Podcast transcript

Shift your business model into gear.

Podcast with Dr. Andreas Ball, Partner, Tax, KPMG in Germany

Musical intro

Announcer:

Hello and welcome to the KPMG podcast series for tax leaders. In today's episode, we hear from Dr. Andreas Ball Partner, Tax, KPMG in Germany. Andreas advices multinational clients in international tax affairs. He has a huge breadth of experience in automotive business, both supplier and OEM's as well as in software and technology industry. I spoke to Andreas on the phone and we discussed how tax teams can manage disruptive business model change in the global automotive industry. Andreas, thanks for joining me today, to set the scene for our listeners, could you talk us through why heads of tax should care about shifting business models in the automotive industry?

Andreas:

Well, a few modern international companies have static business models. Up-to-date, shifting business models mean mainly a transformation to digital business. It is important to be aware that the digital economy is not just tech companies. It is about every business. Consider manufacturing business in general, many products contain digital components, production machine, communicate online with each other and the Internet of Things would transform our industry. If we analyze now the automotive industry in particular, it is quite clear that the transformation process in the automotive industry moves extremely fast compared to other manufacturing industries. In our experience, the automotive OEM's transforms from hardware producers into service companies. OEM's are providing digital services on demand to the customer. I would like to give you three examples for function on demand which are already in place. The customer can activate online an already built-in car winter heating for a few months in cold periods. Second, already a reality is also the online update of the GPS software. And third, parking apps indicate available parking space to the driver. The same volume of these services will massively grow, especially autonomous driving will open new dimension of entertainment, advertising, and other digital opportunities. As our business models in automotive are based on the fact that modern cars are collecting many gigabytes of valuable data on every mile. This data can contain weather, traffic and road conditions, but also information about the driver's mobility and his consumption. This data can be analyzed and made available to other companies if the customer agrees. These business models, and that's essential, work globally. Their cross border rollout is technically simple and will be the normal case. And this is where taxes get relevant. The cross border roll out create taxation topics: income taxes, indirect taxes and customs has to be considered.

Announcer:

And what do you see as the real challenges of changing business models in the auto industry?

Andreas:

The main challenge is that the old rules of tax jurisdiction doesn't fit to digital business model. Nevertheless, the tax authorities are creative and trying to apply their existing rules to the digital economy. Cross border services like function on demand, creates a lot of tax question. Agency PE – a prominent establishment is an issue. Do I have an agency PE in the market space if the local dealer support the sales of services? Second, are my services subject to withholding taxes? Third, does this services increase the customs and context value of the car? What other VAT or sales tax consequences. And last but not the least, what is the value of data collected by the car? Does my transfer pricing system recognize the value of data and fit to the digital economy. To sum it up, there are a lot of open questions relating to taxation and the existing role. The compliance requirements have to be handled and you should not underestimate this. One example if a private customer has to file withholding tax return, this can be the pillar for your business model. The existing tax rule, are not the end of the discussion, a further challenge is that the tax law is highly volatile. The OECD BEPS Initiative 2.0 will change dramatically the international business taxation. We expect KPMG that this rule is implemented in 2020. These new rules will affect especially digital business models. So far, many governments have the opinion that the current taxation is not fair. Services were sold without being physically present in a country without having a factory or sales store. It's hard to find a nexus with taxation.

If the agency PE or withholding taxes are not applicable. As a consequences, states like India and France have implemented a digital tax already. Countries like the UK, Austria, Spain and Italy have prepared digital taxes as well and will follow soon if an OECD solution is not found until 2020.

Announcer:

And are there any tax strategies that automotive companies can use when facing changing business models?

Andreas:

Tax strategy of many tax directors are to avoid tax risks, penalties and reputational damages for the corporation. A common strategy available is for the company to apply for tax ruling in advance for text ruling in advance to gain certainty on the tax effects of business model changes such as whether a permanent establishment will be created and whether function on demand payments are qualified as royalties for tax treaty purposes. There measures are appropriate and necessary, but we recommend to go further. We propose to adjust the structure and involvement of the tax department to the need of digital business models. We have five recommendations: The tax department should get involved early in business planning processes to make sure tax measures are upfront. Second, the tax department should encourage the business to hold the launch of new business models until certainty over tax matter is resolved in relevant jurisdiction. For example, until a ruling is gained or until the negotiation with local tax authorities are finalized. Third, the tax department should send a tax member in the company's strategy and business development unit to make sure that the tax issues are appropriately included in the company’s strategy. Fourth the tax department could assign a digital tax manager to coordinate multidisciplinary tax methods. It would be positive if digital tax matters were coordinated by one person and not by several managers in the tax department. And we recommend to observe the international tax policy debate. The whole tax environment as I have already told is highly volatile.

Announcer:

Thanks Andreas, this is great. This is obviously a lot to take in. But if you had one piece of advice that you could give to tax teams facing changing business models what would it be?

Andreas:

Well, as already told, the digital economy moves very fast. So what my advice is, don't let the business run away. The tax function has to be part of the business process.

Announcer:

Andreas, thanks for joining us and I look forward to talking with you again in the future. Join us again next time and please if you have any suggestions for topics that we might cover in this podcast series, please contact us at tax@kpmg.com, we would love to hear from you. Thanks for listening.

Musical exit