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The Systematic challenges for implementing a broader digital tax policy in Zimbabwe.

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Abstract

The world has been grappling to develop an international consensus-based framework for the taxation of the digital economy since 1996 however a concrete solution is yet to be found. Upon realising the potential revenue, Zimbabwe implemented a unilateral tax policy. The revenue realised from such policies however does not match the potential that could be realised. The objective of this study was to examine challenges of implementing a broader digital tax policy in Zimbabwe. The study adopted a qualitative approach because the study was explorative. Data was collected using in depth interviews. The population of the study consisted of tax experts drawn from the Zimbabwe revenue authority (ZIMRA), private sector tax practitioners, development partners supporting taxation administration programs in the country and Civic Society Organisations (CSOs) interested in the area of the taxation. Based on the principle of saturation, a total of 12 tax experts were interviewed. A six-stage thematic analysis was used to analyse data. The study revealed that the systematic challenges that are hindering Zimbabwe from enacting a broader digital tax policy are lack of information, lack of technology and the unilateral stance Zimbabwe has adopted. The study concluded that these challenges can be addressed. Notwithstanding this, international co-operation is paramount.

Key words: Digital economy, Taxation, Digital Services tax, Zimbabwe, Policy.

Introduction

The world's discussion on the taxation of digital economy can be traced back from as early as 1996. Meaningful contributions can however be traced back to the Ottawa Conference of 1998 where the Ottawa Taxation Framework Conditions were set (OECD, 2020). Under this framework, both the OECD and

non-OECD countries agreed that any new taxation rules should adhere to the guiding principles namely neutrality, efficiency, certainty and simplicity, effectiveness and fairness as well as flexibility in order to avoid tax wars and any distortions between conventional and electronic commerce (Cockfield, 2020).

Despite these early attempts to effectively develop an internally consensus-based framework to the taxation of the digital economy, as of 2022, 26 years later, a comprehensive solution is yet to be found. The general characteristics of the transactions of the digital economy are well documented. These include the overreliance of digital economy companies on data, network effects, multisided business models and the ability of companies in the digital economy to scale without mass(OECD, 2020).

Several reports have been published and concerns raised on the increasing ability and practice by multinational enterprises (MNEs) to use aggressive tax planning and exploit gaps in the current tax systems to artificially reduce taxable income or shift profit to low-tax jurisdictions in which little or no economic activity is performed (OECD, 2015; Fair Tax Mark 2019). These concerns are aggravated by the emergence the digital economy and the lack of effective taxation framework for such. In 2013, OECD published a report on the roadmap on the taxation of digital economy (OECD, 2013)



Figure 2.1: The OECD/G20 roadmap on the taxation of the digital economy

Source: (KPMG, 2020)

The OECD published a report on Action Plan on Base Erosion and Profit Shifting in response to the concerns about the under-taxation of the digital economy at the behest of the Group of Twenty (G20). The report clearly stated that while the profit shifting and base erosion practice by MNEs had a tax compliance aspect, the fundamental cause to this was a policy issue as the international tax rules had not been able to keep to base with the changing business environment (OECD, 2013).

Following the report, OECD and non-OECD countries established the Task Force on the Digital Economy (TFDE) which adopted a 15-point Action Plan to address Base Erosion and Profit Shifting (BEPS). After two years of work, in 2015, the taskforce released a report on Action 1: Addressing the Tax challenges of the digital economy whose findings indicated that the challenges to the taxation of the companies in the digital economy were underpinned by the unique features of the companies which operate in this economy namely

mobility, reliance on data and user participation, network effects, multi-sided business models, tendency towards monopoly or oligopoly, and volatility (OECD, 2015).

Following the release of the 2015 report, the OECD/G20 Inclusive Framework on BEPS was established in June 2016 which was open to all interested countries and jurisdictions in order to implement the recommendations of the 2015 report. In 2018, the Inclusive Framework released a follow up interim report the report on tax challenges arising from digitilisation which provided an in -depth analysis of value creation in the digital economy as well as provided a layout of the challenges identified with respect to the continuing effectiveness of international tax standards in light of the issues raised by the digitalisation of the economy '(OECD, 2018).

In the absence of a clear framework of the taxation of the digital economy, countries began to enact or propose unilateral tax measures (KPMG, 2019). In March 2018, the European Union (EU) proposed new rules to ensure that digital business activities are taxed in a fair and growth-friendly way in the EU. The proposal included a reform of corporate tax rules so that profits are registered and taxed where a business a significant economic activity which would be determined by the magnitude of revenues, users and contracts that an MNE has and an interim of 3% tax on profits from user data, services from connecting people and other digital services such as subscriptions to streaming services.

The United States government responded by condemning such a measure and called it “discriminatory against US companies” and hence called for its halt (Stolton, 2018). Globally by the end of 2020 terms of direct taxes, 23 countries had already enacted legislations, 4 countries had drafted draft legislations and were in the public consultations, 10 countries had made public announcements to implement, 3 countries had their proposals rejected, 7 countries were awaiting a global solution the rest of the world have made no developments. In terms of direct taxation legislations, 81 countries had enacted Indirect taxes legislations for the digital economy. 11 Countries had draft legislations and the rest of the world had no developments (KPMG, 2020).

As countries continued to implement or contemplate on enacting unilateral tax measures, in 2020 fearing the adverse effects unilateral measures could have on the global economy, in 2020, under the OECD/G20 program, countries renewed their commitment to a consensus-based framework and released the blueprints of the two-pillar approach to the taxation of the digital economy (OECD, 2020).

On October 8 2021, 136 countries finally agreed on the Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy which will ensure that multinational enterprises (MNEs) will be subject to a minimum tax rate of 15%, and will re-allocate profit of the largest and most profitable MNEs to countries worldwide --(OECD, 2020). Under this framework, countries also agreed to removal and suspend any DSTs or other relevant similar measures while they work on this consensus-based framework with a target implementation date of the two-pillar solution of 2023.

Zimbabwe was one of the countries that enacted a unilateral direct tax policy when other countries were doing so and it has not removed or suspended its policy. Zimbabwe introduced its unilateral tax policy for the digital economy on 1 January 2019 (section 12 A, Income tax Act [Chapter 23.06]). The policy levies a 5% general income tax on income deemed to have accrued from a source within Zimbabwe to non – resident satellite and e – commerce platform service provision. Zimbabwe's general income tax law for the digital economy is very limited in terms of the targeted tax base compared to the digital services taxes that other countries have enacted. The tax policy targets the taxation of revenues from exchange transactions by foreign satellite broadcasters or e-commerce platforms (Income tax Act [Chapter 23.06]). In comparison, digital services taxes that were enacted by other countries such as Brazil, Spain, Italy and UK targeted broader tax bases because their tax laws included the taxation of revenues from the transfer and use of data collected from users in their jurisdictions (OECD, 2020).

Not much revenue has been raised from this tax head since the implementation of the tax policy. A report by ZIMRA (2020), shows that in 2020, the Zimbabwean government only collected about ZWL 500 million (approx. USD5 million) from newly registered tax payers (inclusive of local taxpayers). Statistics however suggest that Zimbabwe has the potential of generating a lot more from this tax head if it is broadened and implemented properly.

In 2019, Zimbabwe shutdown the internet for 144 hours and this costed the economy US\$34.5 million dollars (Chimhangwa, 2019). This implies that Zimbabwe generated more than \$240 000 per hour through the internet.

According to Kemp (2021), in 2021, Zimbabwe's internet penetration rate stood at 33.4% (5.01 million internet users) and this figure was estimated to grow at a rate of 4.2% per year. A further breakdown of this number showed that amongst these internet users, 1.3 million are active social media users and this figure was estimated to grow by 32.7% going forward. According to the same report, during the same period, Facebook, Instagram and Twitter had potential audiences of 1.2 million, 340 thousand and 172 thousand users respectively within the country of Zimbabwe. Data from these company's annual reports show in that 2021, Facebook, Instagram and Twitter had advertising revenues of USD 32,03, USD 18 and USD 11 respectively (Statista Research Department, 2023). An analysis of the users that these companies had within the country and their advertising revenue per users therefore suggests that Facebook, Twitter and Instagram are potentially generating approximately \$38 million, \$6.12 million and \$1.9 million respectively annually in revenues.

Against this background, the objective of the study was to examine the systematic challenges of imposing a broader digital tax policy in Zimbabwe.

Systematic challenges of taxing the digital economy

In a paper which sought to analyse the tax administrative challenges of the digital economy, Hodzic (2019) identified an under-developed information and communications technology, slow development of e-government and business and data security problems as the major weaknesses in the Croatian tax system. Similarly Zhu (2021), identified difficulty in obtaining accurate tax related information, difficulty in determining taxpayers, tax objects and

determining the tax rate to be used as the major challenges in the tax collection and management of the digital economy. The manner and communication process used by the tax administrator has a large effect on the tax enforcement costs by the tax agent in particular reducing information overload and emphasizing action-relevant information seem particularly effective in increasing compliance the effects of deterrence and tax morale intervention (Neve et al, 2021).

Capacity constraints of revenue authorities have also been identified as a major challenge in implementing other tax reforms such as Property tax (Bird & Vazquez, 2019). According to Olov & Fedotova (2020), one of the challenges that impede tax reform in the digital economy is the poor adoption of digital technologies in tax administration. As the number of tax payers increase and the tax collection process is becoming large and complex, one of the technologies that could be deployed to reduce costs and increase the tax collection, management and improve the relationship between the tax collector and the tax payers is Artificial Intelligence (Zheng, WuJing Lin & Chen, 2021). By reviewing the development course of Artificial Intelligence and tax collection and management in China, Li and Zhong (2021), found out that AI intelligent technology can make the complicated tax management work more efficient by increasing the tax inspection ability and evaluation efficiency, and reducing the tax risk and tax cost. AI provides simulated tax risks, which can help more complex human judgments to be made and it can also aid detection of fraud, contributing to its supervision and monitoring by government (Huang, 2018).

The problem of double taxation is also another systematic challenge that had been identified by scholars as a challenge in implementing unilateral tax policies (Geringer, 2021). This is because national digital taxes challenge the concept of fair taxation conditions since most of the time digital services taxes implemented by countries do not fall under the scope of current double tax treaties. Scholars such as Spengel and Christoph (2019), who scrutinised developments in the taxation of the digital economy such as have thus argued that there is no justification for introducing new taxation rules particularly aimed at the digital economy.

Research Methodology

The study adopted a qualitative approach since it is exploratory. The data collection technique used in this research study was in depth interviews (Chetty, 2016). The population consisted of various stakeholders who are involved in policy-making, implementation and evaluation. A total of twelve tax experts drawn from government officials in the revenue authority, private sector tax practitioners, development partners supporting taxation administration programs in the country and CSOs interested in this area were purposively selected as the sample of the study. The sample size of the researcher was based on the principle of saturation. This means that the researcher carried out one interview after another until he observed that additional interviews were no longer yielding any new significant information (Saunders, et al., 2018). A snowballing sampling technique in which a sample is

gradually formed through contacts and references was also used to compliment purposive sampling in coming up with the sample for the study. The participants were coded as A, B, C up to L to protect their identity. Data was analysed using 6 stage thematic analysis and presented using the thematic approach.

Findings

The main objective of the study was to examine challenges of implementing a broader digital tax policy in Zimbabwe and the interrogation came up with three critical challenges. These were lack of information, lack of appropriate technology and unilateral decisions.

Figure 3.1 below summarises the findings.

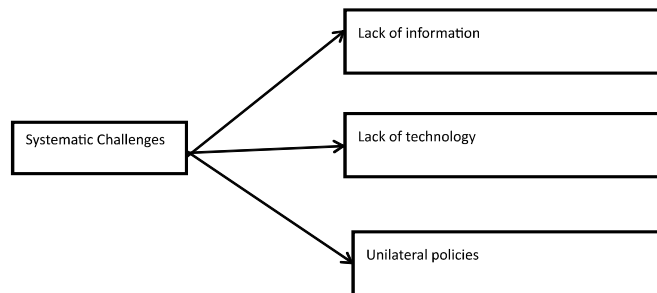


Figure 3.1: Typography showing thematic analysis of results on the systematic challenges of imposing broader digital tax policy in Zimbabwe.

Source: Study (2021)

Lack of information

The study revealed that the lack of information was one of problems that were impeding the ability of Zimbabwe to impose a broader tax policy. In order to design a successful tax policy information that enables the tax administrator to identify elements such as the tax payer, the tax object and the tax rate is required (Zhu, 2021). Scholars such as –Spengel and Christof (2020), also indicated that a lot of information is required to assign value to tax objects such as data before it can be taxed. Participant A for instance noted that:

In order to things such as advertising revenues, there is a lot of information that is needed in order to determine the revenues that are attributable to Zimbabwe. The information includes the global advertising revenues, the global users and the users of a certain service in Zimbabwe. All this information is not easily available.

The view was supported by participant C who indicated that

The current tax policy that Zimbabwe has on the taxation of non-resident digital service providers is based on revenues that pass through the Zimbabwean banks that have to be expatriated to the home country of the digital service providers hence it is easy to gain the information such as the amount to be taxed since a Zimbabwean bank will have that information. But for all other revenues where the revenue does not pass through Zimbabwean banks such as payments made from offshore accounts are difficult to tax

Participant F concurred explaining that

There is no legal requirement for non-resident digital service providers to provide information about their revenues based on the country of operations and as long as this is the case, developing countries which have little power to demand this information will may never be able to impose broader digital

economy policies that tax other revenues were information is not independently available.

These three participants explicitly confirmed that for a broader digital tax policy to be imposed, the government would need a lot of information that is currently unavailable otherwise any broader tax policy announcement would lack the means for enforcement.

Lack of appropriate technology

The findings also revealed that the lack of appropriate technology on the other side of the revenue authority was also a major challenge in implementing a broader tax policy for the digital economy. Technology is essential to ensure the smooth co-operation and communication of tax payers and tax administrators in the digital economy since tax payers are exponentially increasing the tax collection process is becoming large and complex. Participant E summed up this position, pointing out that:

The digital economy is driven by technology hence there is need for sophisticated technology to monitor transactions if the revenue authority is to enforce the taxation of that economy, ZIMRA currently simply does not have such technology needed to do so.

The findings revealed that strong research is needed in technology if the country is to enact a broader digital tax policy that aims to levy tax on other transactions that are non-exchange. This perspective was further expressed by participant L, who indicated that:

One of the key players that ZIMRA needs to collaborate with in terms of taxing the digital economy is the Postal Telecommunications and Regulatory authority (POTRAZ) but that organisation in itself also lacks the needed technology to monitor transactions in the digital economy. Without such

technology any broader digital tax policy would be impossible to enforce.

Unilateral policy making

The study also revealed that one challenge that was hindering Zimbabwe from enacting a broader digital tax policy was the unilateral stance that it had taken in enacting and implementing digital tax policies. Unilateral measures mainly undermine double taxation agreements that are there between countries.

Respondent G revealed this theme by indicating that:

One of the reason why countries in Africa such as Zimbabwe has not been able to enact broader digital tax policies is because they are acting alone to solve an international problem which is an impossible task. A Zimbabwean company cannot effectively tax an American company without the help of America.

Respondent A also posited this view and further explained that:

The reason why even the current general income tax on broadcasting services may never succeed is because it is not consistent with international tax rules and double taxation agreements that Zimbabwe already has. As long as that is the case and Zimbabwe continues to implement tax laws unilaterally, a broader tax policy is bound to fail even more

Discussion

The study revealed systematic challenges that are hindering Zimbabwe from enacting a broader digital tax policy are lack of information, lack of technology and the unilateral approach that Zimbabwe has taken in terms of the taxation of the digital economy.

The finding that lack of information is a challenge in taxing the digital economy resonates with the findings of Zeng et al (2012), who noted that in the digital economy, information about tax payers is difficult to obtain in the conventional

way since a business doesn't need a license and a tax registration certificate to operate in the digital economy. The findings also confirm the findings of Hodzic (2019) who also identified an underdeveloped information and communications technology, slow development of e-government and business and data security problems as the major weaknesses in the Croatian tax system. Similarly Zhu (2021), identified difficulty in obtaining accurate tax related information, difficulty in determining taxpayers, tax objects and determining the tax rate to be used as the major challenges in the tax collection and management of the digital economy. The manner and communication process used by the tax administrator has a large effect on the tax enforcement costs by the tax agent in particular reducing information overload and emphasizing action-relevant information seem particularly effective in increasing compliance the effects of deterrence and tax morale intervention (Neve et al, 2021).

The finding that lack of technology is a systematic challenge in taxing the digital economy also agrees with the findings of Olov & Fedotova (2020), who noted that one of the challenges that impede tax reform in the digital economy is the poor adoption of digital technologies in tax administration. Capacity constraints are a major challenge in tax reform (Bird & Vazquez, 2019). Competence in building modern digital systems which include not only the required technical knowledge but also modern business and managerial skills is a major challenge across Africa in taxing the digital economy (Korovkin, 2019).

The finding that unilateral policy making is also a systematic challenge to imposing a digital economy concurs with the finding of Erdos & Kiss (2019), analysed EU e-tax law and concluded that International taxation conflicts may

arise from the differences in tax systems due to problems of double taxation. In order to prevent the problem of double taxation, most countries have entered into Double Taxation Agreements (DTAs) with other countries. These double taxation agreements provide for a fair and effective tax sharing between source based and residence tax jurisdictions (Bruggen, 2019.). Under these double taxation agreements, profits are taxed based on the residence of the enterprise and not based on the source of revenues unless the profit is attributable to a permanent establishment in a source country in which case the profits are taxable in the place where the permanent establishment is situated.

Conclusion

The study concludes that the systematic challenges that are hindering Zimbabwe from enacting a broader digital tax policy are lack of information, lack of technology and the unilateral approach that Zimbabwe has taken in terms of the taxation of the digital economy. These challenges can be addressed however international co-operation is paramount.

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