

Anne Michèle Bardopoulos

eCommerce and the Effects of Technology on Taxation

Could VAT be the eTax Solution?

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 Springer

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“To accuse others for one’s own misfortunes is a sign of want of education. To accuse oneself shows that one’s education has begun. To accuse neither oneself nor others shows that one’s education is complete.”

Epictetus¹

Plato contended that “[n]o man should bring children into the world who is unwilling to preserve to the end in their nature and education”.² This manuscript is dedicated to my late grandparents who believed that the greatest legacy that one can bequeath to a child is education. An educated man is an empowered man and “[i]f a man neglects education, he walks lame to the end of his life”³:

Πλάτων Μπαρδόπουλος (Platon Bardopoulos)

Κωνσταντίνη Παπαμανολοπούλου
(Constandina Papamanolopoulos)

¹Epictetus (AD 55 – AD 135). Available at <http://www.brainyquote.com/quotes/quotes/e/epictetus149122.html> [Accessed 27/01/2011].

²Plato (c429 – c347). Available at <http://www.brainyquote.com/quotes/quotes/p/plato397319.html> [Accessed 27/01/2011].

³Plato (c429 – c347). Available at <http://www.brainyquote.com/quotes/quotes/p/plato383526.html> [Accessed 27/01/2011].

Μανόλης Παπαμανολόπουλος
(Emmanuel Papamanolopoulos)

They sacrificed themselves to educate their children and children's children. They never accused others for their misfortunes and they inspired me to neither accuse myself nor others for my misfortunes.

Preface

The introductory chapter of the paper is a synopsis of salient points at issue cardinal to the intellectual basis of the paper, *id est*, the impact of technology on taxation and is VAT the eTax solution? Indeed, it is submitted that the imposition and implication of an eTax on eCommerce in the cyberworld, the formulation of which tax is at once efficient and compliant, is feasible and possible. It is further submitted that VAT, without reconceptualisation or formulation of a new system, is the most effective (actually usable) and practicable solution.

A critical point at issue is rapidly increasing eCommerce transactions and unconstrained amelioration of technology. The issue of an eTax is a compelling field of study because it is both topical and of historical consequence to the extent that the traditional world of tax, commerce and international trade is witnessing the radical evolution of taxation as it rises to meet the unprecedented challenges of eCommerce.

The paper explores the challenge to tax that has thrown the “*application of tax laws into disarray*”.⁴ The point at issue is the marking of “*territory in a seamless digital world . . . of mark[ing] nations and tax jurisdictions in a world that is not based on geography...*”.⁵ It is contended that this challenge pertains primarily to income tax laws to a greater extent than indirect tax laws.

The submission that value-added tax (“VAT”) is the eTax solution is supported by a comparative analysis and application of both income tax principles and VAT to practical examples. It is submitted that such a comparison elucidates VAT’s superior effectiveness and potentiality as an eTax tool in the virtual world. The current escalation of globalisation which in turn has compounded taxation issues has been expedited by the development of the Internet. With the introduction of the Internet and the advent of eCommerce, the traditional concept of international trade

⁴Bird, Richard *Taxing Electronic Commerce: A Revolution in the Making* (September 2003). C.D. Howe Institute Commentary, p4-5. Available at http://www.cdhowe.org/pdf/commentary_187.pdf [Accessed 16/09/2010].

⁵supra.

and commerce can no longer be effectively applied to the new taxing complications and issues manifested by technological amelioration. Unprecedented tax issues in respect of eCommerce transactions in the Internet may be classified as pertaining to the next generation taxing regime. The clumsy attempt to impose “physical world” laws upon a “virtual world” has generated multiple points at issue and has accentuated the impracticability of imposing “physical world” laws on a “virtual world”.

Further to a discussion of tax points at issue and solutions proffered in respect of eCommerce, the eCommerce environment itself and the laws pertaining to such an environment should be examined. Indeed, ignorance of the virtual world and its *modus operandi* precludes competent formulation of effective solutions to points at issue in eCommerce. Acknowledgment of the intricacies and complications of electronic transactions, as well as the continuous evolution of the Internet, will assist in the endeavour to develop a flexible and equitable solution to taxing problems inherent to our new “virtual world”.

Cardinal to the paper is the contention that taxing solutions should not be rigidly tailored to current technology operations and systems. It is essential that proposed tax solutions to all next generation taxing regime issues take cognizance of the current growth rate of electronic technology, that is, taxing solutions to eCommerce should be considered in conjunction with Moore’s Law.⁶ The prevailing tax “challenge” is undoubtedly temporary as it is in the nature of tax to be infinitely adaptable. Taxation is an integral part of human history, past and present, and the virtual world is commerce’s future. It is essential that any taxing system adopted to be imposed upon the virtual world should have the flexibility to be adapted to unpredictable taxing issues precipitated by technological amelioration.

Attempting to enforce a narrow view of tax principles on technology is proving to be increasingly difficult, especially as traditional taxing precepts have fallen victim to the proverbial generation gap and as such are not congruent with contemporary technological concepts of the Y-Generation, particularly with regard to the concept of “physical presence” in the internet. Tax authorities targeting the virtual tax prize may gratify their predilection by espousing the Y-Generation’s philosophy of technology and their concept of being “physically present” in the Internet, which is, furthermore, supported by technology academics.

As the paper is concerned primarily with the analysis and evaluation of VAT as the eTax solution, it is, therefore, imperative to examine some of the inefficiencies of traditional income tax provisions within the eCommerce environment; this relates most significantly to the issues of “residence” and “source” provisions and principles within the income tax analysis. Traditional income tax provisions dismally lack the flexibility to be effectively applied to the virtual world – the

⁶“The ‘law’ was adopted after Intel co-founder Gordon Moore wrote in a 1965 article that the number of transistors on a chip would double every 24 months.” BBC News, Moore’s Law on chips marks 40th (18 April 2005). Available at <http://news.bbc.co.uk/2/hi/technology/4446285.stm> [Accessed 21 July 2009].

theoretical principles upon which traditional income tax is founded are all too often couched in concepts which directly obstruct the necessary adaptability and flexibility of income tax provisions in respect of an ameliorating technological society. The problem of inflexible tax laws is especially pertinent in a society which is still adapting to the concept of being “physically present” within a virtual world. It is, therefore, submitted that current income tax principles are too rigid to adapt sufficiently to the exponentially burgeoning virtual world and technology. Indeed, it may be argued that income tax principles deem that adaptation is the responsibility of technology, the consequences of which are increasingly ineffective application of income tax in eCommerce and increasing loss of tax revenue in respect of government coffers.

The Internet has had a drastic impact on society and, moreover, the economy. It is imperative that we recognise that “*the Internet [is] an important cultural phenomenon . . . [which has, however,] failed to comply with basic economic laws . . . [probably because] it was devised by a bunch of hippie anarchists*”.⁷ Thus, tax authorities should seize the advantage of conceding to the concept that “[t]o get others to come into our way of thinking, we must go over to theirs; and it is necessary to follow, in order to lead”.⁸ Cognizance of the principles and concepts which enmesh the virtual world – the pressing concept of “presence” in the virtual world is a cogent point at issue – is essential to an understanding of the issue of traditional tax principles and virtual world incompatibility. Indeed, a careful scrutiny of the application of income tax principles within the virtual world is significant to the intellectual basis of the paper: “*The impact of technology on taxation*”.

The point at issue is taxation, either direct or indirect, in an eCommerce environment, which is subject to technology and technological concepts, and, as such, it may be proposed that tax adjust its principles and perceptions to those of the technology and communication industry and not demand the reverse. The question begs as to whether the continuing attempt to impose “basic economic laws” on an environment which defies such laws is not in itself a futile exercise. It may be argued that the continuing changes and advancements in technology make such an endeavour a futile exercise, and that the only tax that may possibly work within a “virtual world” may be the imposition of an indirect tax like VAT. The focus of the paper is to highlight the current efficiencies of VAT and consumption taxes in contradistinction to the inefficiencies of income tax principles which have possibly been stretched to their finite point of elasticity. It is submitted that the virtual world, engulfed in its own complications and perplexities, may be more amenable to the application of VAT than to the application of “source-based”, or other income tax, principles.

The issue of countries not implementing a VAT system in respect of eCommerce is a point at issue which posits the challenge as to whether it is possible for VAT

⁷Nolle, Thomas. Available at www.quote garden.com/internet.html [Accessed 8 May 2008].

⁸Shanahan, John M. (Ed). *The Most Brilliant Thoughts of All Times*; Hazlitt, William (1778–1830); Harper Collins, Inc.; New York, USA (1999). p275.

jurisdictions to effectively interact with non-VAT jurisdictions. The inability of VAT jurisdictions to effectively operate in conjunction with retail sales tax jurisdictions would doubtlessly precipitate problematic imposition of indirect taxation within the virtual world. However, a crucial aspect may be that whether a jurisdiction utilises a retail sales tax system or a VAT system, both are indirect taxes. While sales tax may deviate from the principle of neutrality and may not be considered a “general consumption tax”⁹ as is VAT, it is, nevertheless, consumption tax principle based similar to VAT.

While there may be other types of indirect tax systems utilised, VAT and retail sales tax (while the former is more prevalent than the latter) are without a doubt the two prevailing indirect tax systems within the global community. Indeed, 130 jurisdictions currently, as of the year 2010, have adopted and implemented a VAT system. The significant USA jurisdiction utilises a retail sales tax system. Canada, further to this issue, provides a functional example of VAT and retail sales tax co-existing effectively and efficiently in relation to each other, as both VAT and retail sales tax have been implemented in Canada for over 20 years.

eCommerce has not impacted VAT laws to the extent it has income tax laws, but has effectuated an exponential increase in cross-border transactions in respect of which tax laws, depending upon jurisdiction, zero-rate exports and tax imports. Technology has, however, impacted the current retail sales tax systems in effect in the USA instigating an increased urgency to streamline the retail sales tax system. While the paper may not advocate the abandonment of income tax principles in their entirety, comparison of income tax based principles to VAT laws implemented in the various jurisdictions suggests that the virtual world may be more amenable to the application of VAT than to income tax principles. Yet income tax appears to be the primary focus of much research, debate and discussion contingent upon the quantity of tax revenue connected with effective imposition of income tax.

VAT as an effective eTax can be applied to the virtual world in a manner analogous to traditional application precluding administrative difficulties. Inherent to indirect taxes such as VAT, the capacity to expedite eCommerce and facilitate the general operation, management and control of the virtual world is testament to the latter’s potential as an effective eTax tool.

Despite the impact of globalisation on international taxation, disputes pertaining to diverse political agendas predominate most specifically in respect of application of income tax principles. It is not to be implied, however, that indirect taxes such as VAT are insusceptible to disputes extant to conflicting political agendas; however,

⁹Tumpel, Michael, Professor *A Hybrid VAT System in the European Union* (Draft 04/24/2007) p31. Available at http://docs.google.com/viewer?a=v&q=cache:g5ZTN7J6sf8J:www.law.nyu.edu/idcplg?IdcService%3DGET_FILE%26dDocName%3DDECM_DLW_013830%26RevisionSelectionMethod%3DLatestReleased+The+common+framework+for+VAT+created+in+1967+for+the+EU&hl=en&pid=bl&srcid=ADGEESig8c6y5AwqvXsIPGHOW8-asiQcrIqfbzM1dwHa6pTbqOQbLX60f8_nx3d-U1Y3vjQQg2BR8zYGeVnpGPnM9rt5H2Q4RkiAHe0PI_tR6xZFjyqhXg0yx3ZcnIdwyatBM51Kdeyp&sig=AHIEtbSZXkC370HMugv4EdOPt6e-bY4eFA&pli=1 [Accessed 14/12/2010].

existing similarities have promoted harmonisation of indirect taxes on account of cross-border transactions. VAT is not without defect and perplexities relative to both the traditional and virtual worlds. VAT is not the “*silver bullet that will solve all the fiscal problems to which the growth of the borderless economy of cyberspace potentially gives rise*”.¹⁰ Further taxation problems arise with the proliferation of eCommerce which may not be effectively resolved with the application of VAT. Thus, while the paper’s primary focus is to evaluate the effectiveness of VAT in regard to collecting taxes on eTransactions, an examination of these issues in terms of finding or exploring a plausible solution is vital for other spheres of taxation, such as transfer pricing.

The submission that VAT is the eCommerce solution is cardinal to the prevailing discourse of the paper. VAT’s attraction is that it is both flexible and adaptable in respect of eCommerce, and in contradistinction to income taxation can be applied to eCommerce without significant change or amendment. However, amendment, radical change and reconceptualisation of income tax provisions are requisite for effective application to the virtual world. Notwithstanding the applicable amendment of relevant general peculiarities of the virtual world which would unequivocally assist in establishing VAT’s capacity as an effective eTax, it is submitted that VAT is, not only in the interim, a dependable eTax in respect of eCommerce, but will remain a powerful taxing tool in the virtual world.

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¹⁰op cit Bird, Richard *Taxing Electronic Commerce: A Revolution in the Making*, p2.

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“Teachers open the door, but you must enter by yourself.” – Chinese proverb

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As an amateur in technology, I am indebted to Mr. Kosta Kontos, a specialist in Cloud Computing, for reviewing and confirming my assumptions in respect of evolving technology.

I thank my father and mother and my brothers, Marcus Emmanuel and James, for their love and encouragement.

Abstract

Technology has impacted taxation and the manner in which it is effectively imposed. While this paper submits that VAT is the eTax solution, income tax issues relating to “residence” versus “source” have been addressed. A comparative analysis is made in respect of the application of income tax and VAT principles to eCommerce transactions.

Application of VAT within the virtual world does not differ significantly from traditional application. The primary difference pertains to determining the place of “supply”, but apart from such determination VAT principles and concepts can be applied with relative ease within the virtual world. Income tax laws, however, have deemed certain technology to constitute, for example, permanent establishment, and the conflict in “source” and “resident” based systems implemented globally has generated further points at issue. It is submitted that income tax principles may have to be “reconceptualised” in order to be effectively applied to eCommerce transactions because, in their current form they are not conducive to cross-border eCommerce transactions.

It is submitted that the indirect consumption-based VAT system is the most effective taxation system in respect of cross-border eCommerce transactions. Furthermore, VAT is the most amenable tax system in respect of eCommerce, because VAT’s inherently flexible nature enables it to adapt to technical amelioration and the unprecedented and unexplored terrain of a seamless, borderless virtual world. While VAT is not perfect and requires modification if it is to be effectively applied to the virtual world, and although administrative difficulties pertaining to cross-border transactions do require resolution, it is submitted that VAT is, nevertheless, more effective as an eTax than income tax. This assertion is based primarily on the flexibility of VAT principles compared to the inflexible principles of income tax.

Due to the infancy of eCommerce, case studies and data are relatively limited. Nevertheless, case studies of Amazon.com and Second Life are used as examples in an analysis of VAT application in the virtual world, and where possible electronic transactions have been either tested or attempted. A comparative analysis of the application of income tax and VAT principles to practical examples is provided to demonstrate the effectiveness of VAT as the eTax solution.

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Classified Guide to the Paper

1. Abbreviations and Acronyms

ARPA	Advanced Research Project Agency
ATO	Australian Tax Office
AUS	Australia
B2C	Business to Consumer
C2C	Consumer to Consumer
CAN	Canada
CIR	Commissioner of Inland Revenue
CIT	Collector of Income Tax
COT	Commissioner of Tax
CRA	Canadian Revenue Agency
DNS	Domain Name Server
DTA	Double Tax Agreements
EC	European Community
E-Commerce/eCommerce/e-commerce	Electronic Commerce
EU	European Union
GST	Goods and Service Tax (alternative name for VAT. Name and acronym applied in Countries such as Canada, New Zealand and Australia.)
HMRC	Her Majesty's Revenue & Customs
HST	Harmonized Sales Tax (Canada)
IP	Internet Protocol
IRS	Inland Revenue Service
ISP (server)	Internet Service Provider
MC	Model Tax Convention
NBL	Network Load Balancing
NZ	New Zealand
OECD	Organisation for Economic Co-Operation and Development

(continued)

OEEC	Organisation for European Economic Co-Operation
PST	Provincial Sales Tax (Canada)
QST	Quebec Sales Tax (Canada)
RCC	Revenue and Customs Commissioners
RSA/ZAR	Republic of South Africa
SARS	South African Revenue Services
SSTP	Streamlined Sales Tax Program/Project (USA)
SSTP/SSUTA	Streamlined Sales Tax Program (USA)
SSUTA	Streamlined Sales and Use Tax Agreement (USA)
States	As used within the OECD Model Convention, refers to “countries”
TAG	Technical Advisory Group of the OECD
TCP	Transmission Control Protocol
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
USA	United States of America
VAT	Value-Added Tax
WWW/the Web	World Wide Web

2. Currency Symbols

£	United Kingdom Pound currency symbol
\$	Dollar currency symbol used by USA, Canada, New Zealand and Australia. Distinguished by placing the country abbreviation before the currency symbol
Kr/SEK	Swedish currency symbol
¥	Japanese Yen currency symbol
R	South African Rand currency symbol
€	European Union Euro currency symbol
CHF	Swiss Francs currency symbol/abbreviation

3. Footnote Referencing

<i>et al.</i>	And others
<i>ibid</i>	In the same place
<i>Idem</i>	The same
<i>op cit</i>	In the work cited
<i>loc cit</i>	In the place cited
<i>supra</i>	Above

4. Date Formatting

Unless otherwise stated date formats throughout this paper will be as follows:

YYYY/MM/DD	Year/Month/Day
DD/MM/YYYY	Day/Month/Year
Day Month Year	The date written out in full

Chapter 1

A Bird's Eye View

It took the Telephone 38 years to reach 50 million users; Television 13 years to reach 50 million users; Internet 4 years to reach 50 million users. (Nellen, Annette *Overview to E-Commerce Taxation – Guide to Understanding the Current Discussions and Debates* (July 2003) 8. Available at www.cob.sjsu.edu/facstaff/NELLEN_A/ECOMM.pdf [Accessed 24/12/2008])

Abstract Globalization and the dominion of the Internet have confounded traditional international tax systems. Unprecedented tax issues flowing from eCommerce, powered by continuously mutating technology represent the central agenda for the next generation taxing regime. The continuing attempt to impose 'basic economic laws' on an environment which defies such laws is a futile exercise.

Critical points at issue are: 'source'; 'residence' and the virtual world; harmonization; internationally equitable and effective imposition of tax in respect of eCommerce; privacy; introduction between VAT and non-VAT jurisdictions and administrative issues. A further problematical point at issue in respect of eCommerce is the question of tax avoidance or tax evasion. The concept of 'presence; in the virtual world is a cogent point at issue as is the concept that being 'here' and 'there' within the context of the virtual world is synchronically possible.

Such challenges demand that taxing solutions should have the flexibility to adept to the impact of currently unimaginable technological amelioration.

It is submitted that VAT's superior efficiency and potency in the virtual world of cyberspace can be demonstrated in a comparative analysis with income tax principles and the application thereof to practical examples.

This paper explores the implications of globalisation consequent to the dominion of the internet for traditional tax systems and the consequent argument that these developments have thrown the "application of tax laws into disarray".¹ In brief the challenge to tax is posed by the marking of "territory in a seamless digital

¹Bird, Richard *Taxing Electronic Commerce: A Revolution in the Making* (September 2003). C.D. Howe Institute Commentary, p4–5. Available at http://www.cdhowe.org/pdf/commentary_187.pdf [Accessed 16/09/2010].

world . . . of mark[ing] nations and tax jurisdictions in a world that is not based on geography . . .".² Much of the literature deals primarily with income tax laws rather than indirect tax laws.³ However, consumption tax laws have been affected by the need to identify the location of the consumer and the place of supply in terms of the destination principle. However, it may be argued that an indirect tax such as VAT would facilitate the process of determining the consumer's place of consumption by identifying the consumer's IP address as the final place of consumption, use and enjoyment. The submission that VAT represents a potential solution is bolstered by a comparative analysis with income tax principles and the application of income tax principles to practical examples. It is submitted that such a comparison will manifest VAT's superior efficacy and potency in the virtual world of cyberspace.

The current escalation of globalisation which, in turn, has been expedited by the development of the Internet. Globalization, "*the compression of the world and the intensification of the consciousness of the world as a whole*",⁴ has facilitated international trade, which in turn has precipitated complex international taxation issues.

Traditionally, international tax may be defined as "*a subject of study that deals with international tax treaties and international aspects of domestic income tax laws*".⁵ The concept of international taxation could be adequately applied to international trade and commerce to determine taxing rights and, where treaties existed, to limit double taxation that may have arisen as a result of differing domestic taxation laws. However, with the introduction of the Internet and the advent of eCommerce, the traditional concept of international trade and commerce can no longer be effectively applied to the new taxing complications and issues manifested by technological amelioration.

Unprecedented tax issues which flow from eCommerce transactions, powered by continuously mutating technology represent the central agenda for the next generation taxing regime. Multiple concerns and queries are at issue in respect of the formulation of the new system, including:

- How is "source" defined within this new trading environment?
- Is it still possible to implement the "residence" concept in a virtual world?
- How does this new "virtual world" impact the application of international tax?
- Is there a solution to the imposition of an effective tax on eCommerce transactions that will be equitable and fair to all nations seduced by the Internet and its ever-enticing commercial abilities?

²supra.

³As demonstrated in the doctoral theses cited in this paper, for example, Dr Pinto and Dr Rendahl's theses on *E-Commerce and Source-Based Income Taxation* (2003), Netherlands and *Cross-Border Consumption Taxation of Digital Supplies* (2009), Netherlands respectively.

⁴Mainelli, Michael, Professor, Gresham College. Available at <http://www.gresham.ac.uk/printranscript.asp?EventId=514> [Accessed 17 June 2008].

⁵Olivier, Lynette & Honiball, Michael *International Tax, A South African Perspective 2008, Fourth Edition* (2008) 1.

- What are the administrative issues regarding the implementation of an effective taxing system in respect of eCommerce transactions?

The attempt to impose “physical world” laws onto a “virtual world” has been shown not to be adaptable to the “virtual world” environment. It is essential that proposed tax solutions for the next generation taxing regime issues take cognisance of the current growth rate of electronic technology, that is, taxing solutions to eCommerce should be considered in conjunction with Moore’s Law.⁶

The daunting aspect of this “virtual world” raises the pressing problem of which tax evasion diminishes the government coffers at a time of widespread recession and reduction of tax revenues. Indeed, it may be argued as to whether eCommerce participants are deliberately evading tax with the aid of cultivated taxing rights confusion, or if an individual’s tax ignorance is merely amplified by the “virtual world”. It may further be argued that regardless of capricious tax law interpretation, “*when there is an income tax, the just man will pay more and the unjust less on the same amount of income*”.⁷

In turn this raises the need to examine the eCommerce environment and laws pertaining to such an environment. Ignorance of the virtual world and its *modus operandi* precludes competent formulation of efficacious and fruitful solutions to points at issue in eCommerce.

Acknowledgment of the intricacies and complications of electronic transactions, as well as the continuous evolution of the Internet, augments the endeavour to develop a flexible and equitable solution to taxing problems inherent to our new “virtual world”. Thus in the OECD’s⁸ Commentary Note on eCommerce⁹ “source”, for tax purposes, is defined by first applying *traditional taxing principles* as far as possible, and only thereafter referring to OECD guidelines in circumstances where *traditional taxing principles* cannot be applied in determining “physical presence” in order to satisfy the definition of “permanent establishment”.

It will be argued in this paper that no matter the challenge posed by these developments, taxing solutions should not be rigidly tailored to current technology operations and systems, but should have the flexibility to adapt to the impact of currently unimaginable technological melioration.

The Internet has had a profound impact upon the manner in which we conduct business, the imposition of tax and methods of tax collection and has facilitated

⁶“The “law” was adopted after Intel co-founder Gordon Moore wrote in a 1965 article that the number of transistors on a chip would double every 24 months.” BBC News, Moore’s Law on chips marks 40th (18 April 2005). Available at <http://news.bbc.co.uk/2/hi/technology/4446285.stm> [Accessed 21 July 2009].

⁷Plato 427BC-348BC. Available at <http://www.quotesandpoem.com/quotes/listquotes/subject/taxes> [Accessed 22 January 2007].

⁸The Organization for European Economic Co-Operation, otherwise referred to as the OECD.

⁹OECD Committee on Fiscal Affairs, *Classification on the Application of the Permanent Establishment, Changes in E-Commerce: Changes to the Commentary on the Model Tax Convention on Article 5* (2000) OECD Publications.

flagrant tax evasion. “*Legislation governing . . . trade that is technology neutral is required. The use of an electronic medium should not affect the laws that would ordinarily govern the transaction.*”¹⁰ This principle is pertinent to the various codes of law which have been proposed to govern the virtual world, including methods of taxation.

A narrow conception of ‘physical presence’ within the virtual world will induce an inflexible taxing system. It is essential that any taxing system within the virtual world should have the flexibility to be adapted to unpredictable taxing issues precipitated by technological amelioration. Therefore, educated cognizance of technological terms, definitions and concepts is essential. Attempting to enforce a narrow view of tax principles on technology has proved increasingly to be difficult, especially as traditional taxing precepts have fallen victim to the proverbial generation gap and as such are not synchronous with contemporary technological concepts of the Y-Generation, particularly with regard to the concept of ‘physical presence’ in the internet.

Within the context of eCommerce, to impute a *parti pris* definition to ‘physical presence’ would prejudice the issue of ‘physical presence’ in the Internet for the purpose of determining taxing rights, imposition of consumption tax as well as enforcing obligation to collect consumption taxes on behalf of revenue authorities.

By adopting a common broad view of ‘physical presence’ in the virtual world, a more flexible application of real world laws in the virtual world will be possible, especially in the case of the prevalent Functional Equivalence Approach. Furthermore, such a stance may enable the Functional Equivalence Approach to meet the challenge of possible future technological advances such as space ISPs.

Tax authorities who seek to target new sources of revenue and thus pursue the virtual tax honey-pot may espouse the Y-Generation’s philosophy of technology and a concept of being ‘physically present’ in the Internet, which has support from technology academics. Tax authorities should seize the advantage of conceding to Hazlitt’s¹¹ axiom that “[*t*]o get others to come into our way of thinking, we must go over to theirs; and it is necessary to follow, in order to lead”.¹²

Furthermore, it should be possible for tax principles to be applied in a manner compatible with the technology and communication industry’s perception of ‘presence’. The Internet has had a drastic impact on society and, moreover, the economy. It is imperative that we recognise that “*the Internet [is] an important cultural phenomenon . . . [which has, however,] failed to comply with basic economic*

¹⁰Contracting and Trade Laws, Green Paper on Electronic Commerce for South Africa, Co-ordinated and compiled by the Department of Communications Republic of South Africa (November 2000).

¹¹Hazlitt, William (1778–1830). “*English essayist and critic. From about 1812 he wrote many articles on diverse subjects for several periodicals, including the Edinburgh Review and the Morning Chronicle; his essays were collected in Table Talk (1821–2) and The Plain Speaker (1826).*” [The Oxford English Reference Dictionary, Sec. Ed. (1996), p647].

¹²Shanahan, John M. (Ed). *The Most Brilliant Thoughts of All Times*; Hazlitt, William (1778–1830); Harper Collins, Inc.; New York, USA (1999). p275.