Digital Taxation: can it contribute to more just resource mobilisation in post-pandemic reconstruction?

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Executive Summary

The acceleration of global digital services and e-commerce has exposed the outdated nature of many tax regimes around the world. The forgone potential revenues for states, particularly in the context of post-pandemic economic reconstruction has further necessitated the updating of the tax system to address what is an increasingly global and complex challenge. For Africa, the situation is arguably even more precarious with the dawn of the African Continental Free Trade Area, ACFTA, where there is an expected significant drop in conventional physical trade tariffs. As trade barriers begin to ease across the region and e-commerce gradually becomes more pervasive the success of the proposed single digital market will depend on some levels of harmonisation digital taxation policy.

This makes the assessment of the tax regulatory regimes on the continent and the alignment of them with an international tax regime imperative. Such an assessment needs to consider two international processes that are particularly important in this context: the OECD/G20 BEPS tax proposals and its potential and challenges, and, from a trade perspective, the plurilateral negotiations on e-commerce at the WTO. It also requires consideration of various domestic resource mobilisation strategies within the digital markets, especially in the context of post-COVID-19 reconstruction. In this regard, the paper also examines the effects of unilateral taxes on digital services and transnational global platforms, and how this impacts the development of the digital economy in Africa. It also considers the regressive taxation applied in many African countries on end users of social networking services and its negative impact on digital substitution during lockdowns and on social and economic inclusion more generally.

The paper highlights how digitalisation and datafication has posed challenges for traditional tax revenue systems. However, the accelerated growth in digital services and e-commerce also presents new opportunities for Africa's economy. The paper seeks to inform effective governance of global public goods from a developing country and regional lens, exploring the challenges and opportunities created by the digitalisation and datafication of Africa's economy and the policy options for justly expanding the tax base for optimal state formation.

Findings from the paper indicate that the stringent digital tax policies as currently applied on end-users within the continent – rather than the global platforms – as a means of appropriating location-specific rents within the digital economy, have the potential to lower affordability of online services as well as impede the fundamental human right of freedom of speech. While the paper is of the position that the emerging unilateral approaches to digital taxation in Africa can serve as a temporary gateway and a starting point to better grasp the value creation and capture dynamic of the digital economy, it has a significant disadvantage of risking a global impasse for global bilateral trade obligations.

This paper proposes the following key recommendations to optimising the global tax system:

- Within the ambit of an equitable value distribution with reference to developing economies, a revenue threshold that is based on the size of customer payments within the country to a non-resident provider of services – whether they are digitalised or not – is the most effective and easiest to apply in determining the taxable nexus. This optimised approach can be achieved by expanding on the profits-split methodology within the transfer pricing framework that the

  OECD and G20 have put forward. While the current BEPS proposals have unfairly focused on the residual profit-split, there also needs to be an incorporation of the contribution profit split for a fairer assessment, which looks at the contribution of all the firm entities concerned.
- African countries need to build out the required systems for implementing these digital tax proposals on the continent. These need to be cognisant of the institutional endowments of

countries and adapted to meet local contexts. This will require both local research and the building of an adequate evidence-base to inform Africa-led alternatives.

- In the same vein, capacity development efforts in Africa with respect to digital taxation should leverage more South-South rather than the current North-South cooperation model if the existing problems for the region, as espoused within the BEPS process, are to be effectively addressed.
- In addition, the WTO negotiations on e-commerce have through its customs moratorium resulted in huge revenue losses to developing countries via the restriction of the flexibility to regulate the import of digital services. The issue of the moratorium needs to be revisited, as proposed by some African states to create an enabling international trade regime that will promote e-commerce on terms that are more equitable. For this to happen the concerns of countries – the majority of which are currently African countries – that do not feel that that the interests of developing countries are safeguarded will need to be addressed.
- At the regional level, the AfCFTA represents an opportunity for tax harmonisation on the continent, but this may not necessarily be for every form of tax. Here it will be important to assess how African countries are leveraging the new tax opportunities by way of introducing regulations and legislation that would at least capture some of those proceeds that were previously not being taken advantage of.
- Digital service taxes as currently applied on users rather than providers across several African jurisdictions is not ideal from the perspective of good tax design principles, as it is quite likely that the cost of implementation will be passed on to consumers or users. For a continent where the average age is 19 years, and where most people are unemployed or in the informal sector, the regressive nature of indirect taxes are not a good starting place for taxing the digital economy. This is likely to distort markets and be less progressive in general than a direct tax on profits would. The focus should therefore rather be on taxing income generated within digital spaces, which should be the most important basis for taxation, even if this is not immediately achievable.
- By more actively engaging in the BEPS reform of the global taxation regime, African countries may be able to get at least a bare minimum of 15% from global digital players with no physical presence in the country, and from whom they currently receive nothing. This will require relatively few enforcement mechanisms.

1. Introduction

The impacts of the global economic crisis precipitated by the COVID-19 pandemic and associated lockdowns has been uneven, both between and within countries. There is growing evidence that already vulnerable states and marginalised people and communities within states have been hardest hit, both from a public health and an economic perspective (Shadmi et al., 2020; Gupta et al., 2021). This has led to calls by the UN, other multilateral agencies and global leaders for a reset of the global economy, and to deal with economic inequalities through new forms of social compacting.[1]

Although these calls have been given fresh impetus by the pandemic, they are not new. For example, in 2019, UN Secretary General Antonio Guterres identified digital transformation, alongside the climate crisis, as a seismic shift that will shape the 21st century. Both, he said, are likely to widen inequalities even further, unless urgently addressed on a global scale.

The need for dramatic course correction, in this case, to meet the Sustainable Development Goals, was also highlighted by UNCTAD (2019) in its call for a global Green New Deal. As it pointed out, the problem of hyperglobalisation was the result of several intersectional challenges that remained unaddressed, such as prioritising narrow financial interests, stagnant wages, crippling levels of debt, rigged markets, corporate rentierism, and a dearth of productive investment. While there was no "quick fix" to these challenges, they nevertheless further hobbled economic development and had resulted in the recurrent financial crises of a dangerously unbalanced, unsustainable and inequitable world.

While digital exclusion appears to have had a compounding effect on structural inequality during the lockdown, the era of increasing digital interdependence may present an important opportunity for inclusive socio-economic development under the right conditions. As the demands for greater resources to deal with the economic crisis induced by the pandemic and increased demand for social protection and resources for economic reconstruction take centre stage, new opportunities have emerged for domestic resource mobilisation, particularly in the areas of leveraging global processes of digitalisation and datafication and the global governance of these. These processes must however ensure that African countries, with their relatively nascent digital economies, benefit from the changes, specifically with respect to the global tax and trade regimes on digital product and services.

The rapid growth of global e-commerce has further exposed the outdated nature of many tax regimes around the world. This has come at a heavy cost to state revenues and has necessitated the development of updated tax systems to address what is a complex challenge. While historically global processes of digitalisation and datafication have been seen as a threat to the often-marginal tax bases that exist in developing countries, tax base erosion due to profit-shifting by digital platforms is estimated to cost developing countries over USD500 billion annually (Singh, 2018)

Africa's economic structure remains largely commodity dependent with a low-income tax base due to high levels of informality. The tax system therefore constitutes a fundamental development policy instrument and opportunity for resource mobilisation in trade on the continent and a central element

[1] From the World Economic Forum's 'the Great Reset' initiative which aims to help inform all those determining "the future state of global relations, the direction of national economies, the priorities of societies, the nature of business models and the management of a global commons".

in the establishment of the African Continental Free Trade Area (AfCFTA). Although the AfCFTA does not mention the digital economy and issues of digital trade have only been put on the agenda recently, the African Union's Digital Transformation Strategy[2] highlights the importance of the digital economy for the continent.

Currently, only around ten African countries have proposed some form of tax regime for digital goods and services – including Angola, South Africa, Cameroon, Nigeria, Algeria, Senegal and Kenya. However, many of the tax frameworks are still basic and do not take into consideration the full spectrum of the digital economy (Musgrove, 2020). In addition, several African countries (including Uganda, Mozambique, Tanzania, Zambia and Benin) are already imposing unilateral tax measures on some digital economy transactions, especially on foreign service providers. These taxes generally comprise excise duties on digital transactions, value-added taxes (VAT), social media taxes, and online content licence fees, with Over-The-Top (OTT) service fees and profit-targeting equalisation levies.

However, there are doubts with regards to compliance and effective enforcement without multilateral cooperation, and concerns over the unintended consequences for consumer welfare, e-commerce (especially for small businesses and smaller markets in Africa), cross-border trade, foreign investments and innovation within the region's fledgling digital economy. This situation is exacerbated by the growing uncertainty with respect to the scope of application of the new tax regimes, the risks of over-taxation (without corresponding tax credits in countries of residence) (Saint-Amans, 2017), and their congruence with international trade agreements and treaties.

Two international processes are particularly important in this context. The Organisation for Economic Co-operation and Development (OECD) and G20 effort to prevent base erosion and profit shifting (BEPS) aims to achieve transparency in the tax practices of multinationals (including global digital platforms) and restore trust in domestic and international tax systems. Under the Inclusive Framework on BEPS, 139 countries and jurisdictions are collaborating to put an end to tax avoidance strategies that exploit gaps and mismatches in tax rules to avoid paying tax. The BEPS initiative has resulted in some level of consensus on the need for countries to adapt their taxation laws, and agreement that *de minimis* levels at an international level, especially on lower-value online goods, need to be reviewed (OECD, 2019) – though there is not consensus amongst African countries on the issue.

From a trade perspective, there have been plurilateral negotiations on e-commerce at the WTO. A moratorium on imposing customs duties on electronic transmissions has been in place since the 1980s and is being considered for further extension. However, this is something likely to benefit established international players and arguably at the expense of developing states. It has already resulted in huge revenue losses to developing countries via the restriction of their flexibility to regulate the import of digital services.

Di John (2006) points out that of all the methods of resource mobilisation taxation is most closely tied to state formation and capability – arguably the most intractable problem for developing countries and highly dependent on the nature of political settlements (Tyce, 2020). The importance of taxation is also

[2] The Digital Transformation Strategy for Africa (2020-2030). https://au.int/sites/default/files/documents/38507-doc-dts-english.pdf

highlighted in a recent report by the UN Secretary-General's High-level Panel on Digital Cooperation in the Digital Economy. Alongside trade, consumer protection and competition, it is considered one of the "areas of economic policy that require new thinking in the digital age" (United Nations, 2019b). These perspectives emphasise the regional and multilateral policy cooperation that is necessary to be effective if digital public goods are to be viewed as part of a global commons that can, in the wake of the global economic crisis, be governed to shift the pre-pandemic trajectory of deepening economic and social inequality.

It is within this context that this paper explores the challenges and opportunities created by the digitalisation and datafication of Africa's economy and assesses policy options for expanding the tax base, including through the global digital tax being deliberated by the BEPS initiative. It also examines the effects of unilateral taxes on digital services and transnational global platforms, and how this impacts the development of the digital economy in Africa. A key objective is to elucidate the complexities of policy options for African states with the view that these might inform nascent policy decisions for a tax regime that creates a fair distribution of value from the ongoing process of digitisation and datafication within the region's economy.

2. Background

High levels of informality in African economies together with the low levels of industrialisation – and in some cases de-industrialisation – have long posed a challenge to implementing mechanisms devised for more industrialised and mature economies to reduce fiscal inequality in society. Generally, African countries have lacked the tax base to undertake "compensatory redistribution by tax and transfer" or the "… progressive taxation and redistributive social spending" (Unger, 2019) associated with more mature welfarist economies. In many countries, for a variety of historical, economic and political reasons, there appears not to be either the will or the resources for social investment or social welfare.

With the advent of private mobile companies in Africa providing the significant, in some cases only, source of revenue for the state, the response in several countries was to push corporate taxes to levels that either disincentivised critical infrastructure investments or resulted in high corporate taxes to be passed on to end-users (Rogers & Pedros, 2018). Instead of the virtuous cycle intended by market reforms, internet and broadband markets were soon saturated due to the unaffordability of services. With only an elite in the public sector and a miniscule formal economy enjoying the benefits of digitalisation, the critical mass required for the improved information flows and efficiencies associated with economic growth were largely not realised. (Gillwald & Mothobi, 2019)

With the advent of new OTT services and applications such as social networking, operators lobbied regulators at the World Radio Conference (WRC) in 2012 (e.g., the GSMA and the European Telecommunication Network Organisation (ETNO)) to compel OTTs who ran their services on top of networks without having to bear any of the infrastructure investment costs to revenue share with network operators. While OTTs, in particular social networking, were driving demand for data and internet uptake and in many cases driving mobile operators' profitability (Gillwald et al., 2016), operators argued that they were unable to meet the demand with existing infrastructure – especially spectrum – creating congestion problems. This attempt to compel OTTs to revenue share was

unsuccessful as most of the super-profitable giant tech companies offering these services had no presence within countries and any effort to regulate or tax them was beyond the jurisdiction of countries.

The rollout of 4G spectrum agreed to at WRC a few years later took some of the focus off the issues raised by mobile operators, with dominant operators investing in dedicated high demand 'data spectrum' and, initially, late entrants in several countries successfully striking deals with social networking platforms to offer zero-rated services. Albeit briefly, they attracted new customers and grew their market share before dominant operators saw the success of the strategy and started offering similar services (Gillwald et al., 2016).

Operator appeals to their government for intervention backfired when the awareness by some governments of the growth of OTT revenues resulted in their taxation of social networking users through mobile operators rather than the social networks themselves. Mobile operators in some countries then became the victims of these taxes on social networks aimed both at raising revenues for bankrupt treasuries to make debt payments and political control, but which mobile operators had to collect, and which saw a decline in the demand for data (Gillwald, 2018).

In 2018, Uganda introduced a retrogressive excise tax on end-users of 200 Ugandan shillings (USD0.05) daily to use social media applications such as Facebook, Twitter, Instagram, WhatsApp and Skype (Policy, 2020). The tax requires a user to pay USD1.5 per month or USD18.00 per year for daily access to social media apps in addition to the ordinary cost of data. All mobile money transactions were subject to a 1% tax, but this was reviewed down to 0.5%. This approach to revenue generation spread to a number of African countries including Benin, where it faced such strong public resistance that it was abandoned within days of coming into force (Ahmed & Gillwald, 2020).

3. Problem Statement: E-Taxation

The devastation wreaked by the pandemic compounds the existing problems associated with taxation mobilisation as a core aspect of state formation and capability in many African countries, constraining the expansion of the revenue base essential for the reconstruction of a viable state and political stability. As Toye (2000) in Di John (2006) argued in the wake of the 2008 fiscal crises, it has become imperative for states in sub-Saharan Africa and Latin America to design tax systems that can provide incentives for growth. Tax systems also need to meet distributional demands and increase the revenue collection function that are central to a state's viability and effectiveness.

In the context of the digital economy, there is potential for significant resource mobilisation in Africa, but this opportunity brings with it the challenge of developing an effective taxation policy for digital services – the very nature of the problem being that they are global and cross-jurisdictional. Digital platforms such as Facebook, Amazon and Google are leveraging network effects to dominate online services markets even in developing country markets. In Africa alone, there are over 21 million people engaged in e-commerce, with Facebook having a user base of over 200 million (UNCTAD, 2018). The rise of the 'gig economy' in which tasks are fragmented to be completed piecemeal by remote workers enables platform intermediaries to evade the labour taxes that traditionally form the social security net for workers. By avoiding being regulated as employers, platform intermediaries avoid payment of

unemployment insurance, health insurance and occupational safety costs. Although not traditionally regarded as taxes, these levies on earnings are often paid to the state to underwrite social security measures. Shortfalls must therefore be made up in some other way.

Many African states with low levels of industrialisation and large informal sectors have not been able to raise significant taxes and, as a result, the levels of social protection and social investment are generally low. The growing problem of an increase in urbanisation and unemployment without sufficient industrial growth has been compounded by COVID-19 lockdowns and global economic stagnation and has placed more pressure on the state to provide additional social relief.

While Africa's digital economy is fledgling, it is projected to exceed USD300 billion by 2025 (Hope & Stuart, 2019). This phenomenon will largely be driven by mobile internet (second only to Asia-Pacific globally) and expanding internet penetration with a concomitant increase in data traffic (Bukht & Heeks, 2018). Within this purview, while the platform economy facilitates lower entry barriers to international markets by small businesses, it poses a novel risk of "skewed competition provoked by tax optimisation" (United Nations, 2019a) in an era of increasing data flows where data is considered a prized commodity.

At the same time, stringent digital tax policies as currently applied on end-users, rather than the global platforms, and as a result have the potential to lower affordability of online services as well as impede the fundamental human right of freedom of speech. The situation becomes more precarious with the dawn of the AfCFTA regime – where there is an expected significant drop in conventional physical trade tariffs as trade barriers ease across the region and e-commerce gradually becomes the rule not the exception, with few countries having the digital readiness to harness the benefits of a single market. This makes the assessment of the tax regulatory regime in the digital economy critical both in the short and long terms, taking into consideration the OECD BEPS proposals, and their potential and problems.

At the global level, developments both through the BEPS regime reforms and the e-commerce tax dimensions deliberated at the WTO present opportunities for resource mobilisation through minimum taxation rates for multinationals (including big tech corporations) and taxation on income at source of revenue generation, even when companies do not have physical presence in that jurisdiction. However, while WTO efforts to waive customs and excise duties on digital products (like the AfCFTA, potentially) threaten current sources of state revenues, the BEPS provides new opportunities for resource mobilisation.

At the other extreme, even if more rational, progressive taxation instruments are developed at the local level, guarantees are needed that resources mobilised through global co-operative and regulatory efforts will be directed toward social investment and protection, even more acutely required in the context of the pandemic. This guarantee can be uncertain in jurisdictions with poor state formation, and other systemic problems such as corruption.

Based on these digital taxation challenges and opportunities, the research questions for this paper follow below.

4. Research Questions

4.1. How might taxation of previously largely untaxed digital services contribute to state formation and stability under arguably harsher pandemic and post-pandemic conditions?

4.2. What forms do current unilateral approaches to digital taxation in Africa take?

a) What are the advantages and disadvantages of these unilateral approaches (which appear to be effective in meeting their stated objectives)?

b) How might some of the disadvantages of these approaches be addressed or mitigated through a progressive tax policy design that creates a fair distribution of value?

4.3 Can reforms to the global taxation regime, specifically BEPS, but also other forms of global co-operation, contribute to the taxation of hitherto untaxed global digital services?

4.4 How do international and domestics political settlements impact on creation of taxation systems that contribute to just social compacts?

5. Conceptual framework

This policy paper applies a political economy analysis and public goods framing of the internet to consider what a just fiscal compact might look like in the digital era. The concept of tax justice has gained traction in the wake of the 2008 global financial crisis as developed economies were confronted by their fiscal vulnerability to structural and cyclical crisis management. As Leaman and Waris (2013) explain: "Substantial budget deficits and growing accumulated sovereign debt alerted the 8G leaders and of other OECD countries to the fundamental problem of maintaining the supply of public goods over time against the background of increased military expenditure, stagnating or dwindling revenues and increased debt-serving costs". This raised concerns about the impact of corporate tax avoidance and taxation competition with tax havens on wealth creation and social equilibrium. These were practices that long preceded the crisis but, as Leaman and Waris (Leaman & Waris, 2013)(2013) point out, were tolerated because in the decades prior to the crisis they were generally used as "…vehicles for reducing state expenditure in the spirit of neoliberal roll-back programmes and debt reduction rather than as a problem to be examined from the revenue side" (2013).

This was fundamentally different for emerging and developing economies subject to the vagaries of developed economies and far harder hit by the 2008 crises. Leaman and Waris identify several factors that contribute to unjust tax systems. These include uneven integration into the global economy constrains domestic debate on taxation. Together with the dearth of social welfare processes, there is also little expectation or reliance on the state in most African countries, with many citizens more focused on survival than taxation. The inability of developing states to mobilise resources because of poorly constructed tax systems is also a factor. This is compounded by a lack of capacity and reliance on international agencies and banks and lobbying groups not concerned with issues of fairness and justice (and which Mustaq Khan and Di John would attribute to political settlements).

Leaman and Waris also highlight the fundamental interdependence of the global economy, the disadvantages facing poorer states with weaker institutions, and the impact of internationalisation on economic and financial activity and the global governance of these, including the management of corporate taxation arbitrage – the latter provoking the international calls for tax justice. They identify

the need for "interdisciplinary approaches to the multidimensional character of taxation…to account for the behavioural mechanisms involved in its practice and [the need] to develop half adequate prescriptive models for achieving social justice at national and international level" (2013).

This paper does not have the ambitions of proposing prescriptive models. However, it draws on the powerful conceptualisation of tax justice developed by Leaman and Waris to understand the tax implications for developing-countries of the increasingly integrated global economy because of the complex and dynamic processes of digitalisation and datafication. It takes a specifically African perspective, as part of a wider framework of the global governance of digital public goods.

The underlying political economy analysis examines power relations between states, regional blocs and big tech companies and, within states, between governments/regulators, markets and citizens. It considers how governments across Africa might harness the intensifying process of digitalisation and datafication to mobilise resources necessary for effective state formation through progressive e-taxation policy.

In this regard it draws on Di John's (2006) political economy framing of resource mobilisation as central to state formation, not only for economic development. He identifies the failure to place taxation as central to understanding state capacity and governance for the decline in the political economy of resource mobilisation as a focal point of development theory and policy:

> "… among various means of resource mobilization (e.g., forced savings, inflation tax, manipulation of terms of trade, etc.), tax is the most closely related to questions of state formation and capability. Tax also provides one of the principal lenses in measuring state capacity, power and political settlements in a society." (Di John, 2006)

This paper also draws on Kaul et al (2013), who extrapolate the concept of public goods from national to the global level. They identify the internet and knowledge (to which data and cybersecurity can be added) as dimensions of global public goods that require governance. Such global public goods emerge in response to the extent that all countries help produce them (i.e., create the conditions for private delivery of public goods such as the internet, for example, or comply with global agreements or consensus to ensure digital public goods such as cybersecurity are enforced).

Yet while the concept of states paying (either through budget allocations or licences) for national public goods such as free-to-air broadcasting or clean air is widely understood, it is less clear who should be held responsible for global digital goods that serve the common interest. While investment in global public goods has in the past few decades taken the form of official development assistance (ODA), Kaul et al (2013) appeal for new forms of international cooperation and institutions that will support the development of global public goods and ensure more equitable inclusion.

This paper applies this understanding of the need for effective governance of global public goods to the role of developing countries in digital governance. It uses the concept to track and explain the funding of overt technical assistance and the tacit lobbying of the various interests of multilateral agencies, global digital platforms, and industry associations to ensure the implementation of global frameworks at the regional and national level – particularly in relation to their potential for enforcing the legitimate taxation of revenues of global platforms that, without physical presence in countries, are unenforceable.

A political economy lens enables an assessment of the relationships that exist in the distribution of public goods with respect to the institutional structures within which they are embedded (Dencik, Jansen, & Metcalfe, 2018). Considering the increasing complexity of the global communications system, and the inability of traditional forms of international but particularly domestic governance to circumscribe the monopolistic behaviour by global corporations (Di John, 2006), this paper reviews existing and new forms of national regulation and international cooperation to manage the positive and negative implications of datafication and digitisation. Of particular interest is how alternative arrangements could facilitate the legitimate taxation of revenues obtained by global platforms without physical presence in specific countries of operation. This while creating domestic taxation conditions that recognise the downstream value of digital goods as public goods (or at least social or merit goods)[3] that are, more broadly, value creating rather than simply disruptive.

Frischmann's (2016) call for a balance between the exclusive supply-side, commercial valuation in the allocation of resources that has characterised the development of the global digital economy with demand-side valuation informs the analysis of the potential allocation of resources mobilised through global governance. This includes global digital taxes being used to offset regressive digital end-user tax revenues, or for social investment or protection.

The relational imperative between digital taxation and internet governance is critical as the former is a subset of the latter within the 'digital biosphere' and should in conventional circumstance align with the nature of network which is largely global (multilateral), rather than local (unilateral) (Cockfield, 2001).

6. Data collection and analysis

Within this broader political economy framing, a critical qualitative inquiry is adopted. Specifically, the approach entailed exploratory-inductive analysis and an interpretive critique of social inequities from the perspectives of multistakeholder actors (Korth, 2002; Denzin, 2017).

Within this approach, data collection relied on expert interviews (including Africa-focused tax policy experts and policymakers, as well as domain experts on the digital economy), and reviews of policy documents (study reports, policy papers, and policy briefs) for thematic discourse analysis and interpretation of the research questions in relation to the taxation of the digital economy in the African region. A summary of the interview responders is given in Annex 1, in alignment with their reference codes for anonymity. The interviewees were purposively selected based on their domain expertise and practical experience and engagement within the taxation and digital economy nexus in Africa. Responses to requests for interviews from countries that had come under fiscal pressure to pursue unilateral digital taxation came mainly from Nigeria and Kenya, with several governments refusing interviews based on them being in the processes of amending their regimes for purposes of taxing digital services or considering the implication of the BEPS. The continental tax administration association, the African Tax Administrations Forum (ATAF), proved helpful in reflecting these countries'

various positions on digital taxation. The interviews were conducted within a three-month period spanning January through July 2021.

7. Findings and discussion

7.1 Addressing the challenges of resource mobilisation: unilateral digital tax approaches

The impact of digitalisation on taxation is not a novel phenomenon; it has merely intensified existing problems associated with the ability to do business within a country without a physical presence, and therefore without the tax nexus of a permanent establishment. Unilateral approaches to digital taxation were spawned as a reaction to the decade-long delay in reaching any agreeable consensus on the multilateral negotiations primarily via the OECD BEPS process. Jurisdictions prioritised their unique interests, in particular in relation to hosting big tech companies (see Faulhaber, 2019). According to an interviewee involved in the current BEPS negotiations at the multilateral level, "a global consensus is going to take an incredibly long time, if not be completely impossible".

Traditionally, trade and indirect taxation has been harmonised globally, but not direct taxation – because this is a sovereign issue – which slows down multilateral negotiations. This challenge had been accentuated by a general lack of understanding both from a technical and a policy perspective of the digital economy and digitalisation in general for proposing alternate solutions. A number of respondents identified the reason for this as being that most countries, including developed ones, still did not have a full understanding of the kind of value being created and the revenues being generated within the continuously evolving digital economy.

In addition, the complexity of the multilateral negotiations, in particular the BEPS process, had in essence created a situation that requires the global digital platforms to carve themselves up first, fit into countries that they are active in, and then allocate profits to them, raising issues of its feasibility. This leads to transfer pricing difficulties and rules that even developed countries are finding difficult to deal with, let alone most of the developing world. Furthermore, the complexity of the current multilateral solution is exacerbated by the threshold proposals (e.g., the minimum sales tax of 750 million Euros that is proposed under BEPS Pillar 2) that is more likely to be useful for residence rather than outsource jurisdictions, which will mean that most African countries will then not be able to realise significant amounts of revenues in relation to the costs of their implementation.

To temporarily respond to this challenge, countries opted for digital services taxes (DSTs) as a means of appropriating location-specific rents within the digital economy (Turina, 2020). These responses began with India (where it was framed as an equalisation levy on digital transactions), followed by the UK, France, a few other European countries including Italy, and Israel. DSTs are presumptive taxes designed as something between the traditional corporate tax and an indirect sales tax, as basically the taxable nexus was still not fully understood by tax authorities with the evolving avalanche of new digital business structures, products and services.

Africa countries were slow to respond to the emerging challenges of digital taxation. However, this began to change as governments realised the potential of taxing digital services, and started moving unilaterally, cognisant that achieving global consensus was a slow process. These unilateral measures were felt to be even more necessary given that even with the multilateral BEPS process there were

emerging indications that developing country jurisdictions, and in particular Africa, would not really benefit from the proposals when compared to the level of tax avoidance that developing countries have been confronted with. This was because the extra tax revenues accruable to African countries would be modest in contrast to the cost and complexity of implementing the proposals (scoping, profit reallocation and distribution), which were designed mostly with advanced economies in mind. In this respect, even though these multilateral engagements were framed as being 'pro-developing countries', lobbying was strongest from countries in the Global North.

Although the emerging unilateral approaches across the world were implemented by individual countries, they were mostly designed from within the principles engaged in the multilateral processes and coordinated at the regional levels. In Africa, while there has been relatively less coordination at the regional level (with the ATAF only contributing to global debates on digital taxation in the past few years), the trend towards unilateral tax was catalysed by the increasing pressure to raise revenues given the low tax-to-GDP ratios of most countries (Kenya and Nigeria for example), and in some cases by the socio-political desire to restrict public access to digital platforms and social media (as in this case of Uganda and Tanzania). However regionally there was never really consensus with respect to the emerging digital taxation challenges, especially considering the varying economic conditions and technological developments within the economic blocs on the continent.

As summarised from interviewee responses, there are three main unilateral approaches (some proposed, some already being implemented) to taxing the digital economy across the continent:

a) ***Significant Economic Presence (SEP)*:** in this approach, the taxable nexus for a digitalised business (with or without a permanent establishment status) is determined by three factors: revenue, local digital presence, and user-base. Profits are attributed based on thresholds indicated in extant rules and legislation, fractional apportionment or modified presumptive profit methods (Sokolovska & Belozyorov, 2019). Nigeria is a good example of a country adopting this approach.
b) ***Alternative Minimum Corporate Tax (AMCT)*:** in this approach, the taxable nexus is based on the gross revenues (turnover) of the digitalised business (Durst, 2018). While this approach is not based on any multilateral process, its simplicity for overcoming base erosion via profit shifting makes its adoption feasible for a good number of countries with less developed tax systems including Cameroon, Democratic Republic of the Congo, Côte d'Ivoire, Equatorial Guinea, Gabon, Guinea, Madagascar, Mauritania, Senegal and Tanzania.
c) ***Formulary apportionment unitary taxation*:** in this approach, the taxable nexus is determined by a unilateral formula apportioning the taxable base (share of global profits) of all the entities of a corporate group within a jurisdiction, based on assets, labour and sales (Picciotto, 2016). This approach has been considered for South Africa (Cobham & Loretz, 2014; Gupta, 2018).

Advantages of unilateral approaches

A key advantage of these unilateral approaches to digital taxation in Africa is that it can serve as a temporary gateway and starting point to better grasp the digital economy and its implications for taxation, at least with respect to company reporting protocols instituted within the regimes. Without this gateway, there is no formal access to the operations of foreign-based digital companies within the economy. This is because these companies ordinarily have no legal obligation to disclose this

information within these jurisdictions. It becomes almost impossible under these circumstances to assess the level of economic penetration by these companies in relation to the size of the value being created and captured within the countries, as well as to get a sense of the emerging income classifications with respect to high, mid and low earners within the digital economy for longer-term fiscal planning.

Disadvantages of unilateral approaches

A significant disadvantage of the unilateral approaches in Africa is the risk of a global impasse and backlash, as they risk impeding bilateral trade negotiations. More so, as the unilateral taxes that are emerging are not necessarily direct taxes, but more of an evolving combination of direct taxes, tariffs, and indirect sales taxes, they cannot be governed only by direct tax regimes that are emerging internationally.

Unilateral measures being adopted also currently target only a very small proportion of the population in the region who operate a formal digital business. This means that they will most likely not generate any massive socio-economic outcomes for the continent, with potentially several unintended consequences such as quashing nascent local startups or digital businesses already in an unequal struggle with big tech companies.

Although the continent has made significant progress in upscaling mobile connectivity, it however still lags other regions globally in access to the internet. According to the World Bank,[4] less than 30% of Africa's population have access to both the internet and reliable electricity – fundamental infrastructures for the digital economy – and which has resulted in a low digital ID penetration. This has slowed the adoption of digital technologies by the mostly informal businesses operating in the region.

Therefore, the focus on regressive taxes for digital services is demonstrably misguided for African countries,[5] especially with the reality of more economically viable sectors for the region, such as the extractive industries and commodities market (even if they are transacted via digital channels), and the potential for the taxation of super profitable giant global tech companies through the reforms to the international tax regime, that should be considered priority areas.

In addition, some of the unilateral tax measures are being used as political instruments by governments to deal with political dissent. In particular, the digital service taxes that focus on social media activity or web downloads impinge on the rights of citizens to access information, as well limiting technological innovation within these domains. More so given that technological innovation and the digital economy requires often young people to be online almost all the time and require vast amounts of information (which are mostly online) for their work or businesses, especially those operating in the gig economy.

This negative impact becomes even more significant in the COVID-19 era with the virtualisation of most social services, including education and health information. In this regard, unilateral digital taxes have

[4] Digital Economy for Africa Initiative TICAD Seminar Series: DE4A initiative - June 24, 2019. Every African Individual Business and Government to be Digitally Enabled by 2030. http://pubdocs.worldbank.org/en/312571561424182864/062519-digital-economy-from-africa-initiative-Tim-Kelly.pdf

5 See Stork & Esselaar, (2018) ICT Sector Taxes in Uganda: Unleash, not squeeze, the ICT sector, Research ICT Solutions, https://researchictsolutions.com/home/wp-content/uploads/2019/01/Unleash-not-squeeze-the-ICT-sector-in-Uganda.pdf

the potential to alienate those marginalised from digital services further, rather than focusing on levelling the playing field for the digital economy so that everyone is paying their fair share of taxes.[6]

7.2 Digital tax policy design for a fair distribution of global value

There are two fundamental issues in designing a tax policy. The first is defining the taxable nexus (threshold for tax purposes), while the second, and even more complicated question, is defining the tax base (the portion of taxable income generated within a jurisdiction) and the consequent profits allocation within any particular jurisdiction. While the taxation debate has assumed a global commons vs fiscal sovereignty framing those countries are familiar with, multilateral tax policy demands that each country receives an equitable share of tax revenues from cross-border transactions between source and residence jurisdictions (OECD, 2001).

Within the ambits of an equitable value distribution with reference to developing economies, a revenue threshold that is based on the size of customer payments within the country to a non-resident provider of services – whether they are digitalised or not – is the most effective and easiest to apply in determining the taxable nexus. The BEPS Pillar One[7] have developed an approach based on sourcing rules for determining the tax base, which incorporates a methodology for attributing profits from sales where appropriate to users. However, this approach will not be equitable for developing economies such as those found in African countries without an optimised formulary apportionment (using the three-factor components – sales, physical assets, and people or employees) for resolving the issue of allocating what are essentially global profits according to the activities of the global firms in each country.

This optimised approach can be achieved by expanding on the profits-split methodology used in the transfer pricing framework that the OECD and G20 have put forward. While the current BEPS proposals have unfairly focused on the residual profit-split (which first applies the transfer pricing methods to define a routine profit from so-called routine activities, and then only splits the so-called residual profits), there also needs to be an incorporation of the contribution profit split for a fairer assessment, which looks at the contribution of all the firm entities concerned. Moreover, even within the residual profits, there needs to be an expansion of the businesses in scope, and crucially for African and developing countries in general, the inclusion of business-to-business (B2B) services – a significant segment for profit shifting especially in developing regions for the past several decades.

There also needs to be an objective measure for an expansion of the data provisions within the OECD Pillar One value calculations, as they fully discount machine-generated data. This is a significant component of the data value chain that is growing exponentially and is used by digital companies in creating same and cross-side network effects through the algorithms that they build. This consideration is an imperative with regards to an optimal determination of the tax base for developing countries

[6] See Ahmed S and Gillwald A (2020) Multifaceted challenges of Digital Taxation, https://researchictafrica.net/publication/multifaceted-challenges-of-digital-taxation-in-africa/

[7] https://www.oecd.org/tax/beps/tax-challenges-arising-from-digitalisation-report-on-pillar-one-blueprint.pdf

where user-generated data (in relation to internet penetration) is relatively low, which means lower tax revenues will be generated.

7.3 Required technical and policy support for effective implementation

Several people interviewed contend that to build out the required dynamics for implementing these digital tax proposals in Africa, a robust tax research system is required. This process is imperative for developing Africa-led alternatives to processes that are largely driven by developed countries, and that take into greater consideration the contextual conditions in the region to bridge the knowledge gaps. In congruence with this perspective and given the limited understanding of the enormous value resident within the continuously evolving digital economy, there is need for holistic and multi-disciplinary research standing committees at the regional level (especially at the African Union level, because the technology challenges affect all African countries). Their mandate should encompass assessing the technical aspects of the digital economy, in collaboration with regulatory and policy experts at the national level, in framing model legislations periodically, as well as determining contextual tweaks for local implementation. Outputs will then need to be coalesced for the adoption and use by tax administration agencies, with revenue experts assessing how all of these will come down to tax implementation for revenue collection and fair re-distribution. However, propositions for enhancing capacity must be country-tailored, considering unique levels of development of each country's digital economy. This will first require in-country studies to assess their corresponding priority areas within the digital economy as they relate to taxation for tailor-made propositions to be developed, otherwise recommendations might become impractical.

In the same vein, capacity development efforts in Africa with respect to digital taxation should leverage more South-South rather than the current North-South cooperation model if the existing problems for the region, as espoused within the BEPS process, are to be effectively addressed. Global North countries developed their expertise and are wedded to tax principles favourable for capital-exporting countries. As an alternative, African countries should engage more with countries from the South who have a different perspective, particularly India and Brazil (key countries for Africa), some others in Latin America, such as Argentina, as well as China – countries outside the OECD orbit that have advanced their taxation of the digital economy.

Another consistent challenge in any taxation system beyond even the digital economy will be the level of transparency that will be required to implement any propositions. Information on elements such as user bases, IP addresses connecting through platforms, the location of digital infrastructures etc. will require a higher level of transparency than currently obtains across the continent. The current country-by-country reporting espoused in BEPS Action 13 for global digital platforms with respect to jurisdictional locations – such as number of employees, revenue generation, infrastructure expenses, signatures behind programme codes (who contributed to the creation of these codes that yield the value for the companies, and where they were when doing this) – are consolidated at a level that tax authorities in African countries cannot use to determine the taxable nexus and corresponding tax base.

Bridging these transparency deficits will require a significant amount of goodwill on the part of the global digital platforms themselves. This is not likely in the short term, giving the unwillingness to engage more transparently with the current European push back against platform power. This situation

will require regulations or some other forms of compulsion at the global governance level. The huge gaps in intra-country tax transparency will also need to be improved, considering the deficits in tax information exchange in Africa as indicated in the Africa Initiative Progress Report (2019).[8] The bridging of this transparency deficit will be fundamental for best practice exchange between countries, peer review, and cross-agency fiscal intelligence cooperation, considering the differences in the levels of tax systems capacity across the continent.

The WTO negotiations on e-commerce have through its moratorium resulted in huge revenue losses to developing countries via the restriction of the flexibility to regulate the import of digital services. It is time to start considering the lifting of this moratorium, which the Africa cohort within the WTO are in favour of doing. This issue, as well as the data residency debates on the jurisdictional location of some of the data flowing across the digital platforms, will most likely become hot policy buttons at the WTO. This is expected to be more so with the change in the WTO leadership, with the organisation now headed by an African. Current arguments led by developed countries for not enforcing data localisation conditions on digital companies or even disclosing the coding parameters of their software so that where they were developed cannot be easily traced will restrict the level of transparency that will be required to implement some of the digital tax propositions here. This of course will be discriminatory against developing countries, especially in Africa.

At the regional level, while the AfCFTA does not specify any tax proposition with respect to e-commerce, the implications of the WTO moratorium will need to be brought into perspective as the agreement's implementation takes full throttle. The AfCFTA represents an opportunity for tax harmonisation on the continent, but this may not necessarily be for every form of tax. Here it will be important to assess how African countries are leveraging the new tax opportunities by way of introducing regulations and legislation that would at least capture some of those proceeds that were previously not being taken advantage of. For example, there are taxes that will be relevant for trade to occur – VAT, corporate income tax, and personal income tax – but which are mostly domestic taxes that fall outside of the international tax regime. This is particularly the case with consumption taxes such as VAT that has been a consistently strong performer for the continent, with a collection rate of around 30% in the region. Stabilising country VAT systems will be critical in mobilising revenues for the continent in the digital economy, but will fundamentally require updates on interest deductibility laws, permanent establishment (PE) laws, transfer pricing laws, and the simplification of vendor registration for MNEs operating within the continent's jurisdiction, as a means of ensuring business continuity and shored-up revenue collection. This intervention is critical for Africa because if the tax harmonisation issue within the AfCFTA is not resolved tax risks becoming a non-tariff barrier (Ezenagu, 2019).

Digital service taxes are however not ideal from the perspective of good tax design principles, as it is quite likely that the cost of implementation will be passed on to consumers or users. For a continent where the average age is 19 years,[9] and where most people are unemployed or in the informal sector,

[8] Global Forum on Transparency and Exchange of Information for Tax Purposes. Tax Transparency in Africa 2020. Africa Initiative Progress Report 2019. https://www.oecd.org/tax/transparency/documents/Tax-Transparency-in-Africa-2020.pdf

[9] https://www.worldometers.info/world-population/africa-population/#:~:text=The%20median%20age%20in%20Africa%20is%2019.7years.

the regressive nature of indirect taxes are not a good starting place for taxing the digital economy. This is likely to have a more distortive and less progressive impact in general than a direct tax on profits would have and as mentioned at the start of this paper, regressive taxes have a negative impact on both innovation and political freedoms. The focus should therefore rather be on taxing income generated within digital spaces, which should be the most important basis for taxation, even if this is not immediately achievable.

7. Conclusion

This paper began by highlighting the importance of digital taxation for resource mobilisation in African states – this within the context of global economic restructuring that is necessary to right the economic distortions that have emerged between countries, and that have been exacerbated by the Covid-19 pandemic. It assesses policy options, current and potential, for expanding the tax base for optimal state formation, more important than ever in Africa, on the context of the pandemic and the post-COVID-19 economic and social reconstruction. It has examined some of the effects of unilateral taxes on digital services and transnational global platforms, and how this impacts the development of the digital economy in Africa.

Drawing on a series of interviews with global and regional stakeholders, and with a particular emphasis on Nigeria – which was one of the first countries to impose unilateral digital taxes – it outlined the three main kinds of unilateral taxes (implemented or potentially applicable), as well as the advantages and disadvantages a unilateral approach to taxation. In particular, it draws attention to the problems of digital services taxes as a regressive tax and the likely negative consequences of this on economic growth, digital innovation, and political freedoms. In its analysis of the two main global frameworks impacting on digital taxation – the WTO e-commerce negotiations, and the BEPS initiative – it pointed out that although the BEPS project aims to address the problem of taxing the digital services of MNEs even when they do not have a physical presence in a country, like the WTO negotiations, African states do not have sufficient negotiating power to influence the process. Therefore, the implications for these processes on local businesses, entrepreneurs and innovation is largely out of their control.

Nevertheless, this paper promotes the view that although African voices have been absent from the BEPS process it does provide an opportunity for African states to access the super profits of big tech companies for resource mobilisation. It should therefore be more vigorously engaged with by states as a bloc to offset the tendency to impose regressive digital taxes, such as on social network users.

Several interviewees argue that a key challenge for African states is that direct taxes on income for digital services, particularly as they relate to MNEs, are not yet viable as a fiscal mechanism for African states. Besides the reluctance of countries to concede to new rules that would adequately allow African countries to tax global digital companies on a basis of multilateral or bilateral cooperation, there is the practicality of administration. Even prior to the digitisation era, it was difficult for African countries to tax MNEs. However, while African countries engage continental and internationally on how best to implement taxes within the digital economy, interviewees emphasised the importance of gathering and collecting reliable data with respect to the digital economy. This should serve as a base for developing fiscal policies based on these data within a process that is transparent and more likely agreeable to stakeholders.

While the BEPS initiative is an appropriate process for engagement for African states at the global level, at the regional level, coordinating a common tax regime will be difficult to achieve in contrast to trade tariffs harmonisation. Interviewees argue that the latter is much easier to control through leveraging the several customs unions and free trade areas – from the Economic Community of West African States (ECOWAS) to the Southern African Development Community (SADC) to the East African Community (EAC) – and that it has been easier to reach consensus on trade tariff harmonisation between African states. Therefore, instead of creating binding directives at the regional level on a common digital tax regime, there could be good practices or conducts (norms) as a guide for individual countries to follow as has been effectively implemented in the European Union (EU) as a single market. This would also need to take into account the different levels of development and therefore the taxation priorities of the different countries. This will require close collaboration and synergies between the relevant regional institutions on the continent, including the economic blocs, the AfCFTA and the ATAF secretariats, in the evolution of a policy process that allows African countries to debate these issues between themselves without fragmentation, and as a first chance of effectively negotiating their way out of the current North-South hegemony.

The potential of global governance to realise digital public goods at the national level will require African states to participate more actively in global initiatives that will compel multinationals, especially super-profitable technology corporations and global platforms, to pay taxes in the country of revenue generation. This while ensuring domestic taxation environments arise from more progressive fiscal and social contracts that distribute these revenues in ways that produce equitable and just social and economic outcomes.

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8. Acronyms

AfCFTA: African Continental Free Trade Agreement

ATAF: African Tax Administration Forum

AU: African Union

CIT: Companies Income Tax

EU: European Union

OECD: Organisation for Economic Co-operation and Development

PIT: Personal Income Tax

VAT: Value Added Tax

WRC: World Radio Conference

WTO: World Trade Organisation

Annex 1: Interview Respondents Profile

Interviewee code	Designation	Gender	Country/Institution
1	Digital Economy Consultant	Male	Nigeria
2	Telecommunications Operator	Male	Nigeria
3	International Regional Tax Officer	Male	Continental (ATAF)
4	Tax Consultant	Female	Nigeria
5	Technology Expert	Male	Nigeria
6	Professor of Taxation & Development	Female	Kenya
7	Developing Economy Taxation Research Lead	Female	Kenya
8	Assistant Professor of Tax Law	Male	Nigeria
9	Emeritus Professor of Tax Law	Male	Britain (Lancaster University, UK)
10	Global Trade Expert	Female	Belgium
11	PhD candidate in international corporate income tax	Male	Denmark | Copenhagen Business School (CBS)
12	Research Fellow at the Institute of Development Studies	Male	UK (ICTD)
13	Tax Researcher	Male	Nigeria
14	Tax Consultant	Male	Nigeria