**Weekly insight:** Europe introduces VAT on e-commerce of digital products and services

**Highlights**

- Europe introduces VAT on e-commerce of digital products and services from July 1st, 2003. Online sales of digital products and services to European customers will include VAT, no matter whether the vendor belongs or not to any of the Fifteen Member States.
- This new rule is perceived as a frontal attack on US policy. In order to boost e-commerce, the US Government approved the Internet Tax Freedom Act (IFTA) by which, until November 2003, American businesses are exempt from taxes on the sale of digitally delivered products—items such as children’s games, music or other services that are sent electronically to a consumer’s home computer.

According to European Commissioner Frits Bolkestein, this tax "will remove the serious competitive handicap that EU firms currently face in comparison to non-EU suppliers of digital services both when exporting to world markets and when selling to European consumers.” (In *News.com*) [Full Story](http://www.ebcenter.org/newsletter/newsletters/EnglishNewsletter/EnglishNewsletter_13_05_02.htm)

**Highlights**

- The new rules will apply to the **supply over electronic networks** of software and computer services generally, plus information and entertainment or similar services between companies and consumers (B2C),
as well as to broadcasting services by subscription or pay-per-view.
- Taxes collected on digital products and services, to be enforced from July 1st. 2003, will be at the "standard" rate for each country. This rate may differ from 15 to 25% on the price of the product.
- Under these new rules, non-EU suppliers will have to register with a VAT authority in any one Member State of their choice, and to levy VAT at the rate applicable in the Member State where the customer is resident. The country of registration will re-allocate the VAT revenue to the country of the customer.
- The U.S., which threatened in February to take the case to the World Trade Organization (WTO), says it believes the rules are discriminatory and says it will put additional administrative pressure on U.S. companies.

Press Review
From The Guardian
"Although the market remains small at present, most big internet players are banking on an increase in the number of people buying music, software and even films in this way as demand for broadband increases. (...) The move presages the introduction of a similar law due to come into force next year that will force US based Internet service providers such as AOL to pay VAT in the countries in which they operate."
[Full Story]

From Wired
"The EU's new tax rules come at a time when the bloc is locked in a trade battle with the United States over steel duties it has imposed on European and some other foreign companies. EU trade officials are meeting on Tuesday in Brussels to give further consideration to plans drawn up by the European Commission to hit back at the U.S. steel duties with sanctions. Under the commission's plans, a first set of sanctions will come into force from June 18, hitting a range of goods including U.S. citrus fruit and some steel products, with duties of 100 percent in a move worth more than $300 million."
[Full Story]

From New York Times
"This formula marks a significant change from the current tax rules, which permit EU residents to buy the same MP3 from EMusic.com without paying tax. But if a European customer buys the MP3 from, say, Stockholm-based eClassical.com, an online vendor of classical music, tax is levied on the sale. Under the system, as now, European consumers will pay only their own country's so-called value-added tax. U.S. companies will be forced to charge customers the prevailing rate in force where their customers live. Each of the EU's 15 countries taxes different products at different rates. General value-added rates vary from 15 percent in Luxembourg to 25 percent in Sweden. The U.S. Treasury Department fears U.S. firms will be required to charge the EU's value-added tax at higher rates than their EU competitors. The department -- and American vendors -- also worry that EU rules will breed a complicated, difficult-to-enforce tax system that hampers e-commerce in general."
[Full Story]

From e-Business Center
"The fact that a consumer of any country can purchase goods and services in any part of the world and in real time is a positive historical change that should not be affected by lack of harmonisation that regulates e-business operations. That is why there is a need to change the European Union's will towards the promotion of e-business use and development amongst the citizens of the Member States. A good way of doing so would be through the tax exemption for this type of commercial operations."
[Full Story]
From EcommerceTax.com
"It is interesting to note that, if other countries adopt similar rules, EU sellers will face compliance burdens that are substantially greater than those now. For instance, if the United States adopts rules to impose its sales tax on imports of digital products and services, EU sellers could be forced to deal with as many as 7,600 different sales tax jurisdictions. If many countries adopt Europe's rules, tax compliance for online sellers could involve dozens of different countries, and dozens of languages.

The EU's new system could dampen a seller's enthusiasm for seeking customers there. For instance, to avoid tax compliance burdens, a U.S. seller may prohibit European customers from making online purchases. If other countries adopt similar rules, cross-border commerce in digital products and services could be greatly inhibited. This is, of course, one of the things the worldwide community has feared; imposition of substantial compliance burdens on online commerce, which can only succeed in impeding its growth."

[Full Story]

Commentary by...
Joan Hortallà i Vallvé, finance inspector on long-term leave and an expert in online tax at Landwell-PwC

Online VAT taxation: a solution in search of problems

The new rules approved by European institutions must be analysed from two different points of view: the EU's versus the rest of the World's and within the EU itself.

As far as the relations between European companies and non-residents in the EU are concerned, the measure seems very appropriate. Thanks to it, when an Argentinean or a Japanese person downloads software from the web of a Dutch company he/she won't have to pay VAT, something which happens (or should happen) at present.

However, the rule expects that when a company from Ohio charges an EU consumer for the download of a digital photograph, it adds to the price a VAT amount which will be deposited in some European revenue service. Do they really believe that the mentioned company will charge it? What's more, in the case the company charges VAT on the sale, do you think it will be lodged in the revenue service? If the company doesn't do it, who will compel it to do so, the Internal Revenue Service (IRS) maybe? It is not very likely that the US Treasury will be very interested in levying a tax that harms American companies and later to lodge it in the coffers of a European country.

Lastly, in Europe the norm implies that downloaded services from the Net pay tax applied at the point of origin. For instance, a French consumer who downloads the same service from his home will pay 25% VAT if he does so from a Danish website while it will only be 16% if he does it from a Spanish site. If the website is in the US, it will probably be 0%. Where is the neutrality in indirect taxation in the same place of consumption defended by the Sixteenth Directive?

Summarizing, the European industry's competitiveness is improved in non-EU markets, making fiscality equal, not better, for the rest of the world's industries. On the other hand, in our market, the result is chaos and there is a clear winner: companies outside the EU who nobody will be able to force them to charge VAT when selling to end users.

EBCENTER ARTICLE
How to build up loyalty amongst users in the Internet business
Francesc Riverola, Researcher ebcenter

The portals that offer personalised treatment to users can retain them more easily and avoid their going over to the competition. [Full Story]
REPORTS

Government Web site improves interactions with government for 60% of American users

**Title:** The rise of the e-citizen  
**Source:** Pew Internet & American Life  
**Date:** April 2002

**Abstract:** While many government site users focus on their personal needs in dealing with government agencies, there is abundant evidence that a new "e-citizenship" is taking hold: 42 million Americans have used government Web sites to research public policy issues, 23 million to send comments to public officials about policy choices and 14 million to gather information to help them decide how to cast their votes. Some 60% of government Web site users say such sites have improved their interactions with at least one level of government and 80% say they find what they are seeking on the Web sites. About 77% of those who use government Web sites get tourism and recreational information, 70% do research for work or school and 63% download government forms. However, just 16% of government Web site users have filed taxes online and only about 12% have renewed an automobile registration online. [Full Story]

Internet advertising revenues declined 9.8%

**Title:** IAB Internet Advertising Revenue Report  
**Source:** Interactive Advertising Bureau and PricewaterhouseCoopers  
**Date:** April 2002

**Abstract:** Internet advertising in the United States totalled $1.79 billion for the third quarter of 2001 and $5.55 billion for the first nine months of 2001, 9.8% less than the third quarter in 2000. This is one of the major findings of the PwC and IAB survey, which blames economic recession for the decline in the overall advertising market. The research highlights that there is a diversification in advertising formats: classified ads grew to 17% of revenues in the third quarter of 2001, from 9% in the same period in 2000. The categorization of ad types was expanded to include slotting fees, at 7% of the third quarter revenues, and wireless and ITV, both at less than 1% of revenues for the same period. Ad banners accounted for 35% of total revenues during the third quarter of 2001, down from the 46% reported in the same period in 2000. Moreover, Internet advertising remains concentrated and the 10 leading companies accounted for 75% of total 2001 third quarter revenues, up from 68% reported for the same period in 2000. [Full Story]

About 43% of hackers look for intellectual stimulation and improvement of their skills

**Title:** The Boston Consulting Group Hacker Survey Release 0.3  
**Source:** The Boston Consulting Group in cooperation with OSDN  
**Date:** January 2002

**Abstract:** The Boston Consulting Group has conducted a survey about open source and hackers, who unlike the crackers, aren't malicious meddlers. The study describes the open source flow of work, where virtual teams, for profit companies and users participate. According to BCG, the model is based on three obligations: to give, to receive and to reciprocate. About 43% of hackers look for intellectual stimulation and improvement of their skills, while 34.2% act because they state that code should be open. 71.4% of them would work on a closed-source software project if they received enough money to support their lifestyle. Just 6.0% would never participate in proprietary software development. [Full Story]

COMPANIES
Icon Medialab Stockholm files for bankruptcy
International Internet consultancy Icon Medialab announced that it is to stop supporting its operations in Stockholm and France. The company wants to reach operational profitability by mid-2002 for the whole company and doesn't consider it a viable option to continue to invest heavily in locations that they believe will not perform in the short term. From Ad Age Global. [Full Story]

Microsoft to buy Navision
The giant from Redmond wants to buy Danish enterprise software firm Navision for $1.33 billion in one of their biggest takeovers. Microsoft's aim is to expand in the SME market segment and last year acquired American Great Plains. Now, Bill Gates's company needs to have a real presence in the European SME market segment, and Navision is one of Europe's manufacturers of software that helps medium-sized businesses run their operations and finances. From Reuters. [Full Story]

Terra Lycos will invest more than $6 million in an ad campaign
The portal is aiming to boost traffic with a new, $6 million television ad campaign. Terra Lycos wants to promote its travel, sports, games and finance sites. The site plans TV, newspaper and magazine ads in key markets. From Internet News. [Full Story]

Spanish Satellite TV Deal
Canal Satélite Digital, one of the Spanish satellite pay-television services, has closed a deal to merge with his rival Vía Digital, owned by Telefónica. Nevertheless, the planned merger will have to be referred to the European Union's competition authorities. From Financial Times. [Full Story]

WE RECOMMEND
E-Business forecasts
The term "e-business" is so discredited that General Motors, -which incessantly plugged its e-GM unit from 1999 until folding it into its info-tech department last fall-now insists on calling its continuing e-business efforts "digitization." The phrase "profitable Internet company" has become a sniggering joke and even e-business leaders such as Amazon.com and Cisco face continuing doubts about their business models. To Business Week, the same decades-long build-out that marked the post-crash railroad revolution will play out during the Information Revolution, led today by the Internet. Despite the rapid rise and collapse of the bubble, the cycle can take at least 50 years to play out from initial breakthrough to maturity. According to the authors, the next phase of e-business will be nothing like the dot-com era. The Web will be a tool to improve business processes-not a business unto itself and much of the work will be aimed, instead, at helping existing companies use the Internet to cut costs, serve customers better, and open new markets. From Business Week. [Full Story]

Learn from e-learning projects
Web-based courses offered by American universities, that have spent at least $100 million on them, have failed. New York University recently closed its Internet-based learning venture, NYUOnline. Now the groves of academe are littered with the detritus of failed e-learning start-ups as those same universities struggle with the question of how to embrace online education but not haemorrhage money in the process. On one hand, creating an online course isn't migrating painlessly from classroom onto the Web. On the other hand, the idea that many students would pay $500 or more for them prove a miscalculation. Part of the problem has been an emphasis on technology thus university administrators confused tools with
education. However, there are a few success stories. The technically oriented University of Phoenix has an online enrolment of more than 37,000, with four-year and post-graduate degree programs aimed at older students. The university's success comes from its expertise in **branding**, **marketing** and **infrastructure**. That could be the combination for success in distance education. From *New York Times*. [Full Story]