incur transaction costs for its upkeep and distribution.¹⁴ With that in mind, consumers may reasonably conclude that it is worthwhile to purchase intangible goods instead of tangible goods.¹⁵

⁷ Basu, S. (2007) *Global perspectives on e-commerce taxation law* (London: Ashgate) at 55.

⁸ Basu, S. (2007) *Global perspectives on e-commerce taxation law* (London: Ashgate) at 55.

⁹ See paragraph 2.2 below.

¹⁰ Silver, M. & Beneke, C. (2015). *Deloitte VAT Handbook* 10th ed at 3.

¹¹ Silver, M. & Beneke, C. (2015). *Deloitte VAT Handbook* 10th ed at 4.

¹² Silver, M. & Beneke, C. (2015). *Deloitte VAT Handbook* 10th ed at 4.

¹³ Gordon, A. & Bhowan, K. (2005). Factors that influence online shopping behaviour *Alternation* 12(1): 150.

¹⁴ European Parliament (2011). *Consumer behaviour in a digital environment* at 29. Available at [http://www.europarl.europa.eu/RegData/etudes/etudes/join/2011/464441/IPOL-IMCO_ET\(2011\)464441_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/etudes/join/2011/464441/IPOL-IMCO_ET(2011)464441_EN.pdf). Accessed 25 October 2017.

¹⁵ European Parliament (2011). *Consumer behaviour in a digital environment* at 29. Available at [http://www.europarl.europa.eu/RegData/etudes/etudes/join/2011/464441/IPOL-IMCO_ET\(2011\)464441_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/etudes/join/2011/464441/IPOL-IMCO_ET(2011)464441_EN.pdf). Accessed 25 October 2017.

The online cross-border purchase of digital goods by consumers creates challenges for VAT collection and tax authorities.¹⁶ The challenges are compounded by the seemingly lack of international guidelines on the implementation of VAT collection mechanisms on the online cross-border trade of digital goods.¹⁷

The current lack of international guidelines for the collection and remittance of taxes is even more detrimental for small and medium business enterprises in that it perpetuates revenue deficits and escalates compliance costs.¹⁸ Governments face the unenviable prospect of losing significant revenue in an era where e-commerce transactions, by nature, creates a niche market for the purchase of a large quantity of inexpensive digital goods.¹⁹ The online purchase of digital goods has the propensity to generate tax liability which leads to a notable rise in administrative costs for tax authorities.²⁰

Until recently, South Africa's tax laws did not match the rise of the digital economy.²¹ The advent of the Taxation Laws Amendment Act 43 of 2014 has brought about change in that electronic services, as defined, supplied by foreign businesses to South African consumers are now subject to VAT.

Legislation, in the form of the Value Added Tax Act 89 of 1991 (VAT Act) (as amended), currently provides for registration and the reverse-charge mechanism as a means to collect VAT. Online transactions involving the supply of digital goods by foreign businesses to South African consumers are now susceptible to VAT.

¹⁶ OECD. (2014). *Addressing the tax challenges of the digital economy* at 18. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

¹⁷ OECD. (2014). *Addressing the tax challenges of the digital economy* at 18. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

¹⁸ OECD. (2014). *Addressing the tax challenges of the digital economy* at 18. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

¹⁹ OECD. (2014). *Addressing the tax challenges of the digital economy* at 18. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

²⁰ OECD. (2014). *Addressing the tax challenges of the digital economy* at 18. Available at <http://www.oecdilibrary.org/docserver/download/2314251e.pdf?expires=1447015283&id=id&accname=guest&checksum=5748F58F355A1981B097C2E1AB83CC5D>. Accessed on 8 November 2015.

²¹ De Wet, C. (2015) Tax and the digital economy: Value Added Tax *Tax Breaks* Newsletter 353: 4.

Van Zyl and Schulze submit that the collection of VAT on the supply of digital goods by means of the registration mechanism is ineffectual if there is no collaboration between existing states.²²

Furthermore, there are various challenges that arise as a result of the use and implementation of the registration collection mechanism.²³ Thus, the application of the registration mechanism is a burdensome form of VAT collection for tax authorities.²⁴

The result of an inefficient and inadequate VAT collection mechanism in cross-border transactions may lead to the erosion of the tax base and VAT fraud.²⁵

Thus, this study examines the different VAT collection models in order to determine if the current registration and reverse-charge mechanisms are effective VAT collection mechanisms from a South African perspective.

1.3 RESEARCH OBJECTIVES

The aim of this study is to answer the following research questions: Are the current VAT collection mechanisms in the South African VAT Act sustainable in light of the continuous rise in technological advancements in the digital economy?

This study will also look to answer the following questions:

- What are the problems posed by e-commerce and what are the ways in which these problems can be assessed?
- What are the collection mechanisms currently implemented in the European Union (EU) and other foreign jurisdictions?

²² Van Zyl, S.P. & Schulze, W.G. (2014). The collection of value added tax on cross-border digital trade – part 2: collection by banks *Comparative and International Law Journal of Southern Africa* 47: 317.

²³ See paragraph 3.2.4 below.

²⁴ Van Zyl, S.P. & Schulze, W.G. (2014). 'The collection of value added tax on cross-border digital trade – part 1: registration of foreign vendors *Comparative and International Law Journal of Southern Africa* 47: 175.

²⁵ Alfredo, J. (2012) 'Applying VAT to international trade – The challenge of economic globalisation: The challenge for tax administrations' *First meeting of the OECD global forum on VAT* at 54. See also Van Zyl, S.P. & Schulze, W.G. (2014). The collection of value added tax on cross-border digital trade – part 1: registration of foreign vendors *Comparative and International Law Journal of Southern Africa* 47: 184.

- What is the most effective and efficient collection mechanism that can be adopted in South Africa?
- Is there a cohesive and consistent system of identification of the parties involved in electronic transactions?
- Are there any compliance verification and penalties available where foreign businesses do not adhere to the South African VAT Act?
- Does South Africa have adequate infrastructure for the collection of taxes garnered through electronic transactions?

1.4 RESEARCH METHODOLOGY

This study is conducted by means of a literature or qualitative approach. Various sources are used to carry out this study including legislation with particular emphasis on the South African VAT Act, journal articles, published reports, books, internet sources and existing statistics.

These sources are used interchangeably to formulate the answers to the research question and objectives above.

1.5 HYPOTHESIS

Effective VAT collection mechanisms are essential and the different collection models must be explored to develop a mechanism unique to the South African tax system having regard to the growth of the digital economy.

It is submitted that the VAT Act should be amended in order to implement a more effective and less strenuous mechanism in order to collect VAT on electronic supplies.

1.6 LIMITATIONS OF THIS STUDY

This study is done with the viewpoint that there is currently a dearth of litigation or case law relating to VAT collection mechanisms and the digital economy in South Africa. This is highlighted in Chapter 2 of this study.

This study is a mini dissertation and will only look at the possibility of implementing an alternative method of collecting VAT on e-commerce transactions from a South African perspective rather than from a broader international perspective.

For instance, Chapter 4 of this study will restrict the discussion to VAT collection mechanisms in the European Union and a few other foreign jurisdictions. This study will not look at issues pertaining to VAT fraud, place of supply rules in detail, key principles including source, residence and physical presence. Legal issues such as the constitutional right to privacy and contracts concluded over the internet are beyond the scope of this study.

1.7 CHAPTER OVERVIEW

Chapter 1: Introduction

The objective and outline of this study is established along with the research problem.

Chapter 2: VAT collection mechanisms for e-commerce transactions in South Africa

The VAT collection mechanisms that are prescribed by the VAT Act are discussed.

Chapter 3: How VAT can be collected on B2C transactions – lessons from the OECD

The different VAT collection mechanisms as prescribed by the Organisation for Economic Cooperation and Development (OECD) are discussed. The recommendations adopted by the OECD in relation to the collection mechanisms will also be discussed.

Chapter 4: VAT collection on B2C e-commerce transactions in foreign jurisdictions

This chapter will discuss the current VAT collection mechanisms on e-commerce transactions in the EU (since VAT originates from Europe) and other foreign jurisdictions.

Chapter 5: Recommendations and Conclusions

In this chapter, conclusions pertaining to chapters 2, 3, and 4 are drawn. In view of this study, recommendations are made so that further research may be conducted.

CHAPTER 2

VAT COLLECTION MECHANISMS FOR E-COMMERCE TRANSACTIONS IN SOUTH AFRICA

2.1 INTRODUCTION

VAT is an important source of revenue for governments around the world. In South Africa, VAT accounts for 26.3 per cent of total revenue.²⁶ This represents more than a quarter of total revenue collection in South Africa. It follows then that VAT is a significant source of revenue for the South African government.

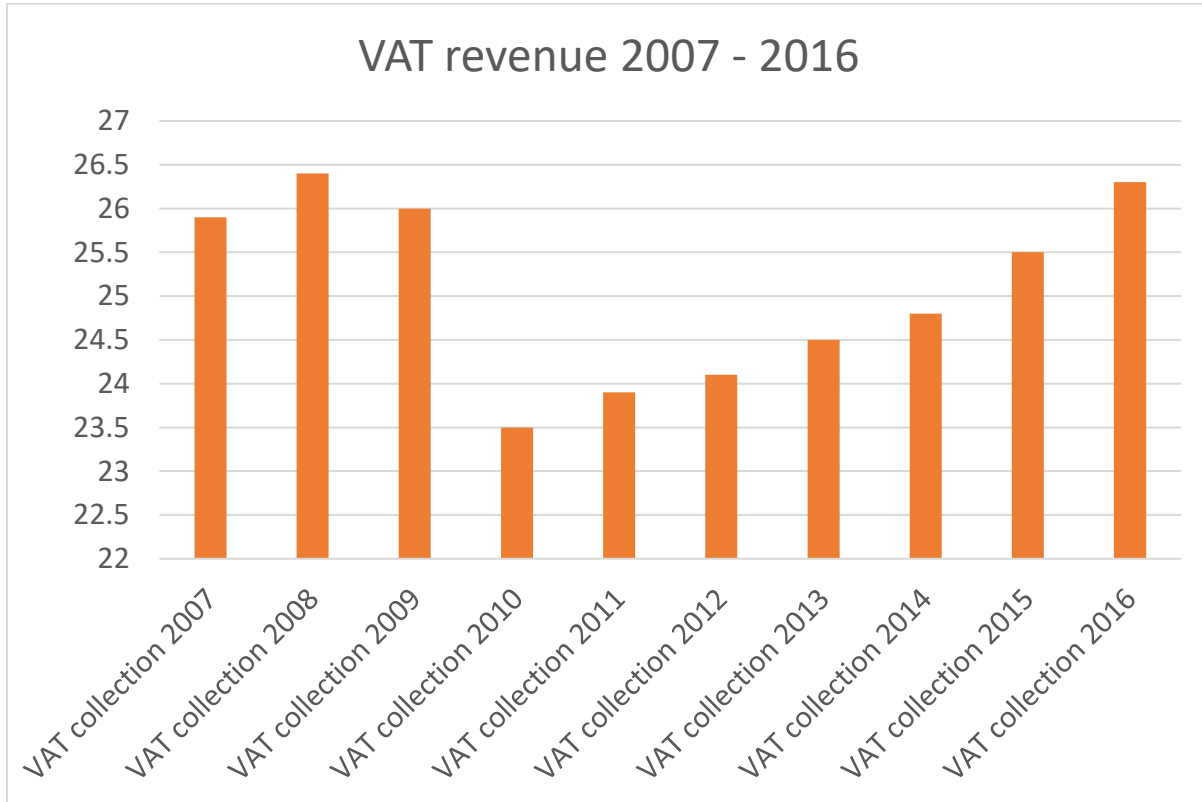


Figure 1 Illustrates the percentage of VAT collected by the South African Revenue Service (SARS) from 2007 – 2016. Adapted from 2016 SARS Tax statistics.

²⁶ This is based on the 2016 SARS Tax statistics. Available at <http://www.sars.gov.za/AllDocs/Documents/Tax%20Stats/Tax%20Stats%202016/Tax%20Stats%202016%20Full%20document%20web.pdf>. Accessed on 26 April 2017.

The above graph illustrates the amount of VAT collected by SARS from the year 2007 until 2016. The graph also shows steady increments of VAT revenue collection from the year 2010 to the year 2016. The increase may be attributed to various factors, not least of which include improved tax compliance; the rise of e-commerce; and an increased number of imports.²⁷

Since VAT is an important source of government Gross Domestic Product (GDP) in South Africa, VAT collection by necessary implication becomes an important aspect of the fiscus. For if a state does not have the appropriate tax collection mechanisms, tax authorities will find it difficult to collect taxes.

There is a correlation between an adequate and efficient tax collection mechanism and revenue collection. This correlation is ideal for a government as possessing a tax collection mechanism that is progressive and efficient results in a larger chunk of revenue available for expenditure that will be allocated to basic services like infrastructure, health, and education, to mention but a few.

The need for an improved, modernized and efficient tax collection mechanism has been heightened by the ongoing growth of e-commerce. E-commerce creates a seamless, borderless, niche market on the internet where parties transact with each other without necessarily knowing each other's identity or location.

The inability to determine the identities and locations of parties during e-commerce transactions poses difficult challenges for tax authorities. The inability to determine the party's identity or location surmises an inability to pinpoint the precise location of the consumption of goods or services. The effect is that tax authorities are not able to collect the necessary tax that would have been due to them.

This chapter critically analyses the VAT collection mechanisms in South Africa. The analysis will indicate whether the current mechanisms are viable, sustainable and efficient considering the growth of e-commerce. This chapter attempts to answer the

²⁷ SARS (2016). 2016 SARS Tax statistics at 7. Available at <http://www.sars.gov.za/AllDocs/Documents/Tax%20Stats/Tax%20Stats%202016/Tax%20Stats%202016%20Full%20document%20web.pdf>. Accessed on 26 April 2017.

question; does South Africa have adequate infrastructure to collect taxes garnered through e-commerce transactions? Moreover, this chapter also attempts to establish whether the VAT Act has compliance verification mechanisms and penalties when foreign businesses do not adhere to the VAT Act.

An understanding of the legal principles of VAT is necessary to answer the questions posed above.

2.2 WHAT IS VAT?

VAT is a form of consumption tax. The term 'consumption' refers to where goods or services are used, consumed, or enjoyed. A person who uses or enjoys these goods or services is known as a consumer. It is the consumer who ultimately bears the onus of paying the tax to the tax authorities.²⁸

VAT is not necessarily a tax on value added, as its name seems to suggest.²⁹ But rather, it is a multistage tax that is collected at every stage of production.³⁰ During the stages of production, each person or business levies VAT on the production and distribution of goods and services.³¹

VAT may also be described as an indirect tax because the tax is levied on goods and services during production before reaching the final consumer who bears the tax.³² When a consumer purchases goods at a counter, the goods will generally be inclusive of VAT unless the goods are exempt from VAT or are zero rated.

²⁸ Silver, M. & Beneke, C. (eds) (2015). *Deloitte VAT Handbook* 10th ed. LexisNexis at 3.

²⁹ Ebrill, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 1. See also Steyn, T. (2010). *VAT and E-commerce: Still looking for answers?* South African Mercantile Law Journal at 232.

³⁰ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 63. See also Cnossen, S. (1989). Broad-based Consumption Taxes: VAT, RST, or BTT? *Australian Tax Forum* 6 at 393. See also De Koker, A. & Kruger, D. (2015). *Value-Added Tax in South Africa: Commentary* at 2.1. See also Ebrill, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 2.

³¹ De Koker, A. & Kruger, D. (2015). *Value-Added Tax in South Africa: Commentary* at 2.1. See also Steyn, T. (2010). *VAT and E-commerce: Still looking for answers?* South African Mercantile Law Journal at 232. See also Schenk, A. & Oldman, O. (2007). *Value Added Tax: A comparative approach* Cambridge University Press at 17. See also m, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 1.

³² Schenk, A. & Oldman, O. (2007). *Value Added Tax: A comparative approach* Cambridge University Press at 5. See also Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 63.

VAT is an indirect tax as it does not affect a person's estate to the extent that it does not reduce a person's income.³³ This contrasts with income tax which diminishes a person's estate.

It follows that the efficacy of VAT collection is largely dependent on the consumer who bears the tax liability.

2.3 THE CHALLENGES THAT E-COMMERCE POSES TO VAT COLLECTION

Before analysing the various challenges that e-commerce poses to VAT collection, a brief discussion of the various types of e-commerce ensues.

2.3.1 Types of e-commerce

One of the characteristics of e-commerce is that it is virtual. This means that it does not exist physically. Instead, e-commerce occurs in the borderless realm of the Internet. Products sold over the Internet include tangible products (such as books), intangible products (music); and services (online advertising).³⁴

E-commerce can be categorized into different categories. These include:

- **Business to Consumer (B2C):** this relates to transactions between a business, such as a retail store, and a consumer.³⁵ For instance, a business that sells tangible or intangible goods and services to a consumer over the Internet.³⁶ B2C transactions

³³ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 55.

³⁴ Azam, R. (2007). E-commerce taxation and cyberspace law: the integrative adaptation model. *Virginia journal of law & technology* 12(5): 7.

³⁵ Pirooska, R. (2014). Taxation of electronic commerce – are the current rules appropriate to tax electronic commerce? *Studia Iuridica Auctoritate Universitatis Pecs* 152: 167. See also Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 59.

³⁶ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 101. See also Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 59.

have grown to include services such as online gambling, online banking, health services information and real estate sites.³⁷

- Business to Business (B2B): this relates to instances where businesses transact with each other.³⁸ A good example would be where a manufacturer of hardware sells its products to a retailer.³⁹
- Business to Administration (B2A): these refer to transactions where businesses or companies use the Internet to provide goods or services to its employees.⁴⁰ Examples of the services that companies offer their employees are online insurance policies or online supply requests.⁴¹
- Consumer to Business (C2B): In this category, a consumer sells products or services to a business and the business pays the consumer.⁴² An individual may offer to sell their music or a book that they have written to a company over the internet.⁴³
- Consumer to Consumer (C2C): this category involves transactions where a consumer purchases goods or services from another consumer through an independent third party.⁴⁴ For instance, if a consumer goes online to purchase a

³⁷ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 101. See also Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 59.

³⁸ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 60. See also Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 100. See also Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

³⁹ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 100.

⁴⁰ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 101. See also Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

⁴¹ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 101.

⁴² Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 101. See also Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

⁴³ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 102. See also Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

⁴⁴ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 102. See also Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 60 – 61. See also Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

motor vehicle that is owned by another consumer. This transaction is facilitated online via a third party wherein the latter charges a commission on the transaction.⁴⁵

- Consumer to Administration (C2A): this category involves transactions between a consumer and public administration.⁴⁶ For instance, when a consumer facilitates payment of health services to an administrator.⁴⁷

This study focuses on B2C e-commerce transactions. The emphasis is on the sale of digital goods by foreign suppliers to South African consumers.

2.3.2 E-commerce and its challenges

As alluded to above, the nature of e-commerce is borderless or non-territorial. E-commerce removes the traditional wholesale distributor or retail outlet that would otherwise have identified the seller and the buyer.⁴⁸ With e-commerce, tax authorities find it difficult to determine the type of transaction; the place of consumption; and the parties to the transaction.

Another challenge posed by e-commerce is the erosion of the tax base.⁴⁹ The base of tax is the platform or source on which tax is built.⁵⁰ It goes without saying that the bigger the tax base, the more revenue will be collected.⁵¹ Basu argued that a tax base is constrained by its exclusions and the general limitations a tax possesses.⁵²

The ability of governments to raise revenue has been curtailed by e-commerce.⁵³ If the tax base is eroded, governments are not able to collect the necessary taxes that they would have collected had there been no base erosion. A loss in revenue for

⁴⁵ Nemat, R. (2011). Taking a look at different types of e-commerce. *World Applied Programming* 1(2): 102. See also Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 60 – 61.

⁴⁶ Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

⁴⁷ Fernandes, J. (2014). *Types of e-commerce*. Available at <http://bloomidea.com/en/blog/types-e-commerce>. Accessed on 2 May 2017.

⁴⁸ Jones, R. & Basu, S. (2002). Taxation of Electronic Commerce: A developing problem. *International Review of law computers & technology* 16(1): 36.

⁴⁹ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 175.

⁵⁰ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 175.

⁵¹ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 175.

⁵² Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 175.

⁵³ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 178.

governments means there is less money available for expenditure. Services such as health care, infrastructure, education and job creation are then allocated a reduced budget for expenditure.

E-commerce transactions that take place over the internet are paperless. They occur online outside the reach of tax authorities. This is challenging for tax authorities as they are not able to trace these transactions. Tax authorities do not have the budget, the time, or the resources to monitor every transaction that takes place on the internet. Transactions that are untraceable escape the VAT net and result in a loss of revenue.

The inability of tax authorities to identify parties to online transactions, handicaps their ability to determine whether or not the transaction is indeed susceptible to VAT. Enforcement of VAT legislation becomes a challenge for tax authorities.

Tax authorities are not able to conduct audits on businesses and consumers if the former cannot verify the identity of the parties and the place of consumption. This adversely affects the role of tax authorities in VAT collection.

The Internet has enabled consumers to buy digital goods and services from around the world. Invariably, this has led to an increase in international trade. Different countries have different VAT legislations. These legislations have different tax rules on how to implement VAT in their respective jurisdictions. This implementation challenge is compounded by the internet as a particular country will have its own tax laws that address a specific aspect of VAT collection only to realize that a different country has different laws that address the same issue.⁵⁴

2.4 THE COLLECTION OF VAT ON B2C TRANSACTIONS IN SOUTH AFRICA

It is imperative to analyse the VAT Act in order to establish how VAT is collected in South Africa. Particular emphasis is placed on how VAT is collected on B2C transactions in view of the recent amendments to the VAT Act. An understanding of the

⁵⁴ Basu, S. (2004). To tax or not to tax? That is the question? Overview of Options in Consumption taxation of e-commerce *Journal of Information, Law and Technology* (1):4.

VAT Act is necessary in order to establish where the challenges lie. An exposition of the VAT Act will thus follow.

Upon completion of the exposition, challenges are identified, and possible remedies are highlighted in the final chapter in an attempt to ameliorate the principles of VAT collection on e-commerce transactions in the South African context.

2.4.1 Analysis of the VAT Act

2.4.1.1 The levying provision

In order to impose VAT on a specific transaction, it is necessary to determine if that transaction falls within the realm of the VAT Act. The charging provision that determines whether a transaction is susceptible to VAT is Section 7(1)(a) of the VAT Act.

In terms of Section 7(1)(a) VAT is levied on the supply of goods and services by a vendor in the course of furtherance of his or her enterprise; on the importation of goods into South Africa and on the supply of imported services into South Africa.⁵⁵

It follows that transactions that fall within the ambit of this provision 'shall' be levied with VAT at fourteen per cent.⁵⁶ The use of the word 'shall' in this section of the Act suggests that the compliance of this provision is peremptory and thus obligatory.

Section 7(2) of the VAT Act states that a vendor shall be responsible for paying tax when the latter supplies goods and services for the furtherance of his or her enterprise. Where a person imports goods to South Africa, that same person shall be responsible for paying tax. The recipient of imported services is liable for tax and shall pay tax to the relevant tax authorities.⁵⁷

This study focuses on the importation of services into South Africa and the supply of services by a vendor in the furtherance of their enterprise.

⁵⁵ Section 7(1) of the VAT Act.

⁵⁶ Section 7(1) of the VAT Act.

⁵⁷ Section 7(2) of the VAT Act.

2.4.2 THE SUPPLY OF SERVICES

2.4.2.1 Where is the supply of services?

South Africa adopts the destination principle as a justification to impose VAT. In terms of this principle, economic activity should be taxed in the jurisdiction where it is consumed.⁵⁸ This means that the South African VAT Act applies to South African residents and to the supply of services to South African residents by foreign suppliers in other jurisdictions.⁵⁹ However, it is often difficult for tax authorities to establish that a supply of services occurred within the borders of South Africa due to the nature of e-commerce transactions. Hence, the concept of 'supply' has become an important concept for tax authorities.⁶⁰

It is paramount to establish where the supply takes place as this determines which jurisdiction will collect the necessary tax.⁶¹ This is also relevant in the South African context because if SARS can establish where the supply takes place, it will be able to significantly bridge the gap in VAT collection on e-commerce transactions.

For instance, if a person imports services into South Africa for personal use, that person should account for VAT on that transaction to SARS.⁶² The foreign supplier of the imported services in this instance does not charge VAT on the transaction.⁶³ If neither party to the transaction accounts for VAT, then revenue due to SARS goes uncollected.

It follows that having explicit place of supply rules, particularly in cases of e-commerce transactions, enables tax authorities to impose VAT on transactions since the place of

⁵⁸ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 61. See also Cockfield, A., Hellerstein, W., Millar R, Waerzeggers, C. (2013). *Taxing Global Digital Commerce* Kluwer Law International at 68. See also Van der Merwe, B. A. (2003). VAT and e-commerce *South African Mercantile Law Journal* 15(3): 374. See also Steyn, T. (2010). VAT and E-commerce: Still looking for answers? *South African Mercantile Law Journal* at 239.

⁵⁹ <https://quaderno.io/blog/digital-taxes-around-world-know-new-tax-rules/>. Accessed on 1 April 2017. See also Silver, M & Beneke, C. (eds) (2015). *Deloitte VAT Handbook* 10th ed. LexisNexis at 25.

⁶⁰ Available at <https://cleartax.in/s/place-of-supply-gst>. Accessed on 6 June 2017.

⁶¹ Van der Merwe, B. A. (2003). VAT and e-commerce *South African Mercantile Law Journal* 15(3): 374.

⁶² Section 14 read with Section 7(1)(c) of the VAT Act.

⁶³ National Treasury (2013). *Explanatory memorandum on the taxation laws amendment bill 2013* at 88. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/ExplMemo/LAPD-LPrep-EM-2013-02%20-%20Explanatory%20Memorandum%20Taxation%20Laws%20Amendment%20Bill%202013.pdf>. Accessed on 22 May 2017.

supply rules will establish which transactions will be deemed to take place in South Africa.⁶⁴

Rooi correctly states that if the place of supply is unidentifiable, then it becomes impractical, ineffective and inefficient to implement the relevant legislation.⁶⁵ The conclusion seems to be that there needs to be appropriate mechanisms or provisions in the VAT Act that will establish the place of supply rules for e-commerce transactions.

2.4.2.2 Services

Services are defined in the VAT Act as the “*granting, assignment, cession or surrender of any right or the making available of any facility or advantage.*”⁶⁶ This definition is far-reaching and encompasses all commercial activities that are not defined as a supply of goods for purposes of the VAT Act.⁶⁷

It follows that digital goods do not form part of the definition of ‘goods’ but as ‘services’ for purposes of the VAT Act. SARS has accepted that digital goods form part of the definition of ‘services’ and a sub category of services (electronic services) has been enacted in the VAT Act in this regard.⁶⁸

The VAT Act merely defines ‘electronic services’ as the services prescribed by the Minister of Finance in the Regulations (researcher’s emphasis).

⁶⁴ Kruger, D. & Moss-Holdstock, C. (2014). The South African VAT Implications for Foreign Suppliers of Electronic Services *Business Tax and Company Law Quarterly* 5(2): 15.

⁶⁵ Rooi, T. (2015). *An evaluation of the practical application of the South African VAT legislation on electronic services: A case study* Unpublished MCom mini-dissertation (North West University of South Africa) at 80.

⁶⁶ Section 1 of the definition of ‘services’ in the VAT Act.

⁶⁷ Silver, M. & Beneke, C. (eds) (2015). *Deloitte VAT Handbook* 10th ed. LexisNexis at 23. See also Meiring, M. (2013). *A critical evaluation of proposed methods to collect value-added tax on electronically supplied services.* Unpublished MCom dissertation (University of Pretoria) at 12. See also SARS Interpretation Note 70 at 13. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-IN-2013-03%20-%20IN70%20Supplies%20made%20for%20no%20consideration.pdf>. Accessed 28 October 2017.

⁶⁸ Section 1 of the definition of ‘electronic services’ in the VAT Act.

Regulation R221 of the South African Government Notice 37489 dated 28 March 2014, with an effective date of 1 June 2014 (the Regulations), lists the services that are classified as 'electronic services' for purposes of the VAT Act.⁶⁹ These include:

- Educational services where the supplier is not regulated by an educational authority in the country. The services include distance teaching programmes, educational webcasts, internet-based courses or education programmes and webinars.
- Games including electronic games, interactive games and electronic betting or wagering.
- Internet-based auction services.
- The digitised contents of any book or electronic book (e-books).
- Audio visual content (any set of moving visual images or other visible signals) and the right to view such content.
- Still images and the right to view such images.
- Music including audio clips, broadcasts not simultaneously broadcast over any conventional network in South Africa, jingles, live streaming performances, ringtones, songs, sound effects and the right the listener has to listen to any of these items.
- Subscription services to any blog, journal, magazine, newspaper, game, internet-based auction service, periodical, publication, social network service, webcast, webinar, website, web application or web series.⁷⁰

2.4.2.3 Critical evaluation of the definition of 'electronic services'

According to SARS, the definitions of the 'goods' and 'services' are expansive to ensure that all economic transactions are included in the tax base.⁷¹ However, a closer

⁶⁹ Silver, M & Beneke, C. (eds) (2015). *Deloitte VAT Handbook* 10th ed. LexisNexis at 30. See also <http://www.taxindaba.co.za/img/downloads/presentations/1.Foreign%20VAT%20Compliance%20Suzanne%20vd%20Merwe.pdf>. Accessed on 29 March 2017.

⁷⁰ Government Notice Number R221: Electronic Services Regulations. Silver, M & Beneke, C. (eds) (2015). *Deloitte VAT Handbook* 10th ed. LexisNexis at 30. See also <http://www.taxindaba.co.za/img/downloads/presentations/1.Foreign%20VAT%20Compliance%20Suzanne%20vd%20Merwe.pdf>. Accessed on 29 March 2017.

inspection of the definition of ‘electronic services’ suggests that other services have been excluded from the definition of electronic services. The definition does not include services like cloud computing,⁷² video streaming,⁷³ applications (apps),⁷⁴ game streaming, multi-player gaming and online advertising services.⁷⁵

This problem may be illustrated by the following example:

Example 1

Mary, a South African resident, has recently started her own business. She would like to advertise her products on the Internet. She pays Company X, an online advertising company, to enable her to advertise her products online. Company X provides Mary with advertising services.

Assume that Company X is carrying on an enterprise in South Africa and is duly registered as a vendor in South Africa because it also supplies digital music to South African customers.

In this instance, although Company X is a vendor, there is no obligation on it to account for VAT to SARS on the supply of advertising services because it does not supply ‘electronic services’ as defined to Mary.⁷⁶ This equates to a loss of revenue for SARS.

The challenge is compounded when different jurisdictions define electronic services differently. For instance, the EU defines ‘electronically supplied services’ as those services which are “*delivered over the internet or an electronic network and the nature of which renders their supply automated and involving minimal human intervention.*”⁷⁷

The EU published a list of what it deems to be electronically supplied services. The list

⁷¹ SARS Interpretation Note 70 at 12. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-IN-2013-03%20-%20IN70%20Supplies%20made%20for%20no%20consideration.pdf>. Accessed 28 October 2017.

⁷² Goetsch, K. (2014). *ECommerce in the Cloud* 1st edition O’Reilly Media Inc at 55. According to Goetsch, cloud computing is “any service delivered over the Internet.” This service includes online photo sharing or web-based email.

⁷³ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 155.

⁷⁴ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 50. According to Laudon and Traver, an app is software application.

⁷⁵ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 382. Online advertising includes displaying banners, games, classifieds and sponsorships.

⁷⁶ Section 7(1)(a) of the VAT Act read with the definition of ‘enterprise’ in the VAT Act. See also the definition of ‘electronic services’ in the Regulations.

⁷⁷ Available at https://ec.europa.eu/taxation_customs/individuals/buying-goods-services-online-personal-use/buying-services/electronically-supplied-services_en. Accessed on 20 May 2017.

includes, but is not limited to, the supply of online advertising services, the supply of digital software and the download of films.⁷⁸ These services are not listed in the Regulations. An EU foreign supplier of films is thus supplying electronic supplied services in the EU but it does not constitute 'electronic services' if that foreign supplier supplies films to South Africa. Instead, the supply of films will fall under imported services in the VAT Act. It follows that services that are not defined in the Regulations will be subject to VAT liability in terms of Section 7(1)(c) of the VAT Act.⁷⁹

It seems clear that a lack of international coordination and cooperation regarding a uniform definition of 'electronic services' results in a lot of confusion and uncertainty especially for foreign businesses. The responsibility is left to foreign suppliers to determine how a jurisdiction defines electronic services before transacting with its customers. Foreign suppliers will need to familiarize themselves with other foreign legislation to ensure tax compliance. The uncertainty may also lead foreign suppliers to avoid transacting with a specific jurisdiction altogether.

SARS should broaden the definition of 'electronic services' to include all the services that have been excluded from the Regulations.

2.4.3 A vendor

A vendor is a person who is required to register for VAT in terms of the VAT Act.⁸⁰ A vendor is required to levy VAT on the supply of goods and services that they make in the course of the furtherance of an enterprise.⁸¹

Generally, a person becomes liable to register as a vendor at the end of the twelfth month if the taxable supplies made during that period exceed R1 million at the end of the twelfth month.⁸² Furthermore, a person will be obliged to register for VAT at the

⁷⁸ Full list available at

http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/common/buying_online/electronically_supplied_services.pdf. Accessed on 20 May 2017.

⁷⁹ See discussion on registration of foreign suppliers at paragraph 2.4.4.1 below.

⁸⁰ Section 1 of the definition of 'vendor' of the VAT Act.

⁸¹ Section 7(1)(a) of the VAT Act.

⁸² Section 23(1)(a) of the VAT Act.

beginning of the month when a contractual agreement entered into stipulates that the person will be making taxable supplies that will exceed R1 million after the commencement date.⁸³

A person is also obliged to register as a vendor if they supply electronic services to South African consumers and the total value of the supply exceeds R50 000 at the end of any given month.⁸⁴

It must be borne in mind that this threshold is an annual threshold and not a monthly threshold. The wording used in Section 23(1A) incorrectly states that it is a monthly threshold but it is submitted that this is in fact not the case and that Section 23(1A) should be amended to rectify this mistake and to avoid uncertainty.

2.4.4 The definition of ‘Enterprise’

The term ‘enterprise’ is an important concept for purposes of the VAT Act.⁸⁵ According to SARS, the definition of enterprise sets out the persons, the economic activities and the types of supply that form part of the tax base.⁸⁶

An enterprise is defined as: -

“In the case of any vendor, any enterprise or activity which is carried on continuously or regularly by any person in the Republic or partly in the Republic and in the course or furtherance of which goods or services are supplied to any other person for a consideration, whether or not for profit, including any enterprise or activity carried on in the form of a commercial, financial, industrial, mining, farming, fishing, municipal or professional concern or any other concern of a continuing nature or in the form of an association or club.”⁸⁷

⁸³ Section 23(1)(b) of the VAT Act.

⁸⁴ Section 23(1A) of the VAT Act.

⁸⁵ SARS Interpretation Note 70 at 2. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-IN-2013-03%20-%20IN70%20Supplies%20made%20for%20no%20consideration.pdf>. Accessed 28 October 2017.

⁸⁶ SARS Interpretation note 70 at 2. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-IN-2013-03%20-%20IN70%20Supplies%20made%20for%20no%20consideration.pdf>. Accessed 28 October 2017.

⁸⁷ Section 1 of the definition of ‘enterprise’ of the VAT Act.

The definition of enterprise is quite broad. It appears that SARS incorporated every possible commercial activity in the definition in order for the activity to be captured by the VAT Act.

The definition of 'enterprise' is not limited to businesses occurring in South Africa. A foreign business that supplies services in South Africa will be deemed to be conducting an enterprise in South Africa.⁸⁸ This provision is subject to the proviso that the recipient of the services is resident in South Africa; the payment for the electronic services originates from a bank in South Africa; and that the recipient has a business, postal or residential address in South Africa.⁸⁹

The term 'resident' is defined as "a resident as defined in the Income Tax Act 58 of 1962" (Income Tax Act).⁹⁰ An extensive discussion of the term 'resident' is not necessary for the purposes of this study. However, suffice to say that residency consists of two tests: the ordinary resident test and the physical presence test.⁹¹ A resident is a person who ordinarily resides in the Republic of South Africa.⁹² Unfortunately, the Income Tax Act does not define the term 'ordinarily resident'. Hence, whether a person is resident in South Africa is a matter of fact. A person will be deemed to be ordinarily resident in South Africa if they call their natural abode as their real home or alternatively, a person's usual or physical residence.⁹³ The physical presence test applies if a person is not ordinarily resident in South Africa.⁹⁴ In terms of the physical presence test, a person will be deemed to be resident in South Africa if they are physically present in South Africa for periods:

- Exceeding 91 days in aggregate during the current year of assessment; and

⁸⁸ Paragraph (b)(vi) of section 1 of the definition of 'enterprise' of the VAT Act.

⁸⁹ Paragraph (b)(vi)(aa), (bb) and (cc) of section 1 of the definition of 'enterprise' of the VAT Act.

⁹⁰ Section 1 of the definition of 'resident' in the VAT Act.

⁹¹ Section 1 of the definition of 'resident' in the Income Tax Act.

⁹² Section 1 of the definition of 'resident' in the Income Tax Act.

⁹³ *Cohen v CIR* 1946 AD 174, 13 SATC 362 371. See also *CIR v Kuttel* 1992 (3) SA 242 (A), 54 SATC 298. See also Croome, B. (ed) (2013). *Tax Law: an introduction* Juta & Company (Pty) Ltd at 28 – 29. See also SARS (2002) Income Tax Interpretation Note 3. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-IN-2012-03%20-%20Resident%20definition%20natural%20person%20ordinarily%20resident.pdf>. Accessed 22 May 2017.

⁹⁴ Croome, B. (ed) (2013). *Tax Law: an introduction* Juta & Company (Pty) Ltd at 30.

- Exceeding 91 days in aggregate during each of the five years of assessment preceding the current year of assessment; and
- Exceeding 915 days in aggregate during the five years of assessment preceding the current year of assessment.⁹⁵

The VAT Act does not state who is liable to establish the residency of the recipient of electronic services. From the wording of the VAT Act, it appears that the onus is on the foreign supplier of electronic services to determine the recipient's residency.⁹⁶ This may be due to the fact that foreign suppliers transact with South African customers on a regular basis. Establishing the recipient's residency would be an unnecessary administrative burden on the foreign supplier of electronic services.

Whether a foreign business conducts their business from inside or outside South Africa is a question of fact. A foreign business will normally have a permanent or fixed address in a foreign jurisdiction. The problem now occurs when a foreign supplier of electronic services does not necessarily have a physical presence but a virtual one and supplies services regularly to recipients in South Africa. In instances like these, it is difficult for tax authorities like SARS to levy VAT on these transactions because the rules on place of supply are not explicitly stated or defined in the VAT Act.

In an attempt to rectify this shortcoming, the VAT Act now requires foreign suppliers of electronic services to register for VAT in South Africa when the total supply of services exceeds R50 000 in any given year.⁹⁷

It appears that National Treasury used the location of the consumer of electronic services as well as payment originating from a South African bank as proxies in order to establish the place of supply for electronic services.⁹⁸ However, it remains to be seen if

⁹⁵ Section 1 of the definition of 'resident' in the Income Tax Act. See also Croome, B. (ed) (2013). *Tax Law: an introduction* Juta & Company (Pty) Ltd at 30.

⁹⁶ Section 7(1)(c) of the VAT Act read with section 7(2) of the VAT along with paragraph (b)(vi) of section 1 of the definition of 'enterprise'.

⁹⁷ Paragraph (b)(vi) of section 1 of the definition of 'enterprise' of the VAT Act read together with section 23(1A) of the VAT Act.

⁹⁸ National Treasury (2013). *Explanatory memorandum on the taxation laws amendment bill 2013* at 88. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/ExplMemo/LAPD-LPrep-EM-2013-02%20-%20Explanatory%20Memorandum%20Taxation%20Laws%20Amendment%20Bill%202013.pdf>. Accessed on 22 May 2017.

these proxies prove to be sufficient in establishing the identity of the consumer of electronic services in South Africa.

2.4.4.1 VAT registration of foreign suppliers of electronic services – how does it work?

Once the required threshold has been met, a foreign supplier of electronic services must register for VAT on the SARS website⁹⁹ and download a copy of the VAT 101 form. After completing and signing the VAT 101 form, it must be emailed together with supporting documents to SARS at eCommerceRegistration@sars.gov.za.¹⁰⁰

A foreign supplier of electronic services is required to issue a tax invoice to a recipient within 21 days of the date of supply.¹⁰¹ The invoice should contain the following particulars:¹⁰²

- The name and VAT registration number of the electronic services supplier;
- The name and address of the electronic services recipient;
- An individual serialised number;
- The date of issue;
- A description of the electronic services supplied;
- The consideration in money for the supply in the currency of any country. If the consideration is reflected in the currency of -
 - (i) The Republic, the amount of the VAT charged or a statement that it includes a charge for the VAT and the rate at which the VAT was charged; or
 - (ii) Any country other than the Republic, the amount of the tax charged in the currency of the Republic or a separate document issued by the electronic

⁹⁹ www.sars.gov.za.

¹⁰⁰ SARS (2015). *VAT registration guide for foreign suppliers of electronic services* at 2. Available at <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/VAT-REG-01-G02%20-%20VAT%20Registration%20Guide%20for%20Foreign%20Suppliers%20of%20Electronic%20Services%20-%20External%20Guide.pdf>. Accessed on 1 April 2017.

¹⁰¹ Section 20 of the VAT Act.

¹⁰² Section 20(5B) of the VAT Act.

services supplier to the electronic services recipient reflecting the amount of the tax charged in the currency of the Republic.

- The exchange rate used.¹⁰³

In 2017, SARS published a second *VAT registration guideline for foreign suppliers of electronic services*.¹⁰⁴ It appears that the guide, which is a revised version of the first guide published by SARS,¹⁰⁵ attempts to simplify the registration process for foreign suppliers of electronic services.

The conclusion seems to be that the registration requirement shifts the burden of accounting for VAT from the recipient of electronic services to the foreign supplier of electronic services.¹⁰⁶ However, the burden shifts to the recipient when he imports services from a non-registered foreign supplier of electronic services. It follows that the foreign supplier of electronic services will account for and remit taxes to SARS.

However, the challenge remains for SARS to enforce this mechanism. Currently, there are no provisions in the VAT Act that will enable SARS to monitor the compliance of foreign businesses. Moreover, there are currently no provisions in place within the VAT Act that will impose penalties on foreign suppliers of electronic services in the event of non-compliance.

2.4.4.2 Effects of VAT registration for foreign suppliers of electronic services

¹⁰³ SARS (2016). Binding General Ruling 28 Issue 1 – 2: Electronic Services at 3. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2015-03%20-%20BGR28%20Electronic%20Services.pdf>. Accessed on 31 March 2017.

¹⁰⁴ SARS (2017). *VAT registration guide for foreign suppliers of electronic services*. Available at <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/VAT-REG-02-G02%20-%20VAT%20Guide%20for%20Foreign%20Suppliers%20of%20Electronic%20Services%20-%20External%20Guide.pdf>. Accessed 2 November 2017.

¹⁰⁵ See footnote 74.

¹⁰⁶ Louw, H. & Botha, D. (2014). *Value-added Tax on electronic services supplied by person outside South Africa* DLA Cliffe Dekker Hofmeyr. Available at <http://www.thesait.org.za/news/168149/Value-added-Tax-on-electronic-services-supplied-by-persons-outside-South-Africa.htm>. Accessed on 5 April 2017.

Upon registration as a VAT vendor in South Africa, a foreign supplier must levy VAT at fourteen per cent on the supply of electronic services.¹⁰⁷ This may be illustrated by the following example:

Example 2

Thomas is a resident of South Africa. Thomas is an avid gamer and has been gaming since the age of ten. Thomas has been looking forward to and would like to purchase a copy of *Call of Duty®: Infinite Warfare* on his Personal Computer (PC). Thomas establishes that a digital version of *Call of Duty®: Infinite Warfare* costs R500 on Steam™. This price is R500 less than the price of the hardcopy version of *Call of Duty®: Infinite Warfare* he saw at a local retail store.

Thomas purchases a digital version of *Call of Duty®: Infinite Warfare* from Steam™ for R500. He is required to furnish his personal details and he duly complies. He pays the purchase price by means of a debit card after submitting his details online.

Thomas' South African bank account is debited with the purchase price and *Call of Duty®: Infinite Warfare* is immediately available for download.

Assume that Steam™ is a registered vendor and is carrying on an enterprise in South Africa.

In the above example, Steam™ supplied electronic services to a resident of South Africa. Payment is effected from a bank in South Africa. Steam™ is required to levy VAT on the above transaction. The purchase price paid by Thomas will increase by fourteen per cent (fourteen per cent of R500 is R70). Thomas will thus pay R570 for the digital version of *Call of Duty®: Infinite Warfare*. Steam™ will be required to account for the R70 and remit that amount to SARS.¹⁰⁸

SARS issued a *Binding General Ruling* for electronic services on 23 February 2016. In it, SARS stated that a supplier of electronic services 'may' advertise the price of its electronic services exclusive of VAT on condition that it has a statement on its website indicating that VAT will be levied on supplies of electronic services to electronic services

¹⁰⁷ Section 7(1)(a) of the VAT act.

¹⁰⁸ See also Coetzee, L., & Meiring, M., (2016). Value-Added Tax on imported electronic services: A critical evaluation of the newly enacted South African legislation *Journal of Economic and Financial Sciences* 9(1): 35 – 36.

recipients.¹⁰⁹ The use of the word ‘may’ is directory and not peremptory. This means that a supplier is not obliged to advertise the price of electronic services inclusive of VAT.

A foreign supplier is not required to have a physical presence in South Africa nor is it required to have a representative vendor in South Africa in order to register for VAT. A foreign supplier may not be familiar with the legislative changes in South Africa. And if that is indeed the case, then there is likelihood that compliance to this provision will be low.¹¹⁰ Harmse argued that this may pose a problem for foreign suppliers as they must establish whether electronic services were indeed supplied in South Africa.¹¹¹

2.5 IMPORTED SERVICES

The VAT Act defines imported services as: “*a supply of services that is made by a supplier who is resident or carries on business outside the Republic to a recipient who is a resident of the Republic to the extent that such services are utilized or consumed in the Republic otherwise than for the purposes of making taxable supplies.*”¹¹²

This definition may be elucidated by means of the following:

Example 3

James purchases a digital version of a book from Amazon. Amazon supplies James, who is a resident of South Africa, with a digital version of the book on his kindle. James utilizes the book for personal consumption. James is not registered for VAT in South Africa.

James’ liability for VAT stems from the fact that the purchase of the digital book qualifies as an imported service for purposes of the Act and the services were used for personal consumption. James has to account for VAT within 30 days of receipt of the digital

¹⁰⁹ SARS (2016). Binding General Ruling 28 Issue 2: Electronic Services at 3. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2015-03%20-%20BGR28%20Electronic%20Services.pdf>. Accessed on 31 March 2017.

¹¹⁰ Harmse, J. (2015). Value-added tax consequences for foreign suppliers of electronic services into South Africa *World Journal of VAT/GST Law* 3(2): 117.

¹¹¹ Harmse, J. (2015). Value-added tax consequences for foreign suppliers of electronic services into South Africa *World Journal of VAT/GST Law* 3(2): 117.

¹¹² Section 1 of the definition of ‘imported services’ of the VAT Act.

book; furnish the Commissioner of SARS with a return and pay the said tax to the Commissioner.¹¹³ This tax collection method is known as the reverse-charge mechanism or the self-assessment collection method. The reverse-charge mechanism is the default tax collection mechanism for the supply of services, including electronic services, in South Africa.¹¹⁴

From the plain reading of Section 14(1) of the VAT Act, it can be said that the recipient of imported services in South Africa has an obligation to account for and remit tax to the tax authorities. This provision creates challenges to VAT collection on e-commerce transactions in South Africa.

2.5.1 Critical evaluation of applying the reverse-charge mechanism to B2C transactions

Firstly, the reverse-charge mechanism relies solely on the integrity of the recipient of imported services. In the example above, if James is not aware of section 14(1) of the VAT Act or chooses to ignore it, there is a likelihood that he will not account for VAT to SARS. Even if James becomes aware of the provision, he may be reluctant to comply due to the fact that he perceives tax collection to be an unnecessary burden and time consuming. In addition to that, there are currently no specific penalties for James to pay for failing to comply with this section. SARS' reliance on a consumer's integrity in order to collect tax places an unnecessary burden on the consumer. It appears that the reliance on the consumer highlights the inadequacies of the reverse-charge mechanism to collect VAT on imported services. Moreover, the conclusion seems to be that SARS does not have any other provision or mechanisms available to enforce tax compliance on the reverse-charge mechanism.

Secondly, James may easily dispose of his digital book without SARS becoming aware of its existence. It then becomes difficult for SARS to establish or to prove that James did in fact import the digital book into South Africa. Furthermore, in order for SARS to

¹¹³ Section 14(1)(a) and (b) of the VAT Act.

¹¹⁴ Section 14 of the VAT Act.

prove that James has imported services into South Africa, SARS will need to ascertain James' identity. SARS is not able to establish James' identity because there are currently no measures in place in the VAT Act that will facilitate the verification of a recipient of imported services on B2C transactions. The conclusion can be drawn that the inability to verify James' identity translates into an ineffective process to conduct an audit on the transaction.

In addition to identifying James, SARS will need to establish the type of service rendered to James. It can only do so if it is aware of the place of consumption of the services.

Furthermore, the definition of a 'recipient' does not specifically include natural persons.¹¹⁵ The VAT Act defines a 'recipient' as a person to whom a supply of goods and services is made.¹¹⁶ The definition does not make it any clearer in an attempt to determine if a natural person is indeed defined in the VAT Act. The difficulty seems to be compounded by the definition of 'a person'. A person is defined as a public authority, a municipality, a company, a body of persons, the estate of any deceased or insolvent person, a trust fund and any foreign donor funded project.¹¹⁷ This definition of a person does not explicitly include a natural person. Silver and Beneke submitted that the definition of 'person' for the purposes of VAT includes a natural person.¹¹⁸ Although the ordinary meaning of the word 'person' may be used to achieve the desired outcome,¹¹⁹ it is suggested that 'natural person' should be added to the definition of 'person' in the VAT Act.

2.6 VAT COLLECTION BY MEANS OF AN INTERMEDIARY

¹¹⁵ Section 1 of the definition of 'recipient' in the VAT Act.

¹¹⁶ Section 1 of the definition of 'recipient' in the VAT Act.

¹¹⁷ Section 1 of the definition of 'person' in the VAT Act.

¹¹⁸ Silver, M. & Beneke, C. (eds) (2015). *Deloitte VAT Handbook* 10th ed. LexisNexis at 20.

¹¹⁹ Botha, C. (2005). *Statutory interpretation: an introduction for students* 4th ed. Juta & Co Ltd at 69.

In 2016, SARS published a draft *Binding General Ruling on electronic services supplied via intermediaries* (the Ruling).¹²⁰ In terms of the Ruling, foreign suppliers of electronic services would not be required to register or account for VAT in South Africa subject to the following provisos:¹²¹

- The foreign supplier supplies electronic services via an intermediary's platform;
- The intermediary is a registered vendor in the Republic;
- The electronic services supplier and the relevant intermediary enter into a written agreement confirming that the intermediary will –
 - (i) Account for VAT on the supply of the electronic services supplied *via* its platform;
 - (ii) Be liable for the payment of VAT in respect of the supply of said electronic services;
- The intermediary will retain accounting records, as envisaged in section 29¹²² of the Tax Administration Act 28 of 2011 for the supply of electronic services by the electronic services supplier falling within this arrangement; and

¹²⁰ SARS (2016). *Draft Binding General Ruling on Electronic services supplied via intermediaries*. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Drafts/LAPD-LPrep-Draft-2016-22%20-%20Draft%20BGR%20on%20electronic%20services%20supplied%20via%20intermediaries.pdf>. Accessed on 9 April 2017.

¹²¹ Visser, A. (2016). *Tax practitioners favour move to simplify VAT rules for foreign e-commerce*. Available at <http://www.thesait.org.za/news/287478/Tax-practitioners-favour-move-to-simplify-VAT-rules-for-foreign-e-commerce-.htm>. Accessed on 9 April 2017. See also SARS (2016). *Draft Binding General Ruling on Electronic services supplied via intermediaries* at 1 - 3. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Drafts/LAPD-LPrep-Draft-2016-22%20-%20Draft%20BGR%20on%20electronic%20services%20supplied%20via%20intermediaries.pdf>. Accessed on 9 April 2017.

¹²² Section 29 of the Tax Administration Act states that: (1) a person must keep the records, books of account or documents that (a) enable the person to observe the requirements of a tax Act; (b) are specifically required under a tax Act or by the Commissioner by public notice; (c) enable SARS to be satisfied that the person has observed those requirements. (2) The requirements of this Act to keep records, books of account or documents for a tax period apply to a person who (a) has submitted a return for the tax period; (b) is required to submit a return for the tax period and has not submitted a return for the tax period; or (c) is not required to submit a return but has, during the tax period, received income, has a capital gain or capital loss or engaged in any other activity that is subject to tax or would be subject to tax but for the application of a threshold or exemption. (3) Records, books of account or documents need not be retained by the person described in: (a) subsection (2)(a), after a period of five years from the date of the submission of the return and subsection (a)(c), after a period of five years from the end of the relevant tax period.

- The intermediary, by entering into this arrangement accepts that it is liable for any outstanding taxes of the electronic services supplier in respect of the supply of the said electronic services as made *via* an intermediary's platform.¹²³

In terms of the Ruling, a foreign supplier of electronic services will not be required to register for VAT if the intermediary is already registered for VAT and the foreign supplier has entered into an agreement with the intermediary that it will account for VAT and that it will pay the VAT to SARS.¹²⁴

It follows that if a foreign supplier does not supply electronic services via an intermediary's platform, the former will be required to register and account for VAT where the supplies at the end of any year exceeds R50 000.¹²⁵

The Ruling defines an 'intermediary' as a person who facilitates the supply of electronic services supplied by an electronic services supplier and who is responsible for, *inter alia*, issuing invoices and collecting payment for the supply.¹²⁶ The Ruling does not go further to define a 'person'. It follows that the definition of 'person' must be gleaned from the VAT Act.

The South African Institute of Tax Practitioners (SAIT) said in its submissions that the Ruling allows South African intermediaries to assume responsibility for VAT *in lieu* of

¹²³ SARS (2016). *Draft Binding General Ruling on Electronic services supplied via intermediaries* at 2. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Drafts/LAPD-LPrep-Draft-2016-22%20-%20Draft%20BGR%20on%20electronic%20services%20supplied%20via%20intermediaries.pdf>. Accessed on 9 April 2017.

¹²⁴ Visser, A. (2016). Tax practitioners favour move to simplify VAT rules for foreign e-commerce. Available at <http://www.thesait.org.za/news/287478/Tax-practitioners-favour-move-to-simplify-VAT-rules-for-foreign-e-commerce-.htm>. Accessed on 9 April 2017.

¹²⁵ SARS (2016). *Draft Binding General Ruling on Electronic services supplied via intermediaries* at 3. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Drafts/LAPD-LPrep-Draft-2016-22%20-%20Draft%20BGR%20on%20electronic%20services%20supplied%20via%20intermediaries.pdf>. Accessed on 9 April 2017. See also Visser, A. (2016). Tax practitioners favour move to simplify VAT rules for foreign e-commerce. Available at <http://www.thesait.org.za/news/287478/Tax-practitioners-favour-move-to-simplify-VAT-rules-for-foreign-e-commerce-.htm>. Accessed on 9 April 2017.

¹²⁶ SARS (2016). *Draft Binding General Ruling on Electronic services supplied via intermediaries* at 1. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Drafts/LAPD-LPrep-Draft-2016-22%20-%20Draft%20BGR%20on%20electronic%20services%20supplied%20via%20intermediaries.pdf>. Accessed on 9 April 2017. See also Visser, A. (2016). Tax practitioners favour move to simplify VAT rules for foreign e-commerce. Available at <http://www.thesait.org.za/news/287478/Tax-practitioners-favour-move-to-simplify-VAT-rules-for-foreign-e-commerce-.htm>. Accessed on 9 April 2017.

foreign suppliers of electronic services.¹²⁷ SAIT also submitted that the Ruling is based on SARS' discretionary power in terms of Section 72¹²⁸ of the VAT Act.¹²⁹

2.7 CONCLUSION

VAT collection mechanisms in South Africa have been discussed in this chapter. The charging provision was analysed to ascertain the VAT collections mechanisms applicable to the various e-commerce transactions. The recent amendments were discussed to determine if they provide any significant improvements in VAT collection on e-commerce transactions.

However, the recent developments are not without difficulties. This chapter has shown that a foreign supplier of electronic services to South Africa may not necessarily be aware of its liability for VAT registration in South Africa. In addition, the requirement for foreign suppliers to issue tax invoices to South African recipients may discourage international suppliers from registering for VAT in South Africa.¹³⁰ The reason being that it places an additional administrative and compliance burden on them.¹³¹ However, Harmse has stated that VAT registration process has been simplified in that the

¹²⁷ SAIT (2016). *Draft binding general ruling relating to electronic services supplied by Intermediaries (VAT)* at 1. Available at www.thesait.org.za/resource/resmgr/2016_Submissions/25_Apr_2016_-_SAIT_BGR_Elect.pdf. Accessed on 9 April 2017.

¹²⁸ Section 72 of the VAT Act states that: if in any case the commissioner is satisfied that in consequence of the manner in which any vendor or class of vendors conducts his, her or their business, trade or occupation, difficulties, anomalies or incongruities have arisen or may arise in regard to the application of any of the provisions of this Act, the commissioner may make an arrangement or decision as to – (a) the manner in which such provisions shall be applied or (b) the calculation or payment of tax or the application of any rate of zero per cent or any exemption from tax provided in this Act, in the case of such vendor or class of vendors or nay person transacting with such vendor or class of vendors as appears to overcome such difficulties, anomalies or incongruities: provided that such decision or arrangement shall not have the effect of substantially reducing or increasing the ultimate liability for tax levied under this Act.

¹²⁹ SAIT (2016). *Draft binding general ruling relating to electronic services supplied by Intermediaries (VAT)* at 1. Available at www.thesait.org.za/resource/resmgr/2016_Submissions/25_Apr_2016_-_SAIT_BGR_Elect.pdf. Accessed on 9 April 2017. See also SARS (2016). *Draft Binding General Ruling on Electronic services supplied via intermediaries* at 2. Available at <http://www.sars.gov.za/AllDocs/LegalDoclib/Drafts/LAPD-LPrep-Draft-2016-22%20-%20Draft%20BGR%20on%20electronic%20services%20supplied%20via%20intermediaries.pdf>. Accessed on 9 April 2017.

¹³⁰ Coetzee, L., & Meiring, M., (2016). Value-Added Tax on imported electronic services: A critical evaluation of the newly enacted South African legislation *Journal of Economic and Financial Sciences* 9(1): 38.

¹³¹ Coetzee, L., & Meiring, M., (2016). Value-Added Tax on imported electronic services: A critical evaluation of the newly enacted South African legislation *Journal of Economic and Financial Sciences* 9(1): 38.

registration is conducted online and there is no need to have a local representative or a bank account in South Africa.

SARS has recently published a *Binding General Ruling* that will not require foreign suppliers to register for VAT if they supply electronic service via an intermediary in South Africa. While this is a welcome addition - to the extent that it aims at easing the compliance burden on foreign suppliers of electronic services,¹³² - it must be borne in mind that a *Binding General Ruling* does not form part of the VAT Act and is thus not law. As such, it can be withdrawn at any stage.¹³³

This chapter has illustrated that the reverse-charge mechanism is not an appropriate mechanism to collect VAT on the supply of electronic services. This mechanism relies on the knowledge and honesty of private consumers of electronic services. Due to a lack of knowledge on tax legislation - the compliance burden is low. Currently, SARS has difficulty enforcing this legislation because the costs of doing so exceed the benefit.

This chapter has also illustrated that there is a need for SARS to put appropriate measures in place to collect VAT in situations where a consumer imports services to South Africa for personal consumption. The inability to verify a consumer's identity means that SARS is incapable of conducting an audit on the transaction. This chapter shows that SARS is not able to enforce the VAT Act on these types of transactions as the reverse-charge mechanism does not adequately cater for the taxation of imported services into South Africa.

The application of the appropriate VAT collection mechanism is dependent on whether a foreign supplier of electronic services is carrying on an enterprise in South Africa. In the South African context, applying the appropriate VAT collection mechanism may also depend on the mechanisms' efficacy to collect tax as well as the mechanisms' facility to

¹³² Visser, A. (2016). Tax practitioners favour move to simplify VAT rules for foreign e-commerce. Available at <http://www.thesait.org.za/news/287478/Tax-practitioners-favour-move-to-simplify-VAT-rules-for-foreign-e-commerce-.htm>. Accessed on 9 April 2017. See also SAIT (2016). *Draft binding general ruling relating to electronic services supplied by Intermediaries (VAT) at 1*. Available at www.thesait.org.za/resource/resmgr/2016_Submissions/25_Apr_2016_-_SAIT_BGR_Elect.pdf. Accessed on 9 April 2017.

¹³³ Visser, A. (2016). Tax practitioners favour move to simplify VAT rules for foreign e-commerce. Available at <http://www.thesait.org.za/news/287478/Tax-practitioners-favour-move-to-simplify-VAT-rules-for-foreign-e-commerce-.htm>. Accessed on 9 April 2017.

ascertain the identity and location of the recipient customer. There is no hard and fast rule as to which mechanism should be applied and, as such, every e-commerce transaction must be judged on its own merits.

CHAPTER 3

HOW VAT CAN BE COLLECTED ON B2C TRANSACTIONS – LESSONS FROM THE OECD

3.1 INTRODUCTION

Chapter 2 investigates and highlights the challenges that e-commerce poses to VAT collection in South Africa. What follows directly below is a critical discussion on the four different types of VAT collection models on e-commerce transactions that have been recommended by the OECD. These models are then analysed in an attempt to find the most appropriate model that may be currently used in South Africa.

Thereafter, a discussion ensues that depicts the various methods of customer verification with the intention of selecting a method that can be adopted in South Africa.

This chapter attempts to answer the question: Is there a cohesive and consistent system of identification of the recipient consumer of electronic services?

3.2 VAT COLLECTION MECHANISMS SUGGESTED BY THE OECD

3.2.1 The use of intermediaries

According to the OECD, the use of an intermediary to collect taxes has existed for some time. An intermediary¹³⁴ is someone who will be required to collect, account and remit tax to tax authorities. Essentially, the intermediary takes over the role of a tax authority and conducts all the administrative functions that a tax authority would normally conduct. The list of functions of an intermediary would include:

- Signing returns;
- Tax collection;
- Remitting tax;
- Liability for tax debt;
- Complete responsibility for all taxpayers' consumption tax obligations.¹³⁵

The functions listed above are not a closed list since different jurisdictions may require additional functions from intermediaries.

There are no hard and fast rules as to who or what constitutes an intermediary. Hence, intermediaries can take the form of financial institutions, an Internet Service Provider (ISP),¹³⁶ businesses,¹³⁷ companies, private persons¹³⁸ or a government legal entity.

The OECD has recommended that an intermediary be located or have a physical presence in the country where taxation takes place.¹³⁹ It appears that the reason behind this requirement is to ensure that the intermediary be held accountable to the relevant

¹³⁴ An intermediary can either consist of a tax collector or an agent. The latter involves an intermediary who steps into the shoes, as it were, of the tax authority and therefore receives and collects taxes on behalf of the tax authority. The former involves an intermediary that by representation has been appointed by law to act on behalf of tax authorities to collect specified amounts of taxes.

¹³⁵ OECD (2005). *Facilitating collection of consumption taxes on business-to-consumer cross-border e-commerce transactions* at 7. Available at <http://www.oecd.org/tax/consumption/34422641.pdf>. Accessed on 10 June 2017.

¹³⁶ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 296.

¹³⁷ See Lubbe, H. (2015). *Alternatives to the enforceability of VAT on imported digital purchases in South Africa*. Unpublished LLM mini dissertation (North West University of South Africa) at 56.

¹³⁸ It appears that the OECD considers that a private person may act as an intermediary for purposes of VAT collection. This is made possible by requiring intermediaries to have 'professional qualifications'. See OECD (2005). *Facilitating collection of consumption taxes on business-to-consumer cross-border e-commerce transactions* at 7. Available at <http://www.oecd.org/tax/consumption/34422641.pdf>. Accessed on 10 June 2017.

¹³⁹ OECD (2005). *Facilitating collection of consumption taxes on business-to-consumer cross-border e-commerce transactions* at 7. Available at <http://www.oecd.org/tax/consumption/34422641.pdf>. Accessed on 10 June 2017.

tax authorities. It follows that if an intermediary does not have a physical presence in the jurisdiction where consumption takes place, it would be difficult for tax authorities to hold the intermediary accountable.

Tax authorities and intermediaries should enter into written contractual agreements whereby the latter is given formal approval to collect taxes on the former's behalf. In some jurisdictions, this may require the intermediary to be familiar with and have basic knowledge and understanding of the jurisdiction's tax laws. An understanding of the tax laws is salient because it will provide the intermediary with a better grasp of its role as a tax collector.

The use of an intermediary for the purposes of tax collection should not be underestimated. Ligthart argued that enabling intermediaries to collect VAT could potentially reduce compliance costs.¹⁴⁰ This could be an important aspect for both foreign suppliers of electronic services and tax authorities. For foreign suppliers, it will enable them to transact with customers with the knowledge that the administrative burden of tax collection has shifted to the intermediary. Hence, they will not incur unnecessary expenses when transacting online with customers. For tax authorities, the burden for tax collection and VAT liability shifts to a third party. Tax authorities' administrative costs are significantly reduced. A tax authority's resources could then be channelled into other activities like consumer tax awareness campaigns; international co-operation; and improving tax policies.

The intermediary should keep records of all transactions for audit purposes. This is perhaps one of the most important requirements. Since e-commerce transactions take place online, it would be apt for intermediaries to have electronic copies of all the relevant transactions. These should be made available to the relevant tax authorities upon request. For this reason, Basu argued that an intermediary should ideally be located in the destination country.¹⁴¹ This is also in line with the OECD's recommendation.¹⁴² However, it is fair to say that this should not preclude tax

¹⁴⁰ Ligthart, J. E. (2004). *Consumption Taxation in a Digital World: A Primer* Tilburg University & University of Groningen at 13 – 14.

¹⁴¹ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 308.

¹⁴² See paragraph 3.2.1 herein.

authorities from concluding agreements with virtual intermediaries for the purposes of VAT collection.

It follows that in order for an intermediary to be able to collect VAT on behalf of tax authorities, the intermediary should be able to identify the foreign supplier of services. By implication, the intermediary should have the appropriate facilities in place to identify foreign businesses. Without the necessary identification facilities, it would be challenging for the intermediary to collect VAT.

The efficacy of VAT collection by intermediaries is also dependent on a uniform classification of intangible services. Currently, there is no universal and uniform classification of intangible services in the international arena.¹⁴³ This poses challenges for tax collectors because it may result in the erosion of tax base. It also poses problems for foreign suppliers for if a service is supplied to different jurisdictions and these jurisdictions define that service differently, it will cause a lot of uncertainty and make tax compliance strenuous for foreign suppliers of services.¹⁴⁴

The viability of adopting an intermediary will mostly depend on a jurisdiction and its laws. It is important for a country's laws to not only clearly define who or what constitutes an intermediary for the purposes of VAT collection but also to establish the intermediary's tasks. Having legislation in place to regulate the role of intermediaries creates certainty. Once a jurisdiction has incorporated the use of intermediaries for VAT collection in its legislation, it may encourage other jurisdictions to do the same. With additional input from organisations like the OECD, a consistent international framework for the use of intermediaries for tax collection can be set. This will allow other jurisdictions to adopt the use of intermediaries as an alternative model for VAT collection.

It appears that whenever an intermediary is used to collect and remit VAT to the relevant tax authorities, it needs to do so in a manner that is more efficient and reliable than the tax authority. The reason being that it would seem sensible to have an intermediary that has the facilities and the means to collect VAT where it has been

¹⁴³ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 304.

¹⁴⁴ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 304.

established that the tax authority has inadequate facilities to collect VAT. The converse of this is that an intermediary should not be less effective at collecting VAT compared to the tax authority. To be more precise, the intermediary should bridge the gap on VAT collection on e-commerce transactions between the tax authority and the taxpayer.

An important question that arises with this tax collection mechanism is who or what should be liable to bear the compliance cost sustained by intermediaries during VAT collection. Compliance costs are costs that are borne by taxpayers, intermediaries and businesses in order to fulfil the revenue laws imposed by tax authorities.¹⁴⁵ It is the nature of a tax system that an entity will spend money in order to observe the tax laws imposed by the relevant tax authorities. Where an intermediary expends capital in order to collect taxes on behalf of tax authorities, the former will have a reasonable expectation that it does so in the knowledge that it will be reimbursed for rendering a service. Tax authorities should thus be able to compensate intermediaries when the latter are required to collect taxes on behalf of the former.

With that in mind, tax authorities will look to intermediaries that will not request excessive reimbursement fees and are cognisant of the fact that tax authorities incur their own expenses in the form of administrative costs. However, having excessive compliance costs and administrative costs does not necessarily equate to having a poor tax system although it does point to a tax system that is predominantly inept.¹⁴⁶

Consider the following two examples:

Example 4

The tax authority in **state A** enters into an agreement wherein intermediary C collects VAT on e-commerce transactions on its behalf. Intermediary C collects and remits taxes to the tax authority in **state A**. Intermediary C is also located in **state A**.

Suppose intermediary C is a government legal entity.

¹⁴⁵ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 306 footnote 53.

¹⁴⁶ Ebrill, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 52.

Example 5

The tax authority in **state Q** enters into an agreement wherein intermediary E collects VAT on e-commerce transactions on its behalf. Intermediary E, which is located in **state D**, collects and remits taxes to the tax authority in **state Q**.

Suppose intermediary E is a private business.

In example 4 above, since a government legal entity acts as an intermediary for the purposes of VAT collection, it could happen that the administrative and compliance costs may be curtailed because the tax authority and government legal entity form part of the same branch of government. This is in contrast to example 5 where the intermediary is a foreign private business. The cost implications for a tax authority in these two examples will differ; largely for the reason that the tax authority in **state Q** will be compelled to compensate Intermediary E, which is located in a foreign jurisdiction, for its efforts in collecting VAT.¹⁴⁷

3.2.2 The self-assessment mechanism

The self-assessment mechanism, also referred to as the reverse-charge mechanism, requires the recipient of services to account for, collect, and remit VAT to the relevant tax authority.¹⁴⁸ Some of the mechanism's deficiencies are mentioned above¹⁴⁹ and shall not be repeated here.

One of the ways that this mechanism can be implemented effectively is if a jurisdiction's tax laws are clear and easy for taxpayers to interpret.¹⁵⁰ The more difficult the laws are to understand, the harder it will be for taxpayers to comply with the laws. Laypersons are not fully versed with every aspect of legislation. It therefore becomes important for tax authorities to draft tax laws in such a way as to make them understandable and

¹⁴⁷ See Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 307.

¹⁴⁸ OECD (2000). *Report by the Technology Technical Advisory Group* at 51. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

¹⁴⁹ See discussion at paragraph 2.5.1 above.

¹⁵⁰ Ebrill, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 141.

accessible to the general population. Doing so could minimise compliance costs and increase tax compliance.¹⁵¹

Another way of implementing this mechanism would be for tax authorities to make the effort, by means of social media or advertising, to inform residents and taxpayers of the significance of tax compliance under this mechanism. The information should be as clear as possible and in as many languages as possible to educate the general population. The information should clearly state the relevant tax laws applicable; the responsibility of the general public to comply with tax laws; the taxes payable; the consequences for non-compliance; and how every resident should collect and remit the taxes to the relevant authorities.¹⁵²

The OECD has highlighted the fact that consumer taxpayers will need to keep records of every transaction they undertake whilst transacting with foreign businesses.¹⁵³ The OECD has suggested that consumer taxpayers purchase accounting software packages for this purpose.¹⁵⁴ It seems that this could yet prove to be a deterrent rather than an incentive for consumer taxpayers. Not only would purchasing the accounting package signify expenses, but it would also mean that taxpayers will need to take time to familiarize themselves with the accounting software package. This translates into an administrative burden that will be borne by the consumer taxpayer.

The role of tax authorities remains considerable because they will need to conduct audits on the consumer taxpayers. Different jurisdictions will have different methods of auditing their taxpayers. In this regard, Tait states that “*the universal method for the control of VAT and the prevention of tax evasion is the auditing and spot checking of records, coupled with a system of adequate penalties for detected cases of fraud.*”¹⁵⁵ The importance of having a good audit system cannot be overemphasized. Where

¹⁵¹ Ebrill, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 141.

¹⁵² Ebrill, L. Keen, M. Bodin, J.P. Summers, V. (2001). *The Modern VAT* IMF at 141.

¹⁵³ OECD (2000). *Report by the Technology Technical Advisory Group* at 52. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

¹⁵⁴ OECD (2000). *Report by the Technology Technical Advisory Group* at 51. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

¹⁵⁵ Tait, A., A. (1998). *Value Added Tax: International Practice and Problems* International Monetary Fund at 288.

auditing facilities are substandard or inefficient, they should be improved and renovated.¹⁵⁶

It appears that for this mechanism to have a significant degree of success, tax authorities should make the process of tax collection as seamless as possible for taxpayers without the latter incurring needless costs when complying with the relevant tax laws. Tax authorities should be aware that the success of this mechanism is dependent on the co-operation of taxpayers. And for tax authorities to ensure compliance, the approach towards tax collection should be made conducive to taxpayers by making the mechanism quick, easy and relieving.

However, it should be conceded that tax paying culture varies from one state to another and the variation extends to developed and developing countries. For instance, in developing countries such as South Africa, residents pay taxes because they are obliged to pay and not necessarily because they want to pay.¹⁵⁷ The obligation stems from tax legislation and tax authorities who compel residents to pay.¹⁵⁸ Failure to comply usually results in hefty penalties for residents; in some cases, the penalty for non-compliance may be double the amount of the tax payable. It is quite likely then that if tax authorities run a rigorous and persuasive campaign to promote tax compliance, residents will have no other choice but to comply.

3.2.3 Tax at source and transfer mechanism

In terms of this mechanism, the foreign supplier is required to collect tax from the recipient consumer and pay over said tax to the foreign supplier's tax authority who then pays it over to the recipient consumer's tax authority.

¹⁵⁶ Bird, R. M. & Gendron, P. P. (2007). *The VAT in developing and transitional countries* Cambridge University Press at 169.

¹⁵⁷ Misra, R. (2004). *The impact of taxpayer education on tax compliance in South Africa*. Unpublished MCom thesis (University of Kwazulu-Natal) at 8.

¹⁵⁸ Misra, R. (2004). *The impact of taxpayer education on tax compliance in South Africa*. Unpublished MCom thesis (University of Kwazulu-Natal) at 8.

From the onset, it appears that this collection mechanism requires a significant amount of co-operation between states. This co-operation would mostly consist of bilateral agreements between states to facilitate the collection and remittance of taxes. A state will thus be reliant on another state to remit the tax collected. This presupposes that the two contracting states have close diplomatic ties for them to even consider having bilateral agreements for the purposes of tax collection. For example, if no diplomatic ties exist between two states, then it would be difficult for them to agree on matters relating to tax collection. The conclusion seems to be that a state will need to maintain good diplomatic ties with another state for the continued use of this mechanism. Any form of political tension or volatility may prove to be problematic for one state when taxes are due and payable to another state.

The foreign supplier may be required to familiarize itself with the tax laws of the recipient consumer's jurisdiction. This also entails calculating the tax payable according to the tax laws in the jurisdiction where the recipient consumer resides. It remains to be seen whether foreign suppliers will have the necessary backing to comply with foreign laws and to calculate the tax payable to tax authorities.

The OECD has suggested that a suitable mechanism be established for the transfer of revenue from the collecting state to the recipient state.¹⁵⁹ Although such a mechanism has yet to be formulated, technology based solutions seem to be the most viable means of implementing this mechanism.¹⁶⁰

3.2.4 The registration mechanism

The registration mechanism requires a foreign supplier of services to register in the country where consumption occurs in order to account, collect and remit tax to the

¹⁵⁹ OECD (2000). *Report by the Technology Technical Advisory Group* at 60. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

¹⁶⁰ OECD (2000). *Report by the Technology Technical Advisory Group* at 60. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

relevant authorities. According to the OECD, this mechanism is better suited for B2C transactions.¹⁶¹

In order for this mechanism to work, the registration process must be as simple as possible. A registration process that is tedious and cumbersome will most likely deter foreign businesses from conducting business in that state. This can lead to a potential loss of revenue for tax authorities.

The OECD has made reference to the fact that the registration mechanism imposes an unnecessary compliance burden on foreign suppliers.¹⁶² This stems from foreign businesses transacting with consumers in multiple jurisdictions.¹⁶³ The conclusion seems to be that a foreign business may have to register in each and every jurisdiction where it has customers. It is fair to assume that this is not a path many businesses will be willing to follow; considering the expenses and resources that may be incurred in facilitating registration in different states situated on as many as six different continents.¹⁶⁴

It has also been stated that the registration mechanism poses an administrative burden on foreign suppliers of electronic services.¹⁶⁵ A foreign business that registers in a foreign state must comply with that foreign state's laws. This can entail familiarizing themselves with laws that they possibly do not understand. Not only will they have to monitor online transactions, but foreign businesses will also need to keep records of all the transactions in instances where foreign law requires them to do so.

The registration process must strike a balance between simplicity and specificity. Foreign businesses should be able to register in the country of consumption effortlessly

¹⁶¹ OECD (2006). *International VAT/GST Guidelines* at 13. Available at <http://www.oecd.org/tax/consumption/36177871.pdf>. Accessed on 9 March 2017.

¹⁶² OECD (2000). *Report by the Technology Technical Advisory Group* at 56. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

¹⁶³ OECD (2000). *Report by the Technology Technical Advisory Group* at 55. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017.

¹⁶⁴ Asia, Africa, Europe, South America, North America and Oceania.

¹⁶⁵ See Van Zyl, S. P. (2013). *The collection of Value Added Tax on online cross-border trade in Digital Goods*. Unpublished LLD thesis (UNISA) at 287. See also Steyn, T. (2010). VAT and E-commerce: Still looking for answers? *South African Mercantile Law Journal* at 251 – 255. See also OECD (2001). *Consumption tax aspect of electronic commerce* at 15. Available at <http://www.oecd.org/tax/consumption/1923240.pdf>. Accessed on 15 June 2017.

and without the need to have a physical presence in that state. This is to ensure that foreign businesses do not incur additional costs by setting up an office in a foreign jurisdiction for the purposes of tax collection. In terms of specificity, the registration form should prepopulate all the necessary information that will enable the tax authority to establish the identity of the business. With this information, the tax authorities should be able to verify a business' identity.

It appears that one of the major challenges that the registration system faces is the ability or perhaps the inability to identify the recipient consumer of electronic services. Establishing the identity of the consumer is key as it determines the jurisdiction where the business will need to register for tax collection. This challenge is compounded by the fact that transactions are done over the internet where facilities are not readily available to identify consumers. In comparison to much bigger and more established businesses this poses an even greater challenge to newly formed businesses, since they do not necessarily have the financial means or resources to acquire facilities that will enable them to identify consumers.

In the event that a foreign business is unable to identify the consumer, does the business simply ignore that specific transaction? Ideally, the foreign business could then turn to the consumption jurisdiction for assistance. The jurisdiction would then be able to authenticate and thus verify the identity of the consumer. That is only possible if the jurisdiction does indeed possess the means to identify consumers in its own right. The lack of customer identification by foreign businesses makes the application of the registration system impractical. The OECD has highlighted systems that can be used to ascertain the identity of the consumer. These include a consumer's IP address, credit card details or digital certificates.¹⁶⁶

The need to identify the consumer raises another challenge for tax authorities. Whenever an online transaction occurs, a foreign business would in principle take responsibility for collecting VAT on that transaction. This implies that the tax authorities in the consumption state will have appropriate enforcement measures in place should a

¹⁶⁶ OECD (2000). *Report by the Technology Technical Advisory Group* at 55. Available at <http://www.oecd.org/tax/consumption/1923248.pdf>. Accessed on 8 March 2017. See also discussion at paragraph 3.3 below.

foreign business fail to comply with VAT collection. This poses a new set of challenges for both the consumption state and the foreign business. Firstly, will the consumption state be able to take legal action against the foreign business for non-compliance? Secondly, will the consumption state be able to monitor the activities of the foreign business and the recipient consumers? If so, how will the consumption state monitor activities to which it is not privy? Furthermore, how will this intervention take place without breaching privacy laws? In the improbable event that a consumption jurisdiction takes legal action against a foreign business, which laws will be used to govern any trial process? A discussion on these questions falls outside the ambit of this study. Suffice to say that further research is required to find solutions to these challenges.

The challenges posed by the registration mechanism illustrate that a single state cannot enforce, monitor and collect VAT without co-operation from other states. The OECD has thus stated that the efficacy of the registration mechanism is largely dependent on international co-operation.¹⁶⁷

3.3 METHODS OF ASCERTAINING THE IDENTITY OF A RECIPIENT CONSUMER OF DIGITAL GOODS

3.3.1 Payment information/Billing address

A foreign supplier of intangibles may use the recipient consumer's billing address or payment information in order to ascertain the latter's identity and location.

A purchaser of digital goods may be required to furnish their personal details, including physical address, contact number and country of residence, to foreign suppliers when transacting online. This information is usually required when a purchaser registers for the first time as a customer on an e-commerce website. However, due to the sensitive nature of this information, a purchaser may be reluctant to divulge their true details.

The challenge posed by this method of identification is that it relies solely on the honesty of the recipient consumer. An anxious consumer may provide false information

¹⁶⁷ OECD (2000). *Report by the consumption tax technical advisory group* at 17. Available at <http://www.oecd.org/tax/consumption/1923240.pdf>. Accessed 15 June 2017.

regarding their residence or even identity when transacting online. This may be due to online consumers having genuine concerns about supplying sensitive data to businesses that are unfamiliar to them. There is also an inherent risk that consumer details may be unlawfully appropriated or sold to unknown third parties. Online consumers fret over sharing too much information online and unless foreign businesses have security mechanisms that will safeguard a client's personal details, there is the likelihood that consumers will supply inaccurate information when transacting online.

In 2016, the OECD published recommendations on consumer e-commerce protection.¹⁶⁸ In the publication, the OECD suggested that a consumer's privacy should be safeguarded by implementing measures that will enhance transparency and consumer data collection as well as consumer participation and choice.¹⁶⁹ Foreign businesses should also employ security measures that correspond to the risks associated with online payments.¹⁷⁰

Consumers use different payment systems when purchasing digital goods from foreign businesses. The propensity to use credit cards or debit cards allows consumers to make quick and easy payments for online purchases. Inevitably, a consumer's card details become available to foreign businesses when the consumer supplies the business with their credentials. It would seem that a foreign business will need to configure a consumer's card credentials in an attempt to verify his or her identity or location. At first glance, this does not seem feasible considering the burden this may place on foreign businesses. Foreign businesses would be required to have verification mechanisms in place that will assist them in authenticating the purchaser's address or payment information details against information known to tax authorities in the purchaser's jurisdiction.

The conclusion seems to be that foreign businesses are not able to accurately establish the identity of a consumer by means of the billing address and or the payment

¹⁶⁸ OECD (2016). *Consumer protection in e-commerce*. Available at <https://www.oecd.org/sti/consumer/ECommerce-Recommendation-2016.pdf>. Accessed on 18 June 2017.

¹⁶⁹ OECD (2016). *Consumer protection in e-commerce* at 17. Available at <https://www.oecd.org/sti/consumer/ECommerce-Recommendation-2016.pdf>. Accessed on 18 June 2017.

¹⁷⁰ OECD (2016). *Consumer protection in e-commerce* at 16. Available at <https://www.oecd.org/sti/consumer/ECommerce-Recommendation-2016.pdf>. Accessed on 18 June 2017.

information supplied. This challenge is heightened by the fact that purchasers are not under any obligation to provide their correct personal details online. This may be due to privacy concerns. There are currently no penalties or regulations that will act as deterrent to purchasers who provide false information about their billing address.

A consumer's confidence in supplying their correct details online is interwoven with a foreign business' ability to provide online security. This can only be possible if the parties to the transaction are certain of whom they are transacting with.¹⁷¹

3.3.2 Nature of the supply

In this method, the nature of the transaction can be used as an indicator to determine whether a purchaser is a consumer or a business. For example, if a purchaser buys the digital version of a game, the suggestion is that the purchaser is a private consumer rather than a business.¹⁷²

However, it is possible for private consumers and businesses to purchase the same type of supply. For instance, a business may purchase advertising services for the purpose of advertising its business while a private consumer may do the same. It follows that in instances like this, a recipient's identity may not easily be differentiated since both the private consumer and the business acquired the same service.

According to the OECD, a combination of other elements such as language, currency and content may be used to indicate the destination of the supply.¹⁷³ This can be illustrated by means of the following example:

¹⁷¹ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 25.

¹⁷² See OECD (2003). *Verifying of customer status and Jurisdiction* at 5. Available at <http://www.oecd.org/tax/consumption/5574687.pdf> . Accessed on 1 March 2017. See also See Van Zyl, S. P. (2013). *The collection of Value Added Tax on online cross-border trade in Digital Goods*. Unpublished LLD thesis (UNISA) at 260.

¹⁷³ OECD (2003). *Verifying of customer status and Jurisdiction* at 7. Available at <http://www.oecd.org/tax/consumption/5574687.pdf> . Accessed on 1 March 2017.

Example 6

Jean-Paul purchases digital software online for his PC from Company Q. The software is in French and Jean-Paul pays in Euros.

Assume that the content of the software is standard computer code.

Based on the OECD's suggestion above, Company Q will consider the different elements and possibly conclude that the consumer's jurisdiction is in France. Company Q's inference is based on the fact that the item purchased is in French and the currency used is the Euro. While this may be the likeliest conclusion, it does not consider the fact that the consumer may also be a resident of Belgium or Luxemburg. Both are French speaking countries and both form part of the EU.

This example shows that nature of the supply is not an effective method that can be used to accurately identify a consumer of intangible goods.

3.3.3 Geo-location technology

Svantesson defined geo-location technology as:

*"The technological methods for ascertaining the geographical location of an Internet user or device."*¹⁷⁴

Ascertaining the exact location of an internet user is simplified by utilizing the user's IP address. The reason being is that an IP address usually contains the city, country or even the latitude and longitude position of a user. Every user has a distinctive IP address and it is thus not possible for two users to have similar IP addresses.¹⁷⁵

An IP address is required in order for a user to get access to the Internet. Every time individuals access a website, either through a PC or a mobile device, such as a mobile phone, information is transmitted between the server of the website being accessed and

¹⁷⁴ Svantesson, D.J.B. (2007) Geo-identification and the internet – a new challenge for Australia's internet regulation *Murdoch University E-law Journal* 14(2): 158.

¹⁷⁵ Svantesson, D.J.B. (2007) Geo-identification and the internet – a new challenge for Australia's internet regulation *Murdoch University E-law Journal* 14(2): 157.

the user's browser. The recipient website then receives information about the user including, but not limited to, proxy settings, ISP, and the domain name.

It is quite possible for individuals to manipulate their own IP addresses by using other advanced technologies in order to 'hide' their true locations. However, it should be stressed that not every user has the necessary capabilities to acquire and utilize those technologies.¹⁷⁶

On face value, it seems that geolocation technology can depict the exact location of a recipient consumer of digital goods. Having said that, geolocation does not prove the true identity of the recipient consumer of digital goods. As a result, it may be difficult for tax authorities to implement the use of geolocation technology in the long run without relying on other methods of identification in order to obtain a higher degree of accuracy.

3.3.4 Digital certificates

Basu defined a digital certificate as a “*digital document or an electronic ‘passport’ that attests to the binding of a public key to an individual or an entity.*”¹⁷⁷ A certification authority (CA) is responsible for issuing a digital certificate.¹⁷⁸ A CA may consist of a private company, an organization or a government authority.¹⁷⁹ A digital certificate contains the name of the user or company; the user or company's public key; a digital certificate serial number; an issuance date; an expiration date; and the digital signature of the certification authority.¹⁸⁰

¹⁷⁶ See Van Zyl, S. P. (2013). *The collection of Value Added Tax on online cross-border trade in Digital Goods*. Unpublished LLD thesis (UNISA) at 268.

¹⁷⁷ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at 300. See also Rouse, M. (2013). *Digital certificate*. Available at <http://searchsecurity.techtarget.com/definition/digital-certificate>. Accessed 24 June 2017.

¹⁷⁸ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 271. See also Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at footnote 45 at 301.

¹⁷⁹ Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at footnote 45 at 301. Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 271.

¹⁸⁰ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 271. See also Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at footnote 45 at 301. See also Rouse, M. (2013). *Digital certificate*. Available at <http://searchsecurity.techtarget.com/definition/digital-certificate>. Accessed 24 June 2017.

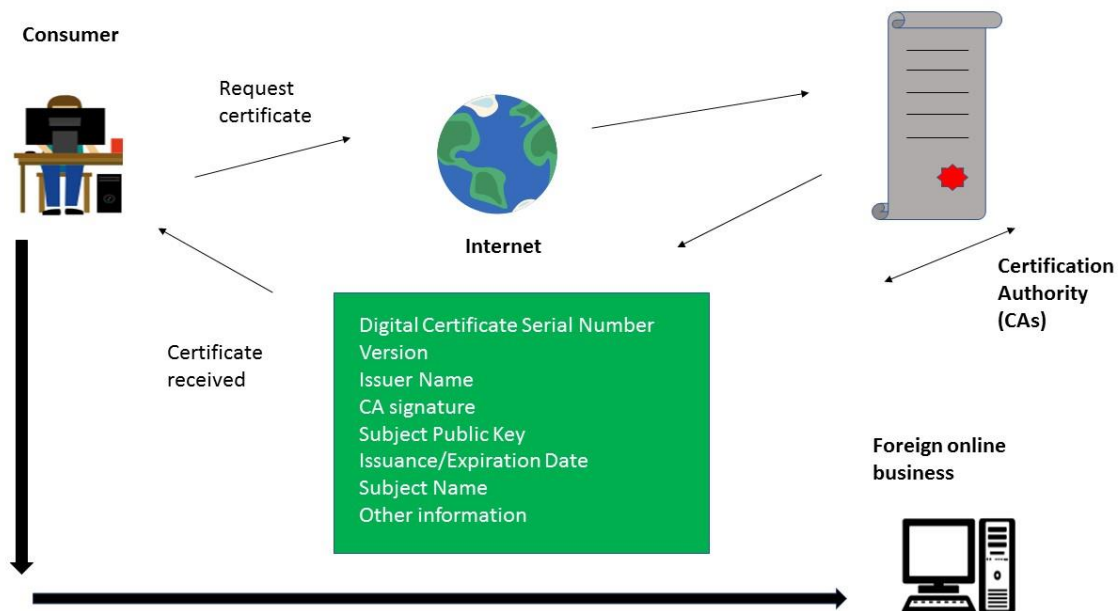


Figure 2 Illustrates how digital certificates work. Adapted from Laudon, K.C. & Traver, C.G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 271. Pictures courtesy of *Piktochart* and *Microsoft Office*.

The information contained in a digital certificate is transmitted over the Internet using a public key infrastructure (PKI).¹⁸¹

A digital certificate allows *person A* to send encrypted messages to *person B* without the message being intercepted by unknown third parties.¹⁸² This ensures that only two persons or entities are privy to the communication. It also improves security and trust between the two persons.

Figure 2 above demonstrates how a digital certificate operates. Suppose Consumer X wants to buy digital goods from an online supplier of digital goods named Company Y. Consumer X requests Company Y's digital certificate. Company Y's digital certificate is issued by a trusted tax authority in its jurisdiction. After obtaining Company Y's public key, Consumer X uses it to decode any messages sent by Company Y as well as using the public key to authenticate Company Y's identity. In turn, Company Y can also

¹⁸¹ Rouse, M. (2013). *Digital certificate*. Available at <http://searchsecurity.techtarget.com/definition/digital-certificate>. Accessed 24 June 2017.

¹⁸² Basu, S. (2007). *Global perspectives on e-commerce taxation law* (Ashgate) at footnote 45 at 301. See also <http://www.worldstart.com/what-is-a-digital-certificate-and-how-does-it-work/>. Accessed 26 June 2017.

request Consumer X's digital certificate from a trusted third party in the latter's jurisdiction in order to establish Consumer X's identity.¹⁸³

According to Laudon and Traver, a consumer creates a public or private key before sending it to a CA for certification.¹⁸⁴ Once a CA has verified a consumer's information, a certificate carrying a consumer's public key is issued.¹⁸⁵

It appears that this method relies on a CAs ability to obtain and verify a person or business's information by means of a public key. The process of verification is essential as without it, online businesses will find it difficult to identify recipient consumers and vice versa.

Using digital certificates to identify parties to e-commerce transactions seems to be reliable, feasible and inexpensive. Online businesses will not be required to incur unnecessary expenses when transacting with consumers. Online businesses will simply require a consumer to provide his or her public key so that it can be verified. Legislation may have to be enacted in both the consumer and business jurisdictions to facilitate the use of digital certificates for the purposes of identification on e-commerce transactions. This will inevitably necessitate a lot of international co-operation and countries may be required to enter into bilateral agreements.

3.3.5 The use of proxies

Proxies can be used to determine the place of consumption of intangible services. The reason being that the VAT collection mechanisms do not accurately establish the identity of the consumer of digital goods nor do they accurately reveal the jurisdiction where the digital goods are consumed. Proxies, used in conjunction with the various VAT collection mechanisms, attempt to pinpoint the precise territory where the digital goods are consumed.

¹⁸³ See Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 272. See also <http://www.anz.com/corporate/products-services/transaction-services/public-key-infrastructure/guide-pki/how-digital-certificate/>. Accessed on 26 June 2017.

¹⁸⁴ Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 272.

¹⁸⁵ See Laudon, K. C. & Traver, C. G. (2014). *E-commerce* 10th edition Pearson Education Ltd at 272.

VAT systems generally use the residence of the recipient of digital goods; the location of the supplier; the location of the subject matter; the place of performance of the supply; and even the place of enjoyment as proxies.¹⁸⁶

For instance, a state that uses the registration mechanism as a method to collect tax may also elect to enact laws that will require suppliers to verify the location of the digital goods. When transacting with the recipient, the supplier will then request the former to furnish the latter with their personal details, which include residence and physical address.

As alluded to above and because it is generally impractical to attain complete accuracy, multiple proxies may have to be used concurrently in order to achieve a higher degree of accuracy.

3.4 CONCLUSION

This chapter discusses the VAT collection mechanisms recommended by the OECD. Each mechanism is critically analysed and discussed. The discussion highlights the strengths and weaknesses of each mechanism. Although no mechanism is without difficulties in its implementation, the use of an intermediary as a collection mechanism appears to be the most viable way to collect VAT in the long run. The reason being that making use of an intermediary shifts the burden from both the supplier of services and the relevant tax authorities. The administrative and compliance costs for foreign suppliers of services are also minimized.

Ascertaining the identity of a consumer recipient of electronic services remains one of the most challenging but important aspects of VAT collection on e-commerce transactions. This is challenging as, due to the nature of e-commerce, there is no hard and fast rule to identify a consumer recipient of electronic services. Identifying the

¹⁸⁶ Millar, R. (2008) Jurisdictional Reach of VAT *University of Sydney Law School: Legal research paper* 8(64): 182. Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1162510. Accessed on 2 April 2017. See also Cockfield, A., Hellerstein, W., Millar R, Waerzeggers, C. (2013). *Taxing Global Digital Commerce* Kluwer Law International at 76 – 78. See also Devereux, M. & de la Feria, R. (2014). Designing and implementing a destination-based corporate tax *University of Oxford* at 15. Available at <http://eureka.sbs.ox.ac.uk/5081/1/WP1407.pdf>. Accessed on 3 April 2017.

consumer recipient of electronic services is important as it determines the place of taxation. Different collection mechanisms deal with this challenge in their own specific ways. However, the OECD has recommended several techniques that can be used to identify the consumer of electronic services.

The methods used to identify the consumer recipient of electronic services have been discussed. Like the VAT collection mechanisms, no method of identifying the consumer recipient is impeccable. This study does, however, indicate that the use of digital certificates is the most viable method to identify a consumer recipient of electronic services. This study also found that the use of a digital certificate is largely dependent on international co-operation.

The following chapter discusses how various jurisdictions collect VAT on B2C transactions.

CHAPTER 4

VAT COLLECTION ON B2C E-COMMERCE TRANSCATIONS IN FOREIGN JURISDICTIONS

4.1 VAT COLLECTION ON THE SUPPLY OF DIGITAL GOODS IN AUSTRALIA

4.1.1 Background

Prior to 1 July 2017, Australian residents who purchased digital goods from foreign suppliers over the internet were not susceptible to the Australian Goods and Services Tax (Australian GST). The relevant legislation in Australia that deals with the taxation of goods and services is A New Tax System Goods and Services Tax Act 1999 (the Australian GST Act).

As of 1 July 2017, all B2C e-commerce transactions relating to the supply of digital goods by foreign suppliers to Australian residents will be subject to Australian GST. This tax is colloquially referred to as the 'Netflix tax'.

Generally, the Australian GST Act imposes an amount of ten per cent on the taxable supplies of goods and services in Australia.¹⁸⁷

4.1.2 Why tax digital goods that are inbound for Australia?

According to the Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016,¹⁸⁸ one of the major reasons for the taxation of digital goods supplied to Australian residents by foreign suppliers was primarily that the Australian GST Act, as it stood prior to 1 July 2017, did not adequately cater for such

¹⁸⁷ Section 9 – 70 of the Australian GST.

¹⁸⁸ Available at http://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5613_ems_80fe4701-d459-4971-9100-126d942757f1/upload_pdf/504670.pdf;fileType=application%2Fpdf. Accessed 31 August 2017.

transactions.¹⁸⁹ Invariably, this led to the under-taxation of services and imposed an excessive compliance burden on foreign suppliers.¹⁹⁰

The rise of e-commerce has made digital goods readily accessible to Australian residents.¹⁹¹ The drawback for local suppliers of similar goods was that they were placed in a difficult position because they were not able to compete with their international counterparts.¹⁹²

Tang opined that the legislative changes are now in line with the destination principle wherein taxation should take place in the jurisdiction where consumption occurs.¹⁹³ Tang also stated that there was a need for legislative changes in order to make the Australian GST Act compatible with the continuous growth of the digital economy.¹⁹⁴

4.1.3 How foreign online businesses determine the residency of the recipient of digital goods

A foreign online business supplying digital goods to Australian consumers is required to charge an additional ten per cent on the value of each and every transaction.¹⁹⁵ An Australian consumer is defined as an Australian resident who is not registered for Australian GST purposes.¹⁹⁶

Whether or not a consumer is an Australian resident for purposes of the Australian GST is a question of fact. However, it appears that the onus to establish whether a consumer is an Australian resident rests solely on the foreign supplier of digital goods.

In order to establish whether or not a recipient of digital goods is an Australian customer, an online business should form a reasonable basis to believe that a recipient

¹⁸⁹ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 3.

¹⁹⁰ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 3.

¹⁹¹ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 11.

¹⁹² Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 11.

¹⁹³ Tang, C. (2016). Australian GST update – 2015 *World Journal of VAT/GST Law* 5(1): 32.

¹⁹⁴ Tang, C. (2016). Australian GST update – 2015 *World Journal of VAT/GST Law* 5(1): 32.

¹⁹⁵ Section 9 – 25(5)(d) of the Australian GST Act.

¹⁹⁶ Section 9 – 25(7) of the Australian GST Act.

is in fact an Australian consumer.¹⁹⁷ This basis upon which the online business relies consists of the typical systems and processes that a business utilizes during day-to-day operations.¹⁹⁸

The following indicators are used to determine whether a recipient is an Australian consumer:

- The recipient's billing address;
- The recipient's mailing address;
- The recipient's banking or credit card details, including the location of the bank or the credit card;
- Location-related data from third party payment intermediaries;
- Mobile phone SIM or landline country code;
- Recipient's country selection;
- IP address;
- Geolocation software;
- Place of establishment of the recipient;
- Representations and warranties given by the recipient;
- The origin of the correspondence;
- Locations, such as a Wi-Fi spot, where the physical presence of the person receiving the service at that location is needed.¹⁹⁹

Foreign suppliers of digital goods have a duty to employ all pertinent information, including personal information provided by the recipient, available on the day of the transaction, to enable them to come to conclude whether or not a recipient is an Australian resident.²⁰⁰ If the foreign supplier is still unable to come to a conclusion on a recipient's residency, then the foreign supplier must weigh the information it has at its

¹⁹⁷ Section 84 – 100(2)(a) of the Australian GST Act.

¹⁹⁸ Australian Goods and Services Tax Ruling 2017/1 at 5.

¹⁹⁹ Australian Goods and Services Tax Ruling 2017/1 at 6 – 7. According to the Australian Government, this list is not a closed list of indicators that point to a recipient's residency.

²⁰⁰ Australian Goods and Services Tax Ruling 2017/1 at 7.

disposal in order to formulate the residency of the recipient.²⁰¹ However, foreign online businesses are not required to attain extra information from the Australian consumer.²⁰²

Alternatively, an online business may take reasonable steps to obtain information that will show whether or not a recipient is an Australian consumer.²⁰³ It follows that the steps taken by an online business are objective and not subjective and every case should be judged on its own merits.²⁰⁴

Consider the following example:

Example 7

Megan subscribes to Netflix. Through Netflix, she is able to stream videos and watch them online. Megan pays for her subscription to Netflix via a credit card issued by the National Australian Bank (NAB) and supplies her billing address, which turns out to be in Perth.

In the example above, Netflix has collected the recipient's billing address as well as the recipient's credit card details as indicators to reasonably establish that Megan is an Australian consumer. Netflix's assumption is based on the fact that Perth is a city in Australia and that the NAB is one of the major banks situated in Australia. Consequently, the subscription fee will be inclusive of ten per cent GST.

It must be borne in mind that the supply must be connected to Australia by falling within the Indirect Tax Zone (ITZ)²⁰⁵ in order for the transaction to be susceptible to Australian GST. In order for a supply to fall within the ITZ, the supply must be made in the ITZ or the supplier must conduct the supply through an enterprise, as defined by the Australian GST Act, in the ITZ.²⁰⁶ Potentially, if an Australian consumer consumes digital goods outside the ITZ then that supply may be GST free.²⁰⁷

Consider the following example:

²⁰¹ Australian Goods and Services Tax Ruling 2017/1 at 7.

²⁰² Australian Goods and Services Tax Ruling 2017/1 at 5 – 6.

²⁰³ Section 84 – 100(1)(a) of the Australian GST Act.

²⁰⁴ Australian Goods and Services Tax Ruling 2017/1 at 9.

²⁰⁵ The ITZ refers to Australia excluding other territories that fall outside the ambit of the GST.

²⁰⁶ Section 9 – 25(5)(a) and (b) of the Australian GST Act.

²⁰⁷ Section 38 – 190 of the Australian GST Act.

Example 8

Keegan is an Australian citizen. He flies to Tokyo via Qantas airways for an international conference. Two hours before the flight approach to Tokyo, Keegan purchases, downloads and reads an e-book on his Amazon Kindle using Qantas airways' Wi-Fi.

In the above example, the supply of the e-book to Keegan falls outside the ITZ. The effective use and enjoyment of the e-book takes place outside the ITZ. In this instance, the supply of the e-book may be GST free.

In situations like the above, it is difficult for the foreign supplier of digital goods to ascertain the jurisdiction where the e-book is used and enjoyed. Furthermore, the Australian GST Act does not currently make provision for the use of proxies in instances where foreign suppliers of digital goods are not able to accurately identify the consumption jurisdiction. As highlighted above,²⁰⁸ various proxies may be used to determine the place where digital goods are used and enjoyed. In the absence of any legislative provision pertaining to the use of proxies in the Australian GST Act, digital goods that would otherwise have been susceptible to Australian GST escape the GST net. This in turn results in under-taxation. The Australian Tax Office (ATO) would then not be able to collect the necessary revenue due to it. It appears that the under-taxation may be resolved by employing proxies in cases where the consumption jurisdiction cannot be easily ascertained.

The rules in legislation pertaining to the place of use and enjoyment may also be implemented as an alternative to using proxies.²⁰⁹ The use and enjoyment principles²¹⁰ may prevail over the use of proxies as proxies aim to simplify the establishment of the location where the digital goods are used and consumed.²¹¹

²⁰⁸ Paragraph 3.3.5.

²⁰⁹ Mesdom, B. (2011). *VAT and Cross-Border Trade: do border adjustments make VAT a fair tax?* Tax Analysts. Available at [http://216.194.248.227/www/freefiles.nsf/Files/MESDOM-15.pdf/\\$file/MESDOM-15.pdf](http://216.194.248.227/www/freefiles.nsf/Files/MESDOM-15.pdf/$file/MESDOM-15.pdf). Accessed 30 September 2017.

²¹⁰ The use and enjoyment principle is currently applied in the EU. See article 58(b) of the EU VAT directive.

²¹¹ Mesdom, B. (2011). *VAT and Cross-Border Trade: do border adjustments make VAT a fair tax?* at 202. Tax Analysts. Available at [http://216.194.248.227/www/freefiles.nsf/Files/MESDOM-15.pdf/\\$file/MESDOM-15.pdf](http://216.194.248.227/www/freefiles.nsf/Files/MESDOM-15.pdf/$file/MESDOM-15.pdf). Accessed 30 September 2017.

The lack of proxies in the Australian GST Act contrasts with current practice in South Africa where proxies are currently used for purposes of ascertaining the location of the consumer recipient of digital goods.²¹² The VAT Act prescribes the following as proxies in South Africa: a person's postal or residential address; where payment for the digital goods is effected from a bank registered in South Africa; and the recipient's residency.²¹³

4.1.4 The collection of GST on B2C transactions in Australia

4.1.4.1 The reverse-charge mechanism

Australian consumer recipients of digital goods, who are not registered or who are not required to register for GST purposes,²¹⁴ are required to pay GST to ATO if they consume digital goods received from foreign suppliers that do not conduct supplies through an enterprise in the ITZ.²¹⁵ A foreign supplier can also enter into an agreement with an Australian consumer recipient of digital goods wherein the GST is paid by the latter.²¹⁶

In these situations, the recipient consumer will be required to do the following:

- Identify the digital goods and services imported during that year;
- Determine which products and services GST should have been paid on;
- Calculate their GST liability for the year;
- Complete a new part of their annual tax return;
- Store records for the relevant length of time.²¹⁷

According to the Australian Parliament, although this collection mechanism is less strenuous on foreign businesses, Australian consumer recipients are the ones that bear the brunt of additional compliance costs.²¹⁸ Also, the ATO's administration burden for

²¹² Part (vi) of the definition of 'enterprise' in the VAT Act.

²¹³ Part (vi) (aa) – (cc) of the definition of 'enterprise' in the VAT Act.

²¹⁴ Section 83 – 5(1)(c) of the Australian GST Act.

²¹⁵ Section 83 – 5(1)(a) and (b) of the Australian GST Act.

²¹⁶ Section 83 – 5(d) of the Australian GST Act.

²¹⁷ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 57.

²¹⁸ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 58.

compliance is extensive as it will necessitate both making changes to the tax system as well as requiring additional means to enable consumer recipients to comply.²¹⁹

4.1.4.2 The registration mechanism

Foreign suppliers of digital goods are required to register for purposes of GST if they carry on an enterprise within the ITZ and have an annual threshold turnover that exceeds \$75 000.²²⁰ That foreign supplier is then required to collect the GST and remit it to the ATO.²²¹ Businesses may choose between two different registration systems.

1. Limited registration

The limited registration system is done online and allows foreign businesses to remit tax to the ATO expeditiously. In terms of this registration method, registration for foreign online businesses is simplified in the following manner:

- The online business is not required to establish its identity;
- Registration will be facilitated online;
- An ATO reference number (ARN) is issued instead of an Australian Business Number (ABN);
- The online business is not entitled to any GST credits;
- The online business must lodge GST returns and pay GST quarterly;
- The online business cannot issue tax invoices.²²²

2. Standard full registration

In terms of the standard registration system, an online foreign business will need to apply for an ABN number. This number will enable identification to a foreign business

²¹⁹ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 58 – 59.

²²⁰ Section 23 – 5 read with section 23 – 15 of the Australian GST Act.

²²¹ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 52.

²²² Available at <https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Doing-business-in-Australia/Australian-GST-registration-for-non-residents/>. Accessed 7 September 2017. See also Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 54. See also PWC (2017). *Changes to Australian GST for cross-border supplies commencing 1 July 2017: are you ready?* *TaxTalk* – Indirect tax at 2. Available at <http://ebiz.pwc.com/wp-content/uploads/2017/06/australia-gst-changes-13jun17.pdf>. Accessed 7 September 2017.

on the ATO system.²²³ The ABN number is obtained after supplying the ATO with evidentiary documentation for the purposes of identification.²²⁴ The downside of this system is that the registration process may be tedious for foreign online businesses.²²⁵

The registration system is beneficial to Australian consumer recipients as their compliance burden will be all but insignificant.²²⁶

4.1.5 The liability for the collection of Australian GST

In certain situations, the liability for the collection of Australian GST on the supply of digital goods is shifted from the supplier of digital goods to the operator of an electronic distribution platform (EDP)²²⁷ if the supply is made through the EDP.²²⁸ The onus to pay the GST will then be borne by the operator of the EDP.²²⁹ The ATO defines an EDP as:

*“A service that allows entities to make supplies available to end-users delivered by electronic communication.”*²³⁰

The ATO identifies a gateway, an online store, a website and an internet portal as examples of EDPs.²³¹ In order for a foreign business to be regarded as an EDP, it must:

- Permit entities to make supplies available to end users;
- Deliver the supplies by means of electronic communication;

²²³ Available at <https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Doing-business-in-Australia/Australian-GST-registration-for-non-residents/#Typesofregistration>. Accessed 9 September 2017.

²²⁴ Available at <https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Doing-business-in-Australia/Australian-GST-registration-for-non-residents/#Typesofregistration>. Accessed 9 September 2017.

²²⁵ Available at <https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Doing-business-in-Australia/Australian-GST-registration-for-non-residents/#Typesofregistration>. Accessed 9 September 2017.

²²⁶ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 55.

²²⁷ Section 84 – 70(1) of the Australian GST Act defines an EDP as: a website, internet portal, store, gateway or marketplace where a service allows entities to make supplies available to end users and the service is delivered by means of an electronic communication and the supplies are to be made by means of electronic communication.

²²⁸ Section 84 – 55(1) of the Australian GST Act.

²²⁹ Note to section 84 – 55(1) of the Australian GST Act.

²³⁰ Available at <https://www.ato.gov.au/business/international-tax-for-business/in-detail/doing-business-in-australia/gst-on-imported-services-and-digital-products---faq/?anchor=GSTonservicesanddigitalproducts>. Accessed 1 October 2017.

²³¹ Available at <https://www.ato.gov.au/business/international-tax-for-business/in-detail/doing-business-in-australia/gst-on-imported-services-and-digital-products---faq/?anchor=GSTonservicesanddigitalproducts>. Accessed 1 October 2017.

- Provide the delivery itself by means of electronic communication.²³²

An EDP operator is not expressly defined in the Australian GST Act. However, an operator of an EDP is a company that operates an online platform or online marketplace wherein a vendor makes use of the online platform in order to sell their digital goods.²³³

An operator of an EDP includes, but is not limited to, eBay and Amazon.²³⁴

Consider the following example:

Example 9

Company X utilizes Amazon's online platform in order to supply its digital books to Australian consumers. Amazon is in control of the purchase price as well as the terms of the sale and the delivery agreement.

In this example, the onus to collect GST on the supply of the digital books will shift from Company X to Amazon. Reason being that the supply of digital goods is made through Amazon and the latter has control of the 'key elements' of the transaction. Company X and Amazon may also enter into an agreement wherein Amazon will take responsibility for GST collection.²³⁵ However, Company X will remain liable to collect GST if it issues a document or invoice to the recipient of the supply and the document or invoice identifies the supply and Company X as being the supplier of the digital goods.²³⁶ The liability to account for GST exists if the operator of an EDP renders a taxable supply.²³⁷

The reasoning behind the shift of GST liability stems from the need to curtail compliance costs for foreign suppliers of digital goods.²³⁸ In addition to this, the perception that

²³² Available at <https://www.ato.gov.au/business/international-tax-for-business/in-detail/doing-business-in-australia/gst-on-imported-services-and-digital-products---faq/?anchor=GSTonservicesanddigitalproducts>. Accessed 1 October 2017.

²³³ See ATO guidelines (2017). *GST on supplies made through electronic distribution platforms* LCG/D4 at 3.

²³⁴ See Tang, C. (2016). Australian GST update – 2015 *World Journal of VAT/GST Law* 5(1): 36.

²³⁵ Section 84 – 60 of the Australian GST Act. See also Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 13.

²³⁶ Section 84 – 55(4)(a) of the Australian GST Act.

²³⁷ Section 9 – 5 of the Australian GST Act defines a taxable supply as: a supply made for consideration and the supply is made in the course or furtherance of an enterprise and the supply is connected with the ITZ and the supplier is registered for or is required to register for GST.

²³⁸ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 13.

online operators have considerable wealth also played a major role in the decision to tax them.²³⁹

At present, South Africa does not have specific provisions in the VAT Act that deal with an EDP's VAT liability. The VAT Act only refers to foreign suppliers of digital goods²⁴⁰ and, as such, it would seem that a foreign EDP operator supplying digital goods to South African recipients will not be susceptible to VAT in South Africa.

4.1.6 Summary of the collection of VAT on the supply of digital goods in Australia

While the taxation of digital goods in Australia is still in its infancy, there are a lot of positives that may be garnered from the new laws. Firstly, the registration procedure has been simplified to allow foreign suppliers of digital goods to register for Australian GST without much fret. With the added incentive of having a choice between two types of registration systems, foreign suppliers may well be encouraged to conduct business in Australia. Secondly, shifting the GST liability from the supplier to the operator of an EDP should be welcomed by suppliers, and it is an addition that SARS may look at implementing in South Africa.

Having said that, the apparent strenuous burden posed on foreign suppliers to actively identify consumer recipient of digital goods must be taken into account. It would seem that the obligation to identify consumer recipients may not be sustainable in the long term as it constantly requires usage of time and resources.

4.2 VAT COLLECTION ON THE SUPPLY OF DIGITAL GOODS IN CANADA

4.2.1 Background

The Canadian Goods and Services Tax (Canadian GST) was established in Canada in 1991 at an initial rate of seven per cent. Currently, the Canadian GST is at five per cent.

²³⁹ Explanatory Memorandum to the Tax and Superannuation Laws Amendment Bill of 2016 at 13. See also Tang, C. (2016). Australian GST update – 2015 *World Journal of VAT/GST Law* 5(1): 36.

²⁴⁰ See definitions of 'supplier', 'person' and 'vendor' in section 1 of the VAT Act.

In addition to the Canadian GST, certain provinces²⁴¹ in Canada apply a Provincial Sales Tax (PST) while other provinces²⁴² apply a Harmonised Sales Tax (HST). HST, applied at a range of between thirteen and fifteen per cent, is a combination of Canadian GST and PST.

Currently, the Canadian Excise Tax Act (Excise Tax Act) does not have specific provisions that deal with the taxation of the supply of digital goods²⁴³ to Canadian consumers. In order for a foreign supplier of digital goods to be liable for Canadian GST, the foreign supplier will have to be carrying on a business in Canada. Whether or not a foreign supplier is carrying on a business in Canada is a question of fact and every case must be judged on its own set of circumstances.

4.2.2 How Canadian GST is collected on the supply of digital goods

In order for a foreign supplier of digital goods to be liable for Canadian GST, the foreign supplier must be rendering a taxable supply for purposes of the Excise Act. A taxable supply is a supply made in the course of a commercial activity.²⁴⁴ A commercial activity is defined as a “*business conducted for profit except to the extent of rendering exempt supplies.*”²⁴⁵

A business is broadly defined in the Excise Tax Act. It includes, but is not limited to, a trade, a profession, a calling or any kind of undertaking.²⁴⁶ It follows that a foreign business will be conducting a commercial activity if it supplies digital goods to Canadian consumers in order to make a profit.

²⁴¹ British Columbia, Manitoba, Quebec and Saskatchewan.

²⁴² New Brunswick, Ontario, Prince Edward Island, Newfoundland and Labrador.

²⁴³ Digital goods are defined as either services or intangible personal property. See CRA (2002). GST/HST Technical Information Bulletin B-090. Available at <https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/b-090-gst-hst-electronic-commerce/gst-hst-electronic-commerce-3.html>. Accessed on 17 September 2017.

²⁴⁴ Section 123(1) of the Excise Tax Act.

²⁴⁵ Section 123(1) of the Excise Tax Act.

²⁴⁶ Section 123(1) of the Excise Tax Act.

4.2.2.1 Carrying on a business in Canada

The liability of a foreign business to pay Canadian GST stems from whether it is carrying on a business in Canada. The term ‘carrying on a business’ is not defined in the Excise Tax Act. The Canadian Revenue Authority (CRA) has published guidelines to aid in determining whether a foreign business is conducting a business in Canada. These factors include:

- The place of delivery;
- The place of payment;
- The place where agents or employees of the non-resident are located;
- The place where purchases are made or assets are acquired;
- The place from which transactions are solicited;
- The location of assets or an inventory of goods;
- The place where the business contracts are made;
- The location of a bank account;
- The place where the non-resident’s name and business are listed in a directory;
- The location of a branch or office;
- The place where the service is performed; and
- The place of manufacture or production.²⁴⁷

It appears that some of the factors suggest that a foreign business needs some sort of physical presence in Canada.²⁴⁸ Be that as it may, the need to have a permanent establishment in Canada is not a prerequisite for a foreign business to be considered to be carrying on a business in Canada.²⁴⁹ A permanent establishment is defined as a fixed establishment or business where a person makes taxable supplies.²⁵⁰

²⁴⁷ CRA (2005). GST/HST Policy Statement P-051R2. Available at <https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/p-051r2-carrying-on-business-canada/p-051r2-carrying-on-business-canada.html>. Accessed 17 September 2017.

²⁴⁸ For instance, the location of a branch or office presupposes that a foreign business might have an office in Canada.

²⁴⁹ See CRA (2005). GST/HST Policy Statement P-051R2. Available at <https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/p-051r2-carrying-on-business-canada/p-051r2-carrying-on-business-canada.html>. Accessed 17 September 2017.

²⁵⁰ Section 123(1) of the Excise Tax Act.

4.2.2.2 The Registration requirement

A foreign business is required to register²⁵¹ for the purposes of tax collection if the foreign business engages in a commercial activity whilst rendering taxable supplies in Canada.²⁵² A foreign business is not required to register if it does not carry on any business in Canada.²⁵³ The registration threshold is currently at \$30 000, unless the foreign business is a small supplier as defined in the Excise Tax Act.²⁵⁴

Consider the following example:

Example 10

Company B supplies digital music to Richard, a Canadian resident. Company B does not have a branch or office in Canada but makes regular supplies to other Canadian residents to an amount exceeding \$30 000.

In the example above, Company B will be required to register for Canadian GST since it carries on a business in Canada. Company B would then be required to collect and remit the relevant tax to the CRA. If Company B was not carrying on a business in Canada then it would not be required to register for Canadian GST. In instances where there is no GST liability for Company B, Richard would then be required to collect and remit the necessary tax to the CRA. Wyonch stated that Canadian recipients of digital goods are not always familiar with the fact that they are supposed to collect and remit taxes to the CRA in the event that foreign businesses are not liable to do so.²⁵⁵

²⁵¹ Registration is done online.

²⁵² Section 240(1) of the Excise Tax Act.

²⁵³ Section 240(1)(c) of the Excise Tax Act.

²⁵⁴ See section 148(1)(a), (b) and subsection (2) of the Excise Tax Act.

²⁵⁵ Wyonch, R. (2017). *Bits, Bytes and taxes: VAT and the Digital Economy in Canada* C.D. Howe Institute Commentary No 497 at 4. Available at https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_487.pdf.

Accessed 18 September 2017.

Canadian residents are required to complete a form²⁵⁶ with the necessary information and submit the form to the CRA.²⁵⁷

4.2.2.3 Summary of the collection of VAT on the supply of digital goods in Canada

Foreign suppliers of digital goods are currently subject to Canadian GST if they carry on a business in Canada. However, it appears that foreign suppliers can easily sidestep GST liability if they do not have some sort of permanent establishment in Canada. This has also been highlighted by Wyonch.²⁵⁸ If that is indeed the case, GST liability is then shifted to the Canadian recipient of digital goods. As alluded to above,²⁵⁹ relying on Canadian consumer recipients may not necessarily be the most viable method of collecting GST on the supply of digital goods.

4.3 VAT COLLECTION ON THE SUPPLY OF DIGITAL GOODS IN NORWAY

4.3.1 Background

Norway²⁶⁰ recently amended its Value Added Tax Act 19 of 2009 (Norwegian VAT Act) to cater for the collection of VAT on the supply of digital goods to Norwegian consumers.²⁶¹ Norway imposes a general flat rate of 25% VAT on the supply of goods and services.

²⁵⁶ GST/HST Return for Imported Taxable Supplies, Qualifying Consideration, and Internal Exchange Charges. Available at <https://www.canada.ca/content/dam/cra-arc/migration/cra-arc/E/pbg/gf/gst59/gst59-17e.pdf>. Accessed on 18 September 2017.

²⁵⁷ See also Wyonch, R. (2017). *Bits, Bytes and taxes: VAT and the Digital Economy in Canada* C.D. Howe Institute Commentary No 497 at 4. Available at https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_487.pdf. Accessed 18 September 2017.

²⁵⁸ Wyonch, R. (2017). *Bits, Bytes and taxes: VAT and the Digital Economy in Canada* C.D. Howe Institute Commentary No 497 at 5 - 9. Available at https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_487.pdf. Accessed 18 September 2017.

²⁵⁹ Paragraph 4.2.2.2.

²⁶⁰ Norway is currently not a member of the EU. As such, Norway is not susceptible to the EU VAT rules.

²⁶¹ Effective from 2011.

This change in the Norwegian legislation stems from the OECD's recommendation that taxation should take place in the country where the services are consumed.²⁶²

As a result of this change, foreign suppliers of digital goods are now required to collect and remit tax to the Norwegian Tax Administration (Skatteetaten).²⁶³

4.3.2 The collection of VAT on the supply of digital goods in Norway

Electronic services are defined in the Norwegian VAT Act as those “*services delivered remotely using the internet; which are obtained through the use of information technology.*”²⁶⁴ An essential part of the definition of electronic services is that the delivery of the services should take place without the involvement of any human element.²⁶⁵

Norwegian recipients of electronic services are liable to pay VAT on the supply of electronic services to them by foreign suppliers of electronic services.²⁶⁶ The recipient of these electronic services must reside within the ‘VAT area’.²⁶⁷ The VAT area is defined as the interior as well as the territorial area consisting of Norway.²⁶⁸ Another requirement is that the supply must be subject to VAT in the VAT area.²⁶⁹ Electronic services delivered over the internet to Norwegian recipients will be subject to VAT.²⁷⁰

Interestingly, if ‘electronic communication services’ are supplied to the VAT area via a ‘fixed terminal’, VAT will be paid on the specific transaction even though the consumer recipient is not resident in the VAT area.²⁷¹ The term ‘fixed terminal’ is currently not

²⁶² <http://www.skatteetaten.no/en/voesnorway/Legal-Information/>. Accessed 18 September 2017.

²⁶³ <http://www.skatteetaten.no/en/voesnorway/Legal-Information/>. Accessed 18 September 2017.

²⁶⁴ Section 1 – 3 of the Norwegian VAT Act.

²⁶⁵ The definition of ‘electronic services’ in section 1 – 3 of the Norwegian VAT Act.

²⁶⁶ Section 3 – 30(4) of the Norwegian VAT Act.

²⁶⁷ Section 3 – 30(4) of the Norwegian VAT Act.

²⁶⁸ Section 1 – 2(2) of the Norwegian VAT Act.

²⁶⁹ Section 3 – 30(4) of the Norwegian VAT Act.

²⁷⁰ Section 3 – 30(1) of the Norwegian VAT Act.

²⁷¹ Section 3 – 30(4) of the Norwegian VAT Act.

defined in the Norwegian VAT Act. Gjems-Onstad opined that the term ‘fixed terminal’ may mean a landline telephone or a computer server.²⁷²

In the event that a foreign business makes use of an intermediary for the purposes of delivering electronic services to Norwegian recipients, both the intermediary and the foreign business will be deemed to have made a supply.²⁷³ From the wording of this subsection, it appears that on every occasion that the services of an intermediary are required for the supply of electronic services both the intermediary and the foreign business must account for and remit VAT to the Skatteetaten.

Having said that, the onus rests on the intermediary to register for VAT in Norway where the supply of electronic services is made to a Norwegian recipient and the same supply is subject to Norwegian VAT.²⁷⁴

4.3.2.1 The Simplified registration system

A foreign supplier of electronic services is required to register for VAT in Norway if the total proceeds of sales exceed NOK 50 000 (Norwegian Krone) over a twelve-month period.²⁷⁵ A foreign supplier may make use of the simplified registration system.²⁷⁶

As a taxable person,²⁷⁷ a foreign supplier of electronic services that does not have a place of business in Norway must be registered through a representative that has a place of business in Norway.²⁷⁸ In this instance, the onus is on the representative and the foreign supplier of electronic services to account for VAT.²⁷⁹ If the foreign supplier of

²⁷² Gjems-Onstad, O. (2013). Cross-border electronic services and the need for international cooperation: the Norwegian experience *World Journal of VAT/GST Law* 2(3): 247.

²⁷³ Section 3 – 1(3) of the Norwegian VAT Act.

²⁷⁴ Section 2 – 1(3) read with section 3 – 30(4) of the Norwegian VAT Act.

²⁷⁵ Section 2 – 1(1) of the Norwegian VAT Act. See also <https://www.skatteetaten.no/en/International-pages/Felles-innhold-benytttes-i-flere-malgrupper/Articles/Diverse-utgatte-artikler/Registration-in-the-VAT-Register2/>. Accessed 19 September 2017.

²⁷⁶ Section 14 – 4(1) of the Norwegian VAT Act.

²⁷⁷ A taxable person is a person who is required to register for Norwegian VAT.

²⁷⁸ Section 2 – 1(6) of the Norwegian VAT Act.

²⁷⁹ <http://www.skatteetaten.no/en/voesnorway/Legal-Information/>. Accessed 18 September 2017.

electronic services has a place of business in Norway, it may not make use of the simplified registration system.²⁸⁰

Registration is facilitated online, and upon registration, the foreign supplier of electronic services is issued with an identification number.²⁸¹ Exchanges between the foreign supplier of electronic services and the Skatteetaten are conducted electronically.²⁸²

4.3.2.2 The duty to keep records

Foreign suppliers of electronic services are obliged to keep electronic records of transactions encompassing the supply of electronic services to Norwegian recipients for a period of ten years.²⁸³ These records must also be made available to the Skatteetaten on request.²⁸⁴ The records should contain enough particularity to enable the Skatteetaten to ascertain that the correct amount of tax was calculated and declared.²⁸⁵

The particulars shall contain the following information:

- Documentation reference;
- Delivery date;
- Name and residential address of customer;
- Currency;
- Fee, inclusive of VAT, where the amount is given in Norwegian Krone; and
- VAT.²⁸⁶

4.3.2.3 Summary of the collection of VAT on the supply of digital goods in Norway

²⁸⁰ <http://www.skatteetaten.no/en/voesnorway/Legal-Information/>. Accessed 18 September 2017. See also Gjems-Onstad, O. (2013). Cross-border electronic services and the need for international cooperation: the Norwegian experience *World Journal of VAT/GST Law* 2(3): 248.

²⁸¹ Section 14 – 5(2) of the Norwegian VAT Act.

²⁸² Section 14 – 5(3) of the Norwegian VAT Act.

²⁸³ Section 15 – 10(4) of the Norwegian VAT Act.

²⁸⁴ Section 15 – 10(4) of the Norwegian VAT Act.

²⁸⁵ Section 15 – 10(4) of the Norwegian VAT Act.

²⁸⁶ Section 15 – 10 – 1 of the Regulation to the Norwegian VAT Act.

The Norwegian VAT Act has provisions that allow for foreign suppliers of digital goods to make use of intermediaries when making supplies to Norwegian customers. Notwithstanding the fact that the intermediary and the foreign supplier are both liable for Norwegian VAT, the use of an intermediary for the purposes of VAT collection is a mechanism that SARS may employ in South Africa in order to negate the compliance burden for foreign suppliers of digital goods.

4.4 VAT COLLECTION ON THE SUPPLY OF DIGITAL GOODS IN SINGAPORE

4.4.1 Background

The Inland Revenue Authority of Singapore (IRAS) published an electronic commerce guide to assist foreign businesses that supply digital goods in Singapore.²⁸⁷ Goods and Services Tax (Singaporean GST) is charged at seven per cent on the supply of goods and services effected in Singapore by a taxable person.²⁸⁸ It is a further requirement that a taxable person²⁸⁹ must be rendering supplies in the course or furtherance of their business.²⁹⁰

The term 'digital goods' is currently not expressly defined in the Singaporean GST Act. For purposes of the Singaporean GST, digital goods are considered to be a supply of services.²⁹¹

Therefore, a foreign supplier must charge seven per cent on the supply of digital goods to Singaporean recipient consumers.

4.4.2 The collection of GST on the supply of digital goods

²⁸⁷ IRAS (2016). *IRAS e-Tax Guide: GST Guide for e-commerce* 3rd edition. Available at https://www.iras.gov.sg/irashome/uploadedFiles/IRASHome/e-Tax_Guides/etaxguide_GST_GST%20Guide%20for%20e-Commerce.pdf. Accessed 1 September 2017.

²⁸⁸ Section 8(1) of the Singaporean GST Act (Chapter 117A).

²⁸⁹ Section 8(2) of the Singaporean GST Act (Chapter 117A) defines a taxable person as a person who is required to register in terms of the Singaporean GST Act.

²⁹⁰ Section 8(1) of the Singaporean GST Act (Chapter 117A).

²⁹¹ IRAS e-Tax Guide: GST Guide for e-commerce at 4.

A foreign business supplying digital goods to Singaporean residents is liable for tax on those transactions.²⁹² This also translates into a foreign business' accountability to collect the necessary taxes.²⁹³

In order for a foreign business to charge and collect GST in Singapore, the foreign business needs to be registered and remit the necessary taxes to the comptroller of taxes in Singapore.²⁹⁴ A foreign business must register for GST purposes in Singapore if the foreign business' taxable supplies exceed \$1 million (Singaporean dollars) in any quarter and the preceding three quarters.²⁹⁵ This compulsory registration may be facilitated online.

A foreign business must then issue a tax invoice to Singaporean consumers within 30 days after rendering a supply. The invoice should contain the following information:

- An identifying number;
- The date of issue of the invoice;
- The customer's name and address;
- The type of supply;
- A description of the goods or services supplied;
- Any cash discount offered.²⁹⁶

The IRAS has also stated that all prices as advertised online must be inclusive of GST.²⁹⁷

4.4.3 How will foreign businesses establish the residency of Singaporean customers?

²⁹² Section 8(3) of the Singaporean GST Act (Chapter 117A).

²⁹³ IRAS e-Tax Guide: GST Guide for e-commerce at 4.

²⁹⁴ IRAS e-Tax Guide: GST Guide for e-commerce at 4.

²⁹⁵ Section 1(1)(a) of the First Schedule to the Singaporean GST Act.

²⁹⁶ IRAS e-Tax Guide: GST Guide for e-commerce at 8.

²⁹⁷ IRAS e-Tax Guide: GST Guide for e-commerce at 9.

A consumer will be regarded as being a Singaporean resident if they ordinarily reside in Singapore.²⁹⁸ A foreign business may make use of the following indications in order to determine the residency of a Singaporean customer:

- If the customer has a Singaporean IP address;
- If the customer has a Singaporean domain name;
- If the customer has a Singaporean address in the foreign business' database;
- In the event that a customer does not have a Singaporean IP address or a Singaporean domain name, then the foreign business may ascertain the customer's residency by obtaining their assertion with regards to their residence in Singapore.²⁹⁹

4.4.4 Summary of the collection of VAT on the supply of digital goods in Singapore

Singapore currently has a registration threshold of \$1 million (Singaporean dollars) for foreign suppliers of digital goods. This threshold is significantly higher than that of South Africa.³⁰⁰ In South Africa, a foreign supplier of digital goods is required to register for VAT if the supplies exceed R50 000 in any given year. The registration threshold in South Africa may prove to be anti-competitive in the sense that a newly formed online foreign business will have longer to set up a clientele base in a country like Singapore before it is required to register for VAT as compared to in a country like South Africa where the registration threshold is low.

SARS may want to re-examine the registration threshold in the VAT Act in view of the registration thresholds in other foreign jurisdictions, like Singapore, in an attempt to make the South African e-commerce market more competitive.

²⁹⁸ IRAS e-Tax Guide: GST Guide for e-commerce at 5.

²⁹⁹ IRAS e-Tax Guide: GST Guide for e-commerce at 6.

³⁰⁰ See section 23(1)(A) of the VAT Act.

4.5 THE COLLECTION OF VAT ON B2C E-COMMERCE TRANSACTIONS IN THE EU

4.5.1 Background

The EU recently changed its place of supply rules for the collection of electronically supplied services.³⁰¹ Electronically supplied services have already been defined above.³⁰² According to the 2006 EU VAT directive, electronically supplied services must be taxed in the jurisdiction where the recipient resides or has a permanent address.³⁰³ The reason for the change stems from the need to bring it in line with the destination principle, which states that a service should be taxed in the jurisdiction where it is consumed.³⁰⁴

This may be illustrated by the following example:

Example 11

Paulo, an Italian citizen, subscribes to online journals and newspapers services from an American online company.

In the example above, the American online company provides electronically supplied services, as defined, to Paulo who is an Italian resident. Since Paulo is in the EU, the American online company must charge VAT at 24%³⁰⁵ on the supply of the online journals and newspapers.

Paulo is a non-taxable person for the purposes of VAT. If Paulo was a taxable person,³⁰⁶ then the electronically supplied services would be taxed in the USA.³⁰⁷

³⁰¹ Effective from 1 January 2015.

³⁰² Paragraph 2.4.2.3.

³⁰³ Article 58 of the EU VAT directive.

³⁰⁴ European Commission (2014). *Explanatory notes on the EU VAT changes to the place of supply of telecommunications, broadcasting and electronic services that enter into force in 2015* at 10. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/telecom/explanatory_notes_2015_en.pdf. Accessed 2 July 2017.

³⁰⁵ Italy currently charges a standard VAT rate of 24%.

³⁰⁶ Article 9 of the VAT directive defines a 'taxable person' as: 'any person who, independently carries out in any place any economic activity, whatever the purpose or results of that activity. Any activity of producers, traders or persons supplying services, including mining and agricultural activities and activities of the professions, shall be regarded as economic activity. The exploitation of tangible or intangible property for the purposes of obtaining income therefrom on a continuing basis shall in particular be regarded as an economic activity.'

4.5.2 How is the location of a customer recipient of electronically supplied services established?

The location of the customer recipient of electronically supplied services is established by using what the EU describes as ‘presumptions’. The presumptions are:

- “Where a supplier of telecommunications, broadcasting or electronically supplied services provides those services at a location such as a telephone box, a telephone kiosk, a Wi-fi hotspot, an Internet café, a restaurant or a hotel lobby where the physical presence of the recipient of the service at that location is needed for the service to be provided to him by that supplier, it shall be presumed that the customer is established, has his permanent address or usually resides at the place of that location and that location and that service is effectively used and enjoyed there.”³⁰⁸
- “If the location referred to above is on board a ship, aircraft or train carrying out a passenger transport operation effected within the community the country of the location shall be the country of departure of the passenger transport operation.”³⁰⁹

The above two presumptions are deemed to be ‘irrebuttable’ for the purposes of locating the customer recipient of electronically supplied services.³¹⁰ The ‘rebuttable’ presumptions for the location of a customer are:

- “Where telecommunications, broadcasting or electronically supplied services are supplied to a non-taxable person through his fixed land-line, it shall be presumed that the customer is established, has his permanent address or usually resides at the place of installation of the fixed land-line”;³¹¹
- “Through mobile networks, it shall be presumed that the place where the customer is established, has his permanent address or usually resides is the

³⁰⁷ Article 43 of the VAT directive.

³⁰⁸ Article 24a of the EU council implementing regulation No 1042/2013.

³⁰⁹ Article 24a of the EU council implementing regulation No 1042/2013.

³¹⁰ Cockfield, A., Hellerstein, W., Millar R, Waerzeggers, C. (2013). *Taxing Global Digital Commerce* Kluwer Law International at 310.

³¹¹ Article 24b of the EU council implementing regulation No 1042/2013.

country identified by the mobile country code of the SIM card used when receiving those services”;³¹²

- “For which the use of a decoder or similar device or a viewing card is needed and a fixed land line is not used, it shall be presumed that the customer is established, has his permanent address or usually resides at the place where the decoder or similar device is located or if that place is not known, at the place to which the viewing card is sent with a view to being used there”;³¹³
- “Under circumstances other than those referred to in Article 24a and the points above, it should be presumed that the customer is established, has his permanent address or usually resides at the place identified as such by the supplier on the basis of two items of non-contradictory evidence as listed in Article 24f of the Regulation.”³¹⁴

The evidentiary information used to identify the location of the customer recipient of electronically supplied services includes the customer’s billing address; the customer’s bank address; the customer’s IP address; the customer’s fixed land-line through which the service is supplied; the Mobile Country Code (MCC) of the International Mobile Subscriber Identity (IMSI) stored on the Subscriber Identity Module (SIM) card used by the customer and any other commercially relevant information.³¹⁵

4.5.3 The collection of VAT on electronically supplied services in the EU

Online businesses that provide electronically supplied services can register and account for VAT in the jurisdiction of the identified customer if the online business does not have a permanent establishment in that jurisdiction.³¹⁶ This mechanism, known as the Mini

³¹² Article 24b of the EU council implementing regulation No 1042/2013.

³¹³ Article 24b of the EU council implementing regulation No 1042/2013.

³¹⁴ Article 24b of the EU council implementing regulation No 1042/2013.

³¹⁵ Article 24e and Article 24f of the EU council implementing regulation No 1042/2013.

³¹⁶ European Commission (2013). *Guide to the VAT mini One Stop Shop* at 2. Available at http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/tel_ecom/one-stop-shop-guidelines_en.pdf. Accessed 1 July 2017.

One Stop Shop (MOSS), is optional; online businesses are not compelled to utilize it. MOSS is available to online businesses situated inside and outside the EU.³¹⁷

Upon registration in an EU state, an online business declares the transaction to the relevant tax authorities and pays the VAT due by means of a web portal in the state where the identity of the customer has been established.³¹⁸

An online business that has a fixed or permanent establishment in the EU may not use the MOSS to collect VAT for the supplies made in another EU state in which it has a permanent establishment. An online company that has no fixed or permanent establishment in the EU and is not registered in the EU may make use of the MOSS.³¹⁹ The EU VAT directive does not define the term ‘permanent establishment’. The definition can however be found in the implementing regulation. A permanent or fixed establishment is an “*establishment that is characterised by a sufficient degree of permanence and a suitable structure in terms of human and technical resources to enable it to receive and use the services supplied to it for its own needs.*”³²⁰

An EU online company that utilizes the MOSS must register in the EU state where it has identified the consumer.³²¹ When the online company registers for VAT purposes, it is issued with a VAT identification number. A VAT identification number is also issued to a non-EU online company that supplies services to an EU state where the consumer has been identified.³²²

This may be illustrated by means of the following example:

³¹⁷ European Commission (2013). *Guide to the VAT mini One Stop Shop* at 3. Available at http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/tel_ecom/one-stop-shop-guidelines_en.pdf. Accessed 1 July 2017.

³¹⁸ See also Dale, S. & Vincent, V. (2017). The European Union’s approach to VAT and e-commerce *World Journal of VAT/GST Law* at 2.

³¹⁹ European Commission (2013). *Guide to the VAT mini One Stop Shop* at 3. Available at http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/tel_ecom/one-stop-shop-guidelines_en.pdf. Accessed 1 July 2017.

³²⁰ Article 11 of the EU council implementing regulation No 282/2011.

³²¹ European Commission (2013). *Guide to the VAT mini One Stop Shop* at 6. Available at http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/tel_ecom/one-stop-shop-guidelines_en.pdf. Accessed 1 July 2017.

³²² European Commission (2013). *Guide to the VAT mini One Stop Shop* at 6. Available at http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/tel_ecom/one-stop-shop-guidelines_en.pdf. Accessed 1 July 2017.

Example 12

Online Canadian Company Y provides electronically supplied services to Robert a French citizen. Company Y has no fixed or permanent establishment in France.

In the example above, since Company Y has no fixed or permanent establishment in France, it may make use of the MOSS to account for and remit VAT to the French tax authorities. If Company Y was a French online company, it would have been able to use the MOSS if it had its place of business in the EU or it had a fixed or permanent establishment in the EU.

It appears that having some sort of permanent establishment is a prerequisite for the utilization of the MOSS. The need to have a fixed or permanent establishment could stem from the necessity to establish the identity of the business and the place of taxation for the supply of electronically supplied services. Mikutiené stated that the fixed establishment concept can be used to determine the place of supply for B2B as well as B2C transactions.³²³ According to Mikutiené, the fixed establishment concept “*strongly influences the entitlement of the Member States to tax supplies and affects the cash flow of both the Member States and the businesses supplying and acquiring cross-border services.*”³²⁴

4.5.3.1 Successes, challenges and further improvements of the MOSS

The European Commission stated that the implementation of the MOSS has been largely successful. According to its findings,³²⁵ an amount of €3 billion of VAT was paid and collected in the year 2015. During that same period, 12 000 businesses made use of the MOSS system. Furthermore, the use of the MOSS has led to the reduction of costs for businesses to the tune of €500 million. The MOSS also covered 70% of EU

³²³ Mikutiené, R. (2014). The preferred treatment of the fixed establishment in European VAT *World Journal of VAT/GST Law* 3(3): 166.

³²⁴ Mikutiené, R. (2014). The preferred treatment of the fixed establishment in European VAT *World Journal of VAT/GST Law* 3(3): 166.

³²⁵ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 8. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

turnover on electronic services. All in all, businesses were satisfied with the implementation of the MOSS and revenue collection rose significantly as a result.³²⁶

According to the European Commission, one of the main challenges when using the MOSS is the compliance costs that businesses face when transacting in different states.³²⁷ Online businesses have to deal with as many as 28 different states when transacting with customers in the EU. And with the EU having 24 official languages,³²⁸ it seems almost impossible for online businesses to familiarize themselves with each and every language when dealing with the EU states.

Online businesses have identified market distortions as another impediment.³²⁹ An online business transacting with EU states will encounter different VAT rates that could apply to the same type of electronic services. For instance, a supply of computer software will be subject to VAT at 24% in Italy and 19% in Germany. These market distortions could lead to little or no taxation of that electronic service.³³⁰

Interacting with customers in different states translates into an engagement with different legal frameworks.³³¹ An online business transacting in the EU will encounter multiple sets of legal rules relating to things such as the law of contract, privacy and data protection.³³² These rules are set out differently in each EU state. Familiarising itself with and complying to these separate rules could prove to be burdensome for an online business.

³²⁶ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 8. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³²⁷ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 12. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³²⁸ http://ec.europa.eu/education/official-languages-eu-0_en. Accessed 5 July 2017.

³²⁹ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 13. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³³⁰ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 8. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³³¹ Ecommerce Europe (2015). *Analysis of the survey "barriers to growth"* at 12. Available at <https://www.ecommerce-europe.eu/app/uploads/2016/07/survey-barriers-to-growth-ecommerce-europe-2015-1.pdf>. Accessed on 5 July 2017.

³³² Ecommerce Europe (2015). *Analysis of the survey "barriers to growth"* at 12. Available at <https://www.ecommerce-europe.eu/app/uploads/2016/07/survey-barriers-to-growth-ecommerce-europe-2015-1.pdf>. Accessed on 5 July 2017.

Krinis³³³ argued that the MOSS poses additional challenges for online businesses. These include difficulties with the identification of customers, recordkeeping and home country audits. In terms of recordkeeping requirements, an online business is required to keep records for a period of ten years.³³⁴ Krinis stated that the time frame for recordkeeping should be reduced.³³⁵ Krinis also stated that home country audits should be introduced for online businesses in the state where the customer has been identified.³³⁶ Moreover, Krinis declared that two items of evidence³³⁷ may be used to establish the identity of the customer.³³⁸

Along with these improvements suggested by Krinis, the European Commission has also highlighted other enhancements that can be applied to the MOSS. Firstly, the European Commission agrees with Krinis and has acknowledged that the ten year recordkeeping period is lengthy and that other avenues should be explored.³³⁹ Secondly, better communication is required between micro-businesses, Member States and the European Commission.³⁴⁰ Thirdly, as micro-businesses have stressed the lack of a threshold as a problematic area, the European Commission aims to introduce thresholds to the amount of €10 000 and €100 000 from 2018 to assist micro-businesses and SMEs.³⁴¹ Fourthly, identification of the customer remains a concern.³⁴²

³³³ Krinis, D. (2016). *VAT challenges of the Digital Economy – an EU perspective* unpublished Master of Accounting dissertation (Universidade do Minho Portugal) at 66. Available at <https://repositorium.sdum.uminho.pt/bitstream/1822/42303/1/D%C3%B3ra%20Krinis.pdf>. Accessed 4 July 2017.

³³⁴ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 19. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³³⁵ Krinis, D. (2016). *VAT challenges of the Digital Economy – an EU perspective* unpublished Master of Accounting dissertation (Universidade do Minho Portugal) at 67. Available at <https://repositorium.sdum.uminho.pt/bitstream/1822/42303/1/D%C3%B3ra%20Krinis.pdf>. Accessed 4 July 2017.

³³⁶ Krinis, D. (2016). *VAT challenges of the Digital Economy – an EU perspective* unpublished Master of Accounting dissertation (Universidade do Minho Portugal) at 85. Available at <https://repositorium.sdum.uminho.pt/bitstream/1822/42303/1/D%C3%B3ra%20Krinis.pdf>. Accessed 4 July 2017.

³³⁷ See paragraph 3.4.2 above.

³³⁸ Krinis, D. (2016). *VAT challenges of the Digital Economy – an EU perspective* unpublished Master of Accounting dissertation (Universidade do Minho Portugal) at 69 - 70. Available at <https://repositorium.sdum.uminho.pt/bitstream/1822/42303/1/D%C3%B3ra%20Krinis.pdf>. Accessed 4 July 2017.

³³⁹ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 9. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³⁴⁰ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 9. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³⁴¹ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 9. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017. See https://ec.europa.eu/taxation_customs/business/vat/digital-single-market-modernising-vat-cross-border-

This challenge was underscored by Krinis as stated above. As a way to simplify the identification of consumers, Veltrop suggested that a universal pricing system should be adopted to entice consumers to provide the correct personal details to suppliers.³⁴³ Veltrop also stated that as a means to reduce compliance costs for suppliers, ‘fast and simple’ ordering systems should be made accessible to consumers.³⁴⁴

Other commentators have underlined the need for the harmonization of EU VAT rules in order to reduce the compliance burden on suppliers.³⁴⁵

4.6 CONCLUSION

This chapter discusses the collection of VAT on the supply of digital goods in foreign jurisdictions. Australia has recently introduced what is known as the ‘Netflix tax’ on the supply of digital goods by Foreign businesses to Australian consumer recipients. A foreign supplier of digital goods must charge Australian GST on those supplies and account for and remit the taxes to the Australian tax authorities. Australia has incorporated a simplified registration system to enable foreign businesses to register for and collect Australian GST. Similarly, Norway has a simplified registration method that enables foreign suppliers to register for and collect tax on the supply of digital goods to Norwegian residents.

While Canada does not have specific legislation that deals with the taxation of the supply of digital goods, the taxation of digital goods is couched in whether a foreign supplier of digital goods is carrying on a business in Canada. The term ‘carrying on a business’ is not expressly defined; as such, foreign suppliers make use of guidelines in order to determine their GST liability.

[ecommerce_en](#). Accessed 5 July 2017. See also Dale, S. & Vincent, V. (2017). The European Union’s approach to VAT and e-commerce *World Journal of VAT/GST Law* at 2.

³⁴² European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 9. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³⁴³ Veltrop, M., M., J., A., (2014). *How to Identify Customers of e-Services in VAT* Maastricht University 1:137.

³⁴⁴ Veltrop, M., M., J., A., (2014). *How to Identify Customers of e-Services in VAT* Maastricht University 1:137.

³⁴⁵ See <http://www.thetaxadviser.com/issues/2017/jun/european-mini-one-stop-shop-indirect-tax-compliance.html>. Accessed 4 July 2017.

This chapter also discusses the collection of VAT on B2C transactions in the EU. The EU has recently changed its place of supply rules. In terms of these new rules, the taxation of electronically supplied services will take place in the jurisdiction of the consumer. Online businesses can register in the jurisdiction of the customer to facilitate VAT collection. This process is known as the mini one stop shop mechanism.

However, the implementation of the MOSS has not been plain sailing. Although it has helped tax authorities to collect an increased amount of VAT, MOSS has given rise to a set of challenges. Among those challenges faced by online businesses is the unenviable task of dealing with 24 different languages, 28 different legal frameworks and, potentially, audits from 28 different states. There is a need for the relevant rules, policies and legal frameworks to be harmonized to stem the trend of under-taxation.

The European Commission is in the process of improving the MOSS. These improvements will be implemented over an extended period of time. Seeing that the EU is the recognized forerunner in the implementation and use of the MOSS,³⁴⁶ perhaps other jurisdictions will follow suit in adopting mechanisms that are similar to the MOSS.

The implementation of the MOSS has brought about a shift in the way VAT is collected in the EU. The MOSS, albeit not flawless, or a mechanism akin to the MOSS may be employed in the Southern African Development Community (SADC). Its implementation in the SADC³⁴⁷ region would enable foreign suppliers of digital goods to register for and account for VAT in one country in the SADC region instead of registering in each country in the SADC. A model similar to that of the MOSS will not be easy to implement without examining the current MOSS; improving on it where the need arises; harmonizing the VAT rules in the SADC region; greater co-operation between member states; and expanding the tax administration, among other things.

³⁴⁶ European Commission (2016). *Modernising VAT for cross-border B2C e-Commerce* at 9. Available at https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_379.pdf. Accessed on 5 July 2017.

³⁴⁷ Currently consisting of Angola, Botswana, Malawi, Lesotho, Namibia, Zimbabwe, Swaziland, Democratic Republic of Congo, Mozambique, Zambia, Madagascar, Tanzania, South Africa, Seychelles and Mauritius.

CHAPTER 5

CONCLUSION AND RECOMMENDATIONS

5.1 INTRODUCTION

The main objective of this study was to explore the various VAT collection mechanisms prescribed by the OECD so as to determine the suitability and the efficiency of the VAT collection mechanisms currently in place in South Africa.

Secondary objectives were also identified. These were the identification of:

- i. The problems posed by e-commerce in relation to the taxation of digital goods. These are addressed in Chapter 2 of this study.
- ii. Whether South Africa currently has adequate infrastructure for the collection of taxes garnered through electronic transactions. This question is addressed in Chapter 2 of this study.
- iii. Whether there are any compliance verification mechanisms and penalties available in the event that foreign businesses do not adhere to the VAT Act. This is addressed in Chapter 2 of this study.
- iv. The most effective and efficient collection mechanism that can be adopted in South Africa. This is addressed in Chapter 3 of this study.
- v. Whether there is a cohesive and consistent system of identification of parties involved in electronic transactions. This is addressed in Chapter 3 of this study.
- vi. The collection mechanisms currently implemented in foreign jurisdictions such as the EU and Canada. This is addressed in Chapter 4 of this study.

5.2 FINDINGS OF THIS STUDY

South Africa currently employs the registration and the reverse-charge mechanisms as the means to collect VAT on the supply of digital goods to South African recipients.

It has been argued that the tax authorities in South Africa have difficulty in ascertaining whether a supply of electronic services occurred in South Africa. This is simply because

there are presently no mechanisms in place in the VAT Act that will aid the fiscus to identify consumer recipients of digital goods. This problem is compounded by the fact that the current VAT Act does not have explicit place of supply rules.

This study found that the rise of e-commerce has blurred the traditional way in which tax authorities collect VAT. Although it is relatively simple to determine where the supply and consumption of physical goods take place, the same cannot be said about digital goods. The reason being is that digital goods are virtual and intangible. As a result, it is difficult to trace the exact locations of these goods and where they are consumed. Although this problem is not limited to South Africa, the South African tax authorities have attempted to address this by amending the VAT Act to enable them to determine the precise location of the consumer recipient of digital goods. This has been facilitated by the introduction of proxies to the VAT Act.

Despite the introduction of proxies, it seems that the burden is on the foreign suppliers of digital goods to ascertain the jurisdiction of the consumer recipient of digital goods. This study argues that this is an unnecessary burden on the foreign suppliers of digital goods.

This study also argues that the current definition of 'electronic services' in the VAT Act is lacking to the extent that it does not cater for other services that would have otherwise constituted electronic services.³⁴⁸ A lack of international cooperation and coordination regarding what constitutes 'electronic services' has compounded the problem. Furthermore, since the amendment of the VAT Act, no new regulations have been published to include additional services that constitute 'electronic services'.³⁴⁹

This study found that although the reverse-charge mechanism is currently the default mechanism for the collection of VAT on the supply of electronic services in South Africa, the mechanism has significant shortcomings. The study concluded that most recipients of electronic services are unaware that they should account for VAT when receiving electronic services from a foreign supplier or vendor of electronic services. This lack of awareness leads to under-taxation.

³⁴⁸ See paragraph 2.4.2.3 above.

³⁴⁹ As at 11 November 2017.

This study has uncovered that SARS may be considering using intermediaries to alleviate the administrative and compliance burden posed by the VAT Act on foreign suppliers of electronic services. Although this may be a good initiative, it seems that the use of an intermediary for the purposes of VAT collection may not be implemented via the VAT Act but via a *Binding General Ruling*. The consequences of which are highlighted above.³⁵⁰

This study argued that it is difficult for a single state to apply the registration mechanism effectively without cooperation from other states. The conclusion seems to be that if other states are reluctant or unwilling to cooperate then the efficacy of the registration mechanism becomes tenuous.

In this study, it is maintained that the use of an intermediary seems to be an appropriate way of collecting VAT on the supply of digital goods. One of the major benefits of using an intermediary is that it reduces the compliance costs that would otherwise have been borne by foreign suppliers of digital goods. Moreover, the obligation to collect and remit VAT would then lie with the intermediary who would be in a better position since it has greater knowledge and understanding of the tax laws in the consumption state.

It is also contended that digital certificates should be used as a method of ascertaining the identity of the consumer recipients of digital goods. Not only would it be more economical and dependable to use digital certificates but, it also appears that digital certificates provide a heightened degree of accuracy as compared to other methods of identification.

This study explored how VAT is collected on the supply of digital goods in foreign jurisdictions like Norway and Australia. Best practices were identified and highlighted for the benefit of VAT collection in South Africa. SARS should take note of these in order to improve VAT collection in South Africa.

5.3 THE SIGNIFICANCE OF THIS STUDY

³⁵⁰ Paragraph 2.7 above.

This study was undertaken because there was a need to assess the current VAT legislation in order to determine if it can cater for the continuous growth of e-commerce. E-commerce has proven to be a niche, but challenging, form of trading. There is a likelihood that e-commerce will continue to grow in the years to come. With the growth of e-commerce comes the possibility of new technological advancements. These new technological advancements will bring about a new set of encounters for tax authorities.

If tax authorities do not find ways to come to terms with the growth of e-commerce, the conclusion is that the taxes due will go uncollected. This becomes an obstacle, particularly in developing countries where there is an overreliance on VAT as a source of revenue for government expenditure. If the necessary revenue is not collected, consumers end up bearing the brunt of government and fiscal inefficiency as little or no revenue is allocated to healthcare, housing, job creation, education and infrastructure, to mention but a few.

The responsibility to collect VAT is twofold. In as much as it is the government's responsibility to administer and collect VAT, consumers also need to take the initiative and collect VAT; particularly where legislation allows for the reverse-charge mechanism as a form of VAT collection. Consumers cannot simply turn a blind eye in the hope that the government will assume all the responsibility. Consumers need to play an active role and share the responsibility of VAT collection.

Tax authorities should ensure that consumers are aware of VAT liability in instances where the reverse-charge mechanism is applicable. Awareness campaigns may be facilitated, among others, via newspapers, advertisement boards, television advertisements and social media. The significance of VAT liability should be highlighted so as to aid government in attaining a greater revenue target.

5.4 RECOMMENDATIONS

In view of the findings shown in this study, the following recommendations are made:

- The VAT Act should be amended to allow for the collection of VAT on the supply of digital goods to South African consumers by using intermediaries *in lieu* of utilizing the reverse-charge mechanism, which is currently the default mechanism for collecting VAT on e-commerce transactions.
- The VAT Act should be amended to make provision for specific place of supply rules.
- The VAT Act should be amended and provision should be made therein for the use of digital certificates to enable SARS to identify the recipients of digital goods in South Africa.
- The definition of 'electronic services' should be amended and additional services be included in the definition.
- The VAT Act should be amended and provision should be made for VAT liability of the operators of EDPs.
- The current registration threshold should be positively adjusted in order to make the e-commerce market more competitive.
- SARS and the South African government should consider implementing a MOSS like collection system in the SADC region. South Africa is a member of SADC and should take the initiative in this regard.

5.5 VAT COLLECTION – A WAY FORWARD

It is trite that the collection of VAT differs from country to country (as highlighted in Chapter 4). A collection mechanism that seems to work for country A may not necessarily work well for Country B. The reasons for success vary from one jurisdiction to another. While South Africa may study how VAT is collected in other jurisdictions, South Africa should adopt a collection mechanism that fits with the current VAT policies and legislation.

The efficacy of VAT collection will largely depend on the policies and legislation in place at the relevant time. In order to improve VAT collection, the relevant policies and legislation will have to be amended to cater for a mechanism that is more suitable and is tailor made for the collection of digital goods.

It may be necessary for South African tax authorities to use technological solutions to tackle the challenges brought by the growth of e-commerce and VAT collection. This statement is reinforced by a famous adage, “fight fire with fire”. A discussion on which technological solutions may be employed is beyond the scope of this study. Further research needs to be conducted with the intention of adducing concrete and efficient technological solutions that will aid in improving VAT collection on the supply of digital goods.

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