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by Ana Paula Maciel and Ernesto Levy

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LATIN AMERICAN PERSPECTIVES

Taxing Digital Services in Argentina, Brazil, and Colombia

by Ana Paula Maciel and Ernesto Levy

As countries in Latin America chase new sources of revenue in response to economic pressures, jurisdictions throughout the region are simultaneously striving to adhere to the OECD's standards governing the collection of VAT on cross-border sales.[1] These factors, in conjunction with the soaring use of electronic services in an increasingly digital global economy, are causing countries to rethink how they tax electronically supplied services (ESSs).

The European Union has taken the lead in implementing digital-era regulations governing the taxation of ESSs. These rules determine which services qualify as electronically supplied and how VAT is applied based on where the services are consumed. (Prior coverage: *Tax Notes Int'l*, Jan. 5, 2015, p. 33.) The EU's actions have inspired other countries around the world, including those in Latin America, to reconsider how they apply VAT on cross-border virtual services. The ESS taxation approaches in Argentina, Brazil, and Colombia are worth highlighting because they characterize the frequently contentious, confusing, and complex evolution of ESS taxation in the region.

This evolution will affect taxpayers as more countries in Latin America and around the world follow the EU's lead by implementing new ESS taxation rules and interpretations. These changes also promise to add another layer of intricacy to Latin America's already formidable tax complexity.[2]

The EU Approach

Before focusing on Latin America, it helps to understand the EU's approach to ESS taxation, which largely reflects an effort to accrue tax revenue from services-related transactions where those services are consumed.[3] The EU recognized that many traditional tax policies, structures, and collection processes are not keeping pace with the digital transformation of business and, more broadly, with the global economy.

Taking a cue from the EU, other regions and countries have begun to implement similar legislation in an attempt to modernize their tax codes to more effectively counter base erosion and put foreign and domestic companies on an equal footing. Australia, Japan, New Zealand, South Africa, and South Korea figure prominently among the countries following the EU's lead on ESS taxation changes.

The EU's definition of an ESS includes several core components. To qualify as an ESS,[4] an offering must be:

- a service;
- delivered over the internet or an electronic network;
- generated in an ''essentially automated'' manner that involves minimal human intervention; and
- impossible to deliver in the absence of IT.

The EU legislation provides more than 20 examples of ESSs. Some of these services are straightforward and specific (for example, online newspapers, music downloads, streaming video, online data storage, and website hosting). Other items on the list are broader and require a lengthier description:

> Internet Service Packages (ISP) of information in which the telecommunications component forms an ancillary and subordinate part (i.e. packages going beyond mere Internet access and including

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[1] OECD, International VAT/GST Guidelines (June 11, 2015).

[2] Ana Paula Maciel and Ernesto Levy, ''Transactional Tax Complexity in Brazil, Argentina, and Mexico,'' *Tax Notes Int'l*, Apr. 18, 2016, p. 285.

[3] *See* European Commission, Taxation and Customs Union, ''Electronically Supplied Services,'' *available at* http://ec.europa.eu/taxation_customs/common/buying_online/buying_services/electronically_en.htm.

[4] Council Implementing Regulation (EU) 282/2011.

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Basic EU VAT Rules for Electronically Supplied Services

Transaction Type	Supplier	Customer	Place of Supply
Import	Non-EU supplier	EU business	Subject to VAT in the country where the customer is established (no VAT charged, reverse-charge mechanism applies)
Import	Non-EU supplier	EU consumer	Subject to VAT in the country where the customer is established
Export	EU supplier	EU business	Subject to VAT in the country where the customer is established
Export	EU supplier	EU consumer	Subject to VAT in the country where the customer is established

other elements such as content pages giving access to news, weather or travel reports; playgrounds; website hosting; access to online debates etc.).[5]

The ''place of supply,'' the nature of the transaction (import versus export), and the parties (domestic or foreign) involved in the service transaction play a crucial role in the EU's often complex determination of which companies have an obligation to register for VAT in the EU, as the table illustrates.[6]

Argentina, Brazil, and Colombia

Tax complexity is pervasive throughout Latin America, where cross-border services are usually subject to a levy in the country where the service has been used or enjoyed, in accordance with the destination principle for international trade.

VAT on business-to-business (B2B) service transactions in Latin America is generally collected through a reverse-charge mechanism. For business-to-consumer (B2C) service transactions, VAT regulations tend to either shift the tax liability to the end consumer or leave the transactions outside the scope of VAT. The first approach poses significant auditing challenges for tax authorities. The second approach affects the neutrality of the tax in the context of international transactions: Foreign suppliers that do not pay VAT have a tax advantage over domestic suppliers whose services remain subject to local taxation.

These approaches are evolving as can be seen in the following discussion of ESS taxation developments and challenges in Argentina, Brazil, and Colombia.

Argentina

Argentina imposes VAT at the federal level. The import and export of services adheres to the use-and-enjoyment principle.

According to Argentinean VAT law, digital goods (for example, software, images, and information downloaded from the internet) that are subject to a use license agreement qualify as services, rather than intangible goods, and are therefore subject to the 21 percent Argentinean VAT rate. This treatment is consistent with the EU's current ESS rules.

Other Argentinean ESS taxation approaches, such as those that apply to some B2C services, diverge from the EU legislation. While B2B transactions related to the import of services follow the EU legislation and are subject to a VAT reverse-charge mechanism, when imported services qualify as B2C they fall outside the scope of Argentinean VAT. As a result, the seller of those services has no obligation to register for VAT in the country. (The EU would require the foreign supplier to register for VAT.)

Argentina's turnover tax, which is imposed at the provincial level by all of the country's 24 jurisdictions, marks another important indirect tax that affects electronic services. For example, the city of Buenos Aires recently began applying a levy on foreign suppliers of online subscription services like streaming services and online games.[7] The levy is applied through a withholding tax mechanism whereby debit and credit card companies are required to withhold 3 percent of the net amount on any payments remitted to them.

Other jurisdictions in Argentina are considering the possibility of implementing similar legislation to capture new revenue.

Brazil

Brazilian tax authorities have not yet provided specific guidance regarding their stance on the EU legislation's interpretation of what constitutes an ESS for purposes of taxation.

This lack of clarity creates confusion and, at times, instances of double taxation. The uncertainty has helped make ESSs a hot-button issue that provokes

[5]Council Directive 2006/112/EC and Council Implementing Regulation (EU) 282/2011.

[6]*See* http://ec.europa.eu/taxation_customs/taxation/vat/how_vat_works/telecom/index_en.htm.

[7]Administración Gubernamental de Ingresos Públicos (AGIP), Resolution 593/14.

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contentious debate among the country's numerous states and municipalities and adds fuel to the so-called Brazilian fiscal war.

In some situations, taxpayers must contend with conflicts in ESS taxation approaches among different municipalities. One municipality may tax an ESS based on where the service is used, while another municipality may tax the same service based on where it was created or developed. In other situations, taxpayers must enter into discussions with states and municipalities to determine whether a specific service should be subject to a state VAT (Imposto sobre Operações relativas à Circulação de Mercadorias e sobre Prestações de Serviços de Transporte Interestadual e Intermunicipal e de Comunicação, or ICMS) or a municipal service tax (Imposto Sobre Serviços, or ISS). In these situations, a taxpayer may ultimately avoid the tax or be subject to double taxation (that is, pay both ISS and ICMS).

Brazil's current ESS issues stem from past decisions: Before 2003, the taxation on a service (for all purposes, including the payment of ISS) was essentially determined by the location of the service provider's incorporation, or its tax domicile. Under this approach, to attract taxpayers to their regions, some municipal tax authorities granted benefits (for example, reducing rates or reducing the basis) and created mechanisms for taxpayers to obtain favorable tax treatment.

In 2003 Brazil's federal government sought to curb the proliferation of these tax-related incentives while leveling the competitive playing field among municipalities. Complementary Law 116 (LC 116/03), published in July 2003, identifies which services should be taxed by municipal-level VAT (ISS). The law also determines which location — where the services provider is based or where the buyer is located — has the right to impose tax on the service. The law states that the ISS tax should be collected by the city in which the service provider is established — or, in the absence of such an establishment, by the service provider's preestablished tax domicile. The law further defines ''service provider establishment'' as the place where the taxpayer develops the activity of providing services, whether permanently or temporarily, regardless of the denomination given (for example, headquarters, branch, and so forth), and lists the exceptions.[8] As a result, the 2003 law provided more clarity and consistency.

The law also lists which services are subject to the ISS tax.[9] The list includes technology services related to computer activities, such as technical assistance, programming, planning, consulting, data processing, web hosting, technical advice, the collection and processing of data, and much more.

However, there are several noteworthy omissions on the list of taxable services. For example, some well-known electronic services provided by technology companies, including the provision of internet services and software downloads, were not mentioned. These and other omissions gave rise to new ESS taxation conflicts between states (which apply ICMS taxes) and municipalities (which apply ISS taxes). Disputes over the taxation of internet-access services resulted in a string of court cases and subsequent judgments.

Some of this jurisprudence held that internet providers offer value-added services specific to telecommunications, as described in Brazil's General Telecommunications Law,[10] and should therefore be subject to ISS taxation. Other court judgments defined internet services as communication services that should therefore be subject to ICMS taxation.[11]

Despite the omission of some electronically provided services, the original LC 116/03 service list and its subsequent revisions have helped eliminate confusion caused by differing interpretations of previous laws.

Even so, Brazil's Supreme Court of Justice maintained the understanding previously stated that ''Computer programs made by companies on a large scale and uniformly are commercialization of goods, subject to the ICMS. Customized software developed for specific user, express true rendering of services subject to ISS.''[12]

Still, the constantly changing nature of technology means that tax authorities must remain vigilant in ensuring that their tax policies and auditing activities keep up with technological advancements. The Brazilian government's Sistema Público de Escrituração Digital (SPED) program represents a major effort in this regard. (Prior analysis: *Tax Notes Int'l*, Aug. 5, 2013, p. 545; and *Tax Notes Int'l*, Jan. 26, 2015, p. 357.) The SPED program, which began about eight years ago, has standardized and digitized the relationship between tax authorities and taxpayers. The federal government now has real-time digital access to all activities that affect not only the tax calculations but also tax compliance (tax registers, returns, reports, and so forth) performed by taxpayers, which provides immediate verification and minimizes fraudulent taxation.

Under the SPED program, taxpayers must demonstrate rigorous tax compliance to avoid inquiries and fines.

Colombia

As is the case in most Latin American countries, VAT qualifies as a federal tax in Colombia. The country's general rule on the taxation of services is that

[8]Complementary Law 116 (July 31, 2003), article 3.

[9]Service List Annex to the Complementary Law 116/03, item 1.

[10]Law 9,472 (July 16, 1997), article 61, section 1.

[11]Superior Court of Justice (STJ), Pronouncement 334/2006.

[12]STJ, RMS 5934, RJ 1995/0032553-5.

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only those services rendered within Colombian territory are subject to taxation. There are a few exceptions to this general rule, however.

The most notable exception concerns professional services supplied by a foreign party and delivered to a customer located in Colombia; these services include consulting, advisory (including technical-assistance services), and auditing.

Colombian tax authorities (DIAN) recently issued a ruling clarifying the tax treatment of hosting services supplied by a foreign provider to a local customer.[13] In that ruling, the DIAN identifies hosting services as technical services[14] as opposed to technical assistance services.[15]

The difference is significant: ''Technical services'' are those that do not include the transmission of knowledge or training; ''technical assistance'' services include the transmission of knowledge or training. This classification means that hosting services provided by a foreign supplier are not considered advisory services and are therefore excluded from VAT in Colombia. However, a Colombian-based services provider delivering those same hosting services is subject to VAT.

This disparate treatment imposes a tax burden on Colombian service providers, ensuring that ESSs will be a hot-button topic for some time.

Conclusion

The ever-changing world of technology means that ESS taxation in Latin America and around the world will remain a pivotal issue in the years to come.

Just as traditional industries have been affected by internet companies, traditional approaches to taxation and collection will be affected by the growing adoption of digital practices and transactions.

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[13]Dirección de Impuestos y Aduanas Nacionales (DIAN), Ruling 27059 (Sept 17, 2015).

[14]DIAN, Ruling 76974 (Nov. 28, 2002).

[15]Fourth Section Administrative Dispute Tribunal, Judgment 13623 (Feb. 12, 2004).

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