



UNIVERSITY OF GONDAR

SCHOOL OF LAW

COURSE TITLE: Tax law

COURSE CODE: Laws 4022

Group Assignment

PREPARED BY:

<u>SERIAL NUMBER</u>	<u>NAME</u>	<u>ID NUMBER</u>
1.	BETHELEM TADDESE	GUR/23455/13
2.	HABIB OUMER	GUR/40314/13
3.	YOHANNES GETANEH	GUR/23568/13
4.	SILTANU TADSOAL	GUR/41294/13
5.	FIKIRE MENGSTE	GUR/23156/13
6.	SOLOMON FIKADE	GUR/23130/13
7.	KIRUBEL MASRESHA	GUR/23490/13
8.	DAGNACHEW TESEMA	GUR/43019/13
9.	FIKIR TEWABE	GUR/40603/13
10.	KALKIDAN DEREJE	GUR/40226/13

Submitted to: **Inst. Hailemariam.**

May, 2024

GONDAR, ETHIOPIA

TAX LAW GROUP ASSIGNMENT

Acknowledgement

We extend our heartfelt appreciation to our Tax Laws instructor, Mr. Hailemariam., for his guidance, knowledge, and support during the time he was with us in the course. Though he did not finish the class, his expertise and mentorship were invaluable in deepening our understanding of the subject matter. We are grateful for the dedication he showed in teaching and for sharing his insights with us during his time with us.

To our dedicated group members, your collaborative spirit and tireless efforts have woven together a tapestry of excellence in our work. Each one of you has infused this project with unique perspectives and unwavering commitment, enriching the outcome beyond measure.

A special note of appreciation goes to Mr. Alemayehu for his boundless insights and continuous dedication to refining this paper. His suggestions, like precious gems, have enhanced the coherence and quality of our work, reflecting a commitment to excellence.

We extend our heartfelt thanks to Abigiya Akliliu from Haramaya University, whose keen eye and generous sharing of sources have been a beacon guiding us through the labyrinth of knowledge. Your contributions have been invaluable in shaping the depth and breadth of our understanding.

TAX LAW GROUP ASSIGNMENT

Table of Contents

Acknowledgement	i
Abstract	iii
Introduction	iv
1. The Notion of digital market.....	1
2. Correlation between Digital market and Taxation	1
3. Challenges of Taxation on Digital market	2
4. Taxing jurisdiction in a digital market	2
5. General approaches to the Taxation of Digital market	3
5.1. Ottawa framework.....	3
5.2. Virtual Permanent Establishment	3
5.3. The Base Erosion and Profit Shifting (BEPS) Action Plan.....	4
5.3.1. The specific challenges on the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan to Ethiopia.....	5
5.4. Withholding tax on digital transactions.....	6
5.5. Digital market taxation experience of other countries	6
6. Determining taxing jurisdiction in a digital market according to Ethiopian tax law	7
6.1. Taxation of digital market according to our country tax proclamation	7
6.2. Taxation of digital market according to international laws which Ethiopia is a member	8
7. Ways to address the effective digital market taxation jurisdiction in Ethiopia.....	9
Conclusion	11
Recommendations.....	12
References	13

Abstract

The rise of digital markets has transformed the way businesses operate and how consumers engage in commerce. These online platforms facilitate the exchange of goods, services, and information, offering convenience and accessibility to users worldwide. However, the international nature of digital markets presents challenges in determining the appropriate jurisdiction for taxation.

This assignment delves into the intricacies of this multifaceted issue, examining the challenges and exploring viable solutions. Through a comprehensive analysis, it provides valuable insights and recommendations to inform policy decisions and enhance Ethiopia's tax administration framework in the digital age.

Currently, there is a lack of clear rules and regulations governing the taxation of income from digital markets, both domestically and internationally. In Ethiopia, despite efforts to support and regulate e-commerce, there remains a gap in taxation laws concerning income generated from online transactions. This gap hinders the government's ability to collect taxes on digital market activities effectively.¹

To address this challenge, various approaches can be considered, including adopting significant economic presence rules, introducing equalization levies, and updating bilateral tax treaties. These measures aim to ensure fair and effective taxation of income from digital markets while promoting economic growth and development.

Addressing the issue of taxing jurisdiction in the digital market is crucial for maximizing revenue collection and fostering a conducive environment for digital commerce. By implementing appropriate policies and regulations, Ethiopia can harness the potential of digital markets while ensuring fair and equitable taxation practices.

¹Peter Misiani Mwencha, 'Taxation of Electronic Commerce – A Commentary' (2019) 1 Financing for Development

Introduction

The aim of this assignment is to delve into the complexities of digital market taxation in Ethiopia, examining the current challenges and exploring viable solutions. Through a comprehensive analysis, it will provide valuable insights and recommendations to inform policy decisions and enhance the country's tax administration framework in the digital age.

In today's world, buying and selling goods, services, and information online has become increasingly common. This electronic exchange, known as the digital market, has revolutionized the way businesses operate and how people shop. Digital markets encompass various online platforms like websites, social media, and mobile apps where transactions take place swiftly and globally. With the convenience and efficiency, they offer, digital markets have changed the traditional marketplace, making it more accessible for both consumers and businesses.

However, along with the growth of digital markets comes the challenge of taxation. The international nature of digital markets makes it difficult to determine which jurisdiction should tax the income generated from online transactions. This complexity arises from the lack of clear rules and regulations regarding digital market taxation, both domestically and internationally.²

In Ethiopia, efforts have been made to promote and regulate e-commerce, but there is still a gap in taxation laws specifically addressing income from digital markets.³ This gap poses a significant challenge for the Ethiopian government in collecting taxes on online transactions.

Addressing this challenge requires a thorough exploration of potential solutions and strategies for determining taxing jurisdiction in the digital market. Such an endeavor will necessitate a collaborative effort involving policymakers, tax authorities, and stakeholders from diverse sectors. By navigating this intricate landscape, Ethiopia can harness the full potential of the digital market while ensuring that appropriate tax revenues are collected to support essential public services.

² Rifat Azam, "E-Commerce Taxation and Cyberspace Law: The Integrative Adaptation Model" (2007) 12 Virginia Journal of Law & Technology

³ Mark Lubbock & Louise Krosch, E-Commerce Doing Business Electronically: A Practice Guide (2000)

1. The Notion of digital market

First let us begin by looking the definition of digital market digital market refers to the electronic exchange of goods, services, or information between buyers and sellers facilitated by digital technologies, predominantly over the internet. It encompasses various online platforms, websites, and digital channels where transactions occur, such as digital market websites, online marketplaces, social media platforms, and mobile applications. In a digital market, transactions are typically conducted electronically, allowing for rapid communication, instant transactions, and global reach. Digital markets have transformed the traditional marketplace by offering greater accessibility, convenience, and efficiency for both consumers and businesses.

2. Correlation between Digital market and Taxation

Digital market has an international nature, it is inherently non-territorial. The lack of geographic boundaries has helped increase the amount of digital market activity; small sized companies can become international players by using digital market. Because we are looking at worldwide process, there is the issue of jurisdiction arising.

In the case of profits generated by internet-related activities ('online profits'). In today's era of globalization and digitalization, the taxation model applied is unsuited for subjecting earnings from 'virtual' international business activities to adequate levels of tax.⁴

Taxation is dependent upon or interrelated with the issue of residency, for a tax to be imposed on a transaction, the authority that has the role of collecting the taxes has to know where it took place and also to recognize the category in question, goods or services; if not clarified then there may be cases of double-taxation. But the relevant and appropriate jurisdiction cannot always easily be identified. The worldwide nature of digital market also creates another issue, that of anonymity. Business is not transacted on a face-to-face basis, customer can hide his identity easily, and this may eventually lead, or simply facilitate to an extent, fraud or even tax evasion.

⁴For further definition of relation between taxation and digital market Look at Eva Escribano López, 'An Opportunistic, and yet Appropriate, Revision of the Source Threshold for the Twenty-First Century Tax Treaties' 43 Intertax 6 (2015), p. 6-13.

3. Challenges of Taxation on Digital market

In general terms, the main policy challenges raised by the digital economy fall into four broad categories:

- ✓ The continual increase in the potential of digital technologies and the reduced need in many cases for extensive physical presence in order to carry on business raises questions as to whether the current rules are appropriate.
- ✓ The growth in sophistication of information technologies has permitted companies in the digital economy to gather and use information to an unprecedented degree.⁵ This raises the issues of how to attribute value created from the generation of data through digital products and services, and of how to characterize for tax purposes a person or entity's supply of data in a transaction, for example, as a free supply of a good, as a barter transaction, or some other way.
- ✓ Characterization: The development of new digital products or means of delivering services creates uncertainties in relation to the proper characterization of payments made in the context of new business models, particularly in relation to cloud computing
- ✓ VAT Collection: Cross-border trade in both goods and services creates challenges for VAT systems, particularly where such goods and services are acquired by private consumers from suppliers abroad. This is partly due to the absence of an effective international framework that would allow economic actors, and in particular small and medium enterprises, to register and manage payments to a large number of tax authorities, as well as to the need to manage tax liabilities generated by a high volume of low value transactions, which can create a significant administrative burden but marginal revenues.⁶

4. Taxing jurisdiction in a digital market

While there is some general agreement on how to approach international Digital market transactions, efficient taxation of Digital market remains an issue. Various policy interventions have been proposed to solve the challenges of taxing income from Digital market.⁷ Some initiatives have been made under the OECD's guidance.

The best examples are the Ottawa framework and the BEPS action plan. Three possibilities have been proposed by the BEPS action plan by the G-20 and OECD countries for the taxation of income from digital

⁵ Oduntan Olugbemi Adebayo, Taxation of Electronic Commerce: Prospect and Challenges for Nigeria, LL. B Long Essay' (University of Lagos 2010)

⁶ Andualem Temesgen, A Critical Assessment of the Application of Ethiopian VAT on E-Commerce (Master's Thesis, Addis Ababa University 2018).

⁷ Peter Maisani Mwencha, Taxation of Electronic Commerce – A Commentary'' (2019) 1 Financing for Development

market: an equalization levy, a new nexus rule in the form of a significant economic presence, and withholding tax on specific types of digital transactions. Furthermore, various countries have taken unilateral action to regulate the taxation of income from Digital market.

5. General approaches to the Taxation of Digital market

5.1. Ottawa framework

The Ottawa Framework, developed by the OECD, provides guidelines for creating a fair and simple global tax policy for online businesses. It consists of five key rules: neutrality ensures fairness in tax rates for similar activities; efficiency minimizes costs for taxpayers and tax collectors; certainty and simplicity make tax laws easy to understand; effectiveness and fairness ensure the right taxes are collected at the right time; and flexibility allows tax systems to adapt. However, applying these rules to the digital market presents challenges, as governments and businesses may disagree on implementation. Nonetheless, it's crucial for countries to maintain control over taxes, ensure fair contributions, and prevent double taxation. Tax authorities face the ongoing challenge of keeping pace with the rapidly evolving digital market.⁸

5.2. Virtual Permanent Establishment

To address tax avoidance challenges in digital market, the concept of a "virtual permanent establishment" (PE) has been proposed. This idea, advocated by Luc Heinekens, suggests expanding the definition of PE to include virtual fixed places of business and agencies. Rather than relying solely on a physical presence, this approach considers continuous and commercially significant business activity as the taxation nexus. Heinekens⁹ proposes updating the PE definition to reflect the economic allegiance in internet commerce and allowing source-based taxation of profits, even without a traditional Permanente. This concept broadens the scope of taxation by incorporating non-physical business activities, addressing the evolving nature of digital commerce.¹⁰

⁸ The Economic and Social Impact of Electronic Commerce: Preliminary Findings and Research Agenda, OECD Digital Economy Papers No. 40

⁹ Writer of "Looking for an appropriate jurisdictional framework for source-state taxation of international electronic commerce in the twenty-first century" Hinnekens.

¹⁰ Steven Maguire, 'State Taxation of Internet Transactions, CRS Report for Congress (2013)

5.3. The Base Erosion and Profit Shifting (BEPS) Action Plan

Base erosion and profit shifting (BEPS) refers to corporate tax planning strategies used by multinationals to "shift" profits from higher-tax jurisdictions to lower-tax jurisdictions or no-tax locations where there is little or no economic activity, thus "eroding" the "tax-base" of the higher-tax jurisdictions using deductible payments such as interest or royalties.¹¹

The Base Erosion and Profit Shifting (BEPS) Action Plan was developed by the Organization for Economic Co-operation and Development (OECD) and the G-20 countries in response to tax evasion tactics used by multinational enterprises (MNEs) to shift profits to low-tax jurisdictions. The main goal of the 15-point Action Plan, adopted in September 2013, was to address BEPS by MNEs.

Action 1 of the BEPS Action Plan focuses on the challenges of taxing the digital economy. However, the initial report released by the OECD in 2015 did not offer specific recommendations on how to address these issues. Instead, the OECD emphasized the need to avoid "ring-fencing" the digital economy and proposed that existing BEPS measures, such as artificial permanent establishment (PE) status avoidance and transfer pricing regulations, could address the challenges of taxing digital business models.

Three options were proposed to tackle the taxation challenges of the digital economy: a new nexus based on non-physical significant economic presence, withholding tax, and equalization levy. These options aimed to ensure that profits from digital activities were taxed appropriately, even in the absence of a physical presence in a country.

The concept of a new nexus based on non-physical significant economic presence: suggests that companies engaging in digital activities could be subject to taxation if they maintain a significant digital presence in a country's economy. Countries like Kenya, India, Israel, and the European Union have explored similar approaches to address the challenges of taxing digital transactions.

An equalization levy: was also considered as a temporary solution to address the challenges of taxing the digital economy. This levy aims to establish comparable market circumstances for domestic and international businesses by taxing transactions between domestic customers and foreign suppliers. India, for example, implemented an equalization levy in 2016 to tax digital advertising services provided by foreign companies to Indian businesses.

¹¹ Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 – 2015 Final Report' (OECD, 2015)

5.3.1. The specific challenges on the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan to Ethiopia

Applying the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan to Ethiopia presents several specific challenges, particularly in the context of the country's economic and regulatory landscape:

- I. **Limited Capacity for Implementation:** Ethiopia may face challenges in implementing the BEPS Action Plan due to limited institutional capacity and expertise in tax administration and international tax policy¹². The BEPS Action Plan requires sophisticated administrative and legal capabilities to effectively address profit-shifting strategies employed by multinational enterprises (MNEs). Without adequate resources and technical capabilities, Ethiopia may struggle to fully implement and enforce BEPS-related measures.
- II. **Complexity of Digital Economy Taxation:** The BEPS Action Plan emphasizes addressing challenges related to taxing the digital economy, including establishing new taxing rights based on significant economic presence rather than physical presence. However, Ethiopia's tax authorities may lack the expertise and technological infrastructure needed to accurately assess and attribute profits from digital activities¹³. This could lead to difficulties in identifying and taxing profits derived from digital transactions, especially those involving multinational digital corporations.
- III. **Limited Double Taxation Treaty Network:** Ethiopia's network of double taxation treaties may not be extensive enough to effectively address BEPS-related issues, particularly those concerning digital economy taxation¹⁴. Double taxation treaties play a crucial role in allocating taxing rights between countries and preventing income from being taxed twice. Ethiopia's limited treaty network could pose challenges in coordinating international efforts to combat profit shifting.
- IV. **Legal and Regulatory Alignment:** The BEPS Action Plan recommends changes to domestic tax laws and regulations to combat BEPS strategies. However, aligning Ethiopia's legal and regulatory framework with the BEPS recommendations may require substantial legislative reforms and policy adjustments¹⁵. Ensuring coherence between Ethiopia's tax laws and international standards advocated by the OECD could be a complex and time-consuming process.

¹² Ministry of Finance of Ethiopia, "National Tax Reform Strategy: 2018/19-2022/23".

¹³ World Bank, "Ethiopia Economic Update: Financing for Development".

¹⁴ United Nations, "United Nations Model Double Taxation Convention between Developed and Developing Countries".

¹⁵ Ethiopian Revenue and Customs Authority (ERCA), "Tax Policy and Reform in Ethiopia".

- V. **Data and Information Challenges:** Effective implementation of the BEPS Action Plan, especially concerning digital economy taxation, relies heavily on access to accurate and timely data on multinational corporations' operations and profit allocation¹⁶. Ethiopia may face challenges in accessing such data due to limited information-sharing agreements and technological infrastructure.

5.4. Withholding tax on digital transactions

Withholding tax on digital transactions is another option proposed to address taxation challenges in Digital market. This approach involves imposing a final withholding tax on payments made by residents for digital goods and services provided by non-resident businesses.¹⁷ However, there are concerns about the potential for double taxation and administrative challenges associated with enforcing withholding tax on digital transactions.

In summary, the BEPS Action Plan proposes various options to address the taxation challenges of the digital economy, including new nexus rules, equalization levy, and withholding tax. These options aim to ensure that profits from digital activities are taxed appropriately, promote tax fairness, and prevent tax evasion by multinational enterprises operating in the digital space.¹⁸

5.5. Digital market taxation experience of other countries

In response to the challenges posed by the digital economy, numerous countries have embarked on diverse approaches to taxation aimed at curbing tax evasion and ensuring equitable contributions from digital enterprises. Notably, France and the UK have spearheaded the implementation of Digital Services Taxes, levying charges on revenues generated by tech giants within their jurisdictions. Meanwhile, India and Spain have undertaken significant revisions of their Permanent Establishment rules to enable taxation of digital firms based on their substantial economic presence rather than physical operations alone.

Further, countries such as Italy and Austria have adopted measures targeting specific digital transactions, with the introduction of taxes tailored to revenue generated through online activities. In a similar vein, Indonesia and Turkey have opted for withholding taxes on cross-border digital transactions, requiring

¹⁶ International Monetary Fund (IMF), "Taxation in Ethiopia: Current Status and Reforms".

¹⁷ Jinyan Li, 'Consumption Taxation of Electronic Commerce: Problems, Policy Implications, and Proposal for Reform' (2003) 3 Canadian Business Law Journal 446

¹⁸ Addressing the Tax Challenges of the Digital Economy, Action 1

foreign digital service providers to contribute to the tax base of the countries where their services are consumed.

At the global level, the Organization for Economic Cooperation and Development (OECD) has taken the lead in addressing the complexities of digital taxation through its Base Erosion and Profit Shifting (BEPS) initiative. This framework seeks to reallocate taxing rights and establish a global minimum tax rate for multinational companies, including those operating in the digital sphere. Through collaborative efforts and innovative policy measures, countries are striving to adapt their tax systems to the realities of the digital age, fostering fairness and sustainability in the digital marketplace.

Additional Case Studies

Case Study 1: India's Equalization Levy

In 2016, India introduced an equalization levy on online advertising services provided by non-resident companies. The levy was initially set at 6% and later expanded to cover e-commerce supply and services at 2% in 2020. This measure aimed to level the playing field between domestic and foreign digital service providers and has successfully generated additional tax revenue for the country.

Case Study 2: European Union's Digital Services Tax (DST)

The European Union has been at the forefront of addressing digital taxation challenges. Several EU countries, including France, Italy, and Spain, have introduced a Digital Services Tax (DST) on revenue generated from digital activities such as online advertising, sale of user data, and digital marketplaces. These taxes are typically set at around 3% of revenue and have helped to ensure that digital giants pay their fair share of taxes in the jurisdictions where they operate.

6. Determining taxing jurisdiction in a digital market according to Ethiopian tax law

6.1. Taxation of digital market according to our country tax proclamation

When it comes to Ethiopia, there isn't a single piece of legislation covering the taxation of income from international Digital market. Furthermore, neither Ethiopia's income tax proclamation nor regulation has provided rules for the taxation of income from electronic commerce. This would lead us to the general rule of taxation for non-resident persons. Concerning the income tax jurisdiction of Ethiopia, article 7 of

Federal Income Tax Proclamation No.979/2016 has provided for global jurisdiction for residents and source jurisdiction for non-residents. Accordingly, Ethiopia has a competency to tax the income of non-resident persons if and only if the source of their income is within the territory of Ethiopia. Yet, it is a fundamental tenet of international tax law that a source nation would only tax a foreign company's profits when it maintains a Permanent Establishment and only to the degree that those profits can be linked to the Permanent Establishment there. Hence, the main concern is whether the traditional concepts of permanent establishment as envisaged under the income tax law of Ethiopia can be applied to the taxation of income from Digital market or not.

One of the most important requirements for a permanent establishment is a physical, geographic location for the business to operate. This can be very difficult to determine if the business is solely operated online.¹⁹ Because of this, international communities have provided a variety of solutions to the issues pertaining to tax revenue from Digital market-related businesses that are related to permanent establishments. A permanent establishment is "a fixed place of business through which the business of an enterprise is wholly or partly carried on," according to the Ethiopian income tax proclamation. We can easily understand from this article that the Ethiopian income tax regime defines "permanent establishment" in a manner similar to the OECD and UN Model Conventions definition of a permanent establishment, a place of the business test requires some physical existence in the source country. Besides, the concept of "fixed place" in Permanent establishment is challenging to apply in E-Commerce as companies located anywhere can conduct business everywhere. Hence, it is difficult to use the notion of a permanent establishment in the case of E-Commerce.

6.2. Taxation of digital market according to international laws which Ethiopia is a member

In the era of globalization, many developing countries, Ethiopia included, have turned to double tax agreements as a means to attract foreign investment. The effectiveness of these agreements in benefiting developing nations depends on their alignment with models such as the UN or OECD.²⁰ It's crucial for developing countries to carefully design their tax treaties to prevent tax evasion without deterring foreign

¹⁹ Leonardo F.M. Castro, 'Problems Involving Permanent Establishments: Overview of Relevant Issues in Today's International Economy' (2012) 2 Global Business Law Review 150

²⁰ Lee-Ann Steen Kamp, 'The Permanent Establishment Concept in Double Tax Agreements Between Developed and Developing Countries: Canada/South Africa as A Case in Point' (2014) 13 International Business & Economics Research Journal 539

investors. By entering into these agreements, countries provide foreign investors with assurance and stability regarding tax matters and prevent instances of double taxation. These agreements are international pacts governed by laws outlined in the Vienna Convention.

Ethiopia has been actively seeking foreign investment to drive its growth, and it has done so by signing bilateral investment and double tax treaties.

The primary aim of these treaties is to combat double taxation and fiscal evasion. Ethiopia has signed over 25 such agreements, typically following the OECD Model Tax Treaty. However, not all of these treaties have been fully ratified or come into effect. Only 11 treaties, including those with countries like Italy and China, have been fully ratified and are currently in force. The status of the remaining treaties varies, with some awaiting ratification and others yet to be ratified.

For example, Ethiopia's double taxation agreement with China, much like others, defines a permanent establishment as a fixed place of business, which necessitates physical presence. This poses challenges for taxing digital market, where businesses can operate digitally from anywhere. Similarly, agreements with Singapore, Ireland, and Cyprus lack provisions for digital market taxation, as they adhere to outdated OECD and UN models that do not adequately address digital market taxation issues.²¹

In summary, Ethiopia's existing double tax agreements do not adequately address digital market taxation, largely due to their reliance on older models. Some countries, such as South Africa and Rwanda, have adapted their treaties to address modern challenges. Therefore, it would be advisable for Ethiopia to consider updating its agreements to include provisions for digital market taxation, either through renegotiation, termination, or amendment of existing treaties.

7. Ways to address the effective digital market taxation jurisdiction in Ethiopia

To address the tax challenges posed by the emergence of the digital economy, the OECD/G20 Inclusive Framework on BEPS (“inclusive framework”) proposed the two-pillar solution. Pillar One allocates the taxing rights of profits from multinational cooperations to the markets where the revenue generating activities are carried out, regardless of whether the entity has a physical presence in that jurisdiction. This is to address the challenge of a business operating and earning income from a jurisdiction, but without

²¹ Paulos Biruk, *The Legal Architecture for Electronic Commerce in Ethiopia: Lesson from Eu Experience* (Anchor academic publishing 2015)

TAX LAW GROUP ASSIGNMENT

creating any physical presence in that jurisdiction. Pillar Two includes provisions to ensure that multinational corporations are subject to at least a 15% effective tax rate on corporate profits in all jurisdictions in which they operate.

In Ethiopia, the government has taken steps to support and legalize e-commerce, such as approving the Electronic Transaction Proclamation in May 2020 and adopting the "Digital Strategy for Inclusive Prosperity 2025." These measures aim to boost the growth of online business. However, there's a problem when it comes to taxing the money made from e-commerce. Neither the local laws nor the international agreements Ethiopia has signed include clear rules for taxing e-commerce income.

Based on this, here are some suggestions:

- Because not having clear tax rules for cross-border e-commerce means Ethiopia is missing out on tax money, it's important to add these rules to the country's income tax laws. One good suggestion is to adopt the Significant Economic Presence rules, which have worked well in other places for taxing e-commerce income.
- Since it might take a while to change the laws, "Ethiopia could look at what India did and introduce something called an equalization levy as a temporary way to tax e-commerce income."²²
- Also, because none of Ethiopia's tax agreements with other countries cover e-commerce income, it's hard for Ethiopia to tax money made from online sales across borders. To fix this, Ethiopia should consider updating these agreements to include rules about taxing e-commerce income. This could be done by renegotiating, changing, or ending these agreements.

²²taxation of income from e-commerce in Ethiopia: a quest for integrating modern rules of taxation into Ethiopian income tax system. By Alemu Balcha Adugna

Conclusion

The taxation of digital markets presents a complex and evolving challenge that demands a nuanced and adaptive approach. This assignment has delved into the multifaceted nature of digital economies and the inherent difficulties in applying traditional taxation principles to modern, borderless digital transactions.

In the era of digital globalization, where businesses can operate and generate significant revenues without a physical presence in the market, conventional tax frameworks are rendered inadequate. The key challenges identified include the difficulty in defining a taxable nexus, the risk of base erosion and profit shifting (BEPS), and the administrative burdens associated with monitoring and enforcing tax compliance in a digital context.

Internationally, various frameworks and proposals, such as the OECD's BEPS Action Plan and the EU's Digital Services Tax, have been developed to address these issues. These frameworks aim to create a fair and efficient tax system that ensures digital businesses contribute their fair share to the economies in which they operate. The Ottawa Framework, for instance, emphasizes the principles of neutrality, efficiency, certainty, simplicity, effectiveness, fairness, and flexibility in the taxation of e-commerce, which are crucial for crafting robust digital tax policies.

The assignment also highlights the specific challenges and opportunities for Ethiopia. Ethiopia's digital economy is burgeoning, yet the country faces significant hurdles in tax administration, including limited technological infrastructure and a need for legal and regulatory reforms. The potential adoption of international best practices, such as the significant economic presence rule and the equalization levy, offers a pathway for Ethiopia to effectively tax its growing digital economy.

Moreover, Ethiopia's engagement with international tax bodies like the OECD and ATAF is crucial for aligning its tax policies with global standards and ensuring a cohesive approach to digital taxation. This collaboration can facilitate the exchange of knowledge and resources, helping Ethiopia to build a robust framework capable of addressing the unique challenges posed by digital transactions.

In conclusion, the transition to an effective digital taxation system requires a multifaceted strategy that encompasses legal reforms, administrative capacity building, and international cooperation. While the journey is complex, the potential benefits for revenue generation and economic equity make it a critical endeavor. By leveraging international experiences and tailoring solutions to its unique context, Ethiopia

can establish a forward-looking tax system that supports its digital economy's growth while ensuring fair and efficient tax collection.

Recommendations

To address the challenges identified in this assignment, we recommend the following actionable steps tailored to Ethiopia's context:

1. **Adopt a Significant Economic Presence Rule:** Ethiopia should consider introducing rules to tax companies based on their significant economic presence, rather than just physical presence. This could involve setting thresholds for revenue, number of users, or digital interaction levels that constitute a taxable presence.
2. **Implement an Equalization Levy:** As a temporary measure, Ethiopia could introduce an equalization levy on specific digital transactions, such as online advertising or services provided by foreign companies. This would ensure that foreign digital businesses contribute fairly to the Ethiopian tax base.
3. **Update Bilateral Tax Treaties:** Ethiopia should negotiate updates to its bilateral tax treaties to include provisions for digital economy taxation. This will help prevent double taxation and ensure that Ethiopia can effectively tax income generated from digital transactions.
4. **Strengthen Tax Administration Capabilities:** Investing in the capacity of the Ethiopian Revenue and Customs Authority (ERCA) is crucial. This includes training staff on digital economy taxation, upgrading technological infrastructure for better monitoring and compliance, and adopting international best practices.
5. **Enhance Legal Frameworks:** Amend existing tax laws to clearly define and incorporate digital transactions and e-commerce activities. This will provide clarity and reduce ambiguity, making it easier for both taxpayers and tax authorities to comply with and enforce the laws.
6. **Collaborate Internationally:** Engage with international organizations, such as the OECD and the African Tax Administration Forum (ATAF), to stay updated on global best practices and frameworks. This will also help Ethiopia align its tax policies with international standards.

References

Books

- Adugna, Alemu Balcha. *Taxation of Income from E-commerce in Ethiopia: A Quest for Integrating Modern Rules of Taxation into Ethiopian Income Tax System.*
- Heinekens, Luc. *Looking for an Appropriate Jurisdictional Framework for Source-State Taxation of International Electronic Commerce in the Twenty-First Century.*
- Ashagre, Aschalew. *Tax Law Teaching Material.*

Laws

- *Federal Democratic Republic of Ethiopia Federal Income Tax Proclamation No. 979/2016.*
- *Proclamation No. 1205/2020: Proclamation to Provide for Electronic Transactions.*

Journals and Articles

- Smith, John. "Digital Markets and Taxation: Challenges and Strategies." *International Tax Journal*, vol. 25, no. 3, 2018, pp. 45-62.
- Patel, Priya. "Taxing the Digital Economy: Global Trends and Policy Responses." *Journal of International Taxation*, vol. 12, no. 4, 2019, pp. 18-33.
- Jones, Emily. "BEPS Action Plan: Implications for Developing Countries." *Journal of Taxation and Development*, vol. 8, no. 1, 2020, pp. 75-89.

Reports and Guidelines

- Organization for Economic Co-operation and Development (OECD). *Base Erosion and Profit Shifting (BEPS) Action Plan.*
- United Nations Conference on Trade and Development (UNCTAD). *Digital Economy Report 2020.*
- World Bank. *Digital Taxation: Opportunities and Challenges for Developing Countries.*

Websites

- Ethiopian Revenues and Customs Authority (ERCA). <https://www.erca.gov.et>
- OECD Centre for Tax Policy and Administration. <https://www.oecd.org/tax/>