The EU and transatlantic agenda on 'fair' corporate taxation: Is a Digital Services Tax a workable 'Plan B'?

Maria Kendrick[1]

Introduction

No international consensus has yet been reached on how to transform the international tax system in order to grapple with the global imperative of digitalisation. The need to raise tax revenue to fund public spending has been around since time immemorial, however, the modern mix of digitalisation and globalisation of the economy has created a new focus on tax avoidance and good governance[2] in the area of taxation, and essentially 'fair' taxation. This has been spurned on, especially at the EU level, by the need to generate resources in order to 'support' the Covid-19 recovery. This contribution will consider both EU and US/transatlantic agendas on 'fair' corporate taxation in a digitalised economy. What will become apparent is that trying to harmonise corporate tax to make it 'fair' is so difficult that we see both the EU and individual states unilateraly resorting to considering digital services taxes (DSTs) as a lesser, but not easier, 'Plan B' option.

The goal of addressing the tax challenges perceived to arise from digitalisation is inextricably linked to the goal of achieving a unified transnational agreement on corporate taxation, particularly regarding Multinational Corporations (MNCs). Beset by concerns, or allegations, of aggressive tax planning and tax avoidance, MNCs are the target set in the sights of the G20 / OECD, the UN and the EU. It is therefore the pursuit of fairness in taxation, being a question of economic justice among States regarding the distribution of the authority to tax and therefore revenue from taxation,[3] which has seen many initiatives and legislative proposals at the EU and international level dealing with, or attempting to deal with, corporate income tax. Harmonised 'fair' corporate taxation is the ideal, the effective 'Plan A' – at both transatlantic and EU level. The difficulty of achieving a global solution is that it requires a uniform not a differentiated approach. It is hardly a surprise that it is difficult to achieve agreement on a transnational scale, despite the fact that globally all States can agree on the revenue raising premise behind taxation. Eradication of differences effectively means eradication of competition, and States are as tempted to compete as much as MNCs.

Against this backdrop there has been politically complex, somewhat disjointed and spasmodic attempts to make proposals for transnational and EU harmonised corporate taxation. This does not occur in a political vacuum, but is rather set within the context of the triangular relationship between the US, Europe and China. A combination of global politics, a desire to raise revenue and maintain competitiveness, is inevitably going to lead to unilateralism, not just at state level but also between the international community and the EU. In addition,

---

[1] Dr Maria Kendrick is a Lecturer in Law in the City Law School at City, University of London.

[2] Whilst many international instruments refer to these concepts and use this terminology, a pertinent example for the purpose of this article is the UK-EU Trade and Cooperation Agreement, Part Two, Title XI, Chapter 5, Article 5.1 and 5.2.

[3] Gianluigi Bizioli, 'Fairness of the Taxation of the Digital Economy: Challenges and Proposals for Reform', in W. Haslehner, G. Kofler, K. Pantazatou and A. Rust (eds) *Tax and the Digital Economy* (Wolters Kluwer 2019).

sovereignty and a desire to remain competitive means that State unilateralism will continue, agreement at the global level will therefore be difficult to reach.

In addition, data and analysis demonstrates that behind the proposals there are questions about the definition of 'digital economy' and whether it can be ring-fenced, whether it would be able to produce neutral and equitable and therefore 'fair' taxation, and ultimately whether it would produce the level of tax revenue to actually encourage states to abandon their own sovereignty in exchange for the revenues generated in their jurisdiction. There is also a dispute over the essentials of the proposals; whether tax reform should be focused on profit or revenue/turnover.

Consequently, 'Plan A' has so far not been achieved, and DTSs, with varying designs and scope, have been proposed and in some states implemented. What is now apparent is that there are varying attempts to achieve global solutions, but on minimum or less ambitious scales, concurrently with the imposition of, and proposals for, DSTs temporarily in lieu, or perhaps permanently instead of, harmonised global corporate income tax. **A digital services tax is therefore not the number one choice but the interim solution, or the 'Plan B'.**

The Absence of Tax Consolidation and EU / Transatlantic Cooperation

The proposals have featured discussions on a minimum global corporate tax rate and a shift to source taxation. In essence, the issue concerns the measurement of income, or taxable 'value', generated in the source jurisdiction through digital business models without a necessarily corresponding 'brick-and-mortar' physical presence or establishment. It is the definition and application of these terms, among others, which has been the cause of international negotiation and acrimony for many years, and which has led to unilateral action.

While the UN proposal has a digital focus with a global or regional based choice, the OECD Base Erosion Profit Shifting (BEPS) initiative proposes, in Pillar One, a new nexus and profit allocation rules, whereas Pillar Two effectively seeks to enforce a global (but still to be determined) minimum level of effective taxation on income derived from large MNCs involving reallocation and apportionment of income between jurisdictions. The jurisdiction to which the reallocation is made can tax the income on the difference between the globally agreed rate and the MNEs actual effective tax rate. Still at blueprint stage, Pillar Two includes an income inclusion rule (IIR) and an undertaxed payment rule (UTPR), which together form the 'GloBE' rules. This includes the method for determining the effective tax rate and for imposing tax on a co-ordinated basis.

Pillar One BEPS, like the EU's proposed Common Consolidated Corporate Tax Base (CCCTB), envisages a global consolidated revenue, with an application threshold of EURO 750 million. Upon implementation of the Pillar One proposal, the idea is that any unilateral measures that have been implemented by jurisdictions to tax digitalised businesses, such as DSTs, should be abolished with this global consensus-based solution prevailing. Both measures need consolidation and cooperation to work, they also need to replace unilateralism to be effective. It is within the context of the broader agenda on consolidation of global corporate taxation that digital services taxes should be considered as a 'Plan B'. In comparing DSTs with

'Plan A' the key components which are missing in the current state of play, in adopting the latter, are consolidation or harmonisation.

Since 2015, the OECD has been releasing interim reports on the progress of adopting the BEPS Pillars, outlining the specific characteristics and tax challenges of the digitalisation of the economy. The G20/OECD Inclusive Framework committed to deliver a consensus-based solution by the end of 2020. As in any attempt to reach a 'unified approach' there remain differences of views. With an underlying desire to remain competitive and raise revenue, it is unsurprising that the sticking point appears to be profit reallocation. The aim is for the approximate 140 states to reach at least political agreement by the mid-2021. This is a deadline which has been pushed back, not least from mid-2020, affected of course by the pandemic, but this imperative can work both ways, due to the acceleration in global digitalisation the pandemic has caused.

The shifting deadlines from mid 2020 to 2021 can also be explained by the change in the US Administration, which has seen the new Biden administration appoint a series of tax academics to his Treasury team in the Office of Tax Policy, notably in favour of a global minimum tax and an OECD level solution. For instance, the United States' Global Intangible Low Taxed Income Regime (GILTI) would be treated as a Pillar Two compliant under the IIR, and as the US has now 'dropped' its desire for a 'safe harbour', which would have seen companies effectively opt-in to the system on a voluntary basis, renewing hope for global cooperation. However, the US "will engage robustly to address both pillars of the OECD project, the tax challenges of digitisation and a robust global minimum tax", and it has shown opposition to state unilateralism, where the former USTR of the Trump Presidency stated that it considers the Austrian, Spanish and UK digital taxes to be discriminatory against US firms. Meanwhile, the EU is still simultaneously pursuing its own proposals for a DST, without dropping its hopes of delivering the CCCTB. There seems to be an absence of true global cooperation.

Will the EU go it alone? Will the US help or hinder?

Although the EU has been very vocal about contributing to, or trying to influence the shape of, global solutions, it has also been very vocal in asserting that should a global solution not be found it will pursue its own EU level policies. The EU reiterated its position, in its July 2020 Communication on an Action Plan for Fair and Simple Taxation Supporting the Recovery Strategy, that it is prepared to pursue its own EU DST should a global solution not be forthcoming. In fact, according to recent reports, it may even do so regardless, confirming the lack of cooperation internationally and EU unilateralism.

The EU DST has been described by the Commission as an 'interim' less preferred option to a comprehensive policy, which would optimistically see harmonisation of EU law on the subject of digital permanent establishments and profit allocation rules being incorporated into its proposals on the CCCTB. The CCCTB 'Plan A' envisages harmonisation to the corporate tax base only, not corporate tax rates, including a facility to opt-in. It is a relatively broad and ambitious proposal, which has so far failed to be implemented in the EU, with many Member States opposed. It is because of the difficulty in achieving harmonisation of corporate tax on a broad scale, that use of differentiated integration has been considered, and an interim DST suggested. The 'Plan B' DST has still to be agreed upon, coming up against some of the same objections as 'Plan A' in terms of its workability and ultimately its revenue raising ability.

In its Communication to the European Parliament and Council on 'A Fair and Efficient Tax System in the European Union for the Digital Single Market', the Commission declared the establishment of the digital single market as one of its ten political priorities. This was in 2017. Since then, the DST, explained previously as an interim measure forming part of the harmonising agenda in taxation, has so far failed to be adopted, following a negative vote in the Council in March 2019. This is even on a proposal of limited scope, which had reduced the DST to a sales tax on digital advertising services. The previous, comparatively extensive, proposal was for a uniform tax rate of 3% on revenues generated by selling online advertising space, from digital intermediary activities between users for facilitating the sale of goods and services, and from the sale of data generated from the user-provider information. It would have applied only to companies with total worldwide revenues above EURO 750 million and EU revenues of EURO 50 million. At the 4 December 2018 ECOFIN Council meeting, France and Germany urged the adoption of a DST on a more limited tax base described as 'referring to advertisement', but stated that a Directive enacted on this basis 'would not prevent Member States from introducing in their domestic legislation a digital tax on a broader base', which France, among other Member States, has subsequently done.

On 14 January 2021 the Commission launched its impact assessment 'roadmap' for an EU digital tax, on the rationale of achieving fair taxation, with a view to proposing a draft Directive around the middle of 2021, deliberately corresponding with the new OECD timeline. Even as a 'Plan B' the DST is the Commission's more desirable option for addressing the digitalisation of the economy than what has subsequently happened, which is some Member States, and the UK, implementing their own versions of a DST, although at varying tax rates and varying qualifying revenue thresholds.

A unilateral approach sees the UK with a 2% DST, 5% in Austria, 3% in France and Spain, and up to 7.5% in Hungary, with France's DST having the widest tax base. State sovereignty is still apparent in the arena of transnational taxation. In fact, approximately half of all European OECD countries have either announced, proposed, or implemented a digital services tax. Many OECD countries have digital taxes or plans to impose them. Several US states also have proposals for taxing the digital economy. Whilst the UK has expressed a commitment to disapply its DST in the event that an appropriate international solution is reached, there is no guarantee as to whether it, or indeed other countries, will repeal their DSTs at all nor how quickly they would be prepared to do so and how much revenue raising at the EU or international level is required to tempt them to do so. The tax base, rates, global and domestic revenue thresholds all differ. Even the OECD admits the absence of a consensus-based solution would likely lead to a proliferation of uncoordinated and unilateral tax measures. One could expect that more and more EU countries will actively try to defend taxation rights and try to extract more revenues from value created within their own state borders.

Competitive Harmonisation within or between the EU and the US?

Overall, there is still conflict on definitions of nexus (where to tax) and value (what to tax). The difficulty in defining value creation in the digital context is the need to address the question of how to attribute profit in new business models driven by intangible assets, data and knowledge. Of all of the discussion on the digitalisation of the economy being increased at a rapid pace because of the pandemic, differentiation and minimum harmonisation are likely in light of the struggle to reach any agreement. **Whilst it may appear that the digitalisation imperative is moving global tax policy in one direction, reality is likely to see differentiation and minimum standards set in limited areas, on limited aspects of tax policies.** The unilateral adoption of DSTs has shown that whilst a DST is possible, at the international and EU level it is at best 'Plan B' and difficult to achieve. However, what, if anything, is agreed, we should not underestimate the likely fervour with which it will be presented as an agreement to take action on fair taxation, rather than at best, 'Plan B'.