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HOW TO TAX THE SHARING ECONOMY

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Abstract - The sharing economy refers to online market places that bring sellers and buyers of goods and services together. The sharing economy is rarely taxed, rarely reported to and rarely controlled by the Tax Authorities. In this paper two main problems concerning taxing the sharing economy are identified. Firstly, the sharing economy is difficult to control, since there are many small providers. Secondly, different tax treatment for businesses and private individuals makes it difficult for small providers to know how to comply with tax obligations. The solution is not the introduction of a digital services tax (DST) imposed on the intermediary platforms. Such a tax can contribute to tax the sharing economy, but not replace income tax or VAT/GST. Income tax and VAT/GST systems throughout the world are based on a scenario of businesspeople versus private individuals dating from the 20th century, which is now out of date. A solution could be to tax business persons and private individuals in a uniform way, which would provide a simpler tax system that would be easier to comply with.

Keywords - Sharing Economy, Peer-To-Peer Economy, Taxation, Tax Law, Intermediary Platforms, Gig Economy, Circular Economy.

I. INTRODUCTION

The sharing economy refers to online market places that bring sellers and buyers of goods and services together. It is also known as the collaborative economy, gig economy, circular economy, on-demand economy, platform economy or peer-to-peer (P2P) economy. It is a system in which people share assets or services for free or for a fee by means of the internet. The market places for P2P exchanges of services are specialised, such as in the short-term rental of housing or office spaces, transportation services for short trips in passenger vehicles and the lending of tools and other items. The sharing economy is said to be rarely reported to and rarely controlled by the Tax Authorities and for obvious reasons even more rarely taxed.

The aim of this paper is to identify the fundamental problems in taxing the sharing economy and to discuss whether a digital services tax (DST) provides a solution to these problems. There are many different definitions of the sharing economy. There is a broad definition, suggested by the campaigning group “The People Who Share” which defines the sharing economy as a socio-economic ecosystem built around the sharing of human and physical resources. There is also a narrow definition, which only includes consumer-to-consumer (C2C) transactions, and not business-to-consumer (B2C) transactions. According to the narrow definition, the sharing economy should be understood to only include transactions where consumers provide temporary access to goods, not the permanent transfer of ownership of the goods. Furthermore, it should only include transactions regarding physical assets. In this paper, traditional B2B or B2C transactions are not in focus, but the scope is not as narrow as the narrow definition. One important tax issue is however, that active participants in the sharing economy, sometimes unknowingly, become businesspersons for tax purposes. The line between the personal and the professional spheres is not always easy to draw. Therefore, the traditional separation between B2C and C2C is complicated when you look at the sharing economy from a tax perspective.

The subject of this paper is tax law. As in most legal research, the point of departure is the legal dogmatic method. The legal dogmatic approach includes studies of law as such, without considering it in economics, politics, ethics and other social sciences. What is studied when this method is applied is law in its pure form, namely concepts, structure, models and legal technique. National laws from different countries of the world are however not analyzed in this paper. National primary sources such as case law, written law from legislative bodies and binding rulings from administrative bodies are not dealt with at all. The methodological focus in this paper is rather prospective and problem-oriented. Identifying problems and proposing suggestions for solutions of these problems is what is mainly done in this paper. The over-all method of this paper is therefore a legal scientific research method in a wider sense than legal dogmatic, including also policy discussions.

The paper proceeds as follows. First, an introduction to the sharing economy is provided. Thereafter, tax issues in the sharing economy are identified. After that the proposed and now also abandoned EU DST is dealt with, followed by a discussion on whether taxing intermediary web platforms provides a solution to the tax issues. The paper ends with my concluding remarks.

II. THE SHARING ECONOMY

The use of the internet is growing steadily. In March 2019, 56.8% of the world’s population had access to the internet. There are still differences between different parts of the world. Internet use is distributed
as follows: Africa 37.3 %, Asia 51.8 %, Europe 86.8 %, Latin America/Caribbean 67.5 %, Middle East 67.2 %, North America 89.4 % and Oceania 68.4 %.

The widespread access to the internet has enabled people to exchange goods and services easily and efficiently over internet platforms for a relatively low service fee. People earn money on their un-used capacity in assets they own, for example, by letting their flat out to tourists or by renting out their tools. They may spend their spare time cooking meals, driving people around, driving rubbish to the rubbish dump, babysitting or mowing the lawn for other people, and they may lend their spare money to people who need it to set up a company. What was for some originally an extra income has developed into their main source of income and a successful business.

Two main types of businesses can be identified in the sharing economy – labour platforms and capital platforms. Labour platforms connect customers with workforce. Capital platforms link customers with people who are willing to rent or barter their assets. There is nothing new about sharing goods and services. This is something friends, neighbours and family have always done, and it has also been enabled through advertisements in traditional media and on billboards etc. What a wide use of the internet and the digital economy provides is a fast and easy way for people who were previously strangers to meet as suppliers and customers of goods or services. There are also other drivers to the sharing economy, such as the value of being eco-friendly by using the world’s limited natural resources efficiently. The online rating of providers in the sharing economy is an important factor for trust in the sharing economy.

According to the Nielsen Global Share Community Report, more than two thirds (68 %) of the global respondents were willing to share or rent out their personal assets for financial gain. Two thirds (66 %) of the global respondents claimed that they were willing to share and rent out products and services to others in a sharing community. Respondents from Asia-Pacific were most willing to share and rent out personal goods of their own and others. The findings in the survey were based on respondents with online access in 60 countries. Hence, non-internet users were not included in the study.

The forecast is that the sharing economy will continue to grow. In 2014, PwC estimated that the global revenue generated by five key sectors of the sharing economy was approximately $ 13 billion in 2013 and it was expected to grow to $ 335 billion by 2025. Another study, carried out for the European Parliament in 2016, estimated the potential future value of annual consumption in Europe relating to the sharing economy at $ 572 billion. Taxing the revenues of the sharing economy is therefore an issue that is becoming increasingly important.

### III. TAX ISSUES IN THE SHARING ECONOMY

3.1. Mapping out the tax issues

The general sharing business model in the sharing economy consists of three parties. The provider, the intermediary platform and the user. The provider supplies goods and services, the intermediary platform connects the providers with the users, and the user consumes the goods or services. The intermediary platform normally charges a fee for its services from the provider.

Understanding tax laws in relation to the sharing economy is normally not a difficult operation. The provider either acts as a private individual or as a businessperson, depending on how active the provider is in supplying goods or services. Many tax systems differentiate between the taxation of private individuals and the taxation of businesspersons.

Under income tax law, businesspersons may be taxed at a different tax rate, have other opportunities to deduct costs and apply different allocation rules for their income and deductions. Furthermore, they are normally liable to charge a sales or use tax, such as value added tax (VAT) or general sales tax (GST). If the provider acts as a private individual, there may be certain thresholds, under which the income is tax-free. Private individuals are normally not liable to charge VAT or GST on their sales. If the private individual is not independent from the intermediary platform, the tax status of the individual may be one of an employee rather than an independent operator.

The intermediary platforms are normally held by legal persons, but can also be held by individuals. Since the activities carried out by the intermediary platform are in general not incidental but an ongoing activity for which consideration is charged, the income earned is normally business income. The goods or services may be exempt from VAT/GST depending on the kind of goods or services supplied.
The owners of the platforms are normally subject to unlimited tax liability in the jurisdiction they belong to, and their income is hence taxable there. Thus, what is so difficult about taxing the sharing economy? In my view, there are two basic problems:
1. The sharing economy is difficult to control
2. Businesses and private individuals are normally treated differently for tax purposes

3.2. Problems with control
The sharing economy happens both in real life, where the goods and services are actually carried out, and on the internet, which is the meeting place for providers and users. The digital economy as such is difficult to control for many reasons. If the intermediary platform were to provide its services offline, the business would require more staff. In that scenario, the services carried out automatically by the platform would have to be carried out by employees. This would also create a need for a greater physical presence, i.e. staff would work and meet the customers. When the services are provided over the internet, the need for a physical presence is much smaller. The physical presence can be more decentralized, in other words IT services can be acquired from one place while the people actually running the business are in another place and so on. A business that is not dependent on a certain location can also easily be placed in a jurisdiction where the laws and the business climate are favourable.

When the sharing economy does not only replace traditional P2P trade but also takes market shares from traditional business activities, such as for example taxis, hotels, banks, car rentals and restaurants, and also creates new business lines, the structure of the sector changes. In the sharing economy, the intermediary platform simply connects providers and users. Those that actually supply the goods and services are the providers, and there are normally many of them. The number of providers creates certain control issues. When the Tax Authorities wishes to audit a hotel chain, it has one major company, or a group of companies, to audit. If the Tax Authorities would like to audit, for example, the business that is coordinated by Airbnb or a similar actor, it would have to audit all the providers, which will mostly be individuals, but may also be legal entities. Above all, they will be small entities and many of them, and hence resource-consuming. It may also be the case that the Tax Authorities would not normally audit such small taxpayers in such a large scale.

In addition, the intermediary platform may be located in a jurisdiction where it is not easy to obtain access to information about the providers, through, for example, third-party audits. Both the fact that the intermediary platforms are internet-based and the fact that the providers are many in number as well as small creates problems with control.

From a control perspective, there are also advantages with the sharing economy. Since the intermediary platforms are on the internet, the payments and the communication between the parties leave traces. The possibilities to pay the intermediary platforms using cash are limited. Hence, it is technically possible to track the trade carried out via the platform. States can also impose obligations on platform owners to report data on their users to the Tax Authorities.

In order to find the providers, an obligation for the platforms companies to report the earnings of the respective users could be imposed. Then the tax agencies would get knowledge about the single taxpayers’ income from the sharing economy without auditing. This information could also be exchanged internationally.

An interesting solution is the so called full VAT/GST liability regime proposed by the OECD not for the sharing economy but for e-commerce with small value goods. Under this regime, the intermediary platforms are required to register in the jurisdiction of taxation and declare and remit the VAT/GST there in accordance with applicable rules in the jurisdiction. Using the intermediary platforms not only to report but also to remit the VAT could be a simple and efficient way to tax the sharing economy.

3.3. Differences between the taxation of businesses and the taxation of individuals
One reason why the sharing economy is rarely reported may be that in many tax systems there is a fundamental difference between acting as a businessperson or as a private individual. This can be seen in double tax treaties, such as the OECD Model Tax Convention on Income and Capital where business profits is taxed in accordance with article 7 whereas income from employment is taxed under article 15 and other income under article 21.

In order to become a businessperson for tax purposes, you normally have to register as such both for income tax and VAT/GST purposes. Furthermore, you have to have accounts for your business. Running a business instead of acting as a private individual is more burdensome as regards the administration, since there are more rules and obligations to comply with. There are, however, also advantages in acting as a business rather than as a private individual, such as the fact that you may deduct input VAT/GST and normally have greater possibilities to deduct costs for income tax purposes.

The sharing economy attracts many people who were previously not in business, and are now small business operators. If you are un-employed, entering into the sharing economy can be a source of income, without need for any major capital investments. For many, taking the plunge and starting a business instead of acting as a private individual is just too big a step to take. It is also possible that many providers, even when they are very active in the sharing economy, do not perceive themselves as...
businesspeople, even if they obviously belong to that category under existing tax laws.

IV. THE EUROPEAN UNION DIGITAL SERVICES TAX – IS TAXING THE INTERMEDIARY INTERNET PLATFORMS A SOLUTION?

In 2018, the European Commission developed a proposal for an EU-wide provisional tax on certain income from digital activities called the digital services tax, or the DST. The substantial tax rules regarding the intermediaries work well, as long as the platform company either is registered or has a physical presence in the state where the actual use takes place. This is however not always the case. The EU Commission has tried to readdress this problem by proposing a digital services tax.

The DST was proposed to be levied as from 1 January 2020 and would apply to income deriving from digital intermediary activities through which users can come into contact with each other or sell goods and services to each other. It was proposed that the tax rate would be set at 3 per cent of the gross income. The tax should have been collected by the Member States where the users were located and only from companies with annual revenues of at least 750 million euros worldwide and at least 50 million euros within the EU.

This proposal was abandoned by the EU in March 2019. Some Member States were in favour of the DST and have even already introduced one at a national level. It was, however, not possible to reach a unanimous decision among the Member States. The main criticism was that an effort only at the EU level would not solve the problem of taxing the sharing economy. It might instead be counterproductive, in that the tax would only apply within the EU. The view was that it would be better to deal with the issue at the global level.

The DST was also criticised because it only included major players from the sharing economy. This meant that there would be a strong incentive to stay below the threshold. Since small startups were to be exempt, consolidations that would get them into the digital services tax system would have been discouraged. Another objection to the tax was that it would be imposed on gross income, irrespective of whether the platform suppliers were profitable or not. A tax that does not take the ability to pay tax into consideration may harm companies that are not yet profitable.

The fact that the EU will not proceed with the proposal does not mean that the idea of a DST has been abandoned. The OECD has expressed the intention of proceeding with a global initiative. Also the G20 is pushing ahead with plans to close international loopholes used by tech giants to lower their tax bills through a digital tax. Even if there were a more or less global DST without such a high threshold for taxability, a relevant question to ask would still be whether a DST really is the best way to tax the sharing economy.

Imposing tax on the digital platform has the advantage of ensuring that the sharing economy contributes to the financing of the public sector to a greater extent than before. It does not, however, solve the problems described above, namely the control problems and the differences in taxation between businesses and private individuals. It is unlikely that the imposition of a DST on the platform providers would lead to the providers of goods and services not being taxed for their revenues. Not taxing revenue only because the goods and services that the revenue stems from were supplied over an intermediary platform would cause severe problems, because all providers of goods and services would have a strong tax incentive to trade their products over the internet. Hence, the providers of goods and services would still be subject to income tax and, if applicable, also VAT/GST.

If many people who are liable to pay tax escape tax due to control problems, there is a risk that the general trust in the tax system will decrease. This is harmful, since there are only two ways to make people pay their taxes, namely trust and control, and no tax authority in the world can control every potentially taxable entity. It is therefore important that the tax due can also be collected efficiently. To achieve this the obstacles to paying the right amount of tax should therefore be reduced as much as possible. If a tax system is based on differentiating between businesspeople and private individuals, something that is not relevant in the sharing economy, it will be difficult for an individual to even know that he or she has suddenly become a businessperson for tax purposes. Moreover, if there are too many hurdles in the form of registration etc. to overcome in order to be able to become a businessperson for tax purposes, when the person has understood and accepted that he or she actually is one, that person might still not comply with the rules. Together with the fact that small taxpayers are seldom controlled, what is achieved is a parallel tax system, where the sharing economy is not taxed or where it is taxed but not as competing businesses are taxed. Therefore, changes in the substantial tax laws as well as in tax procedural law are needed to tax the sharing economy in an efficient and neutral way.

There is another issue with imposing a tax on a certain business line. Excise duties are imposed on certain categories of goods and services. The objective of excise duties, however, is to steer people’s behaviour, in order to make them refrain from buying items subject to excise duties. This does not prevent excise duties from also being efficient sources of income for the state. If the intention is not to steer the trade away from the intermediary digital platforms, it might be worth being cautious when burdening them with another tax.
V. FINAL ANALYSIS

Taxing the sharing economy is not easy. A digital service tax may contribute to taxing the sharing economy. It cannot, however, replace income tax or VAT/GST on the supplies of goods and services. Replacing other taxes would make tax avoidance very attractive. Already in 1998, when e-commerce was emerging on a broad front, the OECD concluded that the taxation principles which guide governments in relation to conventional commerce should also guide them in relation to electronic commerce. Already at that time, in the so-called post-Ottawa Agenda, a concrete substantive step in order to tax e-commerce accurately was identified as developing an international consensus on ways to simplify taxation systems to minimise the cost of tax compliance.

In order to achieve a more efficient taxation of the sharing economy, the most important thing would most probably be to simplify compliance for taxpayers. If it is easy to comply with the system, the likelihood that taxpayers actually do comply will be greater. It is probable that the traditional difference in taxation between businesses and private individuals is not relevant in the sharing economy. Therefore, it may be time for tax reforms to be introduced in countries where Income Tax Acts are not based on presumptions concerning the economy and society that stem from the beginning or middle of the 20th century. People are neither employees/workers nor businesses anymore. This is not unique for the sharing economy, but the majority of sharing economy providers use online platforms to supplement wages or otherwise earn a part-time income, which makes their tax status more difficult to define. The best way would probably be to tax private individuals and businesses in a similar way.

The VAT/GST raises other issues, since private individuals bear the burden of the tax and they are not taxable entities. This does not, however, prevent every individual from being a taxable entity for VAT/GST purposes, but not always acting as such. In that case, there would not be any obstacles to begin charging VAT/GST on supplies over a certain threshold.

To sum up, a DST helps to tax the sharing economy, but if the tax is not truly global, it may also lead to tax competition. Income tax and VAT/GST systems throughout the world are based on a scenario of businesses and private individuals dating from the 20th century, which is now out of date. The sharing economy proves this point. In my view, taxing the income of private individuals and businesses in a uniform way would help to solve this problem. These changes might seem radical, but in order to make the tax system robust and efficient, it must be simple and easy to comply with and also reflect the society of today, not the one of 100 years ago.

CONCLUSIONS

The sharing economy is challenging the traditional tax system, when small independent suppliers become important stakeholders and platform companies are playing a new role. The line between businesses and private individuals as well as between employees and businesses is not always so easy to draw. As the co-founder of Airbnb Brian Chesky has put it: “there were laws created for business and there were laws for people. What the sharing economy did was to create a third category: people as businesses.” The main conclusion is that the tax systems should not be based on the presumption that people are either businesses or private individuals. The different tax treatments between the two makes it difficult to shift from being a private individual to become a business person, which makes it difficult to comply with tax obligations. A tax system that is easy to understand and to comply with can make the taxpayers trust the system and make them willing to comply voluntarily. Control is also important for compliance. An advantage with e-commerce is that all transactions leaves traces and are hence possible to track.

My suggestions are the following:

- Tax businesses’ and private individuals’ income uniformly
- Everybody should be an in principle taxable person for VAT/GST purposes and VAT/GST should be levied for supplies over a certain threshold
- A DST has the potential to tax the sharing economy, but it has also the potential risk of distorting competition
- The intermediary platforms should be obliged to report the earnings of the respective providers to the tax administrations

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