SUGGESTED APPROACH TO DRAFTING SIGNIFICANT ECONOMIC PRESENCE LEGISLATION

JULY 2025

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FORUM SUR L'ADMINISTRATION FISCALE AFRICAINE

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INTRODUCTION

The need to address the tax challenges arising from the digitalisation of the economy continues to be critical especially among developing countries. ATAF has explored these challenges in-depth in various publications including: the 'ATAF Suggested Approach to Drafting Digital Services Tax Legislation' and the 'ATAF Policy brief in Taxing Digital Firms in Africa'. We now advance the work on addressing these challenges through this Suggested Approach to Drafting Significant Economic Presence (SEP) Legislation.

Multinational enterprises (MNEs) that provide digital services carry on that business in African countries with no or very limited physical presence in those countries. With the current international tax rules only allocating taxing rights to a country where a non-resident enterprise creates sufficient physical presence in that country (referred to as a tax nexus), the risk of tax base erosion and negative spill overs (including loss of revenue and un-level playing field) persists and are significant. This Suggested Approach to Drafting SEP Legislation aims to address the shortcomings of the existing tax nexus rules by introducing the concept of a significant economic presence; premised on revenue derived by a MNE from predefined in-scope transactions and materiality thresholds to ensure the economic presence is ***'significant'***.

This SEP legislation is an alternative to a Digital Services Tax (DST). Generally, both SEP legislation and DST aim to tax a non-resident that does not have a physical presence in a country and provides digitally enabled services and activities to customers and users in that country (i.e. it is an economic activity that is market-based). Whilst a DST and SEP legislation have similar design features such as relying on levels of revenue to establish nexus, having similar scope of the targeted digital services as well as similar rules for determining the location of users, there are some differences particularly on the determination of tax base and their interaction with Double Taxation Agreements. A DST imposes tax on gross revenue while SEP charges tax on the profit or deemed profit of a non-resident. Additionally, SEP is usually designed as an income tax provision that would be within the scope of Double Tax Agreements. However, DST may be designed within or outside the scope of income tax law hence not subject to Double Tax Agreements. ATAF members may wish to consider a SEP, instead of a DST, because of the position taken with respect to DSTs in the Pillar 1 Amount A Multilateral Convention (MLC) text.[1]

The Amount A MLC text that was released in October 2023, whilst not yet agreed by the Inclusive Framework, states that, 'upon adoption and ratification of the Amount A MLC a country must repeal any DSTs and relevant similar measures'. The Amount A MLC further defines a 'DST and relevant similar measure' in three cumulative conditions

[1]OECD, THE MULTILATERAL CONVENTION TO IMPLEMENT AMOUNT A OF PILLAR ONE (OECD 2023)

under Article 39. The cumulative conditions are that: the legislation is market based, it is ring fenced to non-resident persons only and is not subject to existing tax treaties.

This Suggested Approach embodies a SEP legislation that is part of the Income tax legislation and in light of the Amount A MLC text, means that: a country is able to impose an income tax on a non-resident on a market-based criteria, the law is ringfenced to non-residents and is subject to existing tax treaties in force in that country. Therefore, within the definition of a 'DST and relevant similar measure' in accordance with the provisions of article 39 of the Amount A MLC, this SEP legislation is not within scope of that definition. This approach is suited to countries that prefer to align their tax measures to the outcomes of the Amount A MLC provisions. If a country signs and ratifies the Amount A MLC then it will be required to "switch off" its SEP rules for those MNEs in scope of Amount A from the date Amount A comes into effect in the country.

The key provisions of this Suggested Approach include:

- The taxable person that the legislation seeks to bring into the tax net;
- What it means to have a SEP in a country, including the use of materiality thresholds in defining a SEP;
- The digital services revenue in scope of a SEP;
- The rules for attributing revenues to a SEP;
- The mode of determining the taxable profits of a SEP using a deemed profits amount based on those attributed revenues; and
- The registration and filing requirements of taxable persons under a SEP.

All of the above design elements have been drafted in the rules below and further explained in the Explanatory Notes.

SUGGESTED APPROACH: LEGISLATION FOR SIGNIFICANT ECONOMIC PRESENCE

PART I: LIABILITY TO TAX ON A SIGNIFICANT ECONOMIC PRESENCE

Section 1: Charge to tax

1 Where a non-resident person derives revenue, directly or indirectly from or attributable to [Country], in respect of a significant economic presence in [Country], that person shall be liable to income tax.

Section 2: Definition of SEP

2. For the purposes of Section 1, a non-resident person shall be deemed to have a significant economic presence in [Country], in a chargeable period, where:

a) the revenue derived, directly or indirectly from or attributable to [Country] is greater than USD [X] or its equivalent in local currency; and

b) the revenue is in respect of services delivered over the internet or an electronic network or through online platforms including the following services:

i. Online Advertising Services;

ii. Data Services;

iii. Services delivered through an Online Marketplace or Intermediation Platform, including an Accommodation Online Marketplace, a Vehicle Hire Online Marketplace and any Other Transport Online Marketplace;

iv. Digital Content Services, including accessing and downloading of digital content;

v. Online Gaming Services;

vi. Cloud Computing Services;

vii. Services other than those services above, delivered through a Social Media Platform;

viii. Services, other than those services above, delivered through an Internet Search Engine; or

ix. Any other service which meets the criteria set out in Section 2(b) ("other digital services").

Section 3: Profits of SEP

3. Where Section 1 applies, the taxable profits shall be deemed to be [X per cent] of the revenues derived directly or indirectly from or attributable to [Country] by a non-resident person, in respect of a significant economic presence in [Country].

Section 4: In-scope revenue

4. Revenue derived, directly or indirectly, from or attributable to [Country] by a non-resident person in a chargeable period in respect of a significant economic presence in [Country] shall include but not be limited to the following:

a) Revenue attributable to [Country] arising from Online Advertising Services, in accordance with Section 7;

b) Revenue attributable to [Country] arising from Data Services, in accordance with Section 7;

c) Revenue derived from users located in [Country] arising from the provision of Online Marketplace or intermediation platform services, other than those services described in subsections d), e) and f);

d) Revenue derived from users, no matter where located, in respect of the facilitation of rental or use of real property located in [Country];

e) Revenue derived from users, no matter where located, in respect of transactions for vehicle hire services through a Vehicle Hire Online Marketplace, where the user commences using the vehicle in [Country];

f) Revenue derived from users located in [Country] arising from Digital Content Services, Online Gaming Services and Cloud Computing Services; or

g) Revenue attributable to [Country] arising from any other service which meets the criteria set out in Section 2(b), in accordance with Section 7 ("other digital services").

Section 5: Attribution of revenue

5. For the purposes of Section 4(a), (b) and (g), revenue attributable to [Country] means:

a) In the case of revenue falling within Section 4(a) above, the higher of:

i. Revenue derived from persons resident in [Country], or persons operating through a permanent establishment in [Country], in respect of Online Advertising Services, or

ii. The amount calculated using the following formula:

(aa) Determine the non-resident's global revenues arising in respect of Online Advertising Services.

(ab) Determine the number of users located in [Country] viewing the advertisement.

(ac) Determine the total worldwide number of users viewing the advertisement.

(ad) Divide (ab) by (ac) to determine the [Country] proportion and multiply the result by (aa).

b) In the case of revenue falling within Section 4(b) above, the higher of:

i. Revenue derived from persons resident in [Country], or persons operating through a permanent establishment in [Country], in respect of Data Services, or

ii. The amount calculated using the following formula:

(aa) Determine the non-resident's global revenues arising in respect of Data Services.

(ab) Determine the number of users located in [Country] of one or more online platforms through which the data is derived.

(ac) Determine the global number of users of those online platforms.

(ad) Divide (ab) by (ac) to determine the [Country] proportion and multiply the result by (aa).

c) In the case of revenue falling within Section 4(g) above, the higher of:

i. Revenue derived from persons resident in [Country], or persons operating through a permanent establishment in [Country], in respect of any other service which meets the criteria set out in Section 2(b) ("other digital services"), or

ii. The amount calculated using the following formula:

(aa) Determine the non-resident's global revenues arising in respect of other digital services revenues.

(ab) Determine the number of users located in [Country] of one or more of those other digital services.

(ac) Determine the global number of users of those other digital services.

(ad) Divide (ab) by (ac) to determine the [Country] proportion and multiply the result by (aa).

Section 6: Definition of user

6. A user means any person that uses, views, or otherwise engages with an online platform, and includes:

a) Persons involved in transactions for the rent or other use of real property through an Accommodation Online Marketplace, including those persons providing the property for rent or use and those persons renting or using the property;

b) Persons involved in transactions for vehicle hire services through a Vehicle Hire Online Marketplace, including drivers and passengers;

c) Persons involved in transactions for the purchase or sale of any goods or services, including digital content, through an Online Marketplace;

d) Persons purchasing or subscribing to Digital Content Services, Online Gaming Services or Cloud Computing Services.

Section 7: Location of user

7. The location of a user is determined in accordance with the following subsections.

a) With regards to Online Advertising Services, Data Services and other services which meet the criteria set out in Section 2(b), for the purposes of Section 5(a)(ii), 5(b)(ii) and 5(c) (ii) the location of the user shall be determined according to:

i. The user profile, which means, information regarding the ordinary location of the user, which is accumulated by the online platform over the course of the user's engagement with the online platform, or

ii. If (i) is not available, the geolocation associated with the device at the time the user engaged the online platform, or

iii. If (i) and (ii) are not available, the user's IP address associated with the device at the time the user engaged the online platform.

b) With regards to an Online Marketplace, the location of users who purchase goods or services through the online platform shall be determined according to:

i. If the user purchases physical goods and services, the user's physical delivery address; or

ii. If (i) is not available, the geolocation associated with the device at the time of entering the relevant transaction through the online platform; or

iii. If (i) and (ii) are not available, the user's IP address associated with the device at the time of entering the relevant transaction through the online platform.

c) With regards to an Online Marketplace, the location of users who sell goods or services through the online platform shall be determined according to:

i. The registered address associated with the account through which the transaction took place; or

ii. If (i) is not available, the billing address associated with the account through which the transaction took place; or

iii. If (i) and (ii) are not available, the geolocation associated with the device at the time of entering the relevant transaction through the online platform; or

iv. If (i), (ii) and (iii) are not available, the user's IP address associated with the device at the time of entering the relevant transaction through the online platform.

d) With regards to Digital Content Services, Online Gaming Services and Cloud Computing Services, the location of users shall be determined according to:

i. If the user is a business, the registered business address of the user receiving the services;

ii. If the user is a person other than a business, the billing address of the user receiving the services;

iii. If (i) or (ii) are not available, the location of the user's bank or financial account used to make payment for the services;

iv. If (i), (ii) and (iii) are not available, the geolocation associated with the device at the time of purchasing the service;

v. If (i), (ii), (iii) and (iv) are not available, the user's IP address associated with the device at the time of purchasing the service.

PART II: ADMINISTRATION

Section 8: Registration of non-resident for tax

8. A non-resident person who derives revenue, directly or indirectly from or attributable to [Country] in respect of a significant economic presence, shall register for income tax purposes in accordance with the following subsections:

a) Registration shall be made under the simplified tax registration framework; and

b) The registration under subsection 8(a) shall be made within [60 days] of the person becoming liable for that tax.

Section 9: Information to be included in registration

9. A non-resident person required to register under section 8, shall do so through a registration form prescribed by the Commissioner, and in accordance with the following subsections.

a) The registration application shall include the following information:

i. the name of the applicant's business including its trading name;

ii. the name of the contact person responsible for tax matters;

iii. the postal and registered address or addresses of the business;

iv. the telephone number of the contact person;

v. the e-mail address of the contact person;

vi. the websites or uniform resource locator of the applicant through which business is conducted;

vii. the national tax identification number issued to the applicant in the country of residence;

viii. the certificate of incorporation issued to the applicant's business; and

ix. any other information that the Commissioner may require.

b) Upon registration, the Commissioner shall issue the applicant with a [Tax Identification Number] for the purpose of filing return and payment of tax.

c) A person registered under these provisions who ceases to derive revenue, directly or indirectly from or attributable to [Country] in respect of a significant economic presence, shall apply to the Commissioner for deregistration in the prescribed form.

Section 10: Duty to File Returns

10. A non-resident person who derives revenue, directly or indirectly from or attributable to [Country] in respect of a significant economic presence in a chargeable period must file a [significant economic presence] tax return with [Tax Administration] for that chargeable period.

a) The [significant economic presence] tax return for the non-resident person is due on the day following the end of [Y] months from the end of the chargeable period.

Section 11: Obligation to provide information

11. A non-resident person who derives revenue, directly or indirectly from or attributable to [Country] in respect of a significant economic presence in a chargeable period shall be required to submit to the Commissioner any information or documents the Commissioner considers necessary to substantiate the information required under Sections 1 – 15 or regulations issued thereto.

Section 12: When is tax under Section (1) Due and Payable

12. Income tax in respect of a chargeable period is due and payable on the day following the end of [Y] months from the end of the chargeable period in accordance with the following subsections.

a) A chargeable period is the accounting period of the non-resident person unless that accounting period exceeds 12 months when the chargeable period will be the 12 months from the commencement of the accounting period.

b) The obligation to pay the tax due shall be that of the person with the duty to file the return under Section 10.

Section 13: Interaction with Withholding Tax

13. Where revenue referred to under Section 2(b) is also subject to withholding tax in accordance with the Act, Section 1 shall not apply to the extent that the same revenue is subject to the withholding tax.

Section 14: Application of law to Multinational Enterprise Groups

14. Where a non-resident person to whom Section 1 applies is a member of a Multinational Enterprise Group, the following adjustments apply.

a) The threshold in Section 2(a) relating to the revenue derived, directly or indirectly from or attributable to [Country] is tested by aggregating the relevant revenue of all members of that Multinational Enterprise Group;

b) The attribution of revenue to [Country] as per Section 5 shall be done by aggregating each of the relevant data points of all members of that Multinational Enterprise Group;

c) The Multinational Enterprise Group may elect one member to be a designated entity on behalf of all of its members for the purpose of the administration of the SEP provisions;

d) For the purpose of Section 8, the designated entity shall register;

e) For the purpose of Section 9, the designated entity must provide the Commissioner with the details of each member of the Multinational Enterprise Group which would otherwise be separately liable under this law, including the name of each entity, its county of tax residence, and its national tax identification number issued by the country of residence;

f) For the purpose of Section 10, the designated entity shall file the return including the relevant information covering all members of the Multinational Enterprise Group that have revenue derived, directly or indirectly from or attributable to [Country];

g) For the purpose of Section 12, the chargeable period is the accounting period of the ultimate parent entity of the Multinational Enterprise Group, and the tax under Section 1 is due and payable on the day that is [X] months from the end of the chargeable period;

h) For the purpose of Section 12, all members of the Multinational Enterprise Group that have revenue derived, directly or indirectly from or attributable to [Country] are jointly and severally liable for the obligations under this law, and may be subject to penalties for non-compliance.

Section 15: [Regulations/Orders] with respect to Administrative Requirements and obligations

15. The [Minister of Finance] may publish, from time to time, [regulations/orders] regarding the administrative requirements and obligations of [non-resident persons] and the [Tax Administration], with respect of a significant economic presence, including but not limited to the following:

a) Filing of income tax returns;
b) Other simplified tax registration requirements;
c) Record keeping requirements;
d) Penalties for non-compliance;
e) Interest on overdue amount;
f) Amendment of return;
g) Audits returns and related procedures;
h) Assessments;
i) Appeals and objections;
j) Payments and payment notices;
k) Provision of guidance to taxpayers.

DEFINITIONS

Accommodation Online Marketplace

An accommodation online marketplace means an online platform that facilitates the rental or use of accommodation, including hotel accommodation, by a user from another user.

Cloud Computing Services

Cloud Computing Services means the provision of any computer hosted services through the internet.

Data Services

Data services means the sale or license of, or access to user data or information collected through user engagement with an online platform, whether it is sold or licensed directly or indirectly, aggregated or disaggregated, anonymised or used in any other form.

Digital Content Services

Digital content services mean the sale, licensing or streaming of, or access to, digital content including software however defined.

Intermediation Platform

Intermediation Platform means an online platform that facilitates transactions or interactions between buyers and sellers, or between users, including for the sale, purchase or use of tangible goods, digital content or services.

Internet Search Engine

An internet search engine means a website, service or system that systematically searches the internet for information specified by users, usually inputted in the form of a textual web search query.

Multinational Enterprise Group means

i) collection of entities that are related through ownership or control such that the assets, liabilities, income, expenses and cash flows of those entities are included in the Consolidated Financial Statements of the Ultimate Parent Entity or would have been so included if the Ultimate Parent Entity had prepared Consolidated Financial Statements, where at least two members are located in different jurisdictions; or

ii) an entity that is located in one jurisdiction and has one or more permanent establishments located in other jurisdictions provided that the entity is not a part of another Multinational Enterprise Group described in the i) above.

Member of MNE Group means entities that form part of a multinational enterprise group including a permanent establishment.

Non-resident

Non-resident means [Cross Reference to Country Legislative Reference].

Online Advertising Services

Online advertising services means the inclusion in a digital interface, of its own or of third parties of adverts directed to the users of that interface

Online Gaming Services

Online gaming services means the provision of services related to:

(a) Any games, including video games, that are either partially or primarily played through the internet; and

(b) Any kind of gambling, including casino games, virtual poker and betting, lotteries and prize competitions that are partially or primarily conducted through the internet.

Online Marketplace

An online marketplace means an online platform which facilitates the sale or provision by users of any services, goods or other property to other users and is not limited to a virtual asset exchange platform.

Other Transport Online marketplace

A transport online marketplace means an online marketplace that facilitates the purchase of any form of transport, other than vehicle hire, by a user from another user.

Online Platform

An online platform means a digital service that uses the internet or any other electronic means to facilitate interactions between two or more distinct but interdependent sets of users (whether firms or individuals) and includes an accommodation online marketplace, intermediation platform, online marketplace, a social media platform and a vehicle hire online marketplace.

Resident person

[As defined in the Country's domestic tax law]

Social Media Platform

A social media platform means an online platform that meets the following conditions:

(a) the platform promotes interaction between users (including interaction between users and content on the platform provided by other users)

(b) the platform enables content to be shared with other groups of users (or with other users).

Vehicle Hire Online Marketplace

A vehicle hire online marketplace means an online platform that facilitates the hire by a user of a passenger or goods vehicle, including taxis or similar, and, where appropriate, car hailing, ride sharing and the services of a driver.

EXPLANATORY NOTES

Section 1: Charge to tax

Section 1 sets out the person liable to income tax in [Country] in respect of specified revenue streams earned from a significant economic presence (SEP) in that country. Section 1(a) states that the person liable to income tax is a non-resident who derives revenue, directly or indirectly from or attributable to [Country], in respect of a SEP in [Country] during a chargeable period. While the provisions in the SEP law set out the scope and calculation of the taxable profits of a SEP, those profits are then subject to the rate of tax as specified under [Country's] domestic income tax law. The Section further envisages that there would be two possible revenue streams, namely revenue that may be directly or indirectly paid from a country (e.g., payment for streaming digital content or advertising fee) and revenue which may be attributed to a country as a result of user participation (e.g., viewing of online adverts). These provisions only apply to non-residents. Any residents that are earning this kind of revenue would be taxed under the ordinary income tax law provisions.

Section 2: Definition of SEP

Section 2 defines what it means for a non-resident to be deemed to have a SEP in [Country]. The definition contains two cumulative conditions that must both be satisfied for a non-resident to be treated as having a SEP in [Country].

Section 2(a) sets out a materiality threshold i.e., the quantum of revenues derived from in-scope services from or attributable to [Country]. A country must determine this revenue threshold based on what levels of economic activity would be deemed to be 'significant' for the purpose of SEP legislation. Countries might consider conducting an assessment of their digital economy to inform the setting of this threshold. Revenue thresholds not only aid in determining what revenues are considered significant for SEP legislation but they also assist in promoting the growth of the digital sector by purposeful exclusions of insignificant transactions and only targeting larger transactions by more established and profitable digital businesses. This approach has also been recommended in the ATAF Suggested Approach to drafting Digital Services Tax legislation especially where the rule is designed to apply to resident taxpayers as well. In this case, excluding certain categories of businesses e.g. start-ups and small and medium enterprises (SMEs) is encouraged.

Section 2(b) sets out the type of services whose revenue is in-scope of this legislation. It starts off with a broad scope whereby revenues from services delivered over the internet or by electronic network including through an online platform are in-scope. In addition, the Section goes on to provide a list of in-scope services. The meaning of these in-scope services is included in the definitions section. However, the provision uses the word “including” which means that the list is not exhaustive. This means that if a service is not included in the list under Section 2(b), that does not necessarily exclude it from being an in-scope service for the purposes of a SEP as long as it is in scope of primary rule in section 2 (b)

Section 3: Profits of SEP

Section 3 sets out the provision for determining the taxable profits of a non-resident arising from revenues derived directly or indirectly from or attributable to a country, in respect of a SEP in that country.

The section provides for a deemed profit provision where the deemed taxable profit for a non-resident in respect of a SEP is set at a percentage of the revenues derived directly or indirectly from or attributable to the SEP in that country. The Suggested Approach has left that percentage as a placeholder for each Country to determine the appropriate rate having regard to their policy considerations. However, it is recommended that countries should consider deemed profit rates ranging from 10% to 20%.

[Optional drafting for Section 3]: A country may opt for legislation that contains two provisions for determining the taxable profits of a non-resident arising from revenues of a SEP as follows:

1) Where Section 1 applies, the non-resident person liable to tax shall determine the taxable profits relating to the significant economic presence and furnish the Commissioner with the necessary documentation.

2) Where the non-resident person fails to determine the taxable profit as required under subsection 1, the taxable profits shall be deemed to be [X percent] of the revenues derived directly or indirectly from or attributable to [Country] by the non-resident person, in respect of a significant economic presence in [Country].

Subsection 1 would require the non-resident who is liable to tax in respect of a SEP to determine the taxable profits relating to the SEP and furnish the Commissioner with the necessary documentation. Subsection 2 would act as a back-stop to subsection 1 in that, should a non-resident fail to determine the taxable profits relating to the SEP, then the deemed profits provision is triggered.

The Optional drafting is in use by some states; however, it contains critical administrative challenges. These challenges mainly centre around verification of the accuracy of the non-resident person's determination of taxable profits. In practice, many developing countries have limited access to documentation and information that would aid in verifying declarations by non-resident entities; an issue exacerbated by limited treaty networks affording fewer opportunities for exchange of information. The optional drafting may also give rise to challenges in terms of integrity, certainty and fairness, because it does not provide a substantive set of rules or principles by which the non-resident should make this determination. This gives the tax administration very little room to challenge the basis on which the MNE has made its own assessment. This may also create risks that one taxpayer performs its analysis on a different basis to another, arriving at different outcomes. This can give rise to competitive concerns and can undermine the favourability of a country as a place to do business.

For these reasons, this Suggested Approach did not include this option in the main rules, and instead embraces a deemed profit provision for ease of administration of SEP legislation.

Section 4: In-scope revenue

Section 4 states what is included in revenue derived, directly or indirectly, by a non-resident in a chargeable period and attributable to [Country] in Section 2. Once again, the use of the word "including" means the list is not exhaustive.

Section 5: Attribution of revenue

Section 5 sets out how the non-resident's revenue from the provision of certain specified in-scope services will be attributed to the country enacting the SEP legislation. This applies to those referred to in Section 4(a) (Online Advertising Services), Section 4(b) (Data Services) and Section 4(g) (other service which meets the criteria set out in Section 2(b).). The provisions in Section 5 are necessary because the revenue in these cases is not necessarily directly earned from a payor in [Country] but may be attributable to users in [Country]. Revenue in respect of Section 4(c), 4(d), 4(e) and 4(f) is directly earned from a payor in [Country], and therefore specific attribution rules are not needed.

The provisions in Section 5 in each case provide two alternative ways that revenue is identified: either directly from a payor located in [Country], or attributable to users located in [Country]. In each case, the revenue is the higher of those two amounts.

Subsection 5(a)(i) attributes revenue which relates to payments directly made for Online Advertising Services which the non-resident derives from persons who are resident in the country or non-resident persons operating through a permanent establishment in that country. This subsection is referring to cases where the non-resident (e.g. a search engine) is selling advertising to a taxpayer in [Country], and that taxpayer is directly paying the search engine for this. That payment is the revenue counted in subsection 5(a)(i).

Revenue attributable under subsection 5(a)(ii) refers to cases where the non-resident (e.g. a search engine) is showing advertisements to people located in [Country] (i.e. the users). The revenue is what was received from the person buying the advertisement to the extent it was shown to [Country]'s users. This revenue is calculated as follows: Firstly, the global revenue of the non-resident arising from the provision of Online Advertising Services must be determined (aa). Then the number of users in [Country] that viewed the advertisement must be determined (ab) and finally the number of users who have viewed the advertisement worldwide must be determined (ac). The revenue attributable to [Country] is then calculated by the following formula:

Revenue = (ab/ac) *aa

This revenue will only be attributable to the country if it exceeds the revenue directly attributable under sub-section 5(a)(i).

In case the non-resident's revenue is from the provision of Data Services, the revenue attributable to [Country] will be calculated in a similar manner to the attribution of revenue which relates to online advertising services.

Subsection 5(b)(i) attributes revenue which relates to the provision of Data Services which the non-resident derives from persons who are resident in the country or non-resident persons who are operating through a permanent establishment in [Country]. This subsection is referring to cases where the non-resident (e.g. a search engine) is selling user data to a taxpayer in [Country], and that taxpayer is directly paying the search engine for this data. That payment is the revenue counted in subsection 5(b)(i).

Revenue attributable under subsection 5(b)(ii) refers to cases where the non-resident (e.g. a search engine) is selling data about people located in [Country] (i.e. the users). The revenue is what was received from the person buying the data to the extent it about [Country]'s users. This revenue is calculated as follows: Firstly, the global revenue of the non-resident arising from the provision of Data Services must be determined (aa). Then the number of users in [Country] of one or more online platforms through which the data is derived must be determined (ab). Finally, the number of global users of those online platforms must be determined (ac). The revenue attributable to [Country] is then calculated by the following formula:

Revenue = (ab/ac) *aa

This revenue will only be attributable to the country if it exceeds the revenue directly attributable under sub-section 5(b)(i).

In case of the non-resident's revenue is from the provision of any other service which meets the criteria set out in Section 2(b), the revenue attributable to [Country] will also be calculated in a similar manner to the attribution of revenue which relates to online advertising services.

Subsection 5(c)(i) attributes revenue which relates to the provision of other digital services which the non-resident derives from persons who are resident in [Country] or non-resident persons who are operating through a permanent establishment in [Country].

Revenue attributable under subsection 5(c)(ii) is calculated as follows: Firstly, the global revenue of the non-resident arising from the provision of any other service which meets the criteria set out in Section 2(b) must be determined (aa). Then the number of users in [Country] of one or more of those online platforms must be determined (ab) and finally the number of global users of those online platforms must be determined (ac). The revenue attributable to [Country] is then calculated by the following formula:

Revenue = (ab/ac)*aa

This revenue will only be attributable to the country if it exceeds the revenue directly attributable under subsection 5(c)(i).

The indirect attribution of revenue as set out in the above formulae is necessary for taking into account the contribution of users to value creation in the country. For instance, in the case of Online Advertising Services, digital companies use data collected about users which is used by the digital company's customers to develop targeted adverts for such users. These targeted adverts are significant value streams for the advertising companies as they create brand value for those companies and enhance the demand for their products leading to increased sales in the market of the users viewing the adverts. This in turn leads to greater revenues for the digital company as they are able to charge higher advertising fees to these companies for the online advertising services without the need for the digital company to have a physical presence in such markets.

With regards to service revenue relating to Data Services, the attribution of revenue to a country recognises the fact that user data is valuable and may be monetised by a company. The monetisation transaction (e.g. sale or licensing) may not create a direct payment from the country where the users are located but rather such payments may arise from other jurisdiction(s). The attribution formula seeks to ensure that in cases where there is no direct payment from the users' country (as may often be the case), some revenue relating to the monetisation transaction is allocated to the country of users. This will ensure alignment of taxing rights and value creation.

[Optional Formula for attribution rule]: Use of the global allocation key for profit attribution under a SEP.

A country may opt to adopt the global allocation key metric that ensures services revenue is apportioned to all jurisdictions in proportion to their respective share of final consumption expenditure. Final consumption expenditure is macroeconomic information usually published by the UN or WBG. This metric can be a reasonable proxy for the contribution of users in the country for allocation of revenues under SEP legislation.

The optional drafting suggestion for Section 5 is set out below and subsequently explanatory notes on this alternate approach:

(a) In the case of revenue falling within Section 4(a) above, the higher of:

i) Revenue derived from persons resident in [Country], or persons operating through a permanent establishment in [Country], in respect of Online Advertising Services, or

ii) The amount calculated using the following formula:

[TC/GC] *A

Where: -

A – The total online advertising revenue of the non-resident person.

TC – The amount of the final consumption expenditure of the [Country] as published by the United Nations or by the World Bank based on the latest available data, for the period preceding the year of income.

GC – The total amount of the final consumption expenditure of all jurisdictions as published by the United Nations or by the World Bank based on the latest available data, for the period preceding the year of income.

(b) In the case of revenue falling within Section 4(b) above, the higher of:

i) Revenue derived from persons resident in [Country], or persons operating through a permanent establishment in [Country], in respect of Data Services, or

ii) The amount calculated using the following formula:

[TC/GC] *D

Where: -

D - The total Data Services revenue of the non-resident person.

TC – The amount of the final consumption expenditure of the [Country] as published by the United Nations or by the World Bank based on the latest available data, for the period preceding the year of income.

GC – The total amount of the final consumption expenditure of all jurisdictions as published by the United Nations or by the World Bank based on the latest available data, for the period preceding the year of income.

(c) In the case of revenue falling within Section 4(g) above, the higher of:

i) Revenue derived from persons resident in [Country], or persons operating through a permanent establishment in [Country], or

ii) The amount calculated using the following formula:

[TC/GC] *S

Where: -

S - The total services revenue that meets the criteria set out in Section 2(b) of the non-resident person.

TC – The amount of the final consumption expenditure of the [Country] as published by the United Nations or by the World Bank based on the latest available data, for the period preceding the year of income.

GC – The total amount of the final consumption expenditure of all jurisdictions as published by the United Nations or by the World Bank based on the latest available data, for the period preceding the year of income.

Explanatory Notes on global allocation key metric

Revenue attributable under sub-section 5(a)(ii), 5(b)(ii) and 5(c)(ii) is calculated as follows:

Firstly, the global revenue of the non-resident arising from the provision of Online Advertising Services, Data Services and services revenue that meets the criteria set out in Section 2(b), as the case may be, must be determined and is referred to in this context as (A), (D) and (S) respectively. Then, the amount of the final consumption expenditure of the [Country] as published by the United Nations (UN) or by the World Bank Group (WBG) for the period preceding the year of income must be determined (referred to as TC). Finally the total amount of final consumption expenditure of all jurisdictions as published by the UN or WBG must be determined (GC). The revenue attributable to [Country] is then calculated by the following formula:

For online advertising services revenue = (TC/GC) *A

For Data services revenue = (TC/GC) *D

For any other services revenue that meets the criteria set out in Section 2(b) = (TC/GC) *S

This revenue will only be attributable to [Country] if it exceeds the amount of revenue attributable under subsection (a)(i), b(i), or c(i), as applicable.

The global allocation key is drawn from the revenue sourcing rules of the draft Amount A Multilateral Convention The global allocation key can be simpler for taxpayers and tax administrations to calculate and can therefore reduce compliance costs and risks of disputes. Countries that opt to use the global allocation key to attribute profits to a SEP should consider incorporating a 'knock-out' rule. The aim of this rule will be to eliminate the final consumption expenditure of certain countries from the calculation of Global Consumption expenditure, and in doing so would increase the result of the revenue attributed to [Country] under the formula. The considerations for elimination ought to be on the basis that no revenues could reasonably be expected to arise from those jurisdictions due to legal, regulatory or documented structural commercial considerations. This makes the use of the global allocation key more accurate, to account for cases where the non-resident is not selling at all to such countries, and as such, no revenue should be apportioned to those countries in the formula.

Section 6: Definition of user

Section 6 provides a very broad definition of the term "user" to ensure that SEP legislation is broad in scope. This is necessary to ensure that the variety of ways that digital businesses generate value and profits from a market jurisdiction is captured by the SEP. This includes showing advertisements to users, exploiting user's data, making available social media platforms for users, and intermediating online transactions between users. As digital companies can generate value and profits with respect to users, the SEP suggested approach in several places makes the determination of the relevant revenue, and therefore the deemed SEP profits, by reference to users. Whilst the term "user" is broad, if the legislation also includes an appropriate materiality threshold as per Section 2(a), this should ensure a balanced outcome of only bringing into scope significant profits that are generated in the jurisdiction.

Section 7: Location of user

Section 7 sets out how the location of a user is to be determined. This will vary depending on the in-scope services being provided by the non-resident. Given that imposing taxation in relation to a SEP relies on identifying the users in [Country] as the reference for the value created for the digital company in that market, the location of a user is of utmost importance.

This provision provides a hierarchy of data points to determine the location of the user. This is necessary to account for the fact that different businesses will have access to different kinds of information depending on their business model, and ensuring alternative data points for determining a user's location maximises the ability of the non-resident to apply the rule and attribute revenue to a country.

In the case of Online Advertising Services, Data Services and other digital services, the location of the user is determined according to the user profile. This means information regarding the ordinary location of the user, which is accumulated by the online platform over the course of the user's engagement with the online platform. If there is no user profile data, the location is determined by the geolocation associated with the device at the time the user engaged the online platform. Finally, if there is no user profile data and no geolocation data, the location is determined by the user's Internet Protocol (IP) address associated with the device at the time the user engaged the online platform. These indicators are critical data points from which information on the location of the user can be deduced. User profile data as defined below is information that is that an online platform acquires either: by creating it based on information that the online platform has available about the user and can include a user's usual location and other demographic characteristics, or information created by the user in their interactions with the online platform. Based on the fact that user profile data is generally information readily available to online platforms because they use it in the course of running their business, the guide in this suggested approach is that it is a reliable means of ascertaining the location of a user.

In the case of Online Marketplace services, the location of users who purchase goods or services through the online platform shall be the user's physical delivery address if the user purchases physical goods and services. In all other cases, it will be the geolocation associated with the device at the time of entering the relevant transaction through the online platform. If there is no information of the user's physical delivery address or geolocation data, the location will be the user's IP address associated with the device at the time of entering the relevant transaction through the online platform.

In the case of Online Marketplace services, the location of users who sell goods or services through the online platform shall be the registered address associated with the account through which the transaction took place. If the registered address is not available, the location shall be the billing address associated with the account through which the transaction took place. If neither the registered address nor billing address is available, the geolocation associated with the device at the time of entering the relevant transaction through the online platform will be the location. If none of the above are available, the location will be the user's IP address associated with the device at the time of entering the relevant transaction through the online platform.

In the case of Digital Content services, Online Gaming Services and Cloud Computing Services, the location of users where the user is a business will be the registered business address of the user receiving the services. If the user is a person other than a business, the location will be the billing address of the user receiving the services. Where the registered business address or billing address are not available, the location will be the address of the user's bank or financial account used to make payment for the services. Where that address is also not available the location will be the geolocation associated with the device at the time of purchasing the service. Where none of the above are available the location will be the user's IP address associated with the device at the time of purchasing the service.

User profile relates to the information provided by the user at the time of registration or updates of the registration details and information that digital companies accumulate over time about users. Such information may include user's historical locations, usual residence, user's demographic data, internet browsing data, historical purchasing patterns and general preferences of the user.

The **geolocation** is based on GPS data or any other information which may be used to determine the location of user from the device used. When users activate the location sharing in their devices, it is possible to determine their exact location. Digital companies generally have access to this information, hence it is a reliable criterion of determining location of users whenever it is activated.

The **Internet Protocol (IP)** address is the number that is assigned to each device connected to a computer network. As certain IP addresses are assigned to specific countries, it is easy to determine the location of users using such addresses. However, where a Virtual Private Network (VPN) is used, there may be challenges of reliance on the IP address to determine the location of the user as use of VPN may lead to hiding the real location of the user. It is for this reason that the IP address is listed as the lowest data point in the hierarchy, but one which still provides a backstop in case the MNE does not have any of the other data points available.

Section 8: Registration of non-resident for tax

Section 8 sets out the registration requirements in a country for non-residents who derive revenue from or attributable to a SEP in that country. This provision makes it mandatory for the non-resident to register for income tax purposes in that country under the simplified tax registration framework. Under this framework, a country is at liberty to relax some of its obligatory tax compliance requirements for purposes of incentivizing the uptake of SEP legislation by non-residents and to ease the administration of this regime. . These include: requirement for less details upon registration, less supporting documentation, simplified tax returns, relaxed tax payment procedures among others. The simplified tax registration framework has proven effective in enhancing revenue collections from non-residents who derive revenue from in-scope services, in the countries that operate the framework for both VAT and Income tax purposes.

Section 9: Information to be included in registration

Section 9 sets out the key information to be included in the registration application by the non-resident under the simplified tax registration framework prescribed in Section 8. It further informs of the requirements of de-registration for tax purposes upon cessation.

Section 10: Duty to file returns

This section provides details of the obligation to file the [Significant Economic Presence] return by the in-scope taxpayer. The in-scope taxpayer is a non-resident that meets the criteria set out in section 2 including deriving service revenues in scope of the rule in a chargeable year from a country. It is important to clarify that even where the revenue is attributed to the country as a result of the activities of users located in that country (such as attribution of advertising revenue to a country due to viewing of digital adverts), such revenue is deemed to have been derived from that country by the non-resident, as the case may be.

The simplified tax registration framework assists in addressing the challenge of enforcing compliance by in-scope taxpayers. The [SEP] return must be filed by the contact person responsible for tax matters under the simplified registration framework.

Section 11: Obligation to provide information

Section 11 sets out the obligation for a Non-resident to provide information the Commissioner considers necessary to substantiate the information required under this legislation. This provides the Commissioner with a broader scope to request information that might be necessary to validate declarations and the transactions of the in-scope taxpayers. However, careful consideration is required on the potential compliance burden to the in-scope taxpayers whilst requesting such additional information.

Section 12: When is tax under Section 1 due and payable

This section defines the chargeable period of the tax under SEP legislation, the due date of the tax and the obligation to pay the tax due. The suggested approach sets out the chargeable period as the accounting period of the non-resident person. However, if that accounting period exceeds 12 months, then the chargeable period will be the 12 months from the commencement of the accounting period.

With regards to the due date for payment, the tax in respect of a chargeable period would be due and payable a few months after the end of the chargeable period. Countries would therefore need to determine the appropriate period to give taxpayers to pay the tax for the preceding accounting period. From an Income Tax perspective, commonly observed periods range from 3-4 months, but this is a decision of the country. Considering that most of the companies may not have physical presence in the country, it is advisable to make this period short while acknowledging that the companies would need to prepare financial statements to accurately determine the appropriate amount of revenue for a chargeable period.

Subsection 3 specifies the person obligated to pay the tax due. The subsection connects the obligation to pay the tax with the filing obligation by providing that the tax shall be paid by the non-resident required to file a [SEP] Tax Return as per the provisions of Section 10.

Section 13: Interaction with withholding taxes

This section provides guidance in the event that any category of service as defined under Section 2(b) also attracts a withholding tax under the same Income Tax Act. This Suggested Approach gives the guidance that the withholding tax provisions would take precedence over SEP rules and no income tax would be charged under the SEP rules. This approach enables countries to apply their withholding tax provisions including the applicable Double Tax Agreements in respect of in scope service revenues without being restricted by the SEP rules. Effectively, SEP would be a backstop rule to ensure that in scope service revenues are taxed to the extent that no withholding tax has already been charged.

Section 14: Application of law to Multinational Enterprise Groups

This section provides for the application of SEP legislation to a non-resident person who is liable to tax under Section 1 and is a member of a Multinational Enterprise Group and the critical adjustments that may apply. This is intended to ensure that all members of such groups are captured in the SEP legislation, irrespective of the size of an individual member, because of the aggregation of the relevant thresholds which is tested by reference to the entirety of the group. It is also intended to make compliance more streamlined, for example to allow for a single filing entity on behalf of the group.

Section 15: [Regulations/Orders] with respect to Administrative Requirements and obligations

Section 15 provides for the making of [regulations / orders] to give effect to the SEP law. This can include further details on administrative provisions, enforcement, and other practical matters.

Definition Section

This Section provides the definitions for crucial concepts used throughout this Suggested Approach. They provide clarity specifically on the services referred to under Section 2(b) above and platforms referred herein. However, given the rapid development of digital technology in recent years, this list may not be exhaustive but rather acts as a guide on how to draft the provisions of the Suggested Approach.

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