PES Discussion paper

Fiscal justice in the digital sphere

FEN, 26 February 2019

Introduction

The Party of European Socialists – in line with the OECD[1] – defends the principle that we should tax value where it is created. The dissociation between physical presence and revenue-generation brought about by the internet revolution has made it harder to live up to this principle, which is why we support changing the century-old tax rules that determine where profits are taxed. Users across several jurisdictions play an indispensable part in the functioning of many online platforms: individuals are both consumers and part of the product. Despite this, profits derived from this value-creation are only taxed where firms have a physical presence.

We must acknowledge the difficulties in ring-fencing the 'digital economy'. Holistic reform of tax laws to address profit shifting by all types of firms should remain our long-term objective. It is only through fundamental change to the way we tax firms that we will be able to ensure fair taxation for 21st century business models without creating market avoidable market friction or excessive compliance costs both for firms and tax administrations.

However, we can identify platforms that rely exclusively on individual's usage for monetisation, be it through the sale of user data, intermediation services or access to targeted advertising. The firms involved in this sector face comparatively low effective tax rates in the jurisdictions in which they operate, clearly contributing to the kind of tax injustice that the PES has long fought against. Pending radical global rule-change, we believe the EU should seek to ensure a more level playing field in parts of the digital economy by introducing temporary measures regarding these digital services.

[1] OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing, Paris. https://doi.org/10.1787/9789264202719-en.

Party of European Socialists
10-12 Rue Guimard
B-1040 Brussels
Belgium

1. Two strands of work

Efforts to improve the way that we tax the digital economy have so far taken two forms, or strands of work:

1. The first strand of work aims to redefine the concept of permanent establishment so as to include companies that have a 'significant digital presence' in a market without any accompanying physical presence. A company with a significant digital presence in a country would become liable for corporate income tax in that country, just as if it had a physical presence there. This long-term strand is centred on the work of the OECD/G20 Base Erosion and Profit Shifting (BEPS), which aims to address the broader issues surrounding profit allocation.
2. The second strand consists of a stopgap measure – a 'digital services tax' (DST) – designed to prevent profit shifting by pre-emptively taxing revenues resulting from the sale of targeted online advertising, user data, and intermediation services. The idea is that a DST would expire as soon as an OECD-level agreement were found on the first strand.

2. EU-wide digital services tax

Different designs for a DST mainly derive from the Commission's March 2018 proposal for an EU-wide scheme[2]. According to the Commission, Member States will be able to raise an estimated €5bn annually, if the scope of the DST includes their proposed three types of service: data sales, intermediation services and targeted advertising[3]. The Commission's proposal was discussed at the ECOFIN Council meetings on 6 November and 4 December 2018. The lack of consensus on the Council Presidency's compromise proposal[4] led France and Germany to issue a joint declaration pushing for an advertising-only DST by 2021[5].

In table 1 we outline the key characteristics of the Presidency compromise. We include the corresponding sections of ECON committee report adopted by the Parliament on 13 December 2018[6], although as this is a taxation matter under Art. 113 TFEU the Parliament's role is merely consultative.

---

[2] European Commission (2018), Proposal for a Council directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services, COM (2018) 148 final. https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM%3A2018%3A148%3AFIN

[3] European Commission (2018), 'Questions and Answers on a Fair and Efficient Tax System in the EU for the Digital Single Market'. http://europa.eu/rapid/press-release_MEMO-18-2141_en.htm

[4] Council of the European Union (2018), Proposal for a Council directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services. 2018/0073(CNS), http://data.consilium.europa.eu/doc/document/ST-14886-2018-INIT/en/pdf

[5] Council of the EU (2018), Franco-German joint declaration on the taxation of digital companies and minimum taxation. https://www.consilium.europa.eu/media/37276/fr-de-joint-declaration-on-the-taxation-of-digital-companies-final.pdf

[6] European Parliament (2018), Report on the proposal for a Council directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services, A8-0428/2018. http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A8-2018-0428&language=EN

Table 1: DST directive state-of-play in the Council and Parliament

	Council compromise text	**ECON committee report (consultative only)**
Application date	1 January 2022	1 January 2020
Taxable revenues	'(a) the placing on a digital interface of targeted advertising; (b) the making available to users of a multi-sided digital interface; (c) the sale of data collected about users and generated from users' activities on digital interfaces.'	'(a) the placing on a digital interface of advertising targeted at users of that interface; (b) the making available to users of a multi-sided digital interface which allows users to find other users and to interact with them, and which may also facilitate the provision of underlying supplies of goods or services directly between users; (c) the **processing** and transmission of data collected about users and generated from users' activities on digital interfaces. (ca) the making available to users of **content on a digital interface** such as video, audio, games or texts using a digital interface.'
Rate	3%	3%
Deductibility	'This Directive **should not prevent a Member State from allowing businesses to deduct the DST** paid from the corporate income tax base in their territory…'	'…a **future Union wide common solution** will have to be found on allowing businesses to deduct the DST paid as a cost from the corporate income tax base in their territory…'
Exemptions	Making available a digital interface where the main purpose is for the supply of digital content, of payment services or of communication services. The supply of **regulated financial services**. Sale of data from **sensors** and **from regulated financial entities**. Revenues from **intra-group provision**.	'Making available a digital interface where the main purpose is for the supply of digital content, of payment services or of communication services, **provided that no further revenues are generated** thanks to the processing, transmission or sale of users' data.'
Revenue threshold	€750m worldwide, **€50m EU**	€750m worldwide, **€40m EU**

Expiry	If **sufficient progress** has been made at OECD level by Dec 2020 the Commission may postpone/repeal.	This Directive shall expire **with the adoption** either of the Directive laying down the rules on a significant digital presence, the Directives on a CCCTB, or a Directive implementing OECD political agreement.

3. National DSTs

France, Spain and Austria are all moving forward with their own national DSTs. So long as they remain compatible with (and eventually substitutable by) the EU-wide DST, Tax Commissioner Pierre Moscovici sees these schemes as important first steps in moving the debate forwards despite obstruction from certain Member State governments[7].

Spain's proposed DST follows the design of the Commission's proposal (i.e. including data sales and intermediation), with the threshold adjusted to Spanish revenues of €3m[8]. France's finance ministry will present its proposal for a '*taxe GAFA*' in February, but it is purported to include a threshold of €25m in French revenues and a rate varying from 3 to 5%[9]. Some lawyers believe these DSTs could be challenged on the ground of state aid[10].

4. Digital significant presence

The **OECD/G20 Inclusive Framework on BEPS** published its interim report in March 2018. They conceded the difficulties of finding consensus on changing the rules on significant presence and profit allocation, acknowledging states' right to move forwards individually, and defining the parameters that unilateral measures should seek to operate within (most notable compliance with bilateral tax treaties[11].

On 29 January 2019 the Inclusive Framework published a policy note outlining the different scenarios currently under consideration[12]. The first group of scenarios (or 'pillar') addresses the digital economy specifically, with three proposals revising the rules of permanent establishment based either on marketing intangibles, user contribution, or significant economic presence. The second pillar refers to the remaining BEPS issues, and consists of a move to allow countries to tax profits if they consider they are being taxed too lightly in another jurisdiction. The later would naturally extend beyond the digital economy. A public consultation by the Taskforce on the Digital Economy will begin in March, after which the Inclusive Framework will elaborate a detailed programme of work to be presented to G20 Finance Ministers in June 2019.

---

[7] Valero, J. (2018), 'Moscovici: We are quite close to an agreement on the digital tax', *EURACTIV.com*. https://www.euractiv.com/section/digital/interview/moscovici-we-are-quite-close-to-an-agreement-on-the-digital-tax

[8] Ministero de Hacienda (2018), Anteproyecto de ley del impuesto sobre determinados servicions digitales.http://www.hacienda.gob.es/Documentacion/Publico/NormativaDoctrina/Proyectos/Tributarios/ANTEPROYECTO%20LEY%20IDSD.pdf

[9] Fossat, M. (2019), 'Taxe GAFA: Bruno Le Maire annonce qu'un projet de loi sera présenté en février', *BFMTV.com*. https://www.bfmtv.com/economie/taxe-gafa-bruno-le-maire-annonce-qu-on-projet-de-loi-sera-presente-en-fevrier-1615829.html

[10] Buell, T. (2019), 'National Digital Taxes Could Face State Aid Challenge In EU', *Law360 Tax Authority*. https://www.law360.com/tax-authority/federal/articles/1125172/national-digital-taxes-could-face-state-aid-challenge-in-eu

[11] OECD (2018), Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264293083-en

[12] OECD (2019), Addressing the Tax Challenges of the Digitalisation of the Economy – Policy Note: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project. http://www.oecd.org/tax/beps/policy-note-beps-inclusive-framework-addressing-tax-challenges-digitalisation.pdf

The European Commission's proposal for directive laying down rules on significant digital presence[13] received an overall-supportive opinion from the European Parliament adopted on 13 December 2018[14]. The proposal would complement the mooted Common Consolidated Corporate Tax Base, and would define a significant digital presence in a Member State if one or more of the following criteria were met: revenues from digital services of €7m, 100,000 users, or 3,000 business contracts for digital services. This model is one of the ones under consideration by the Inclusive Framework.

5. Conclusion

The various proposals for digital services taxes (be they EU-wide or national) are an important contribution to the ongoing debate around tax justice. The business models of firms operating in the digital economy have facilitated tax avoidance and encouraged rate competition between states, and the interim introduction of DSTs is an important first step in remedying this. However, the problem goes beyond the kind of online services that are easily isolated. This is why the progress announced by the Inclusive Framework regarding a global rewrite of tax rules is such good news.

At our 2018 Lisbon Congress, the PES adopted a resolution on the 'Progressive Economy' which called for the EU to support 'the creation of an international organisation, possibly under the UN, aiming at promoting social and fiscal fairness on a global scale'. The fact that several practical solutions appear within reach has strengthened our resolve to keep pushing for fiscal justice in the digital sphere.

For discussion

- The lack of progress regarding an EU-wide DST is likely to lead to one of two outcomes: the maintaining of the status quo or the implementation of national DST regimes that create friction in the Single Market. Is the cost of this friction too big a price to pay for a move towards fairer taxation?
- Even if the EU-wide DST were adopted, it would risk creating worldwide friction in the market for digital services; it also risks provoking retaliation against other sectors from countries that feel targeted (bearing in mind the context of the incipient EU-US 'trade war'). Are these risks worth taking to ensure European exchequers are no longer short-changed by digital companies?
- The proposed DSTs' thresholds are all revenue based, making no distinction regarding profitability. Will this harm emerging digital champions that are known to start with huge losses in their drive to broaden revenue? Can this be fixed?
- Supposing the recent G20/OECD breakthrough on profit shifting is able to demonstrate clear progress and offer a solution reachable in the next 2-3 years, should interim measures be postponed?

---

[13] European Commission (2018), Proposal for a Council directive laying down rules relating to the corporate taxation of a significant digital presence, COM (2018) 147 final. https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX%3A52018PC0147

[14] European Parliament (2018), Report on the proposal for a Council directive laying down rules relating to the corporate taxation of a significant digital presence, A8-0426/2018. http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A8-2018-0426&language=EN

- Despite the lack of enthusiasm in the Council, is the Commission's definition of significant digital presence suitable? Should it serve as a model for G20/OECD discussion?
- Is the shift to qualified-majority voting for tax policy in the Council of the European Union advocated by Commissioner Moscovici achievable? Is it a necessary step in the fight for fiscal fairness?
- Is an UN-sponsored 'Global Tax Agency' necessary to ensure developing economies are able to benefit from the structural changes in corporate taxation rules?

For more information with regards to the paper please contact elli.chrysanthakopoulou@pes.eu

Further reading

- EY (2018), 'ECOFIN agrees to extend discussions on Digital Services Tax, taking into account a new proposal from France and Germany', *Global Tax Alert*. https://www.ey.com/gl/en/services/tax/international-tax/alert--ecofin-agrees-to-extend-discussions-on-digital-services-tax---taking-into-account-a-new-proposal-from-france-and-germany
- European Parliament (2018), 'Common system of a digital services tax on revenues resulting from the provision of certain digital services', *Legislative Observatory*. https://oeil.secure.europarl.europa.eu/oeil/popups/summary.do?id=1566750&t=e&l=en
- OECD (2019), 'International community makes important progress on the tax challenges of digitalisation'. http://www.oecd.org/tax/international-community-makes-important-progress-on-the-tax-challenges-of-digitalisation.htm