

## Trade and Investment

### Commission on Taxation

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#### ICC Comments on EU consultation on fair taxation of the digital economy

ICC appreciates the opportunity to provide input on the European Union (EU) consultation regarding fair taxation and a new digital levy. ICC advocates for a consistent global tax system, founded on the premise that stability, certainty and consistency in global tax principles are essential for business and will foster cross-border trade and investment. ICC fully supports a harmonised approach to ensure that international tax rules remain relevant and applicable in an increasingly digitalised global economy.

ICC respectfully acknowledges the commitment by the European Commission (EC) to establish a common EU approach on the taxation of the digital economy that would provide an efficient tax framework that stimulates economic growth and job creation in the region. The current initiative for a new digital levy expresses the aim “*to ensure fair taxation in the digital economy, while at the same time contributing to Europe’s recovery. Fair taxation and ensuring that Europe is fit for the Digital Age are top priorities for the European Commission.*”

Taxpayers and tax authorities are currently burdened by a myriad of different measures seeking to address the tax challenges of the digitalisation of the economy—corporate income taxes, the OECD Pillar One and Two Blueprints, existing DSTs, etc, which would be compounded by the EU digital levy. ICC is concerned that continued pursuit of a multitude of international digital tax measures will lead to a high degree of unnecessary complexity, uncertainty, and inevitable multilayer taxation. ICC believes that the on-going work at the OECD, with the active participation of the EU members and the European Commission, will provide solutions to this issue.

#### General comments

##### *Need for global co-operation and co-ordinated effort within OECD Inclusive Framework*

ICC wishes to reiterate the importance of a harmonised and collaborative global approach within the context of the OECD Inclusive Framework to address the tax challenges of digitalisation. ICC strongly recommends that any new measures should be developed on the basis of international tax rules and seek an alignment with global efforts to ensure consistency and coherence, be non-discriminatory and avoid double and over-taxation.

As digitalisation continues to increase in importance as a driver for global economic growth, policies related to the taxation of the digitalised economy should seek to promote, and not hinder, economic growth and cross-border trade and investment. For the ICC business community, the integrity of the international tax system is of critical importance — coherent and co-ordinated implementation of international guidelines is essential in establishing a consistent global tax system that better facilitates cross-border trade and economic growth. Unilateral disparate tax rules that introduce double or multiple standards create compliance challenges for business, risk double taxation, and undermine the consistency of the international tax system. Such measures should be withdrawn at the time a political agreement is reached.

ICC remains concerned that exploring proposals for an EU digital levy in parallel to ongoing work within the OECD Inclusive Framework could undermine existing efforts to reach global agreement.

ICC believes that the EU and its Member States should continue focusing their efforts on supporting and advancing the ongoing discussions within the OECD Inclusive Framework, with the aim of reaching agreement on a multilateral solution by the mid-2021 deadline. A co-ordinated and well-integrated approach agreed at global level would enable consistent implementation by countries in accordance with internationally agreed rules. The proliferation of unilateral, national measures will result in further fragmentation of the global tax system and other effects such as growing trade tensions and a slowing of economic growth.

ICC notes and supports the European Commission's intention, as expressed in its Inception Impact Assessment (IIA), "to not interfere with" or "undermine" the ongoing work within the OECD Inclusive Framework, however it is uncertain how the proposals for a digital levy would not essentially have that effect and complicate what are already challenging negotiations at the OECD Inclusive Framework level, in addition to exacerbating trade tensions. ICC holds that the Inclusive Framework should also be given a reasonable period of time to explore the scope for an agreement with the new US administration. Very positive signals have come out of the G20 Finance Ministers meeting on 26 February 2021, with all G20 Finance Ministers confirming strong support for an agreement on both Pillars by July 2021 and US Secretary Yellen making the important step of dropping the request for a safe harbour.

The IIA indicates that the digital levy is to "be designed in a way that is compatible with the international agreement to be reached in the OECD", however it would appear premature to develop a legislative digital levy proposal before such agreement has been reached on the design of the international rules.

ICC encourages all participating countries in the Inclusive Framework, including EU Member States, to garner their collective efforts through a comprehensive, coherent and co-ordinated approach to move swiftly to a global consensus-based, comprehensive income-tax based solution that is applied equally to all segments of the digitalised economy and does not discriminate or create competitive distortions. The new rules should be profits-based, administrable, increase tax certainty, be treaty compliant, reflect long-standing income tax principles, recognise the value of technology intangibles, non-discriminatory, minimise double taxation, and include strong dispute resolution mechanisms.

### *Fragility of global economy as result of COVID pandemic: Need for pro-growth tax policies*

The world is currently enduring a global financial crisis due to the COVID-19 pandemic. As a result, the need for pro-growth tax policies is particularly acute. The OECD has in the past said that corporate income taxes are the most harmful for growth as they discourage the activities of firms that are most important for growth: investment in capital and productivity improvements. The OECD's Interim Economic Outlook (September 2020) noted that global output collapsed by 20% in some advanced and emerging market economies in the first half of 2020. Uncertainty remains high, confidence is fragile, and recovery is not guaranteed. ICC believes that, depending on the design of the digital levy, it could be a growth-depressing measure, at exactly the time when the European economy needs stimulating. The proposed digital levy could have a knock-on effect on the global economy when it is currently in a fragile state as a result of the COVID-19 pandemic. Independent research<sup>1</sup> has shown that SMEs and other parties in the supply chain are negatively impacted by

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<sup>1</sup> Copenhagen Economic (2018), [The Impact of an EU Digital Service Tax on German Businesses](#); Deloitte Taj (2019), [The French Digital Service Tax, an Economic Impact Assessment](#); Prometeia-Netcomm (2018), [Italian DST](#) (in Italian); IFO Institut (2018), [German DST](#) (in German).

digital tax measures, which act as an effective tax on digitalisation and innovation. With the current COVID restrictions, digital channels have enabled businesses to continue their economic activities, which is essential in driving economic recovery. The Commission should be encouraged to undertake detailed economic analyses of the impact of the proposals, interaction with any OECD agreed approach and EU member state unilateral measures.

The 2015 OECD Base Erosion & Profit Shifting (BEPS) Action 1 Report concluded the digital economy is increasingly becoming the entire economy and cannot be ring-fenced for tax purposes. Business models continue to evolve, and digital transformation is just beginning with artificial intelligence, machine learning, IoT, and augmented reality. Digitalisation is creating economic opportunity for small and large businesses and enables economies, including the EU, to significantly improve the economic and social future for their citizens. As a revenue raising measure, an EU official recently acknowledged that ringfencing the digital economy to include only the largest (primarily U.S.) MNE's would not raise sufficient revenues to accomplish the digital levy's objective of funding COVID-19 relief and recovery – defeating any reason for harming this essential sector.

As noted above, ICC fully supports a harmonised approach to ensure that international tax rules remain relevant and applicable in an increasingly digitalised global economy. As such ICC reiterates the need for countries to continue to garner their collective efforts to achieve a global consensus-based solution in the context of the OECD Inclusive Framework.

#### Possible trade tensions

Unilateral taxes, such as the proposed digital levy, when designed with a narrow scope of services covered and revenue thresholds set at levels so as to single out a sub-set of primarily foreign companies for taxation, whilst having very limited effects on local companies, have impacts that reverberate in other policy areas, most notably trade. Such a tax effectively operates as a trade barrier by causing in-scope companies to lose out on business to local rivals that do not meet the revenue thresholds or the strict business model definitions in the tax, establishing a difference in treatment between foreign and domestic competitors. The overall impact negatively impacts the EU Single Market by making it all the harder for businesses and consumers alike to benefit from productivity-enhancing goods and services and contributing to a less friendly business environment. As noted above, this detrimental impact on European firms grows as jurisdictions outside of Europe impose even more expansive national taxation measures. As evidenced by the reaction seen in response to the Digital Service Taxes, some countries may view a digital levy as discriminatory which could result in trade retaliation<sup>2</sup>.

ICC strongly recommends that National Member State Digital Services and Digital Advertising taxes and other unilateral measures should be withdrawn (and no new such taxes can be imposed) at the time of political agreement. A digital levy should not be imposed in addition to national unilateral measures or any OECD agreement.

#### Risk of ring-fencing the digital economy

ICC concurs with the OECD BEPS Action 1 Report conclusions—reiterated in the interim report—that “it would be impossible to ring-fence the digital economy for tax purposes”. In this respect, ICC notes that each one of the three options listed in the Inception Impact Assessment appears to be

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<sup>2</sup> ECIPE (2019), [Digital Service Taxes as Barriers to Trade](#); ECIPE (2018), [The Cost of Fiscal Unilateralism: Potential Retaliation against the EU Digital Services Tax \(DST\)](#).

intended to ringfence the digital economy for taxation purposes. ICC strongly recommends that any measures being considered by the EC be aligned with the international OECD tax framework to ensure consistency and coherence that would go a long way in establishing a level international playing field for business, as well as co-ordinated implementation at global level. International tax co-operation is essential to ensure that any tax reforms should be both practicable and effective. It would, in the view of ICC, be the best way to successfully deal with the issue of fair taxation in the digitalised economy, while not increasing the compliance burden and risk of double taxation for businesses, as well as fostering cross-border trade and investment and economic growth.

### Consultation questionnaire

ICC members note that the consultation questionnaire is drafted in such a way as to lead to a pre-determined conclusion in support of the Digital Levy, rather than canvassing a range of views to allow rounded and objective evidence-based conclusions to be drawn. This calls the credibility and value of the consultation into question.

### Specific comments

ICC believes that the scope of a possible digital levy should be based on thorough economic impact analysis and not specifically target digital businesses. The digital economy is the fastest-growing, most vibrant part of the economy that will drive future prosperity in Europe. As noted above, ICC, therefore, holds that the digital economy should not be ring-fenced and targeted with discriminatory tax measures. Any new measures must be future proof to support the continued growth and expansion of Europe's digital businesses.<sup>3</sup>

### **Purported Justification for Digital Levy:**

- The Inception Impact Assessment outlines the problem the digital levy seeks to address as one in which digital businesses are able to shift profits and are undertaxed. In recent years we have seen the Anti-Tax Avoidance Directives (ATAD 1 and 2), the OECD Base Erosion & Profit Shifting (BEPS) measures and US Tax reform which have changed the tax landscape, eliminated no-tax income (for US companies) and curtailed profit shifting. After U.S. tax reform, U.S. businesses are subject to U.S. tax on their foreign income so there is no more “stateless income” not subject to tax for U.S. businesses. In addition, businesses that report revenue and expenses in the local jurisdiction should be exempt from special taxes, if any.
- The purported justification for the Digital Levy is that digital companies do not pay tax or pay less than traditional businesses. In this respect, ICC highlights academic studies by both ECIPE (“Digital Companies and Their Fair Share of Taxes,” ECIPE Occasional Paper (3/2018))<sup>4</sup> and Copenhagen Economics (“The Proposed EU Digital Services Tax, Effects on Welfare, Growth and Revenue”)<sup>5</sup> which, based on analysis of empirical data on effective tax rates in the digital and other sectors, found that digital business did not in fact pay less tax than other sectors. ECIPE's study concluded that there was no material difference in

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<sup>3</sup> Studies have shown that a narrow definition of some firms as ‘digital’ causes distortions, see Copenhagen Economic (2018), [The proposed EU Digital Services Tax: effects on welfare, growth and revenues](#) and ECIPE (2018), [Digital Companies and their Fair Share of Taxes: Myths and Misconceptions](#).

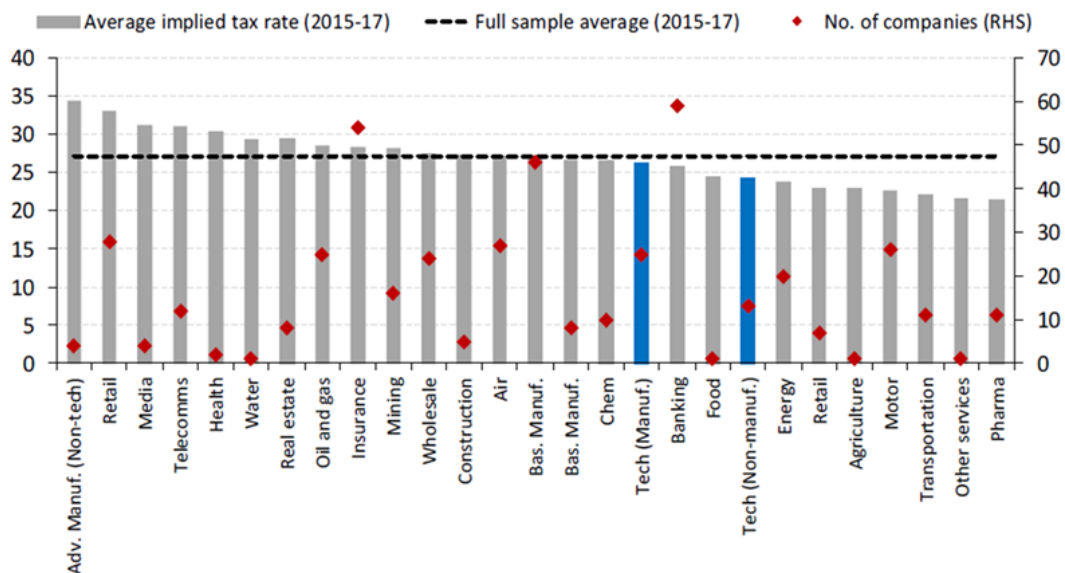
<sup>4</sup> ECIPE (2018), [Digital Companies and their Fair Share of Taxes: Myths and Misconceptions](#).

<sup>5</sup> Copenhagen Economics (2018), [The Proposed EU Digital Services Tax, Effects on Welfare, Growth and Revenue](#)

rates. Professor Spengel from the University of Mannheim, whose work was quoted in the Commission’s DST proposals, also made similar points and noted that work cited in the DST work on tax rates of digital companies had been misinterpreted by the Commission.<sup>6</sup> We also make reference to the IMF Working paper 20/76 - Tec(h)tonic Shifts: Taxing the “Digital Economy”<sup>7</sup> which indicates: “What we see is that the tech sectors report implied average tax rates more or less in line with the average of other Fortune Global 500 firms. What is most striking is that the implied tax rates are certainly non-zero, and therefore we can reject the widely-held hypothesis that on average these companies pay zero or low corporate income taxes at the globally consolidated level.”(pg 71). The working paper also provides a useful comparison of average implied tax rates for Fortune Global 500 companies by sector (pg 72) – extract provided below:

**Annex Figure 11. Average Implied Tax Rates (Income Statement) for Fortune Global 500 Companies, by Sector**

(LHS: Percent; RHS: Number)



Sources: Bureau van Dijk Orbis; Fortune, and authors’ calculations.

Note: Unweighted averages. PSTA=professional, scientific, and technical activities.

- It should be noted that sales by digital businesses to EU customers are fully subject to VAT.
- The Inception Impact assessment highlights a number of features of digital business models as a justification for the digital Levy:
  - **The ability to operate in a jurisdiction and earn revenues elsewhere**  
Remote selling of services is not new nor limited to digital businesses. If this is the issue, ICC members believe that it could be addressed by agreeing a global

<sup>6</sup> Prof. Spengel’s [interview on the EC’s proposal to tax the digital economy](#).

<sup>7</sup> <https://www.imf.org/en/Publications/WP/Issues/2020/05/29/Tec-h-tonic-Shifts-Taxing-the-Digital-Economy-49363>

solution at the OECD where Pillar One applies to all remote sales booked outside of the jurisdiction without need to limit the scope to digital business models.

- **User value creation**
  - An enterprise creates its success through various channels or avenues of value including deployment of personnel and capital resources. Innovation and production create value along with application of the enterprise's investments in advanced computer processing and software tools.
  - Were an extraordinary allocation of taxation rights to the jurisdiction where users reside be justified, the same justification would apply to an allocation to the jurisdiction of the purchasers of luxury goods, high-performance automobiles, or any other product or service.
  
- **Profit shifting through intangibles**
  - In recent years we have seen the Anti-Tax Avoidance Directives (ATAD 1 and 2), the OECD Base Erosion & Profit Shifting (BEPS) measures and US Tax reform which have changed the tax landscape, eliminated no-tax income (for US companies) and curtailed profit shifting. Many groups have proceeded with plans to locate valuable intangible property assets in legal entities which are fully taxable. Anti-hybrid measures have created incentives to locate IP onshore.
  
- **Scale without mass and Network effects**
  - The benefits of network effects and market power are not something new arising as a result of digital business models; these are basic economic concepts which apply equally across all industries. The existence of universal economic forces which are not unique to digitalised business cannot be used as a justification to impose different taxation principles on certain ring-fenced businesses. Network effects or even sheer numbers of active users do not guarantee a company's longevity whether it is an intermediation platform, a news site, a social media company, or a traditional retailer or manufacturer. Users are drawn to sites by services, branding, and features, all of which are a product of a company's entrepreneurial efforts.
  - The Inception Impact assessment refers to digital businesses having scale without mass. Many digital businesses supplying the services described as in-scope, have enormous scale and enormous mass as well.
  - ICC notes that it would be useful to take into account the diverse contributions of participants in a digitalised economy, including the value of research and development and investment in capital assets, as well as the interplay between data and technology. Companies spend billions of dollars annually to create the infrastructure and technology necessary to create the systems that support digitalised services.

#### **Design of Levy:**

- To date, there is little detail (or guidance) from the EU on the design of a digital levy. Each one of the three options listed in the Inception Impact Assessment appears to be intended to ringfence the digital economy for taxation purposes and may discriminate against certain industries – which is incompatible with the expected international agreement to be reached in the Inclusive Framework as well as broader international obligations.
- DSTs and similar unilateral, targeted tax measures share several problematic characteristics, such as their application to gross revenues instead of net profits; multiple

revenue thresholds and other stipulations that target largely non-resident, globally engaged companies and a narrow scope of covered digital activities.

- Taxing corporate revenue, rather than income, is inconsistent with international tax principles – as reflected, for example, in the OECD Model Tax Convention on Income and on Capital, the United Nations Model Double Taxation Convention, and over 3,000 bilateral tax treaties. Revenue-based taxes are inherently flawed and intrinsically discriminatory as they fail to take into account costs and profit margins in different sectors, business models and stage of growth. Revenue-based taxes are all the more concerning where these are no longer viewed as an “interim” solution until consensus is reached within the OECD Inclusive Framework but rather as a revenue-raising measure. A revenue tax of the type mentioned also raises the question of whether the levy would replace or complement existing national DST initiatives (to the extent these can continue to exist following an agreement on Pillar One or if there is no agreement).
- This approach appears to penalise low-margin and loss-making companies and subjects affected companies to potential multiple taxation and significant compliance costs. A unilateral levy would be a significant cost to business, require separate administrative intervention and compliance and make the taxation system more onerous. In addition, there is a risk of double taxation if one country imposes a turnover-based tax which is outside the framework of double tax agreements. Furthermore, a turnover-based tax would create cost-based barriers to entry, undoubtedly penalising European start-ups and stifling innovation. This in turn would have a knock-on effect on jobs and growth. Tax costs would likely be recovered from consumers in larger markets and prevent entry into smaller markets. Adopting such a levy would also adversely affect EU competitiveness and risk economic growth in the region. A digital levy could also have a negative impact on solvency or investment opportunities for business.
- If the intention is to address perceived flaws in the corporate income tax treatment of the digital economy, ICC suggests that revenue-tax based solutions are a poor answer as they struggle to properly address issues around double taxation, loss relief, complexity, administrative burden etc.
- In terms of the “tax on revenues” and tax on B2B “digital transactions”, these appear to unfairly target gross revenues of certain digital activities. It is concerning that the EC appears to be seeking to broaden the scope of existing national-level digital services taxes (DSTs), which are themselves discriminatory and distortive. Tax systems are generally designed to avoid taxing business inputs, e.g., in VAT. Any departure from this system would negatively impact the take-up of digital practices in EU businesses.
- Subjecting companies to an EU-wide corporate tax without regard to whether or to what extent they have a permanent establishment in-country is inconsistent with the international tax laws vis-à-vis bilateral tax treaties as well as international tax principles reflected in the OECD model tax treaty and other instruments, and will, like taxing revenue, create the risk of multiple taxation, significant compliance costs, and greater uncertainty.
- It is unclear how a “corporate income tax top-up” could function in respect of activities in the EU when companies operate from both within and outside the EU, and when corporate income taxes are covered taxes under bilateral tax treaties. From a purely mechanical design perspective, a top-up tax would be the most straightforward option, but it could have a damaging effect on investments in digitalisation and negatively impact economic growth.
- It is unclear how such an EU digital levy measure would interact with an OECD solution.
- With respect to the three policy options, ICC notes that part of the discussions on Pillar One regards so-called “differentiation mechanisms”. More specifically, the question of whether the different components of the Amount A formula should apply similarly in all circumstances, or whether some variations are necessary to increase (or decrease) the amount of profit reallocated to market jurisdictions in some cases. The Pillar One Blueprint notes that such variations could have a significant impact to the general

application of the Amount A rules. An important issue in this respect regards a suggestion to weight amount A based on “digital differentiation.” Such mechanism would account for different degrees of digitalisation between in-scope business activities (e.g., based on the ADS definition used for scope), and increase the quantum of profit reallocated for certain types of business activities. This would seek to target digital businesses, particularly those with lower marginal costs that are seen as deriving greater benefits from scale without mass. The impression is that the current Pillar One discussions (continue to) move away from any ring-fencing of the digital economy and digital differentiation. The consensus-based outcome on Pillar One is (therefore) less likely to reflect digital differentiation. However, this seems in essence what the Commission’s proposal, as reflected through the three policy options, is trying to achieve here. Therefore, as things stand, a separate, additional, unilateral measure to achieve digital differentiation would be at odds with a multilateral consensus-based solution within the context of the OECD. As mentioned above, we believe the EU and its Member States should instead continue focusing their efforts on supporting and advancing the OECD led discussions, with the aim of reaching agreement on a multilateral solution by the mid-2021 deadline.

- There is also little information on the closely connected question of the EU’s next steps both where there is and where there is no agreement on Pillars One and Two at OECD Inclusive Framework level. The publication of the Commission’s “Communication on Business Taxation for the 21st century” outlining the EU’s next steps was originally scheduled for October 2020 but has been delayed a number of times. Based on the limited information in the IIA, the intention seems to be for the digital levy to apply on top of any IF solution or, if there is no agreement at the IF level, an EU, “go it alone”, solution. However, where there is agreement on Pillars One and Two, the digital levy appears to be the type of unilateral measure Pillar One in particular would be looking to eliminate. ICC, therefore, suggests making clear that if there is agreement on Pillar One, a company already subject to a Pillar One allocation would be excluded appropriately from the digital levy to avoid double taxation. Not doing so may also hamper ongoing negotiations.

### Closing remarks

ICC reiterates that unilateral disparate tax rules that introduce double or multiple standards create compliance challenges for business and create the risk of double taxation. ICC supports the multilateral process within the OECD Inclusive Framework and calls for countries to garner their collective efforts for a global consensus-based solution that avoids unnecessary complexity, uncertainty and double taxation. ICC believes that in order to increase cross-border trade and support the recovery of the global economy, the EU and individual countries should be focused on simplifying their tax systems rather than add further complexity and unilateral measures.

The rapid evolution of digitalisation has permeated many spectrums of life, including the way that businesses operate today. ICC fully supports a harmonised approach to ensure that international tax rules remain relevant and applicable in an increasingly digitalised global economy. ICC believes in the importance of staying true to the basic principles of taxation because, as business becomes increasingly digitalised, these solutions will apply to the entire economy.

The digitalisation of the economy raises challenging issues. ICC believes that the on-going work at the OECD, with the active participation of the EU members and the European Commission, will accommodate solutions to this issue. ICC reiterates that any solutions should be capable of accommodating evolutions in business models and should have broad adoption by countries to allow for a seamless application for business.



## **About The International Chamber of Commerce (ICC)**

The International Chamber of Commerce (ICC) is the world's largest business organization representing more than 45 million companies in over 100 countries. ICC's core mission is to make business work for everyone, every day, everywhere. Through a unique mix of advocacy, solutions and standard setting, we promote international trade, responsible business conduct and a global approach to regulation, in addition to providing market-leading dispute resolution services. Our members include many of the world's leading companies, SMEs, business associations and local chambers of commerce.

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