



TAXATION IN ELECTRONIC COMMERCE



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Technological disruptions have permeated every facet of society in today's world. In transportation, energy, communications and in several other areas, society continues to witness the marvels technology offers. Before now, in the world of commerce it was a norm for trading parties to be confined to carry out businesses on goods and services within their physical reach only. However, with the disruption the internet now offers, parties to a transaction and indeed the entire gamut of commercial transactions no longer need to rely on a brick-and-mortar system to facilitate trade.

This technological disruption of commerce now popularly referred to as 'e-commerce', is not without its challenges which typically borders on effective regulation. For instance, laws regulating commercial interactions in developing countries are still mostly conventional as their provisions and approach are tied to the physical presence of transacting parties. Indeed, it is this problem of regulation especially as it concerns taxation, that this article seeks to discuss. In achieving this, this article shall critically analyze the potential impacts of e-commerce on the tax base of developing countries like Nigeria and compare the efficacy of the Nigerian framework for digital taxation vis-à-vis the best international taxation principles on digital taxation.

Meaning and Nature of E-Commerce

The concept of e-commerce which is usually interchanged with the term 'e-business' is simply the buying and selling of goods and services, or the transmitting of funds or data, over an electronic network, primarily the



internet.¹ The United Nations Commission on International Trade Law (UNCITRAL) defines the concept as meaning: “commercial activities conducted through an exchange of information generated, stored or communicated by electronic, optical or analogous means.”

It is germane to understand that e-commerce is not only limited to buying and selling over the internet as it is also concerned with transferring or exchanging products, services or information over computer networks. In other words, it includes other activities such as servicing customers online, collaborating with business partners and exchanging business documents within an organization over the internet.

Impact of E-Commerce in Tax Administration

In the early 2000s, owing to its novelty, controversies arose amongst policymakers over the question of whether e-commerce should be subjected to taxation or not. Indeed, it was the argument in some quarters that the Internet alongside e-commerce platforms should not be taxed since it needed to develop without the stifling effects of taxation. The opposite view advocating for the taxation of e-commerce is however now the more popular opinion as several states all over the world have long resolved that there is a need to grow and prioritize government revenues and hence the need to tax electronic businesses as they are still businesses regardless of the means in which they are facilitated.²

Several questions however arise in light of the now popular opinion that e-commerce should be taxed like other businesses. Indeed, these questions need to be properly answered in order to ensure the implementation of an effective tax administration over e-commerce and they are: How do you ensure tax compliance? What amount of tax should be collected? How do you determine the country to collect a given tax seeing that electronic businesses are most often than not cross jurisdictional in nature?

In response to these questions, various states have adopted a number of taxation policies, methods and structures to ensure an effective e-commerce

¹ Wesley Chei, 'E-Commerce' < <https://searchcio.techtarget.com/definition/e-commerce> > Accessed 2 November, 2021.

² Muhammad M., et al, 'Online Shopping Inventory Issues and Its Impact on Shopping Behavior: Customer View' < https://link.springer.com/chapter/10.1007/978-3-319-59427-9_83 > Accessed 2 November, 2021.



tax regime. The progress recorded is however relative as whilst in more advanced jurisdictions concrete steps have been put in place to ensure effective taxation of e-commerce, the progress achieved in this regard in developing countries like Nigeria is at best fledgling.

For instance, in a more technologically advanced country like China, the Government has put in place policies such as tax neutrality (as it pertains to e-commerce), which ensures that the tax system would not have any influence on the choice between e-commerce and traditional business but would nonetheless encourage the utilisation of hi-tech. China also adopts the impartial tax burden principle as it pertains to e-commerce, which greatly emphasizes that its e-commerce taxation policy should conform to international best policies but should not be marred by tax jurisdiction irregularities such as double taxation.³

It is commendable that in several advanced jurisdictions, constructive steps have been taken to make unilateral policies or enact laws that will enable governments tax electronic businesses. For example, in Europe, most countries have either declared, planned, or implemented a Digital Services Tax (DST), which is a tax on designated gross revenue streams of large digital companies.

Challenges Hindering Effective Tax Collection in A Digital Economy

The proper administration of e-commerce remains a great challenge and its effectiveness is highly dependent on the efficacy of the respective tax authorities especially as regards their ability to obtain relevant information necessary for the taxation process. This process would typically include the identification and also the verification of the businesses within the scope of e-commerce; the connection between the transactions and the taxpayers; and the nature of such transactions. The sophisticated nature of the businesses may sometimes render the respective tax authorities handicapped in terms of acquiring the required tax information needed for taxation purposes. In a similar vein, the taxpayers sometimes vanquish in the

³Nishimura, S. 'The Research on Transition of the PE from Traditional Concept to the New Concept: Over the Avoidance of International Double Taxation' (2014) 3 *Business and Accounting Research*, 49-56.



cyberspace and as a result, reliable records become very difficult to get and audit trails end up getting obscure.⁴

Confronting the taxation challenges arising from the digitalization of the economy has been a leading priority of the Base Erosion Profit Shifting (BEPS) project of the Organization for Economic Cooperation and Development (OECD)/G-20 Inclusive Framework (IF) since 2015.⁵ Studies have shown that the major causes of e-commerce taxation complexities most often than not includes but is not limited to borderless commerce models and digital convergence.

It goes without saying that the proper taxation of international e-commerce is the elephant in the room in light of the problems that abound therein. A common problem for instance is seen in the practice of multinational enterprises (MNEs) who generally pay their corporate income tax where production and services are carried on without recourse to where their products and services are consumed by the end-users. The acts of these MNEs continuously drills a black hole in the economy of the foreign nation, as MNEs derive their incomes from users of their services abroad, but still evade the corporate tax obligation for their operational activities because they do not have physical presence in such foreign countries.

In a bid to proffer a solution to the above problem, on 1st July, 2021, the Organization for Economic Cooperation and Development (OECD) issued a policy statement to address digital tax problems known as the Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy.⁶ These two pillars are:

- 1. Nexus and Profit Allocation Rules; and**
- 2. Global Minimum Tax Rules**

1. Nexus and Profit Allocation Rules

The idea of this rule is to ensure a fairer distribution of profits and taxing rights among countries with respect to the largest MNEs, including digital companies. This will be achieved by the re-allocation of some taxing rights over MNEs from their home countries to the markets where they have

⁴ James Agarwal and Terry Wu, *Emerging Issues in Global Marketing* (Springer 2018) 231-253.

⁵ The Inclusive Framework on BEPS allows interested countries to work with the 38 OECD and G-20 member countries on developing standards on BEPS-related issues.

⁶ The policy has been agreed to by 130 OECD member states out of its 139 members.



business activities and earn profits, notwithstanding that the organization does not have a physical presence in that country. Here, taxing rights on more than USD 125 billion of profit are expected to be reallocated to market jurisdictions annually.⁷

2. Global Minimum Tax Rules

The rationale for this second pillar, is to put an end to competitions over corporate income tax by introducing a global minimum corporate tax rate that countries can use to protect their tax bases. This simply provides for a unified corporate income tax to constructively deal with tax inversions orchestrated by MNEs. The proposed global minimum corporate income tax under this arrangement will be at the rate of 15%.

The Legal Framework for the Taxation of the Digital Economy in Nigeria

In Nigeria, the Company Income Tax Act, 2007 and the Finance Act, 2020 are the principal laws that regulate the taxation of companies. Generally, taxation in Nigeria follows a multi-level tax regime, that is, taxation by the three tiers of government. However, company tax for both domestic and foreign companies carrying out businesses in Nigeria is collected exclusively by the Federal Government through the Federal Inland Revenue Service.

It is without a doubt that company income tax contributes immensely to Nigeria's tax based revenue. For instance, in 2016, the revenue target for company income tax was N1.877 trillion representing approximately 40% of the total projected tax revenue of N4.957 trillion for the year. And in 2020, the realized Company Income Tax was a total of N1.41 trillion.

In Nigeria, resident companies are liable to companies income tax on their worldwide income while non-residents are subject to corporate income tax on their Nigeria-source income.⁸ The taxation of resident companies is fairly straight forward as such companies simply adopt the assessment of taxable income on the basis of self-assessment pursuant to Section 53 of the Company Income Tax Act, 2007 to determine the tax payable.

⁷ Organization for Economic Cooperation and Development, 'Tax Challenges Arising From Digitalisation' <<https://www.oecd.org/tax/beps/beps-actions/action1/>> Accessed 20 October, 2021.

⁸ PWC, 'Corporate - Taxes on Corporate Income' <<https://taxsummaries.pwc.com/nigeria/corporate/taxes-on-corporate-income>> Accessed 15 November, 2021.



By the letters of the Finance Act, the tax rate of these chargeable incomes is currently 30% for companies having more than N100 Million Naira turnover, 20% for companies with a turnover between N25 Million and N100 Million, and no taxable company income for companies having less than N25 Million turnover. The tax is assessed on a preceding year basis (i.e. tax is charged on profits for the accounting year ending in the year preceding assessment).

For non-resident companies (NRC), Nigeria introduced in 2020 the concept of a "Significant Economic Presence" (SEP) as an additional basis of taxing such companies that operates in the digital space (i.e. digital NRC). Although the new rule still covers NRCs that provide services - consultancy, technical, management or professional that are not necessarily digital. The Rule simply provides that Non-resident digital companies (which are not tax resident in a treaty country) that have a significant economic presence (SEP) will be subject to income tax in Nigeria on profit attributable to the taxable presence in Nigeria.

According to **Paragraph (1) of the Companies Income Tax (Significant Economic Presence) Order, 2020**, A foreign entity involved in digital transactions will be deemed to have created an SEP in Nigeria and is therefore liable to tax if it:

- i. derives income of NGN 25 million or equivalent in other currencies from Nigeria in a year;
- ii. uses a Nigerian domain name (.ng) or registers a website address in Nigeria; or
- iii. has purposeful and sustained interactions with persons in Nigeria by customizing its digital platform to target persons in Nigeria (e.g. by stating the prices of its products or services in naira).

For the purposes of (i) above, revenue derived from Nigeria includes that in respect of:

- Streaming or downloading of digital contents.
- Transmission of data collected about users in Nigeria.
- Provision of goods or services directly or through a digital platform.
- Intermediation services that link suppliers and customers in Nigeria.



It is pertinent to note that while a digital NRC is taxed at 30% of taxable profits on specified activities and in some instances where it derives up to N25million turnover from Nigeria, a service NRC only has a Withholding (WHT) tax charge of 10% on income derived from Nigeria.⁹

The aforementioned Order which was published in the Federal Government **Official Gazette No. 21, Vol. 107 of 10 February 2020** by the Honourable Minister of Finance, Mrs. Zainab S. Ahmed is highly commendable as its existence has better defined the possibility of Nigeria to reasonably profit from the taxation of its enviable and rapidly-developing digital economy and technical consultancy services.

However, notwithstanding the laudable steps taken by the appropriate authorities in Nigeria for the realization of taxation in e-commerce, it is pertinent to state that there still exist some foreseeable difficulties and challenges in the taxation of the economic activities of digital entities and NRCs in Nigeria such as ensuring compliance from MNEs. Helpfully, most of these difficulties can be surmounted by adopting the propositions of the Organization for Economic Cooperation and Development (OECD) due to the low percentage rate it offers. The advantage of being a signatory to this proposition is that Nigeria will be able to realize more taxable profits from Multi-national enterprises such as digital companies like Amazon, Google, Facebook, and so on because they will be required to pay the agreed global taxable income regardless of where they are headquartered or the jurisdictions they operate.

Conclusion

The proper and effective taxation of the digital economy remains an area of challenge not only in Nigeria but across the globe. However, tax authorities have significantly taken steps to actualize and reconcile issues emanating from the emergence of e-commerce as seen in the OECD propositions and the SEP Order which have been critically discussed in this article. These ingenious steps are all geared towards providing a lasting solution to taxation in the digital space because as rightly stated by Techcrunch¹⁰, it is rather startling to imagine that Uber, the world's largest taxi company, owns no vehicles.

⁹ Section 13(2) (c) and (e) of the Companies Income Tax Act (as amended).

¹⁰ Tom Godwin, 'The Battle Is For The Customer Interface' < <https://techcrunch.com/2015/03/03/in-the-age-of-disintermediation-the-battle-is-all-for-the-customer-interface/>> Accessed 15 November, 2021



Facebook, the world's most popular media owner, creates no content. Alibaba, the most valuable retailer, has no inventory. And Airbnb, the world's largest accommodation provider, owns no real estate and yet, they rake in millions of dollars in revenue yearly for the benefit of their countries of domicile with no benefits accruing to several of the distant nations where their services are being provided.

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