

DIGITAL TRANSFORMATION CHALLENGES TO THE TAX SECURITY OF THE STATE IN RUSSIA AND OTHER BRICS COUNTRIES

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The digitization of the economy creates new challenges that affect the tax security of a state. These challenges have both positive and negative effects on the economy. This study is devoted to the challenges brought about by a digital economy that result in the necessity of responses from governments and international organizations. First and foremost, there is a lack of necessity for physical presence in the digital state. Second, there is a significant need to offer incentives for IT companies that are, on the one hand, the key leaders of the economy in the modern world and, on the other hand, have been most affected by the conditions of economic crises since 2020. This article is part of a project that is aimed at solving the problem of forming the concept of tax security in order to prevent or neutralize the influence of negative geopolitical and foreign economic factors on the development of the various economic sectors with the help of economic and legal instruments. Thus, this article sheds light on the experiences of the BRICS member states, especially those of the Russian Federation, in facing and addressing the challenges that result from the rise of a digital economy.

Keywords: tax law; tax security; BRICS; digital economy; digital services; tax administration; corporate.

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Introduction

The need to ensure compliance with the fiscal interests of the state requires the transformation of essential approaches to the regulation of tax relations in the current conditions of dynamically changing economic relations. Crisis phenomena in the economy, whether it is the global financial crisis, the fight against the consequences of a pandemic, or the imposition of sanctions, cause a widespread reduction in tax revenues for state budgets. The crisis actualizes the problem of values, the protection of which should be directed to the state's management of taxation and the functioning of public authorities in general. At the same time, such phenomena are viewed as threats to economic and, in particular, tax security.

The theoretical understanding of the emerging new challenges and the formulation of specific strategies for effective economic and legal responses to these new challenges is a problem that has both fundamental significance and practical repercussions. The solution to this problem, due to the decisive importance of taxes for the formation of the state budget and the performance of state functions, determines not only the protection of national interests in the tax sphere but also ensures national security in general.

Consequently, under such circumstances, the need to ensure compliance with the fiscal interests of the state requires the transformation of essential approaches governing the regulation of the system of taxes and fees, taxation principles, elements of taxation, tax administration, both in general and in terms of individual functions, as well as other tax relations. In the absence of a thorough study of this issue on the part of legal and economic experts, the advantages that any crisis represents for state taxation management will inevitably go unnoticed, and the economic and legal

challenges generated by the actions of actors both within the state and globally will remain without an adequate response. Both groups of consequences significantly threaten the fiscal interests of the Russian state, the essence of which also requires reassessment in the context of new challenges.

This study aims to shed light on the necessity of responding to the new challenges posed by the digital economy. These challenges are typically followed by a series of actions undertaken by international organizations, as well as by unilateral legislative measures taken by nations. We will explore how Russia and other BRICS countries have already responded to these challenges and examine ways in which they can respond further.

1. Tax Security of the State in the Era of the Digital Economy

In 2022, the Russian economy, having overcome the consequences of the spread of the pandemic, faced new challenges. These new challenges included the withdrawal of a number of foreign companies from the Russian market, problems with the export of Russian products and the import of certain goods to Russia, disruption of logistics chains and cooperative ties, the imposition of sanctions in relation to the banking sector, and volatility in the securities market. In the economic sphere, these new challenges have affected export-oriented industries, the implementation of investment projects, especially those involving the use of high technologies, and import logistics, among other areas.

At the same time, measures taken to support various sectors of the Russian economy in 2022 were unprecedented and included the following: zero rates for certain types of taxes, deferrals and installments for the payment of taxes and insurance premiums, restrictions on state and municipal control, as well as changes in currency, banking, insurance, and other related spheres. In addition, many different industries have been affected by sanctions restrictions, ranging from IT to logistics.

Tax relations are significantly influenced by two major categories of trends: trends based on international economic integration, such as the increasing influence of multinational enterprises (MNEs) on the national economy, the increasing number of cross-border transactions; and the mobility of taxpayers; and trends based on disintegration, which include the expansion of the practice of economic sanctions in relations between states along with the participation of economic agents under their jurisdiction, resulting in limitations on the activities described above.

The research conducted on the activities of international organizations as well as the works of foreign scholars not only reveals the content of the problems of taxation of the income of MNEs from e-commerce but also provides directions for improving the rules of profit distribution without the need for physical presence in the state in the digital era. The significant studies conducted on the problems surrounding the taxation of income generated by MNEs operating in a country where

users are located without a physical presence, as well as the evaluation of proposals received in connection with this issue, will contribute to the formulation of a common international approach to the adaptation of tax systems in the digital economy.

In order to prevent the impact of negative geopolitical and foreign economic factors on the development of economic sectors and the financial sector, the Government of the Russian Federation, together with the Federal Assembly of the Russian Federation, has adopted a wide range of measures, including speeding up and simplifying settlements carried out at the expense of budgetary funds and providing conditions for flexible management of funds of the National Welfare Fund.¹ Thanks to these measures, the current state of the budgets within the budgetary system of the Russian Federation remains stable.

Therefore, in modern conditions, the problems pertaining to risks and threats in the tax sphere, as well as the methods of countering their progression, are of paramount importance for the state in the system of national and supranational priorities and require adequate analysis.

Since this project seeks to identify and analyze scenarios and tools for the development of Russian tax legislation in the context of changing international regulation of the taxation of profits of global digital companies, it is also necessary to study the actions taken by international organizations, as well as the works of foreign scholars.

As is well known, the OECD has developed a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy.²

On 11 July 2023, the members of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting agreed upon an “Outcome Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy.”³ The Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy will ensure a fairer and more equitable distribution of profits and taxing rights among countries and jurisdictions with respect to the world’s largest MNEs. The Outcome Statement highlights the deliverables developed by the Inclusive Framework to address the remaining elements of the Two-Pillar

¹ Меры Правительства по повышению устойчивости экономики и поддержке граждан в условиях санкций // Правительство России [Government Measures to Increase the Stability of the Economy and Support Citizens in the Face of Sanctions, Russian Government] (Sep. 2, 2023), available at http://government.ru/sanctions_measures/.

² OECD, *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy*, 8 October 2021 (Sep. 2, 2023), available at <https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.htm>.

³ OECD, *Outcome Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy*, 11 July 2023 (Sep. 2, 2023), available at <https://www.oecd.org/tax/beps/outcome-statement-on-the-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-july-2023.pdf>.

Solution, including a Multilateral Convention (MLC), a simplified framework for the arm's length principle, the Subject-to-Tax Rule (STTR), and a comprehensive action plan for coordinated implementation.

On 17 July 2023, the OECD published a consultation document on Amount B under Pillar 1,⁴ building upon the input received on the public consultation document published in December 2022. On the same day, the OECD also published new documents on the implementation of Pillar 2.⁵

There are two alternatives to the scope of Pillar 1 that are presented: "Amount A," which does not require a separate qualitative scoping criterion to identify and exclude non-baseline contributions; and "Amount B," which does require a separate qualitative scoping criterion to identify and exclude non-baseline contributions. According to the consultation document, jurisdictions that support Amount A take the position that a separate scoping criterion will not improve the reliability of Amount B and will instead undermine the objectives of tax certainty. On the other hand, jurisdictions supporting Amount B argue that without a separate qualitative scoping criterion being applied to support the definition of baseline distribution, Amount B will not result in outcomes that are aligned with the arm's-length principle.⁶

The OECD's Two-Pillar Solution focuses on new rules for digital and possibly all consumer-oriented businesses (Pillar 1), as well as on a global minimum tax agreement (Pillar 2). The aim of the OECD is to eliminate the spread of unilateral taxes on digital services, as these taxes create a risk of double taxation. On the other hand, one of the frequent criticisms of the OECD proposals is that they are difficult to implement and that global minimum tax rules put developing countries at a disadvantage.

It should be noted that scholars give different evaluations to the OECD project.⁷ As noted, while G7 countries have celebrated the International Framework agreement

⁴ Consultation Document on Amount B under Pillar 1 (Sep. 2, 2023), available at <https://www.oecd.org/tax/beps/public-consultation-document-pillar-one-amount-b-2023.pdf>.

⁵ OECD, *Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two)*, OECD/G20 Inclusive Framework on BEPS (2023) (Sep. 2, 2023), available at www.oecd.org/tax/beps/administrative-guidance-global-anti-base-erosion-rules-pillar-two-july-2023.pdf; OECD, *Tax Challenges Arising from the Digitalisation of the Economy – Subject to Tax Rule (Pillar Two)*, Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris (2023) (Sep. 2, 2023), available at <https://doi.org/10.1787/9afd6856-en>; OECD, *Tax Challenges Arising from the Digitalisation of the Economy – GloBE Information Return (Pillar Two)*, OECD/G20 Inclusive Framework on BEPS, OECD, Paris (2023) (Sep. 2, 2023), available at www.oecd.org/tax/beps/globe-information-return-pillar-two.pdf.

⁶ OECD Publishes Consultation Document on Amount B Under Pillar One for Simplifying Transfer Pricing Rules (Sep. 2, 2023), available at https://research.ibfd.org/#/doc?url=/data/tns/docs/html/tns_2023-07-17_o2_1.html.

⁷ Philip Baker, *Editorial: The Need for Plan B*, 51(8) Intertax 542 (2023); Vikram Chand & Camille Vilaseca, *Pillar I: The Marketing and Distribution Safe Harbour (MDSH) as Applicable to Licensed Manufacturers and Centralized Business Models: Does It Fulfil Its Policy Objective?*, 51(8) Intertax 572–94; Cees Peters,

(also known as the IF deal) as a breakthrough in “ending the race to the bottom in corporate taxation” worldwide, low- and middle-income countries have expressed frustration and concern about various inequities embedded in this deal, with Kenya, Nigeria, Pakistan, and Sri Lanka refusing to sign on. Despite low- and middle-income countries suffering disproportionately from multinational corporate tax avoidance, the net result of this largely G7-driven tax reform appears to be that it will overwhelmingly benefit only these handful of wealthy countries.⁸

Thus, the BRICS countries could be the headliners in constructing their own rules based on an analysis of the rules of the OECD and the United Nations. It should be mentioned that some of the BRICS countries have already voiced their own different points of view on the various initiatives in the field of international taxation. For instance, Brazil refused to sign the Multilateral Instrument (MLI) due to concerns that it may disproportionately target their countries’ firms and that renegotiating treaties bilaterally would result in terms that are more preferable to their country. As a result, it has decided to renegotiate each of its bilateral treaties with its treaty partners on an individual basis, considering that the country does not have a long list of treaties.⁹

The Russian Federation does not currently participate in OECD projects. Nevertheless, it is important to study and analyze both OECD and UN projects in order to understand which practices can be determined as being best practices and to be able to make informed decisions on whether international measures should be implemented in Russian bilateral tax treaties or in national legislation.

The possibility of using the OECD rules in the Russian Federation should be assessed, first and foremost, from two perspectives:

- 1) from the perspective of the correlation between Pillar 2 rules and the preferential tax regimes established by Russian tax legislation;
- 2) from the perspective of the recent Russian tax policy in terms of concluding and amending double tax treaties.

Due to the current international situation, it is necessary to monitor how international tax rules are being implemented by different countries. It is also necessary to understand which circle of partner countries Russia should focus on when formulating its foreign tax policy. These global matters also influence the formation of the Russian regulatory framework.

Critical Analysis of the General Court’s ‘EU Arm’s Length Tool’: Beware of the Reflexivity of Transfer Pricing Law!, 31(1) EC Tax Rev. 30 (2022).

⁸ Julie McCarthy, *A Bad Deal for Development: Assessing the Impacts of the New Inclusive Framework Tax Deal on Low- and Middle-Income Countries*, Brookings Global Working Paper No. 174 (May 2020) (Sep. 2, 2023), available at https://www.brookings.edu/wp-content/uploads/2022/05/Tax-and-Bad-Deal-for-Development_Final.pdf.

⁹ João Francisco Bianco, *Principal Purpose Test in Brazilian Tax Treaties*, 7 RDTI Atual 247 (2020).

2. A Brief Comparative Analysis of the Approaches of the BRICS Countries to the Taxation of Digital Goods and Services

The problems associated with the development of the digital economy are relatively new for the BRICS countries, and the members of this association have different indicators of the development of the components of the digital economy. National tax laws also differ, as do the specifics of the implementation of international tax rules.

However, we can divide these countries into two groups: countries that are actively creating new projects in respect of the rules of taxation (Brazil and India) and countries that are reticent about imposing new taxes on digital services for MNEs (Russia, China, and South Africa).

Nevertheless, the BRICS countries may continue to operate “inside the system” as a coordinated group. They may focus on their mutual interests, on the specific interests of the individual member countries, or even on the more general interests of the “developing world.” Since inviting more nations to join the BRICS association, this group of nations has gained even more relevance.

The BRICS countries possess the potential to have a significant influence in the sphere of international taxation. As for Russia, the key role of its domestic laws and the country's reluctance to submit to the power of international organizations shape much of its tax treaty policy and may affect its role in future developments, most likely within the BRICS framework.

According to Professor Vinnitskiy, the differences in the fiscal interests of developed and developing countries can predetermine different approaches taken by these countries to the understanding of the concept of permanent establishment, to setting the rates of withholding at source taxation on passive income (dividends, interest, and royalties), and to resolving other issues in the sphere of cross-border taxation. These aspects have been reflected, in particular, in the content of the OECD Model Convention (OECD Model) and in the text of the United Nations Model Convention (UN Model), which, in turn, explains the differences existing between those two models.¹⁰

The BRICS group of nations is continually working to deepen cooperation in the fields of taxation and tax administration. At the same time, states have different approaches to the taxation of the digital economy and the introduction of digital taxes. For example, India has introduced a number of specific tax measures, including the institution of the concept of “significant economic presence,” have been introduced in India, while China, on the contrary, is still approaching the taxation of digital services with caution and using general rules governing the collection of VAT. In Brazil, the taxation of digital services has been stalled at the draft law stage for several years.

¹⁰ Danil V. Vinnitskiy, *The Objectives of International Fiscal Policy of BRICS Countries as Net Exporters of Capital in the Russian Conventions of Double Taxation*, 39(2) Eur. & Asian L. Rev. 29–30 (2020).

Let us now look at the individual experiences of the BRICS states in more detail.

2.1. Brazil

In Brazil, the following two issues in the field of regulation of the digital economy are both crucial and complex: at what level taxes on digital transactions should be levied (at the federal or state level); and whether the tax will be paid in the country of origin or in the destination country.

There are two types of VAT in Brazil: ICMS (Imposto sobre Circulação de Mercadorias e Serviços) which is the tax on the turnover of goods and transport and communication services, a state sales tax; and IPI (imposto sobre produtos industrializados) which is an industrial goods tax, a federal excise tax.

There is also a municipal tax on the supply of goods or services, known as ISS (imposto sobre serviços). It is usually levied by the municipality or city in which the taxpayer provides the service.¹¹

A major problem that arises in the field of digital economy taxation is the lack of universality of the approach to the identification of the object of taxation; in other words, it is often complicated to determine whether the digital product is a good or a service. As noted by Lyutova:

in reality, digital goods can, for example, be downloaded from the manufacturer's website, without the need to transfer its material carrier. This means that it can be realized by sending by e-mail or by uploading to the Internet, organizing appropriate access. Usually, digital products are texts, sounds and video files. It is often difficult to determine which type of product is a digital product, whether it acts as an asset, work or service. For example, in case a digital product is in the form of a temporary link to a training text file or video (audio) record on the site, the nature of such a legal fact is controversial in terms of the classic triad of "products, work, service."¹²

There are various examples of judicial cases on this issue in the BRICS countries. For instance, the Federal Supreme Court of Brazil issued a ruling on 24 February 2021, according to which software transactions are considered services and therefore should be subject to a municipal services tax (ISS), the rates of which range from 2% to 5%.¹³

¹¹ Brazil – Indirect Tax Guide, KPMG Global (Sep. 2, 2023), available at <https://home.kpmg/xx/en/home/insights/2018/10/brazil-indirect-tax-guide.html>.

¹² Лютова О.И. Объект налогообложения в условиях цифровизации // Вестник Российского университета дружбы народов. Серия: Юридические науки. 2020. Т. 24. № 3. С. 695–671 [Olga I. Lyutova, *Object of Taxation Under Digitalization*, 24(3) RUDN J.L. 695 (2020)].

¹³ Brazilian Federal Supreme Court Unravels the Levy of Taxes on Software Licensing, Machado Assos (Sep. 2, 2023), available at <https://www.machadoassociados.com.br/en/2021/05/brazilian-federal-supreme-court-unravels-the-levy-of-taxes-on-software-licensing/>.

Ever since software began to be sold on physical media (and particularly after it became possible to purchase software by downloading), Brazilian states and municipalities have competed for tax revenues in this industry. The states of Brazil have historically imposed ICMS taxes on the sale of software, considering it to be a tangible good due to the existence of the disk or a physical storage media. Therefore, the states wanted to preserve this inherent nature of “goods” even when physical carriers were no longer needed.

In 2016, several other technology services were added to the list, allowing the municipality to levy a local tax. As a result, this tax is now applied to the storage of data, texts, images, videos, applications (including cloud services) and the provision of video, audio, text content, and images over the Internet via streaming.

However, significant changes have occurred since then. In 2023, the Brazilian tax authorities modified their understanding regarding the levy of the Program of Social Integration Tax Import (hereinafter, PIS-Import) and the Contribution for the Financing of Social Security Import (hereinafter, COFINS-Import) on international remittances for software licensing fees through the COSIT Tax Ruling No. 107, published on 13 June 2023. The ruling is based on the abovementioned decision of the Federal Supreme Court in Direct Actions of Unconstitutionality (ADI) No. 5,659/MG and No. 1,945/MT,¹⁴ which determined the levy of the Service Tax (ISS) on software licensing operations, whether standardized (off-the-shelf) or custom-developed, regardless of the means of acquisition (download or physical support).¹⁵ Based on legal precedents from the Federal Supreme Court and asserting the notion that software licensing involves an obligation to perform corresponding to the licensor’s intellectual effort, the Brazilian tax authorities have now classified remittances for software licensing fees as remuneration for imported services, thus making them subject to the PIS/COFINS-importation contributions. The same classification was applied to the many other services related to the licensed software, such as maintenance, updates, support, and training services.

One instance illustrating these problems is a case involving Microsoft.¹⁶ On 2 March 2021, the Supreme Court of India rendered a ruling stating that the payments made

¹⁴ STF Decides for the Levy of ISS, and Not ICMS, on Software Transactions and Defines the Temporal Effects of Such a Decision (Sep. 2, 2023), available at <https://btlaw.com.br/en/2021/02/26/stf-decide-pela-incidencia-de-iss-e-nao-de-icms-sobre-operacoes-com-sofware-e-definir-os-efeitos-temporais-dessa-decisao/>.

¹⁵ Brazilian Tax Authorities (‘RFB’) Changed their Interpretation Regarding the Levy of PIS and COFINS-Import on International Remittances for Software Licensing Fees (Sep. 2, 2023), available at <https://news.fcrlaw.com.br/brazilian-tax-authorities-rfb-changed-their-interpretation-regarding-the-levy-of-pis-and-cofins-import-on-international-remittances-for-software-licensing-fees/>.

¹⁶ *Engineering Analysis Centre of Excellence Pvt. Ltd v. The Commissioner of Income Tax & Another*, Civil Appeal Nos. 8733–34 of 2018 (2021) (Sep. 2, 2023), available at https://www.khaitanco.com/sites/default/files/2021-03/Engineering%20Analysis%20Centre%20of%20Excellence%20v.%20CIT_Ergo_22032021_0.pdf.

by a distributor in India to a manufacturer or non-resident supplier, as a form of compensation, do not entail any obligations to withhold taxes. The court reasoned that these remittances represent the purchase price of a computer program as a tangible commodity (direct sale of software), and the end user is only permitted to utilize the program by installing it on a computer, without owning the ability to reproduce it for commercial purposes or transfer it to others and therefore, not liable for taxes.¹⁷

In 2020–2021, a number of bills were submitted to the Brazilian Parliament proposing regulation of taxation of digital services such as advertising, sponsorship, or merchandising; content targeting; collecting, distributing, or processing user data; stimulating the consumption of services; payment platforms; and the use or distribution of images, text, video, or sound related to an individual or legal entity.¹⁸ However, none of these drafts passed the legislative procedure.

In April 2023, Brazil's finance minister announced a “digital tax” on e-commerce shipments.¹⁹ The proposal would not impose a new tax but rather amend the tax collection system. It obliges e-commerce platforms to collect taxes before shipping goods and exempts consumers from having taxes collected on their behalf during purchases. Brazil recently refrained from ending a tax exemption on international individual-to-individual orders valued at less than USD 50.²⁰

2.2. China

China is reticent about imposing a tax on digital services provided by foreign tech giants, especially American companies. In China, electronic services are subject to VAT in accordance with the general VAT regulations. There are no specific VAT regulations in place for cross-border deliveries of electronic services by non-resident suppliers to customers located in China. This means that customers located in China are obliged to withhold VAT at the established rate from the amounts they are paying out.

¹⁷ Karina A. Ponomareva, *Legal Issues of Taxation of Digital Business Models*, 58 Perm U. Herald, Juridical Sciences 615 (2022)].

¹⁸ Projeto de Lei Complementar no. 131, de 2020 (Sep. 2, 2023), available at <https://www25.senado.leg.br/web/atividade/materias/-/materia/142074>.

PLP 218/2020, Projeto de Lei Complementar (Sep. 2, 2023), available at <https://www.camara.leg.br/proposicoesWeb/fichadetramitacao?idProposicao=2260638>.

PLP 241/2020, Projeto de Lei Complementar (Sep. 2, 2023), available at <https://www.camara.leg.br/proposicoesWeb/fichadetramitacao?idProposicao=2263396>.

PLP 640/2021, Projeto de Lei (Sep. 2, 2023), available at <https://www.camara.leg.br/proposicoesWeb/fichadetramitacao?idProposicao=2271097>.

¹⁹ Brazil Plans ‘Digital Tax’ on Shipments from E-commerce Giants, Reuters, 20 April 2023 (Sep. 2, 2023), available at <https://www.reuters.com/markets/brazil-mulls-digital-tax-shipments-e-commerce-giants-minister-2023-04-20/>.

²⁰ Tommaso Giardini & Maria Buza, *DPA Digital Digest: Brazil* (May 2023) (Sep. 2, 2023), available at <https://digitalpolicyalert.org/digest/dpa-digital-digest-brazil>.

2.3. India

India is an interesting example of a country that started implementing the OECD approaches to the taxation of the digital economy very early on. The approaches adopted by Indian projects have corresponded with the recommendations in the Base Erosion and Profit Shifting (BEPS) Action 1 Final Report.²¹ However, this implementation may not be recognized as successful in all areas.

In 2016, India introduced an equalization levy that applies exclusively to online advertising.²² This was represented as a tax on payments made to non-residents digital service providers for rendering specified services, distinct from the traditional tax on income, outside the scope of Indian double tax treaties, and levied on the gross amount paid for digital transactions.²³ The need for such a levy arose due to a significant number of decisions of the Income Tax Tribunal as well as other High Courts going in favor of the taxpayer and depriving the government of its necessary revenue.²⁴

Since 1 April 2020, international e-commerce operators are required to pay an equalization tax on sales of products and services.²⁵ The scope of application of the equalization levy rules has been expanded to include the sale of goods and services in the field of e-commerce provided by non-resident operators to Indian customers.

Scholars point out that there are perhaps two nuances where the 2020 equalization levy differs from the 2016 one, which has led the 2020 equalization levy to be dubbed controversial and invited the scrutiny of the United States. First, the scope of the 2020 equalization levy is not subject-specific and extends to all classes of supplies, unlike the 2016 equalization levy, which applies only to digital advertisements. Second, the 2020 EQL is a direct liability on the non-residents digital service providers, who themselves must discharge it and undertake compliance, unlike the 2016 equalization levy, for which compliance is the responsibility of the Indian resident service receiver.²⁶

In 2019, another specific concept, referred to as “significant economic presence,” was introduced into the tax legislation of India. However, the Government of India postponed its implementation, stating that there were no effective mechanisms in the country’s international tax agreements for doing so.

²¹ OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project (October 2015) (Sep. 2, 2023), available at: doi.org/10.1787/9789264241046-en.

²² The Finance Act, 2016, No. 28 of 2016.

²³ Mukesh Butani & Tarun Jain, *United States’ 301 Findings on India’s Equalisation Levy – What Next?*, Kluwer International Tax Blog, 21 January 2021 (Sep. 2, 2023), available at <https://kluwertaxblog.com/2021/01/20/united-states-301-findings-on-indias-equalisation-levy-what-next/>.

²⁴ Sayan Basak, *Equalization Levy: A New Perspective of E-Commerce Taxation*, 44(11) Intertax 845 (2016).

²⁵ Chapter VI, Finance Act of India, 2020.

²⁶ Butani & Jain, *supra* note 23.

2.4. South Africa

In 2020, the African Tax Administration Forum (ATAF) released a Suggested Approach to Drafting Legislation on Digital Sales Tax Services (hereinafter, Suggested Approach).²⁷ Many ATAF members have reported difficulties in taxing highly digitalized businesses operating in their countries. Their economies are rapidly getting more digitalized, and this digitalization often enables MNEs to carry out business in African countries even when they have very little to no physical presence in those countries. This trend has increased due to the use of digitalized services necessitated by the COVID-19 pandemic, which led to the vast majority of MNEs with a physical presence in a country closing their physical premises and moving to online trading. This makes it difficult for countries to establish taxing rights over the profits the MNEs are making from those business activities.

The reason behind this trend is that the current international tax rules only allocate taxing rights to a country where a non-resident enterprise creates a sufficient physical presence in that country, sometimes referred to as creating a “nexus” in that country. However, the business models of highly digitized businesses enable MNEs to carry out business in an African nation with very limited or no physical presence in that country, thus causing significant tax risk.

The Suggested Approach, which has been developed by the ATAF Secretariat and the ATAF’s Cross-border Taxation Technical Committee, will help African countries that are considering implementing a digital service tax (DST) to tax the transactions of highly digitalized businesses. It should be noted that some African countries, such as Kenya²⁸ and Nigeria,²⁹ have already enacted digital service tax laws and are in the process of putting those laws into effect. Additionally, several other African countries are considering this option. Hence, this Suggested Approach is intended to provide African countries with a suggested structure and content for their legislation and possibly the regulations. It also provides a framework that draws from the various DST legislation enacted in other jurisdictions, but which has been adapted to meet the specific challenges faced by African countries.

Acknowledging the necessity of ensuring that the DST does not negatively impact the growth of the digital sector in African countries, the Suggested Approach proposes that countries set *de minimis* thresholds to ensure that they only target large and profitable digital businesses. This approach, coupled with the setting up of modest rates of DST, will be crucial for the promotion of investment and growth in the digital economy in Africa.

²⁷ Republic of Kenya, The Finance Bill 2020, Kenya Gazette Supplement No. 66 (National Assembly Bills No. 10), Nairobi, 5 May 2020 (Sep. 2, 2023), available at http://www.parliament.go.ke/sites/default/files/2020-05/Finance%20Bill%2C%202020_compressed.pdf.

²⁸ *Id.*

²⁹ Nigeria to Prioritise Taxes from Digital Non-Resident Firms in 2022, Reuters, 21 January 2022 (Sep. 2, 2023), available at <https://www.reuters.com/world/africa/nigeria-prioritise-taxes-digital-non-resident-firms-2022-2022-01-20/>.

As previously mentioned, the ATAF welcomed the OECD's tax reform, but it also expressed reservations about the effectiveness of the proposed provisions for Africa.

Even though the South African Tax Service has indicated its intention to join the OECD initiatives, it has concerns that the OECD approach will not benefit South Africa as a developing country.

In South Africa, VAT is applied to electronic services. The amendments to the VAT Law in 2019 came into force with the objective of establishing regulatory measures for cross-border online trading of digital goods.³⁰ It should be noted that VAT legislation does not distinguish between B2B and B2C e-commerce operations.

3. Tax Incentives for IT Companies

Investment in research and development (R&D) is a key factor driving innovation and economic growth. Governments across the world adopt various financial support instruments to promote R&D by businesses and increasingly rely on tax incentives to incentivize commercial R&D investment for businesses.³¹ These incentives are used as mechanisms of economic induction to stimulate specific branches of industry, such as IT development. Approaches to R&D, IT, or other types of incentives eligible for tax relief differ across jurisdictions. For instance, tax incentives in China cover a wide range of innovative development, including high-tech companies and products, R&D expenses, accelerated depreciation of fixed assets, the import of high-tech equipment, technology transfer, expenses for the wages of expert and technical personnel, modernization of production, etc. However, the main method used by the Chinese government to implement its policy of tax benefits is to reduce the tax rate that is applied to the profits of enterprises.³²

3.1. Tax Incentives for IT Companies in Brazil

In Brazil, the Law 11.196/05, also known as the Lei do Bem,³³ establishes the granting of tax incentives to legal entities that carry out research, development, and technological innovation. The Brazilian approach to digital taxation is aimed at encouraging the development of information technology products, as well as investments in innovation by the private sector. As a result of this policy of stimulating IT production via tax incentives, companies should invest in RD&I activities. In this

³⁰ Value-Added Tax Act 89 of 1991 in Government Notice 429 of 18 March 2019.

³¹ OECD R&D tax incentives database, 2021 edition, Work Package 1: Information and Indicators of Tax Relief for Business R&D Expenditures, 9 December 2021 (Sep. 2, 2023), available at <https://www.oecd.org/sti/rd-tax-stats-database.pdf>.

³² Karina A. Ponomareva, *Investment Tax Benefits in China: Special Features of Legal Regulation and Comparative Analysis with Russian Practices*, 6(3) *Pravoprimerenienie*, Law Enforcement R. 83 (2022).

³³ Lei. No. 11.196, de 21 de novembro de 2005, conhecida como Lei do Bem, em seu Capítulo III, regulamentada pelo Decreto no. 5.798, de 7 de Junho de 2006.

case, the reduction of the tax burden is made possible through IPI exemptions and financial credits.

Law 13,023/2014³⁴ made changes to the Information Technology Law 8,248/1991 (Lei de Informática),³⁵ which regulates the level of competitiveness in this business sector. The main tax changes enacted by this law are as follows:

- The reduction of 80% of the tax on industrialized products (Imposto sobre Produtos Industrializados, IPI) due, originally granted by Information Technology Law 8,248/1991 and effective until 31 December 2014, available for entities developing or providing information technology goods or services and investing in related research and development, is extended to 31 December 2029, as follows:

- from 1 January 2004 to 31 December 2024: a reduction of 80% of the IPI due;
- from 1 January 2025 to 31 December 2026: a reduction of 75% of the IPI due;

and

- from 1 January 2027 to 31 December 2029: a reduction of 70% of the IPI due.

- Certain goods (for e.g. portable computers and magnetic disk drives) are, however, subject to different reductions, as follows:

- from 1 January 2004 to 31 December 2024: a reduction of 95% of the IPI due;
- from 1 January 2025 to 31 December 2026: a reduction of 90% of the IPI due;

and

- from 1 January 2027 to 31 December 2029: a reduction of 70% of the IPI due.

- Creation of a new reduction of the IPI due in respect of information technology goods (with the exception of the listed goods, which are subject to a differentiated reduction) produced in the regions of Center-West (Centro-Oeste), SUDAM and SUDENE in Brazil, as follows:

- from 1 January 2004 to 31 December 2024: a reduction of 95% of the IPI due;
- from 1 January 2025 to 31 December 2026: a reduction of 90% of the IPI due;

and

- from 1 January 2027 to 31 December 2029: a reduction of 85% of the IPI due.

- Goods developed in Brazil and included in the category of information technology and automation goods according to Information Technology Law 8,248/1991 benefit from a reduction of the IPI as follows:

- from 15 December 2010 to 31 December 2024: a reduction of 100% of the IPI due;

- from 1 January 2025 to 31 December 2026: a reduction of 95% of the IPI due;

and

- from 1 January 2027 to 31 December 2029: a reduction of 90% of the IPI due.

- For entities to enjoy the tax benefits granted by Information Technology Law 8,248/1991, the condition of investing annually at least 5% of the entity's turnover in

³⁴ Lei No. 13.023, de 8 agosto de 2014.

³⁵ Lei No. 8.248, de 23 de outubro de 1991.

research and development related to information technology activities undertaken in Brazil is imposed.³⁶

This legal provision was partially revoked more recently by Law 13,969/2019, which provided for the Industrial Policy for the information technology and communication sectors and the semiconductor sectors. Nevertheless, in this last normative act, the Federal Government maintained the tax incentive policy by granting financial credits both in the CSLL (Social Contribution on Net Profit) and in the IRPJ (Corporate Income Tax), without prejudice to the fact that they may be offset against tax debts managed by the Special Federal Revenue Service of Brazil or that they may be reimbursed in kind, following an act of the Executive Branch. Parallel to all these incentives granted by the Union, the states and municipalities can also grant tax incentives aimed at innovation and technological development locally.³⁷

3.2. Tax Incentives for IT Companies in Russia

Since 2021, Russian IT companies have been stimulated by enhanced tax incentives, which allow them to pay corporate income tax only to the federal budget as well as pay social security contributions at a heavily reduced rate.³⁸

This initiative, or tax maneuver in the IT industry, assumed, in particular, a reduction in tax rates from 1 January 2021 for Russian organizations operating in the field of IT and meeting certain requirements, including the share of income from core activities and the number of employees; the income tax rate was reduced from 20% to 3%; and insurance premium rates were reduced from 14% to 7.6% (para. 1.15 of Art. 284, subpara. 1.1 of para. 2 of Art. 427 of the Tax Code of the Russian Federation as amended by Federal Law No. 265-FZ of 31 July 2020).³⁹

In 2022, the list of support measures provided to IT industry participants has been expanded on the basis of Decree of the President of the Russian Federation No. 83 of 2 March 2022 “On Measures to Ensure Accelerated Development of the Information Technology Industry in the Russian Federation.”⁴⁰

³⁶ IBFD Tax Research Platform, *Brazil-Changes to Tax Benefits related to R&D and Information Technology Implemented* (Sep. 2, 2023), available at https://research.ibfd.org/#/doc?url=/data/tns/docs/html/tns_2014-08-13_br_3.html.

³⁷ Gésio de Lima Veras et al., *Technological Innovation, Tax Incentives and Economic Efficiency in the Brazilian Scenario: Analysis of the Case of the State of Piauí*, 10(4) Int'l Innovation Edu. & Res. 170 (2022).

³⁸ Vladimir V. Gromov, *Features and Problems of Tax Incentives for Small Software Companies in Russia*, 14(1) Fin. J. 9 (2022).

³⁹ Налоговый кодекс Российской Федерации, часть вторая от 5 августа 2000 г. № 117-ФЗ // Собрание законодательства РФ. 2000. № 32. Ст. 3340 [Tax Code of the Russian Federation, Part Two, No. 117-FZ of 5 August 2000, Legislation Bulletin of the Russian Federation, 2000, No. 32, Art. 3340].

⁴⁰ Указ Президента Российской Федерации от 2 марта 2022 г. № 83 «О мерах по обеспечению ускоренного развития отрасли информационных технологий в Российской Федерации» // Официальный портал правовой информации [Decree of the President of the Russian Federation No. 83 of 2 March 2022. On Measures to Ensure the Accelerated Development of the Information Technology Industry in the Russian Federation, Official Portal of Legal Information] (Sep. 2, 2023), available at pravo.gov.ru.

The tax support measures introduced by the Decree include the introduction of a zero percent corporate tax rate for IT companies holding a state accreditation certificate that will apply until 31 December 2024.

The Decree also exempts qualifying IT companies from certain taxes, currency regulations, and other forms of state and municipal control for a period not exceeding three years.

According to the Decree, the list of IT companies enjoying the tax incentives is extended to those generating revenues from the following activities:

- advertising dissemination and placement activities;
- provision of additional services with the use of applications and online solutions;
- distribution, installation, testing, and maintenance of Russian IT solutions.

The qualifying IT companies must be accredited with the Ministry of Digital Development, Communications, and Mass Media. To be eligible for accreditation, a company must be incorporated in Russia with relevant codes of economic activities and carry out the following activities in the field of IT:

- developing and implementing software and databases on physical media or in electronic form, regardless of the type of contract; or
- providing services (i.e. performing work) for the adaptation, modification, installation, testing, and maintenance of software and databases.

Besides, qualifying IT companies are exempt from control and supervisory measures for 2022–2024, with the exception of preventive measures (Art. 26.4 of Federal Law No. 294-FZ of 26 December 2008,⁴¹ Decree of the Government of the Russian Federation No. 448 of 24 March 2022⁴²). In addition, field tax audits of such organizations have been suspended until 3 March 2025 inclusive (Letter of the Ministry of Finance of the Russian Federation of 18 March 2022 No. 03-02-06/21331⁴³ and Letter of the Federal Tax Service of Russia dated 24 March 2022 No. SD-4-2/3586@).⁴⁴

⁴¹ Федеральный закон от 26 декабря 2008 г. № 294-ФЗ «О защите прав юридических лиц и индивидуальных предпринимателей при осуществлении государственного контроля (надзора) и муниципального контроля» // Собрание законодательства РФ. 2008. № 52 (ч. I). Ст. 6249 [Federal Law No. 294-FZ of 26 December 2008. On the Protection of the Rights of Legal Entities and Individual Entrepreneurs in the Exercise of State Control (Supervision) and Municipal Control, Legislation Bulletin of the Russian Federation, 2008, No. 52 (Part 1), Art. 6249].

⁴² Постановление Правительства РФ от 24 марта 2022 г. № 448 «Об особенностях осуществления государственного контроля (надзора), муниципального контроля в отношении аккредитованных организаций, осуществляющих деятельность в области информационных технологий, и о внесении изменений в некоторые акты Правительства Российской Федерации» // Собрание законодательства РФ. 2022. № 13. Ст. 2108 [Decree of the Government of the Russian Federation No. 448 of 24 March 2022. On the Specifics of the Implementation of State Control (Supervision), Municipal Control in Relation to Accredited Organizations Operating in the Field of Information Technology and On Amendments to Certain Acts of the Government of the Russian Federation, Legislation Bulletin of the Russian Federation, 2022, No. 13, Art. 2108].

⁴³ Письмо Минфина России от 18 марта 2022 г. № 03-02-06/21331 «О принятии мер, направленных на освобождение аккредитованных организаций от налогового контроля на срок до трех лет» [Letter of the Ministry of Finance of the Russian Federation No. 03-02-06/21331 of 18 March 2022. On Taking Measures Aimed at Exempting Accredited Organizations from Tax Control for up to Three Years].

⁴⁴ Письмо ФНС России от 24 марта 2022 г. № СД-4-2/3586@ «О назначении ВНП в отношении аккредитованных IT-организаций» [Letter of the Federal Tax Service of Russia No. SD-4-2/3586@ of 24 March 2022. On the Appointment of Field Tax Audits in Relation to Accredited IT Organizations].

However, there are problems that may arise for IT companies when applying for state accreditation. In 2022, Federal Law No. 67-FZ of 26 March 2022⁴⁵ established that the income tax rate for Russian IT companies that meet certain criteria for the tax periods of 2022–2024 will be levied at 0% (instead of 3%).

Since 14 July 2022, the requirements for accredited organizations operating in the field of information technology that are exempt from paying income tax for three years have also changed, as stipulated in paragraph 1.15 of Article 284 of the Tax Code of the Russian Federation.

In addition, the condition on the minimum number of employees was eliminated; before the specified date, it was established that companies with an average number of employees in the corresponding tax period of at least seven people have the right to apply for a preferential income tax rate.

It has been established that the income derived from activities in the IT sector, which is taken into account when determining the tax base, should constitute a minimum of 70% of the organization's total income for the reporting period, rather than the previously established threshold of 90%.

The list of income recognized as income from core activities for the purposes of applying the zero-income tax rate has been adjusted (para. 1.15 of Art. 284 of the Tax Code of the Russian Federation). At the same time, it is worth paying special attention to several points.

The Tax Code now contains definitions of such concepts as proprietary and custom computer programs and databases. According to paragraph 1.15 of Article 284 of the Tax Code of the Russian Federation, the term “own computer programs and databases” refer to programs and databases developed, adapted, and (or) modified by an organization or a person belonging to the same group of persons as the organization. In turn, a person who is directly involved in a taxpayer organization or in which this organization is directly involved is recognized as being in the same group as a taxpayer organization. Also included in the same group are organizations in which a third party is directly involved, that is, sister companies. The share of participation in all these cases should be more than 50%.

Income from the sale of copies of “own programs and databases,” from the transfer of exclusive rights to those programs and databases to the granting of usage rights, including remote access, is recognized as core income.

Income from the performance of work or the provision of services for the development, adaptation, and modification of computer programs, and databases,

⁴⁵ Федеральный закон от 26 марта 2022 г. № 67-ФЗ «О внесении изменений в части первую и вторую Налогового кодекса Российской Федерации и статью 2 Федерального закона «О внесении изменений в часть вторую Налогового кодекса Российской Федерации» // Собрание законодательства РФ. 2022. № 13. Ст. 1956 [Federal Law No. 67-FZ of 26 March 2022. On Amendments to Parts One and Two of the Tax Code of the Russian Federation and Article 2 of the Federal Law, On Amendments to Part Two of the Tax Code of the Russian Federation, Legislation Bulletin of the Russian Federation, 2022, No. 13, Art. 1956].

as well as the resulting programs and databases, is considered customized income in accordance with Article 284 of the Tax Code of the Russian Federation.

Gromov sums up all of the reasons that explain the need for a tax maneuver as follows: stimulating the export of Russian software, increasing domestic demand for such software, increasing the number of domestic IT companies with the expansion of the industry itself, increasing the competitiveness of the tax system and the investment attractiveness of the country, addressing the problem of "brain drain" by returning qualified specialists to Russia, facilitating structural transformations of the economy, implementing anti-crisis policy started during the pandemic against the background of restrictive economic measures, compensating for the lack of tax benefits, and preventing the decline of the industry.⁴⁶

The development of the IT industry necessitates the strengthening of several state-supported measures for IT companies. Investments in the IT industry will help increase the competitiveness of Russian IT products and services in both domestic and foreign markets. It is very important that the proposed tax incentive measures contribute to the development of the industry and ensure its continued growth and expansion, which will create the prerequisites for the development of digitalization in other sectors of the Russian economy.

Conclusion

Thus, the development of a digital economy leads to various issues, such as an increased dependence of the digital economy on data, network effects, the spread of multilateral business models, the tendency towards monopoly or oligopoly, and volatility. There are also problems with logistics in the era of the digital economy because of an increase in the number of cross-border movements of goods, services, and labor, as well as a rise in the number of economic agents working in the system. Such growth creates a significant burden on the tax authorities and may reduce the effectiveness of the application of tax legislation.

The key risk associated with the introduction of a Russian unilateral tax in the conditions of its coexistence with Pillar 1 is that such a tax could lead to significant barriers for business. At the same time, the problem of eliminating double taxation will not be solved, since the Russian tax will not be accepted for offset by the countries participating in the mechanism of the first component of the OECD due to the incompatibility of the two systems.

We propose the idea of developing a mutually beneficial system of international cooperation with Russia in the field of taxation with the maximum number of countries, including other developing countries as well as the BRICS countries. The analysis of experiences of the BRICS countries shows that they use different

⁴⁶ Vladimir V. Gromov, *Favorable Tax Treatment of Russian Software Companies and its Evolution from the Choice of Preferences to the Tax Maneuver in the IT Industry*, 14(3) Financial J. 11 (2022).

approaches to regulating the taxation of their economies; however, each of these countries follows its own interests in protecting its national fiscal base, or, in other words, ensuring the tax security of the state.

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