HM Treasury

Online sales tax:

Assessing an option to help rebalance taxation of the retail sector

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Foreword

Over the last two years the retail industry has – under the most difficult circumstances – provided an essential service to the public and kept households and businesses supplied with the goods they needed. But the pandemic took a toll on our high streets, with a rapid decline in footfall. The government responded, safeguarding businesses and jobs with a wide range of economic support through the pandemic to date. This includes exceptional tax relief for retail, hospitality, and leisure businesses. Longer term challenges do, however, remain.

The pandemic accelerated trends already underway, including a rapid growth in the proportion of shopping carried out online. Some have suggested that the tax system exacerbates the challenges faced by the in-store retail sector. The government recently completed a Review of Business Rates which led to £7 billion of support to reduce the burden of rates over the next five years and brought about reforms which will make the system fairer. The review concluded that the business rates system should not be ripped up, as rates fund vital local services and there is no alternative with widespread support that would raise sufficient revenue to replace them.

Some stakeholders have called for an online sales tax (OST) that could be used to rebalance the tax system, funding business rates relief for the retail sector. Given the significant changes in the retail market and shift online, it is right that the government reassesses the taxation of this sector. The government would like to consider further the case for and against implementing such a tax, including the role it could play in addressing challenges identified by stakeholders. It will be important to assess the effects on consumers and businesses before deciding whether to proceed with an OST.

If an OST were adopted, its design would not be straightforward. Distinguishing between online and offline activity presents a growing challenge. The government would like to hear from businesses on several central questions including which transactions would be taxable; the different forms an OST could take; and how to define an online sale reflecting the range of transaction, delivery, and collection options.

The government recognises that an array of business models operate in UK retail – a mark of the vibrant and innovative sector – and this will lead to a diverse range of opinions. Some retailers with a stronger bricks and mortar presence consider that their sector is overburdened by business rates relative to online competitors. Others view the growing market share of online retail as a signal of consumer choice and innovation which should not be subject to an increased tax burden. Many businesses operate both in-store and online. The government wants to review the evidence in the round.

Technological change, innovative business models, and evolving consumer choice have for generations changed the face of our towns and cities, transforming the way we live. The government recognises the value of vibrant high streets and town centres to local communities as places to live, work, and visit. Town centres have evolved continuously, and the government does not intend to disrupt innovative businesses; however, it is important to remain responsive. Through this consultation the government is considering one proposal that is attracting increasing attention and we look forward to receiving your input.

Chapter 1
Introduction

1.1 The government recently conducted a Review of Business Rates which concluded with a Final Report published at Autumn Budget 2021. The objectives of that review were to reduce the overall burden on businesses, improve the current system, and consider more fundamental changes over the medium- to long-term. One output of that review was to consult on the case for and against introducing a new tax on online sales. The government is now doing so with this consultation.

The changing business landscape

1.2 In some respects, the pandemic brought into greater focus longer-term trends affecting the retail sector. Innovative new business models and the rapid pace of technological change are transforming the way consumers shop. As a proportion of all retail sales, online shopping rose from about 3 per cent in 2006 to about 22 per cent in March 2020, on the eve of the pandemic[1].

1.3 The pace of change has accelerated since early 2020 on account of the pandemic. The proportion of retail sales conducted online rose sharply in the first half of 2020 and again during subsequent lockdowns. Whilst the easing of social distancing restrictions has seen the share of online shopping fall somewhat, it remains significantly above pre-pandemic levels[2]. Footfall, similarly, recovered markedly through 2021 but remains below its pre-pandemic level[3]. Innovation in the retail sector has been essential in supporting households through the pandemic and brought longer-term benefits including higher productivity, improved choice, and convenience. Change has, however, put pressure on retailers serving communities across the country.

1.4 In addition to changing consumer preferences and market dynamics, there are concerns among retailers with physical retail premises that they face an unfair tax burden. This, it is argued, is because they are typically subject to a higher level of business rates than their online competitors, who tend to have a business model that involves lower commercial rents and correspondingly lower rates burdens. This argument is typically focussed on the costs of rent and rates, and does not consider relevant any higher costs

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1 Internet sales as a percentage of total retail sales (ratio) (%) - Office for National Statistics (ons.gov.uk)

2 Impact of the coronavirus (COVID-19) pandemic on retail sales in 2020 - Office for National Statistics (ons.gov.uk) ; Internet sales as a percentage of total retail sales (ratio) (%) - Office for National Statistics (ons.gov.uk)

3 UK Footfall Daily Index | Institute of Place Management

associated with online retail models compared to high street equivalents, such as delivery networks, marketing, or warehousing technology.

Does the tax system need to respond?

1.5 The government's recent review concluded that business rates have a number of key advantages over other taxes. Business rates raise over £25 billion a year in England to fund vital local services. Trying to raise that amount elsewhere in the tax system would come with significant trade-offs, involving substantial increases to other taxes. There is no alternative with widespread support that would raise sufficient revenue to replace business rates in their entirety. For example, raising comparable amounts under the VAT system would require around a 3-4p increase to the standard rate. Similarly, around a 5p increase to the basic rate of Income Tax would be required to raise a similar amount.

1.6 However, the government recognises the challenges facing the retail sector and has provided an unprecedented £16 billion of relief to these businesses throughout the pandemic. At Autumn Budget 2021, the Chancellor also announced a new, temporary relief for the retail, hospitality, and leisure sectors to help high street businesses to evolve and adapt to changing consumer demands until the next revaluation. This support is worth almost £1.7 billion to businesses in 2022-23.

1.7 For business rates, the distribution of the tax is set through revaluations, which periodically reassess and update individual liabilities to reflect changes in the rental market. This helps to ensure that, where shifts in economic activity have driven changes in underlying market values, these changes are fairly reflected in business rates liabilities. The last revaluation took place in 2017, based on rateable values from 2015.

1.8 There has been substantial economic change since 2015, even before the unprecedented shock of COVID-19. The long-term economic effects of the pandemic remain uncertain, but pre-existing trends toward a more digital economy may have been accelerated. The next revaluation will capture the change that has occurred in market conditions and adjust rateable values accordingly. It is too early to tell what the result of that revaluation will be, and the government will consider the impact in the Autumn of 2022 once revaluation outcomes are known.

1.9 The government's commitment to moving to more frequent, three-yearly revaluation cycles represents a fundamental, meaningful improvement in the business rates system, helping to ensure greater distributional fairness and that business rate liabilities are more responsive to changing market conditions.

1.10 Some stakeholders have, however, called for more comprehensive reform. One suggestion is to increase tax on online shopping to fund retail rates relief and thus rebalance the tax system, which some view as unduly skewed against bricks-and-mortar retail. As part of the Business Rates Review Call for Evidence in 2020, the government invited stakeholders to comment on the benefits and risks of such a measure, in the form of an online sales tax (OST).

1.11 OST proponents argue that in-store retailers pay a disproportionate share of business rates. Some retailers argue this makes bricks-and-mortar business models less competitive. Others argue that the existing evidence does not conclusively show business rates to be a major driver in the shift from in-store to online retail, a shift that has been seen globally, including prior to the pandemic[4]. If change is being driven by other factors including technological development and consumer preferences, a new tax – even if coupled with additional relief for in-store retail – would be unlikely to reverse the shift to online. Meanwhile, there is concern that business rate reductions are likely to increase the rent expected for the property, limiting the long-term benefit to in-store retailers which are not the owners of the property they occupy. We would like to explore the evidence surrounding all of these issues in this consultation.

Interactions with international tax reform

1.12 It is important to draw a distinction between the proposal for an OST and the Digital Services Tax. The Digital Services Tax is a tax on revenues from certain digital services, including social media, search engines, and online marketplaces. It is a temporary solution to the challenges posed by digitalisation to the international system for taxing corporations' profits. Negotiations amongst the G20 and the 141 countries of the OECD Inclusive Framework have concluded a landmark agreement to update international corporate tax rules. As part of that agreement the government, along with other countries with similar measures, has agreed to transition away from its Digital Services Tax to a new global tax system when that system becomes operational. The Digital Services Tax will therefore be removed once a solution from "Pillar 1" of the OECD agreement is in place.

1.13 An OST, on the other hand, has been proposed by stakeholders with concerns that the burden of business rates falls disproportionately on retailers with more valuable physical property, rather than on growing online retailers with a lighter, or less valuable, property footprint. If implemented, an OST would be used to reduce business rates for retailers with properties in England and fund the block grants of the devolved administrations in the usual way.

Tax policy principles

1.14 When assessing the case for an OST, as with all tax policy, the government will consider a number of core principles. Tax policy should be: sustainable in view of long-term trends; efficient by incentivising economic growth and minimising distortionary impacts on markets; applied fairly, reflecting the ability to pay; simple, with costs of compliance and collection kept to a minimum; and predictable, allowing businesses and individuals to plan for the future in a stable policy environment.

Purpose of this consultation

1.15 The proposal of an OST, put forward by numerous stakeholders, is attracting increasing public attention. The government has not at this stage decided to

[4] tn_unctad_ict4d18_en.pdf

proceed with an OST or determined the precise design and scope of such a tax were it to be implemented. In this consultation the government would like to test the arguments for and against an OST.

1.16 The government does not see the proposal as a measure to discourage consumers from shopping online. An OST is instead being considered as a measure to raise revenue from the increasing volume of online retail in the UK, with that revenue used to fund a reduction in business rates for retail properties. It is worth noting that an OST levied at 1% or 2% would not raise sufficient revenue to replace in full the business rates levied on retailers.

1.17 Business rates are devolved, so reductions funded by the introduction of an OST would apply to England-only. An OST applied only to sales in England could be burdensome for businesses, requiring them to identify orders by jurisdiction. Additional complexity could result if the Devolved Administrations had similar taxes. Accordingly, if implemented, the government expects an OST would be a UK-wide tax. It would be used to fund business rate relief, which would apply to England-only, and fund the block grants of the devolved administrations in the usual way.

1.18 In order to reach a judgement on the suitability of an OST to fund a reduction in retailers' business rates, a number of practical design questions would need to be considered. These include:

- Which goods and services would be in-scope of the tax?
- How does one define an online sale and should this extend to 'remote' sales made by phone or post?
- What would be the distinction between a reservation and a completed transaction for the purposes of an OST?
- Would any exemptions be appropriate, such as for click and collect purchases or for certain goods and services?
- At what point in the transaction would an OST be levied – consumer, or vendor? And what would be the role of intermediaries such as marketplaces?
- What would be the territorial scope of an OST and how would cross-border sales be treated?
- Would a threshold or allowance be appropriate to account for smaller firms or those with a lower proportion of sales made online?
- How would an OST be reported to tax authorities and what would the payment schedule be? And what data and systems would be required?

1.19 In each case, drawing a distinction between supplies or transaction types would require careful consideration to reduce the risk of distortions or avoidance opportunities. In some cases, certain policy choices would inevitably lead to challenging definitions (for example on the treatment of click and collect or defining certain types of goods if they were to be exempt). This consultation is designed to draw out those design questions and seek input from stakeholders.

1.20 The government would also like to consider the impacts of an OST, including how the various policy decisions described above would alter the impact on different businesses. Chapter Four explores these in more detail, including the revenue an OST would raise for the exchequer; the resulting shape of business rate relief that might be possible; the impact on innovation and online retail in the UK; the distributional impacts of an OST; and environmental considerations.

1.21 This consultation is designed to inform the government's assessment of the identified issues. We invite responses on whether there should be an OST to fund a reduction in business rates for in-store retail and, if so, how various design questions should be approached. We invite respondents to comment on each of the questions set out in the following chapters, and to include in their responses any further thoughts that are otherwise not covered.

1.22 The consultation will be open for 12 weeks, closing on 20 May 2022. The government will then assess the responses and make further announcements on the path forward. We welcome responses from a wide range of interested stakeholders to ensure future policy decisions are well informed. Note that responses may be made public after the consultation closes, and may be subject to disclosure under the Freedom of Information Act.

Chapter 2
Scope

2.1 The boundary between online and offline activity is increasingly difficult to identify. There is evidence that the pandemic has accelerated existing trends in the direction of greater diffusion of online technology even in traditionally in-person industries like vehicle sales and cafeterias. Determining the scope of an OST would, therefore, be challenging.

2.2 The government would need to determine which forms of sale should be covered. For example, whether an OST would apply to transactions conducted over the internet in any form (including, for example, in-store purchases made via an app) or transactions carried out via any remote technology (including, e.g. telephone and mail order). The rationale for the tax put forward by proponents – that in-store retail is disproportionately burdened by business rates – would suggest the kind of properties typically used by different models would be a central determining factor in deciding taxable transactions. Decisions would also need to be taken on the complex distinction between goods and services, and the appropriate treatment of each under an OST.

2.3 A tax with fewer exemptions would generally be simpler for businesses and government to administer, reduce opportunities for avoidance, and raise greater revenue. However, a broader scope might test the boundaries of what is considered an online sale. This chapter explores the issues and options in setting scope when considering an OST.

Defining taxable sales

2.4 When assessing the case for an OST it is necessary to determine which sales would be subject to the tax. The definition would need to be transparent and easily understood so that it was straightforward for taxpayers to work with. It would also need to have a consistent impact on different business operating models selling via the same channels. The government seeks views on how this would best be achieved.

Online only or remote sales approach

2.5 An OST would be used to rebalance the tax burden between sales conducted in-store and those that are conducted remotely, where businesses do not have the same business rates burden that in-person retail premises will have. There is a range of ways that sales or orders can be negotiated and agreed without relying on high-value premises. These 'remote' sales include those made through:

- websites

- apps
- instant messenger services
- email
- fax
- phone
- mail-order

2.6 Stakeholders may consider that the policy rationale behind an OST could apply to justify bringing all ‘remote’ sales into scope of the tax, covering the full spectrum of technologies above.

2.7 Alternatively, stakeholders may think an online sales tax would need to apply to internet sales only, which would require this to be defined. Setting this definition would be difficult. The approach of looking at sales concluded over the internet would cover orders made through an online retailer website or app as expected, but might also capture orders made in-store through apps on customer mobile devices or sales through terminals in-store.

2.8 Orders concluded via the internet may also be considered to include orders made by email or instant messenger but would not be expected to include orders made by phone. However, automated phonelines through which sales can be made share some relevant characteristics with online sales, such as scale and automation. In addition, voice-enabled apps and devices would enable placing orders by simple voice commands over the internet making a distinction between internet and telephone ordering more difficult to justify.

2.9 Whether the definition was based on remote sales or around online, internet-mediated sales (referred to as online sales for the remainder of this section), an OST would require coherent definitions to be drawn to consistently delineate taxable transactions. Any narrowing from the broadest remote sales scope may give rise to distortions and opportunities for avoidance, which would point towards taking a wider view.

2.10 A suitable definition would provide the same tax outcome for economically equivalent transactions as far as possible. The Organisation for Economic Co-operation and Development (OECD) definition of an e-commerce transaction provides an example of a coherent definition: "the sale or purchase of goods or services, conducted over computer networks by methods specifically designed for the purpose of receiving or placing of orders.” Under this definition, the emphasis is on the method of ordering goods or services, but the payment and the ultimate delivery of the goods or services do not have to be conducted online.

Other factors in defining an online sale

2.11 For the purposes of considering an OST, the definition could similarly focus on the method of ordering, or it could make a distinction based on the other factors such as extent of in-person interaction or timing of the sale.

2.12 One factor is the extent of in-person interaction during the course of a transaction. Within a single customer shopping journey culminating in an order, there may be both online and in-store interactions. For example, a customer might test different products in a showroom before ordering them online from home, or the customer might make the order at home online before collecting the product from a local store.

2.13 Other related factors could be the method of payment and structure of a transaction. Consider scenarios where sales are made involving any of the following:

- online reservation with payment in-store on collection
- online order with payment on delivery
- items bought on store credit accounts, with monthly invoicing
- hire purchase agreements
- personal contract purchase or personal contract hire

2.14 The point at which a sale is completed may depend on how a given transaction is structured, but lead to substantially the same economic result. There is a risk that such differences could lead to different taxable outcomes. In some of these circumstances, the outcome might only affect the timing of when sales may be in scope. In other instances, the transaction structure may result in the sale being excluded from an OST altogether while fundamentally similar transactions remained taxed. This could lead to distortions.

Question 1: Would you favour a tax for all 'remote' sales or just the subset of 'online' sales?

Question 2: How should taxable sales be defined and what would the practical implications be?

Question 3: Are there transactions that would be particularly difficult to classify as either online or remote? What are these and how should these be addressed?

Click and collect

2.15 The arguments around the cost of premises for online and in-store retail apply differently to purchases which are collected in-store. Such purchases rely on access to a conveniently located retail space and may continue to generate footfall in physical shops. Some advocates of an OST have called for click and collect sales to be exempted on these grounds.

2.16 However, this argument does not apply to the same degree to all click and collect transactions. The connection to expensive retail space is less strong, for example, in the case of a locker in a transport hub compared to collection from a high street store. An exemption for all click and collect orders could lead to similar transactions – delivery to a residential address versus collection from a locker on a street corner – being treated differently.

2.17 Click and collect models are diverse and could include any of the following, not all of which clearly relate to the rationale for excluding click and collect models from an OST:

- A reservation made online with payment and completion of the transaction in-store
- Orders made online and collected from the premises at which the order was fulfilled (e.g. supermarket where items are picked from the shelves)
- Orders fulfilled at another property owned by the business (e.g. a warehouse) before being transferred to a separate site for collection
- Collection from third-party locations (e.g. from the premises of another business such as a local corner shop)
- Collection from unstaffed lockers, including lockers in non-retail locations
- Orders made over the internet and collected almost instantly from a store location (e.g. coffee shops with an online pre-ordering system)
- Orders made within a store and collected almost instantly (e.g. retailers with installed computer terminals)

2.18 An exemption would require either exempting all of these models, not all of which will seem to be "click and collect", or making a distinction between these different models, which could lead to very similar models being treated differently, causing customers or businesses to change behaviour to avoid the tax. Furthermore, an exemption could have a significant impact on the revenue collected from an OST, with knock-on effects for business rates relief. It is also worth noting that in the event an OST were introduced, the revenue would be used to fund business rate reductions for retail spaces, including those multi-channel retailers operating click and collect models.

Question 4: Should click and collect be exempted? If so, should there be a distinction between the examples listed above? How would that distinction be drawn?

UK-wide scope

2.19 The government's assumption is that, if implemented, it would be necessary to apply an OST across the whole of the UK. An approach that treated the various parts of the UK differently would be burdensome on businesses, requiring the geographical identification of sales within the UK, which is likely to be a more difficult task than separating UK from non-UK orders.

2.20 The government has said that if an OST were to be introduced, the revenue raised would be used to reduce business rates – which are devolved – for retailers with properties in England. Revenues from an OST would also be used to fund the block grants to the Devolved Administrations who can choose to use them to support public services, individuals, or businesses in Scotland, Wales and Northern Ireland.

Goods and services

2.21 OST proponents argue that the burden of business rates falls more heavily on high-street retail than online retail. That argument is made on the basis that commercial rents represent a higher proportion of total costs for in-store retailers operating through high-street properties compared to online retailers whose main properties instead consist of warehouses and distribution centres. In exploring the concept of an OST, the government considers the objective would be to raise revenue to fund business rate reductions for retailer with properties in England and fund the block grants of the devolved administrations in the usual way.

2.22 In terms of which transactions an OST could tax, there are two broad approaches that could be considered:

- A goods only approach
- A goods and services approach

Goods only approach

2.23 Those calling for an OST have generally proposed a tax that would apply to online retail sales of tangible goods. Tangible goods are distinct from other asset classes such as intangible assets, financial assets, and interests in land. They might be thought of as physical objects or products which can be manufactured, stored, transported, marketed, sold, and owned by their buyers. Examples include clothes, white goods, and food. In these product categories, the comparison between online and in-store sale of the goods appears relatively clear. In the case of in-store sales of consumer goods such as these, the business model generally relies on valuable retail premises often on or near the high street, with commensurately high business rates.

2.24 From an implementation perspective, a tax applicable only to tangible goods could ensure that the administrative challenges are more manageable. Businesses may find it easier to identify which products were subject to the tax. This should reduce the burden of calculating liability for an OST for reporting to HMRC.

2.25 However, it would bring other challenges, such as determining whether what has been supplied is a good or a service. For example, there would be questions about how a goods-only approach should apply to takeaways. The distinction between catering services, takeaways, and other food supplies, such as instant grocery delivery, sometimes operated by the same platforms, would require a careful consideration.

Goods exemptions

2.26 Proponents of an OST have largely called for a broad-based tax on all goods. This appears in line with the rationale that an OST should be linked to business rate reductions. Business rates are paid by businesses regardless of the goods being sold including food, medicines, and VAT zero-rated goods. This implies that an OST that excluded certain categories of goods might not be appropriate. It is, however, expected that some stakeholders may call for certain goods exemptions. This would mean retailers of exempt goods may receive business rates relief without their online sales of exempt goods being subject to an OST. Meanwhile, the amount raised by an OST would be lower if goods exemptions were given, making business rates relief less valuable and potentially less widely available.

2.27 The government wishes to understand whether there is an argument for excluding any goods and/or services from an OST. The case for exemptions would have to be weighed against the rationale for an OST, the reduction in tax revenue, and the additional complexity for businesses managing separate regimes for taxable and exempt products.

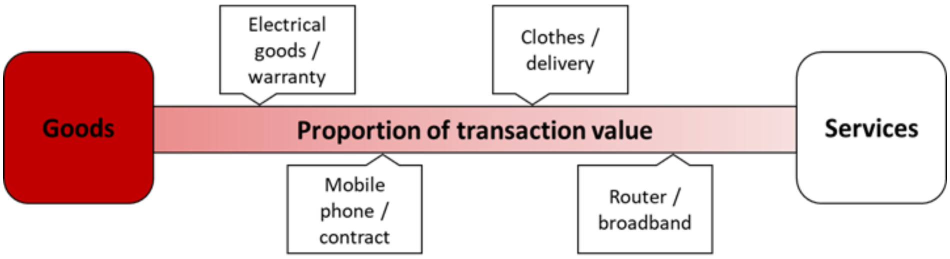
Challenge of value-shifting and avoidance

2.28 Where taxable and non-taxable items are sold together, there may be a risk that value is artificially shifted to the non-taxable elements to reduce overall tax due. This is a form of tax avoidance sometimes referred to as value-shifting. An OST with a flat rate per-transaction would be far less vulnerable than a design which applied the tax to a business's revenue from online sales (these models are discussed in more depth in Chapter Three). If a tax on revenue were pursued, a broad base scope with few exemptions would be most resilient against this risk.

2.29 The complementary nature of some goods and services may mean value shifting would be a particular risk if services were not covered by an OST but goods were. For high value goods and services where the valuation of the components is difficult to verify independently, the tax loss in each transaction could be significant. For lower value goods, the tax loss per-item would be smaller but at a volume which could amount to significant loss to the exchequer. If implemented, an OST would need to minimise opportunities for avoidance that could then undercut sales by compliant businesses.

2.30 Consider a design based on a business's revenue from the online sales of goods, but not services. The following examples are presented to set out common bundles of goods and services, and draw out the difficulty attributing value to the component parts. An example of value-shifting might occur where the revenue received for a tangible good was taxed but the revenue from an associated service, such as delivery, was not. Depending on how the retailer decided to set their prices, the amount of tax due could vary for the same amount received by the retailer and paid by the customer, with a retailer increasing its cost of delivery and decreasing the cost of goods. The end customer would obtain the same goods and services for the same overall price, but the seller would have reduced the tax due for the goods element.

Figure 1: Examples of bundled goods and services



2.31 A potential way to defend against this type of behaviour might be to tax the total transaction value where taxable and exempt elements are sold together. This would mean that, in the examples in Figure 1, services which would be exempt when sold separately would be taxable when sold with goods. As outlined in the diagram, though, bundles of goods and services vary. The application of an OST would differ considerably in each case. In the case of a broadband service and router provision, the broadband service amounts for the majority of the value of the supply, so the increase in tax would be significant. By contrast, the delivery associated with a purchase of several items of clothing would be expected to be a far smaller share of the overall transaction value. This might require assessing the relationship of the exempt element to the taxable element, drawing a line at some point on the spectrum in Figure 1. This could create administrative burdens and economic distortions.

Digital equivalents of physical goods

2.32 A digital product is any product in digitised form, which does not have physical form or substance, for example, eBooks or video games. Many digital products have tangible equivalents in the form of books, newspapers, or Blu-ray discs of games. It is a matter of debate whether digital products should be considered equivalent to their offline alternatives for the purposes of an OST.

2.33 If they were considered comparable, restricting the tax to tangible products would have the effect of an OST taxing some physical products which may have digital equivalents, while purchases of the corresponding digital products would not be taxable (e.g. physical books purchased online might be taxed, while eBooks would not be).

2.34 On the other hand, extending an OST's scope to cover digital products with tangible equivalents would present challenges, potentially requiring a line to be drawn between those digital products with / without tangible equivalents. Keeping all digital products out of scope of an OST would also reflect the difficulty in practice of distinguishing a digital product over which a customer has ownership from content that is accessed on a subscription basis or over the long term.

Goods and services approach

2.35 There may be a case for applying an OST to a broader array of services beyond those connected to the purchase of goods (discussed as a possible solution to the challenge of value-shifting above). Some have argued that, just as online retail operates in competition with in-store retail, certain online services operate in competition with providers of in-store services. This would suggest there are commensurate discrepancies in tax burden from business rates in the services sector which could therefore be relevant in considering the scope of an OST. Services can be grouped into three categories for the purposes of considering an OST:

- Those services which can only be delivered in person, e.g. leisure and hospitality, transport, household services, repairs and customisation. These are not online services, but can be arranged online, for instance through the purchase of tickets or agreement of terms online

- Services which can be delivered online or offline e.g. media, brokerage services such as estate agencies, gambling, education and healthcare, and professional services
- Services that are intrinsically online in nature, with no apparent in-person equivalent e.g. cloud computing and social media

2.36 Taxing the first group of services, where services could be arranged online but delivered in person, would be a very significant extension of an OST into in-person services. An OST could be applied to only the online element (e.g. the booking fee), although this would bring added complexity and the risk of value-shifting (discussed above). More broadly, this approach would bring into scope services which do not clearly fit within an OST's objectives to rebalance the tax burdens between online and in-store business activity.

2.37 Applying an OST only to the second group of services – those with an in-store alternative – may fit more intuitively with the objective of the tax, but could generate a great deal of uncertainty and complexity. For example, some healthcare or professional services may be delivered through a mix of online and in-person engagement. Many professional services which may now be delivered online would not have a high degree of in-person contact previously (e.g. accountancy or architecture). Under this approach, drawing a clear and consistent definition of those services that would be taxable would require careful consideration.

2.38 Media services would be a particularly difficult case, as it is not settled to what extent online media services compete with in-person consumption of media. For instance, online subscriptions to newspapers could be considered equivalent to purchases of physical newspapers from retailers, or a complementary but different channel. Media streaming services could be considered equivalent to in-person consumption of media in cinemas or other public viewing venues, or a distinct service provided to people in their homes.

2.39 An OST could be applied to the third group of services – those with no apparent in-person equivalent. This would significantly broaden the base of an OST beyond a goods-only model and would raise commensurately more revenue. It would though mark a significant departure from the rationale of applying an OST designed to help re-balance the tax system between in-store and online retail. Exemptions for specific services could be considered, such as for financial services and utilities which might otherwise have wider unintended economic impacts, or healthcare because of the potential impacts on individuals. Creating further boundaries between taxable and non-taxable services brings complexity and the potential for further value shifting.

2.40 As for all questions of scope, respondents will want to consider how a scope that includes some services interacts with business rates relief for retailers.

Question 5: Should an OST be applied to all goods? Are any exemptions necessary? If so, what are these and why?

Question 6: How should a goods-only approach apply to takeaway food?

Question 7: Do you think that digital products should be included in an OST? How should a "digital product" be defined?

Question 8: How can the risk of value shifting from goods to services be reduced, for an OST that has services out of scope?

Question 9: Are there other ways you could foresee OST being avoided? How could this be defended against?

Question 10: Do you think that some services (including any digital services) should be subject to an OST, and if so please explain which services and why?

Question 11: To what extent do businesses currently distinguish between their sales of goods and services in business systems? On what basis do they currently make this distinction?

Business to business sales

2.41 In considering the design of an OST, the government would need to determine whether the scope of the tax should extend to any online business-to-business (B2B) transactions. B2B sales can take place electronically or online under two broad headings: sales over a website or sales over an 'electronic data interchange' (EDI). According to analysis published by the Office of National Statistics (ONS), in 2019 there were £336.6bn of UK e-commerce sales over EDI as well as £159.3bn of website sales to businesses / public authorities[1]. As EDI sales will exclusively be B2B sales, this is an estimated total of £495.9bn of B2B sales taking place online or electronically in 2019. For comparison, the ONS analysis shows £197.1bn of website sales to private customers in 2019[2].

2.42 Concerns from stakeholders about the burden of business rates have been focused on retail premises. These are often in locations, such as higher rated high-street premises, for the convenience of their customer base which are usually household consumers. This implies a focus for an OST on online sales to consumers, as this is the segment where stakeholders have argued the tax imbalance lies. The rationale for an OST appears to apply less clearly to B2B transactions. While some businesses will make purchases in-store at high street premises, a high proportion of B2B transactions will take place at a wholesale level or along specific B2B supply chains which will not be accessible to household consumers. In addition, including B2B sales, or any subset thereof, would risk considerable administrative burdens and economic distortions.

2.43 As discussed in Chapter Four, there is evidence that the cost of an OST could be passed on to customers at a high rate. This risk should be taken into account when considering whether B2B online sales would be taxable under an OST. Transaction values are likely to be materially greater in a B2B

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1 https://www.ons.gov.uk/businessindustryandtrade/itandinternetindustry/bulletins/ecommerceandictactivity/2019 - Table 1: UK e-commerce sales, 2009 to 2019

2 https://www.ons.gov.uk/businessindustryandtrade/itandinternetindustry/bulletins/ecommerceandictactivity/2019 - Table 7: UK website sales by type of customer and size of business, 2012 to 2019

context, potentially amplifying any distortive effects of an OST. If an OST were implemented and such sales were included, there is potential for multiple layers of taxation to be created in business distribution and supply chains, increasing the price of the item being sold at each stage.

2.44 For example:

Figure 2: A hypothetical business supply chain of online orders

2.45 In the example in Figure 2, if the B2B sales were subject to an OST, each of the online orders would be in scope of an OST. Additional OST payable would then represent increased operating costs on each of the businesses in the supply chain. As mentioned above, these businesses are likely to pass some of this cost onto their customers creating a cascade effect of increased costs to the end consumer.

2.46 The VAT regime avoids creating a cascading tax through business supply chains by allowing VAT registered businesses to reclaim the VAT they have paid their suppliers alongside collecting the VAT paid by their customers. This effectively removes the burden of the tax from businesses in the supply chain and is paid by the end user. Adopting this approach would not be an appropriate option for an OST. VAT is a broad-based tax generally applicable to the provision of goods and services with many more businesses paying and collecting the tax than could be expected for a more targeted OST.

2.47 While including B2B sales would generate more revenue for the exchequer, the potential cascading effects of increased costs, whether passed on to customers or absorbed by each business in the supply chain, could create wider economic distortions. This suggests that sales made to businesses which then re-sell those items should be excluded from an OST.

2.48 It may be possible to limit an OST's scope to cover only those B2B transactions in which the products sold are consumed by the purchasing business. This would, however, bring considerable administrative burdens. Assuming it was the online seller that would be liable for an OST, an issue explored in Chapter Three, exclusions that required the online seller to gather additional information from their customer would be more difficult to implement. This is particularly the case for information that might not be obvious to the seller at the time of purchase, such as the rationale for the purchase (including use of the product).

2.49 Applying an OST to online B2B sales would raise further complications in cases where a purchasing business operates internationally. It may be difficult to identify whether a sale would be treated as made to a UK customer when the purchased item may not be used in the UK. Moreover, if an OST's scope extended to online sales of services as well as goods (discussed above), adding B2B services, potentially including financial services, would increase further the risk of complexity and distortion.

2.50 Given the lack of connection to the objectives of an OST, and in light of the considerable risk of excessive administrative burden and possible distortions, the case for excluding all B2B online sales appears very strong, with an OST instead limited to sales made to household consumers.

Question 12: Do you agree that an OST should be focused on sales to consumers?

Question 13: Do you agree that an approach of removing all B2B transactions from scope would be preferable to applying the tax according to the individual transactions (e.g. according to the use of the item sold)?

2.51 If an OST did only apply to sales to individuals as consumers, online sellers would need to be able to determine which of their sales would and would not result in an OST liability by identifying if they were sales to consumers. The Consumer Rights Act 2015 defines a consumer as "an individual acting for purposes that are wholly or mainly outside that individual's trade, business, craft or profession". For the Administration of an OST, the following indicators could be used:

- the nature of the goods or services being sold
- the business of the online seller
- the specific customers of the online seller

2.52 These options are explored in more detail below.

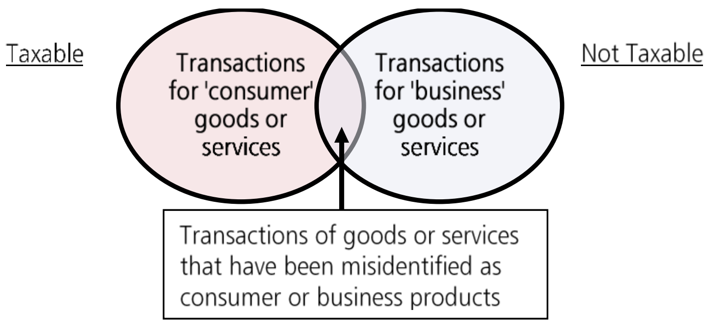
Nature of goods or services sold

2.53 Identifying taxable sales could involve introducing tests for the type of goods or services being sold. For example:

- sales of certain goods or services that are very likely to be inputs to businesses
- goods sold by wholesalers selling only to their wholesale customers
- goods bought in quantities unlikely to be bought by households

2.54 However, it would be difficult to be completely accurate with tests based on the type of items sold. There are many goods that might be purchased by both businesses and household consumers. Consideration would also be needed as to the treatment of sales of items that are used for a mixture of business and consumer purposes. For example, a small business owner might purchase a laptop or mobile phone for work purposes and personal use. Boundaries based on the quantity of goods sold would also likely create cliff-edges that could distort business behaviour and drive economic inefficiencies.

Figure 3: Misidentified consumer and business products

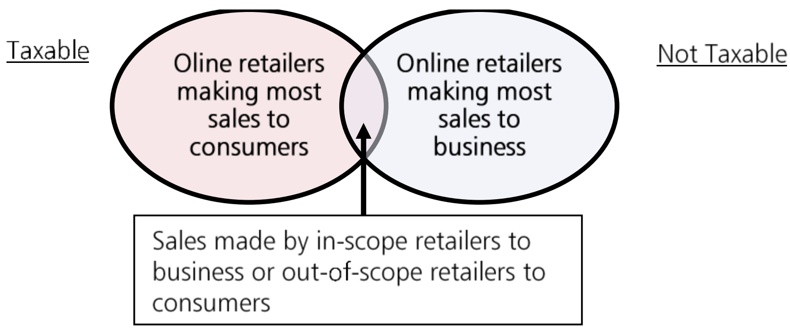


Inclusion by online seller

2.55 It could be decided that if businesses made most of their online sales to consumers, then all of their online sales would be taxable under an OST. Those businesses mostly selling to other businesses would therefore be excluded from the tax. This method could be relatively straightforward to administer, as it would not require online sellers to track individual transactions, goods sold, or assess their customers.

2.56 However, it would only be accurate and effective for online sellers that sold only to businesses or only to consumers. Online sellers that sold to a mixture of businesses and consumers would still need to determine the proportion of sales to businesses to establish whether they were liable for an OST or not. In addition, those either side of the threshold could have greatly different OST liabilities with relatively small difference in proportions of sales to businesses, which could create distortions if sellers sought to stay below the necessary threshold.

Figure 4: Taxable Sales to consumers and business



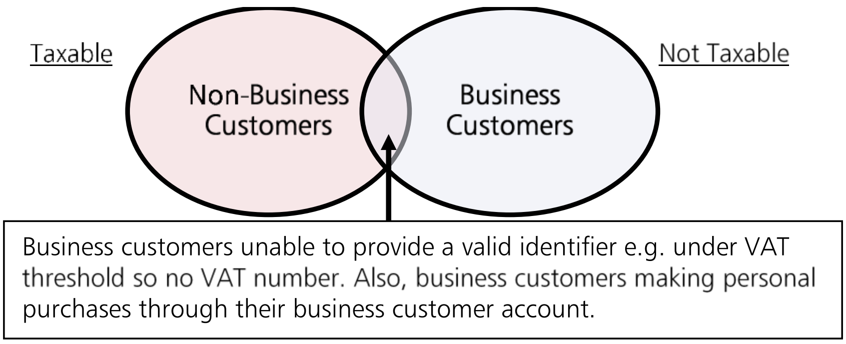
Identifying business customers

2.57 Alternative options would include asking online sellers to assess each of their customers to determine whether they were a business or consumer. Once the online seller had categorised their customer into either category, the online seller would then only include sales to their consumer-customers in their OST liability calculation. However, online sellers would have an incentive to categorise as many of their customers as possible as businesses to keep those sales out of scope. As noted above, the Consumer Rights Act already provides a definition of a consumer to identify which customers have rights provided by that Act. That Act requires the trader to prove which customers are not consumers, without that evidence a sale to an individual is to be considered a sale to a consumer.

2.58 Similarly for an OST, consideration would need to be given to how an online seller could determine whether their customer was a consumer or not. At its simplest, this might be achieved through the customer making a declaration that they are not a consumer. That declaration could be further supported by providing an identifier, for example a company registration number or VAT registration number. However, this would be open to manipulation as this information is readily available for non-businesses to use fraudulently.

2.59 Depending on the definition of business chosen, not all genuine businesses may have an existing suitable reference, such as a company registration or VAT registration number. Many small businesses are operated by individuals that will not have a company registration number. Similarly, many small businesses will not have a VAT registration number as they will have not been required to register as their turnover is under the VAT registration threshold. To an online seller, these small unincorporated businesses could appear very similar to a household consumer, making it difficult to assess if they were a genuine business or not.

Figure 5: Identifying business and non-business customers



Question 14: What is your preference from the above or any alternative approaches to exclude B2B sales from an OST while limiting administrative burdens on business?

Question 15: How do you think a business should be defined for the purposes of an OST?

Question 16: Are there other types of entities or transaction types which should be out of scope of an OST e.g. online sales by charities, public bodies or consumer to consumer transactions?

Chapter 3
Design

3.1 An online sales tax could in theory be applied to the vendor, the marketplace / platform (where this is a different entity), the delivery company, or the consumer involved in any given transaction. If implemented, an OST would raise funds to rebalance the taxation of the retail sector, which suggests that the vendor should bear the tax. When stakeholders have raised the idea of an OST, the expectation has been that it would be paid by the vendor rather than the consumer.

3.2 Assuming an OST was applied to the vendor, the tax could be levied either at an entity or group level. Businesses' preference here may be determined by other design choices of the tax such as thresholds and allowances (see following sections).

3.3 Regardless of the point at which an OST was levied, its incidence (i.e. the extent it is passed to consumers, suppliers, or absorbed into the vendor's profits) is the subject of debate. This is addressed in Chapter Four.

Question 17: Do you agree that an OST would be levied on vendors?

Treatment of online marketplaces and intermediaries

3.4 When businesses sell items online, they can do so on their own or they can sell using the services of third parties, such as online marketplaces, auctioneers, or other intermediaries. These intermediaries may help businesses reach a wider market and can include added services, such as a delivery service, to help facilitate the sale.

3.5 These different arrangements may make it less clear who is responsible for the online sale and who would be liable for an OST. The customer may consider an online purchase to have been from the online intermediary, but from a contractual perspective the seller will be another party. There is then a question as to whether those involved in a sale more widely should play a role in assisting in the administration and collection of an OST.

Online marketplaces

3.6 Online marketplaces are typically services that draw together lots of other businesses into one place to sell. This is beneficial for the customer as they have easier access to a wider variety of goods or services. It is also beneficial for those other businesses as the online marketplace can open up their potential customer base as well as offer additional services for the business.

3.7 Consider an example of a household consumer ordering groceries through a food marketplace app providing access to many different stores. The food marketplace app may have responsibility for collecting payment, relaying the order to the local convenience store, or both. The app provider may also be responsible for arranging delivery of the order to the customer. The local convenience store will be responsible for preparing and fulfilling the order. They will receive the bulk of the payment from the customer, less any commission due to the food delivery app.

3.8 In such a case, consideration should be given to who would be liable for paying an OST. The customer has placed the order, the local convenience store has sold the order, and the food marketplace app has facilitated the order. On the basis that the food marketplace app, as with other online marketplaces, is not making an online sale itself, it is likely to be more appropriate for an OST to look past the intermediary and apply to the local convenience store, or other business, selling through the online marketplace.

3.9 If an OST did apply to businesses operating through an online marketplace, and not the marketplace itself, there would still be potential for the online marketplace to assist in the collection of an OST. A similar approach could be taken as with VAT. Under VAT rules, there are circumstances when the online marketplace is liable for the VAT rather than the overseas seller for goods using the marketplace's services. As discussed below, this approach could be particularly relevant for assisting overseas sellers.

Other intermediaries

3.10 Online businesses can also act as agents, commissionaires or operate a 'drop shipping' arrangement. In these arrangements the online business arranging the sale may not take legal or physical control of the items that they sell to their customers. Close consideration will need to be given to these arrangements to prevent online sellers creating artificial arrangements by which they might avoid being responsible for paying an OST.

Question 18: How should different intermediaries that sell online on behalf of other businesses be treated with respect to an OST i.e. online marketplaces, franchises, auctioneers, agents and commissionaires?

Question 19: Are there situations in which it is not possible to distinguish the vendor from the intermediary, or in which the intermediary plays a crucial role in the sale? How should these be treated?

Question 20: Are there circumstances in which it would be appropriate for an intermediary to be liable for an OST, rather than the underlying seller? What are these?

Cross-border transactions

3.11 As discussed above, an OST is under consideration as a possible means to rebalance the tax burden between in-store shops and online retail, which is typically less dependent on high value property. The rationale for such a tax is therefore limited to sales to UK customers. If implemented, an OST should not advantage sellers based on their location. The tax would need to be chargeable on both overseas- and UK-based sellers making sales to UK customers.

3.12 To calculate OST liability, businesses would need to identify UK customers, which could be defined in a number of ways. The distinction between UK and non-UK customers appears more straightforward for goods purchases, where a delivery address would be required.

Question 21: How would an OST define UK customers?

3.13 The government recognises that engaging with a new tax in this form may be particularly difficult for overseas businesses which may be less familiar with the UK tax system and its administration. If an OST were implemented, one way to mitigate this difficulty for overseas businesses could be to involve intermediaries such as marketplaces or platforms, as discussed above.

Question 22: Should UK-based intermediaries play a role in identifying taxable transactions or be made liable in some cases?

Models for an online sales tax

3.14 After online sellers have identified which of their sales were in scope of an OST, they would be required to calculate the amount due. This calculation requires first determining the amount to be taxed, and then the rate to be applied to that amount.

3.15 There are two options under consideration for calculating the amount to be taxed:

- the revenues generated from relevant sales
- a number based on a relevant online sales metric (e.g. number of online orders, number of items sold online, number of deliveries made)

3.16 When considering either of these options, it is necessary to remember the likelihood that, if implemented, OST costs borne by the online retailer may be passed onto the purchaser. Therefore, consideration should be given on the impacts on the purchasers under these different approaches.

3.17 Consideration should also be given to the administrative burdens these options create for the online retailer and for HMRC to verify. Specifically, any additional data that would need to be collected or records that would need to be kept.

Revenue-based approach

3.18 A revenue-based approach would be a proportionate method for calculating the amount due. The greater the value of online sales made by the retailer, the more OST that would be payable. The amount of tax due would simply be a percentage of the value of the relevant sales made by the retailer.

3.19 No proposal for the rate of an OST has been suggested here. However, the government notes that proponents have generally suggested an OST with a rate of 1-2% would raise sufficient revenue to outweigh the administration burden without creating significant distortions. Revenue estimates and the interplay with business rates are discussed in more detail in Chapter Four.

3.20 As well as being an approach which would mean the tax payable would be proportionate to the value of all the items sold, the benefits of a revenue-based approach include that it is likely be less distortive than a flat-fee approach. As discussed in the next section, a flat-fee approach is more likely to drive changes in consumer or business behaviour, such as bundling orders together. Early analysis on these two approaches also suggests that a revenue-based approach is likely to be less regressive than a flat-fee approach.

3.21 Any challenges of imposing a revenue-based approach would be linked to the final scope and design of the tax. Specifically, as the scope of an OST narrows so that more decisions need to be made about whether a sale is taxable, the likelihood of complexity in identifying the taxable revenues increases.

3.22 There may be scenarios in which the cash cost of the tax for high-value purchases would discourage online sales in favour of those in-store. This could be mitigated with a cap to the amount of OST due on high value items. However, introducing a cap would effectively create a flat-fee tax for items of above a certain value, removing the proportionate nature of the tax. A per-item or per-transaction cap could also create the potential for avoidance behaviours. For example, a retailer could treat individual orders as part-fulfilment of a single high value order subject to a lower effective rate of tax.

Flat-fee approach

3.23 An alternative approach could be to apply a flat-fee to the number of online orders made. Depending on the value of the fee and any thresholds applied, this approach could raise the same levels of revenue as the revenue-based approach.

3.24 The flat-fee approach would mean an online retailer would not need to keep track of the revenue generated from taxable online sales. The online retailer would instead need to count the number of relevant sales they had made (or another similar metric), which most will already be doing to some extent for commercial purposes.

3.25 This approach would mean that a single order that contained a combination of taxable and non-taxable sales would attract the OST charge. The method would not take into account that some of the order was related to non-taxable items. This would be necessary to stop the inclusion of a non-taxable item making the entire order non-taxable.

3.26 A flat-fee approach appears simpler to administer for businesses compared to a revenue-based approach as there is no need to identify the value of the taxable element of any sale. However, it would not be a proportionate approach to take as the relative amount of tax payable would be greater for lower value orders than for higher value orders. At the extremes, the amount of tax due on the order may exceed the underlying value of the item being sold.

3.27 A flat-fee approach may encourage more significant changes in consumer or business behaviour. For example, as the cost is likely to be passed on in the order price, purchasers might be more inclined to group orders together to make a single large order rather than several smaller orders ensuring the transaction attracts the flat-fee only once for the same total number of items, rather than multiple times.

3.28 There are other metrics that could be used for the flat-fee to be applied, rather than number of online orders. These could include the number of parcels dispatched or number of deliveries made. However, these metrics present their own issues and could drive other behavioural changes. For example, it might not be possible for an online seller to control the amount or keep track of the number of parcels dispatched or deliveries made, particularly if they were using an external logistics company.

3.29 It may also be difficult to apply these metrics to subscription or other services where goods or services are delivered on a regular or ongoing basis. For example, one online order may result in recurring daily deliveries. A flat-fee tax on the single order might under tax the significance of the sale, but a flat-fee tax on each daily delivery could be excessive.

Other considerations for both approaches

3.30 In order to make an OST charge more progressive, a tiered approach could be taken when setting the rate of OST to charge. That would see the amount of OST charged, whether that was a percentage of revenue or a flat-fee amount, increase once the value of orders crossed certain revenue bands e.g. £20, £100, £500 etc. While this approach would make an OST more progressive, it might also create "cliff-edges" which could encourage customers or vendors to split their orders to keep the value below different thresholds. Having a tiered structure would undermine the simplicity offered by the flat-fee approach that would otherwise disregard the value of the order when calculating the tax liability.

3.31 Under either model, an OST would not take in to account the profitability of the retailer in determining the amount of tax due. This is similar to business rates that does not consider the amount of the profit the retailer is making. A low margin retailer would therefore see the additional cost of an OST impact its profits, potentially adding to the burdens of an already struggling retailer.

3.32 The different options would also give rise to differing administrative burdens for both the online retailer and for HMRC in verifying the tax due. Specifically, different approaches may require additional data to be collected.

Question 23: Would either a revenue or a flat fee approach have a greater distortive impact on consumer behaviour? What are the scope and design considerations that would lead to distortion caused by both models?

Question 24: Would either approach be particularly preferable? If so, why? Are there any preferences around scope (i.e. different exclusions or exemptions) which would make one of the approaches more preferable?

Question 25: Do you have experience to share of overseas' taxes on online sales using either model, or similar approaches not covered above?

Threshold or allowance

3.33 To ensure an OST would not create additional administrative burdens on small businesses without the capacity to comply with a new tax, and on those overseas sellers with low levels of UK-sales, a threshold could be introduced. This would set an amount of taxable UK online sales a business generates before it would be required to pay OST. This would need to be set at an appropriate level in order to ensure excessive administrative burdens were not placed on businesses making only limited sales online to UK customers. Stakeholders have suggested that a revenue threshold of £1 or 2 million of taxable sales could be appropriate. The government would welcome views from a range of stakeholders as to what an appropriate threshold level might be.

3.34 Additional threshold conditions could be set to further restrict the number of businesses liable to an OST. This could include a threshold based on the number of online orders a business completes in a year. This could be a benefit to businesses that do not frequently make online sales, but when they do, are for particularly high value items. A threshold based on numbers of sales may also be necessary for an OST designed around a flat-rate approach.

3.35 To stop the creation of a hard cliff-edge at the threshold amount, consideration should be given to instead introducing an allowance. Without an allowance, as soon as an online retailer's taxable online sales exceeded the threshold amount, all of those UK online sales would be liable for the tax. With an allowance, OST is due on only the amount of sales above the allowance limit.

3.36 Implementing an OST allowance would also mean that there would not be as direct a link between the total taxable sales by an online retailer and the amount of OST that they would eventually pay. This might be important for an online retailer whose online sales are just above the allowance. The allowance means that the amount of OST they would be required to pay compared to the total online sales is relatively low.

3.37 In order to prevent businesses splitting their activities into smaller units to benefit from multiple thresholds or allowances, it seems preferable to apply an OST to businesses under common control, rather than individual business level.

Franchises and marketplace sales

3.38 Franchise operations require further consideration in determining the operation of a threshold or allowance. A single franchise operator will typically share branding and enjoy other attributes of the wider franchise chain but will often be operated by a separate legal entity with no legal connection to other franchisees. To the consumer it appears as though the purchase is from a large chain, but it may instead be from a small business. If an OST threshold or allowance was to apply to the separate businesses operating franchises, a single retailer might not make sufficient online sales to be required to pay an OST. However, if an OST was applied to the chain of franchised businesses as a whole, then the sales of the franchise would be more likely to exceed a threshold or allowance and be taxable.

3.39 A similar question may arise when sellers use a marketplace. The total value of online sales through the marketplace may exceed the threshold or allowance, but the sales of individual sellers using the marketplace may be below. If a threshold or allowance was set at the marketplace level, with all sales made on it subject to an OST to be paid by the vendor, businesses that would themselves be below it may be subject to an OST. This could discourage businesses' use of marketplaces, creating further distortions.

3.40 As the purpose of the threshold or allowance is to avoid placing the administrative burden of dealing with an OST on businesses making limited online sales to UK customers, it would not seem appropriate to consider aggregates of online sales, either by fellow franchisees or through a marketplace, as determining whether a business should be subject to an OST. Instead, it should be the individual business's activities that determines liability.

Question 26: What factors should be taken into consideration in setting a threshold or allowance? How would this differ for revenue and flat-fee models of an OST?

Question 27: Do you agree that an allowance would mitigate the cliff edges that could be created by a threshold? What would be a reasonable OST allowance to set in order to protect small businesses while also making sure the OST generates sufficient tax revenues?

Question 28: Do you agree that an OST threshold or allowance should apply once to all businesses under common control?

Question 29: Do you agree the threshold or allowance would apply to individual businesses when they operate franchises or sell through online marketplaces?

Reporting and payment

3.41 An OST would require its own administrative framework. Deadlines to submit information to HMRC and pay outstanding tax liabilities are an important element of any such system. In July 2020, HMRC and HMT published a 10-year strategy to build a trusted, modern tax administration system. This notes that built-in delays in the UK tax payment system can make it hard for businesses to manage cashflow and sets the aspiration of bringing UK tax payment more into line with the increasingly real-time nature of tax reporting and other services. This must be balanced against the need for the payments to accurately reflect the liability due. If implemented, OST liability would reflect the level of online sales in a period, this suggests more timely payment, such as quarterly payments, would require more timely reporting to HMRC. However, it may be that businesses would find it simpler to administer a tax following sales figures as prepared for annual accounts purposes, which might point instead to an annual liability and annual reporting.

3.42 HMRC administers taxes under a number of different frameworks with three of the most commonly used by business being the Income Tax Self-Assessment (ITSA), Corporation Tax Self-Assessment (CTSA) and Value Added Tax regimes. ITSA determines liability by reference to a tax year commencing on 6 April, although for businesses basis period rules determine how much profit is attributed to each tax year. Once the profit has been determined

ITSA requires a single annual return with two payments on account in July and January of each year with a final balancing payment also in January. CTSA similarly determines liability on an annual basis and also requires a single annual return but the timing of this is linked to the date the company makes up its accounts. Most companies make a single payment of the annual tax liability although the most profitable companies make payments in quarterly instalments. VAT usually requires quarterly returns and payments, the stagger of which can be set by the business. For ease of administration, there appear to be benefits to all parties of closely mirroring the framework provisions of one of these three frameworks.

3.43 Business rates are due in respect of the financial year starting on 1 April. The business rates bill is typically paid over 10 equal monthly instalments, although options to pay by annual, half yearly, quarterly, or 12 monthly instalments are now available. The nature of business rates being set for the financial year enables the payments to be equal, and known in advance, with the bill for the coming year issued by local authorities in February or March of each year. The frequent and regular payments make it easier for businesses to plan their cashflow requirements. As an OST would be determined by in-year sales, it would not be possible to achieve this level of certainty.

3.44 Given the preference for more timely payments, it would appear that quarterly returns and payments, in a similar way to VAT, would be preferred option. However, it may be that businesses would find it simpler to administer a tax using figures derived from annual accounts submitted to Companies House, which might point instead to annual reporting.

Question 30: Do you consider there to be strong arguments either for or against quarterly or annual reporting? If this hinges on any of the design options laid out in this consultation, please specify which options and why.

New system requirements

3.45 If an OST were implemented, it is likely businesses would require new software, systems, and data collection. The complexity and administration burden could be mitigated by working with data which is already collected by businesses. This may involve using data collected for commercial purposes as opposed to tax purposes, and finding new ways of using it.

3.46 Consider the following demands which might be placed upon business' systems in administering an OST, subject to the decisions reached on the scope and design elements outlined above.

- Identification of sales of goods, distinguished from sales of services, including in a mixed supply
- Identification of sales made online versus sales made through other channels
- Identification of sales made by any remote means (online, over the phone, via email, over fax, by post) as opposed to sales made in person at a physical store premises

- Identification of sales made online which are then collected from an agreed location by the customer
- Identification of sales made to businesses from sales made to customers (B2B versus B2C)

3.47 It would appear that some OST designs would require a very high level of data, which may greatly increase complexity and cost of administration. Even proponents of an OST may find a tipping point at which their support diminishes with certain design choices, which would be helpful to understand.

Question 31: Can you provide insight into the overall burden to administer all systems and processes required to support an OST? Do systems currently allow you to identify the features listed above; if so, please provide further details on how this distinction can be made.

Chapter 4
Impacts

4.1 The growth of online retail sales is down to a wide range of factors. In line with the position set out by most proponents of an OST, if implemented, the tax would not be intended to reverse these trends; instead, it would be about reflecting businesses' concerns about a tax imbalance.

4.2 In that regard, were an OST to be pursued, the government would aim to minimise distortion on both consumers and businesses. Nevertheless, any new tax will have an impact on the business landscape and on consumers. The government would like to explore the impacts of an OST to properly assess its merits and risks. These impacts will vary significantly depending on the scope and design questions discussed above. Stakeholders are encouraged to consider the form an OST could take when considering the overall impacts discussed below.

Revenue from an OST

4.3 If introduced, an OST would not be intended to actively encourage customers to shop in-store rather than online. A potential OST would be used as a way of raising revenue to fund business rate reductions.

4.4 An estimate of achievable revenues from an OST is therefore required to inform scope and design choices and properly assess the case for and against an OST with this policy objective. However, revenue estimates are very uncertain while the scope, rate, and design are not decided. As discussed in earlier chapters, there are many choices on scope, including whether an OST would apply to some or all goods and services, and design, including if an OST would be a flat fee or a revenue tax. Furthermore, all estimates are subject to a high degree of uncertainty given the significant changes to online retail patterns seen during the pandemic.

Cost estimates

4.5 This consultation is designed to inform the government's assessment of an OST without proposing a specific model; therefore, precise cost estimates are not possible at this stage. Should the government decide to proceed with an OST, a thorough cost assessment would be produced.

4.6 However, initial internal estimates suggest that a revenue-based OST with a £2 million allowance, levied at a rate of 1 per cent on online sales of goods from business-to-customer and excluding services, could raise approximately £1 billion per annum, depending on the scope of the final design. Estimates for a flat fee tax with a £2 million allowance, levied at a fee of £1 per-order on deliveries of goods, including grocery deliveries for supermarkets and excluding click-and-collect, are of a similar order. To give an idea of the cost of exempting certain items, if goods subject to a zero-rate of VAT were excluded from a revenue-based OST, this might reduce the yield by around 10% to 20%.

4.7 Respondents may also wish to consider external estimates of an OST's revenue. Various stakeholders have produced such estimates. For example, estimates find that an OST of 2 per cent on revenue from online retail purchases could raise around £1.6 billion[1]. Other estimates find a higher rate up to 5 per cent could increase that amount to £2.5 billion[2]. These numbers are indicative and are meant to offer the respondents to this consultation an idea of the possible revenues raised by an OST.

4.8 As was noted in chapter two, the revenue of an OST would depend on the scope of the tax. An OST with numerous exemptions or a narrower scope would limit the amount of revenue an OST would raise, and could increase the administrative burden for business.

Business Rates

4.9 If an OST were implemented, the government would use the revenue to fund business rates relief for retailers with properties in England and fund the block grants of the devolved administrations in the usual way. It is important to note that the extent to which an OST could fund business rates reductions would be highly dependent on two factors:

- The scope of an OST
- How any business rates support was targeted

4.10 As noted above, initial estimates suggest a revenue-based OST levied at a rate of 1 per cent on online sale of goods to UK customers above an allowance of £2 million would raise approximately £1 billion per annum. Any revenue raised from an OST would therefore not be enough to replace business rates, which raise over £25 billion per annum in England.

4.11 The extent to which an OST could fund business rates reductions in England would be highly dependent on how any support is targeted. To give an impression of reductions that might be available, one can compare indicative OST revenue estimates with business rates revenues from certain categories of business in England. To note again, revenue from an OST would also be used to fund the block grants of the devolved administrations in the usual way. Total business rates revenue from retail properties in England is c.£7.5 billion. Estimated revenue of approximately £1 billion from an OST designed as described above is only around 13% of that. If instead a rates reduction was targeted more widely at properties in the retail, hospitality, and leisure sectors, revenue from an OST as described above is equivalent to around 9% of the total business rates revenue of £11.1 billion.

4.12 Targeting support at lower value properties might allow for more generous reductions – the 11 per cent of retail properties with the highest rateable

[1] https://www.oxfordeconomics.com/recent-releases/The-Economic-Impact-of-an-Online-Retail-Sales-Tax-in-the-UK

[2] https://www.oxera.com/insights/agenda/articles/will-an-online-sales-tax-save-the-uk-high-street/#_ftn6

values (the value of a property on which business rates bills are based), those valued over £51,000, account for 70 per cent of rateable value in the sector. The 2 per cent of retail properties valued over £250,000, account for 40 per cent of rateable value in the sector. Targeting support at small businesses might also allow for greater reductions. An estimated 70 per cent of retail business rates is paid by the largest 1 per cent of retail businesses.

4.13 As discussed above, in terms of scope, a broader based OST would raise more revenue, allowing bigger reductions in business rates. An OST with multiple exemptions would have a smaller impact on business rates.

4.14 Some multi-channel retailers have suggested that if the scale of business rates reductions were markedly reduced, or if they were targeted only at smaller retailers, an OST's benefits may not offset its administrative cost. The impact on firms of an OST and corresponding business rates relief would depend on the design and scope of a tax, the shape of business rates relief, and the balance of online and in-store activity of businesses concerned. The government therefore invites comments on the relative benefits of an OST and corresponding business rates reductions, taking into account the scope of an OST. This consultation is not, however, designed to discuss in detail the design of any business rates relief. Respondents are encouraged to focus on the case for and against an OST.

4.15 Economic theory suggests that the rewards from a cut to retail business rates would flow in large part to the owner of the property, not the retailer. There is evidence of a high degree of capitalisation of business rates into rents, so in the longer-term reducing business rates may result in higher rents being paid.

Question 32: On balance, what would the impact be of an OST with business rates reductions on the scale described above, including on retailers that operate both online and offline?

Question 33: Do the potential revenues from such a tax justify the additional administration that it would require of businesses, as well as the design complexities detailed in the previous sections?

Online Retail

4.16 The online retail sector is thriving in the UK, with several world-leading companies in this space. The sector brings considerable benefits to consumers and the wider economy through increased choice, convenience, and productivity. The government does not seek to stifle innovative business practices.

4.17 Stakeholders who have met the idea of an OST with scepticism have argued it would be a tax on innovation and investment in the UK's growing digital economy and may lead to market distortions. It is argued than an OST would target those that have adapted most successfully to changing circumstances and damage that part of the retail economy that has been performing best.

4.18 To properly assess the case for an OST, the government would like to consider evidence about the tax burden impacts on commercial decisions and the profit margins of different types of retailers (online, in-store, and multichannel).

Question 34: To what extend do you think an OST would impact innovation, efficiency, and productivity?

Question 35: To what extend do you believe that an OST would impact consumers' behaviour in favour of in-store retail?

Question 36: How do you expect online retail to evolve in the coming decade and how should an OST take account of these?

Incidence of the tax and distributional impacts

4.19 In response to the 2020 Call for Evidence, a risk emphasised by respondents was the likelihood that vendors pass on the cost of an OST to consumers, increasing prices and reducing disposable incomes. There are a number of reasons this may be likely, including the high degree of competition in much of the retail industry limiting profit margins and thus firms' ability to absorb a new cost. The proportion of pass-through to consumers is likely to vary between product categories and firms depending on the level of price elasticity and competition.

4.20 The government would like to gather further evidence on the level of pass through and the extent to which it differs depending on the type and value of the goods purchased and the market in which sellers are operating.

Question 37: What is the evidence for the degree of pass-through of the cost of an OST to consumers? To what extent will this vary depending on the type and value of the goods sold?

4.21 Some respondents have argued that the potential pass through could disproportionately affect specific groups. Affected groups might include those that spend a greater proportion of their income on discretionary goods and services; those who live further from a high street or shopping centre; and individuals with reduced mobility. Each of these groups might be more reliant on online ordering and delivering of goods to their home. The government would like to gather further evidence to assess this risk.

4.22 To accurately assess these risks the government is keen to draw on as broad data set as possible.

Question 38: Do you have any data which would support the Government in making an assessment of the incidence of the tax or its distributional impacts?

Question 39: In your assessment, what would be the distributional impact of an OST? Are there particular groups who are likely to be worse affected than others? How would this change if an OST were applied as a flat-fee per transaction (or some other similar metric) versus a percentage of firms' revenue from online sales?

Environment

4.23 The objective outlined by most proponents of an OST in the retail industry is to rebalance the burden of tax between in-store and online retail. The government is considering an OST in this consultation as a possible means to raise revenue to fund business rates relief. While some research has been done, there are no clear conclusions on whether an OST would have an environmental impact or not, including:

- Greenhouse gas emissions
- Energy use
- Noise pollution
- Traffic congestion
- Electric vehicle take-up
- Waste

4.24 Internationally, there have been proposals for a delivery tax (a flat fee tax on the delivery of goods to home addresses) including in New York and Paris, citing potential environmental benefits, such as cleaner air and reduced congestion. On the other hand, if an OST encouraged shoppers to favour in-store shopping (with associated travel requirements) over home delivery, the environmental impact could be the reverse. However, the evidence that a delivery-based or a flat fee OST would have environmental benefits remains unclear.

Question 40: What environmental impact might an OST have? How would its design affect an OST's environmental impact?

Chapter 5
Next Steps

5.1 The government has not at this stage decided to proceed with an OST or determined the precise design and scope of such a tax were it to be implemented. This consultation is designed to inform government policy considerations. There is little existing precedent internationally for a tax akin to an OST. Through this consultation, the government wishes to build its understanding of the issues associated with pursuing an OST and the pros and cons of progressing policy development to a technical phase.

5.2 The government would welcome responses to this consultation by 20 May 2022. Responses can be sent to:

- Email: OSTconsultation@hmtreasury.gov.uk
- Post: Corporate Tax Team, 1 Yellow, HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

Annex A
List of Consultation Questions

A.1 Chapter Two: Scope

Question 1: Would you favour a tax for all 'remote' sales or just a subset of 'online' sales?

Question 2: How should taxable sales be defined and what would the practical implications be?

Question 3: Are there transactions that would be particularly difficult to classify as either online or remote? What are these, and how should these be addressed?

Question 4: Should click and collect be exempted? If so, how?

Question 5: Should an OST be applied to all goods? Are any exemptions necessary? If so, what are these and why?

Question 6: How would a goods-only approach apply to takeaway food?

Question 7: Do you think that digital products should be included in an OST? How should a "digital product" be defined?

Question 8: How can the risk of value shifting from goods to services be reduced, for an OST that has services out of scope?

Question 9: Are there other ways you could foresee OST being avoided? How could this be defended against?

Question 10: Do you think some or all categories of services listed above (including any digital services) should be included in the scope of an OST? Would you add any additional services?

Question 11: To what extent do businesses currently distinguish between their sales of goods and services in business systems? On what basis do they currently make this distinction?

Question 12: Do you agree that an OST should be designed to exclude B2B sales?

Question 13: Do you agree that an approach of removing all B2B transactions from scope would be preferable to applying the tax according to the individual transactions (e.g. according to the use of the item sold)?

Question 14: What is your preference from the above or any alternative approaches to exclude B2B sales from an OST while limiting administrative burdens on business?

Question 15: How do you think a business should be defined for the purposes of an OST?

Question 16: Are there other types of entities or transaction types which should be out of scope of an OST e.g. online sales by charities, public bodies or consumer to consumer transactions?

A.2 Chapter Three: Design

Question 17: Do you agree that an OST would be levied on vendors?

Question 18: How should different intermediaries that sell online on behalf of other businesses be treated with respect to an OST i.e. online marketplaces, franchises, auctioneers, agents and commissionaires?

Question 19: Are there situations in which it is not possible to distinguish the vendor from the intermediary, or in which the intermediary plays a crucial role in the sale? How should these be treated?

Question 20: Are there circumstances in which it would be appropriate for an intermediary to be liable for an OST, rather than the underlying seller? What are these?

Question 21: How would an OST define UK customers?

Question 22: Should UK-based intermediaries play a role in identifying taxable transactions or be made liable in some cases?

Question 23: Would either a revenue or a flat fee approach have a greater distortive impact on consumer behaviour? What are the scope and design considerations that would lead to distortion caused by both models?

Question 24: Would either approach be particularly preferable? If so, why? Are there any preferences around scope (i.e. different exclusions or exemptions) which would make one of the approaches more preferable?

Question 25: Do you have experience to share of overseas' taxes on online sales using either model, or similar approaches not covered above?

Question 26: What factors should be taken into consideration in setting an allowance? How would this differ for revenue and flat-fee models of an OST?

Question 27: What would be a reasonable OST threshold and allowance to set in order to protect small businesses while also making sure the OST generates sufficient tax revenues?

Question 28: Do you agree that an OST threshold or allowance should apply once to all businesses under common control?

Question 29: Do you agree the threshold or allowance would apply to individual businesses when they operate franchises or sell through online marketplaces?

Question 30: Do you consider there to be strong arguments either for or against quarterly or annual reporting? If this hinges on any of the design options laid out in this consultation, please specify which options and why.

Question 31: Can you provide insight into the overall burden to administer all systems and processes required to support an OST? Do systems currently allow you to identify the features listed above; if so, please provide further details on how this distinction can be made.

A.3 Chapter Four: Impacts

Question 32: On balance, what would the impact be of an OST with business rates reductions on the scale described above, including on retailers that operate both online and offline?

Question 33: Do the potential revenues from such a tax justify the additional administration that it would require of businesses, as well as the design complexities detailed in the previous sections?

Question 34: To what extend do you think an OST would impact innovation, efficiency and productivity?

Question 35: To what extend do you believe that an OST would impact consumers' behaviour in favour of in-store retail?

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Question 40: What environmental impact might an OST have? How would its design affect an OST's environmental impact?

Annex B

Processing of Personal Data

This notice sets out how HM Treasury will use your personal data for the purposes of the consultation on the policy proposal of an Online Sales Tax (OST) and explains your rights under the UK General Data Protection Regulation (UK GDPR) and the Data Protection Act 2018 (DPA).

B.1 Your data (Data Subject Categories)

The personal information relates to you as either a member of the public, parliamentarians, and representatives of organisations or companies.

B.2 The data we collect (Data Categories)

Information may include your name, address, email address, job title, and employer of the correspondent, as well as your opinions/answers to the consultation questions and any other elements of your response. It is possible that you will volunteer additional identifying information about yourself or third parties.

B.3 Legal basis of processing

The processing is necessary for the performance of a task carried out in the public interest or in the exercise of official authority vested in HM Treasury. For the purpose of this consultation the task is consulting on departmental policies or proposals or obtaining opinion data in order to develop good effective government policies.

B.4 Special categories data

Any of the categories of special category data may be processed if such data is volunteered by the respondent. These could include political opinions, religious and/or philosophical beliefs, trade unions membership status, or health.

B.5 Legal basis for processing special category data

Where special category data is volunteered by you (the data subject), the legal basis relied upon for processing it is: the processing is necessary for reasons of substantial public interest for the exercise of a function of the Crown, a Minister of the Crown, or a government department.

This function is consulting on departmental policies or proposals, or obtaining opinion data, to develop good effective policies.

B.6 Purpose

The personal information is processed for the purpose of obtaining the opinions of members of the public and representatives of organisations and companies, about departmental policies, proposals, or generally to obtain public opinion data on an issue of public interest.

B.7 Who we share your responses with

Information provided in response to a consultation may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 2018 (DPA) and the Environmental Information Regulations 2004 (EIR).

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information, we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury.

Where someone submits special category personal data or personal data about third parties, we will endeavour to delete that data before publication takes place.

Where information about respondents is not published, it may be shared with officials within other public bodies involved in this consultation process to assist us in developing the policies to which it relates. Examples of these public bodies appear at: https://www.gov.uk/government/organisations

We plan to share responses to this consultation document, including any information specified in section (Annex no) 2 above, with Her Majesty's Revenue and Customs for the purposes of developing effective government policy.

As the personal information is stored on our IT infrastructure, it will be accessible to our IT contractor, NTT. NTT will only process this data for our purposes and in fulfilment with the contractual obligations they have with us.

B.8 How long we will hold your data (Retention)

Personal information in responses to consultations will generally be published and therefore retained indefinitely as a historic record under the Public Records Act 1958.

Personal information in responses that is not published will be retained for three calendar years after the consultation has concluded.

B.9 Your Rights

- You have the right to request information about how your personal data are processed and to request a copy of that personal data.
- You have the right to request that any inaccuracies in your personal data are rectified without delay.
- You have the right to request that your personal data are erased if there is no longer a justification for them to be processed.

- You have the right, in certain circumstances (for example, where accuracy is contested), to request that the processing of your personal data is restricted.

- You have the right to object to the processing of your personal data where it is processed for direct marketing purposes.

- You have the right to data portability, which allows your data to be copied or transferred from one IT environment to another.

How to submit a Data Subject Access Request (DSAR)

To request access to personal data that HM Treasury holds about you, contact:

HM Treasury Data Protection Unit
G11 Orange
1 Horse Guards Road
London
SW1A 2HQ

dsar@hmtreasury.gov.uk

B.10 COMPLAINTS

If you have any concerns about the use of your personal data, please contact us via this mailbox: privacy@hmtreasury.gov.uk.

If we are unable to address your concerns to your satisfaction, you can make a complaint to the Information Commissioner, the UK's independent regulator for data protection. The Information Commissioner can be contacted at:

Information Commissioner's Office
Wycliffe House
Water Lane
Wilmslow
Cheshire
SK9 5AF

0303 123 1113

casework@ico.org.uk

Any complaint to the Information Commissioner is without prejudice to your right to seek redress through the courts.

HM Treasury contacts

This document can be downloaded from www.gov.uk

If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gov.uk