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The Union of Entrepreneurs and Employers' position on the digital levy

We welcome the European Commission's consultation on the digital levy. The consultation document recognizes the progress made thanks to digitization while highlighting the need for regulation of the digital world and placing it within the context of other EU's initiatives. At the same time, the consultation document implies that digital companies do not contribute their fair share in taxation. Furthermore, the initiative does not provide much detail about the construction of the future tax and enumerates three potential approaches, namely a top-up tax on corporate income aimed at digital companies, a tax on revenues and a tax on digital business-to-business (B2B) transactions. There is a number of fundamental problems related to this initiative.

The first relates to **the lack of a clear definition of what constitutes a digital business**. According to the OECD, '[b]ecause the digital economy is increasingly becoming the economy itself, it would be difficult, if not impossible, to ring-fence the digital economy from the rest of the economy for tax purposes.'[1] The lack of a commonly agreed definition also means that the precise scope of the future digital levy is unclear. While EU's initiative aims at creating a level-playing field for the European companies, a tax on digital activities is very likely to burden a vast majority of them and further deteriorate their ability to compete globally. The scope of a possible digital levy should be based on a thorough economic impact analysis and not target digital companies without justification.

The second issue concerns the fact that **the fairness argument is based on incorrect assumptions**. In 2017, the EC has referred to a PWC and ZEW report showing that the effective average rate of digital companies is three times lower than that of traditional ones.[2] Nevertheless, PWC has published a special note explaining that the data presented did not reflect the actual tax rate of specific companies, but only the rates tax rates on returns from investments in intangible assets, and hence they cannot be used to compare the level of taxation of digital and traditional companies.[3] Furthermore, dr. Matthias Bauer from ECIPE has researched the effective tax rates of digital and traditional corporations, which found that the traditional corporations paid slightly less tax than the digital ones (26.8% vs. 27,1%).[4]

The third point, which is in our opinion highly problematic, is **the introduction of the digital levy during the ongoing crisis.** The health and economic crisis caused by the pandemic of coronavirus is far from over. Regardless of its' final construction, the digital levy will increase the costs of the digital services, which

[1] https://www.oecd-ilibrary.org/docserver/9789264218789-en.pdf?expires=1617886901&id=id&accname=guest&checksum=193CF9B4B724F6041E9291393EB34E0A
[2] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52017DC0547&from=PL p. 6
[3] https://www.pwc.com/us/en/press-releases/2018/understanding-the-zew-pwc-report.html
[4] https://ecipe.org/wp-content/uploads/2018/02/ECI_18_OccasionalPaper_Taxing_3_2018_LY08.pdf

have become the primary means of work for many across the globe. Moreover, the Copenhagen Economics study has shown taxes on digitization and innovation effectively burden tahe SMEs and other end-users[5] Finally, it is important to note that the Commission sees digitization as an important motor of a post-pandemic recovery, while increasing the costs of digital services will slow down the recovery process.

Another pertinent point is the **consistency of digital levy with other EU's strategic objectives.** The first and most important concern in this regard relates to **the EU's commitment to multilateralism**. The OECD work on the digital taxation is ongoing. Particularly since the new US administration has re-engaged in the discussions, the EU's unilateral introduction of the **digital levy would undermine the OECD efforts** and possibly lead to trade tensions. The second mismatch exists between the digital levy and **the Tax Action Plan.** The EU has pledged to create a simple tax environment to reduce obstacles for businesses in the Single Market. The digital levy, which will add a new layer to an already overly complicated system (which includes digital service taxes imposed by some countries), stands in opposition to this idea.

Finally, in our view, **the three approaches to the digital levy have certain important limitations**. First, a top-up tax on corporate income would have to be compatible with a variety of corporate tax systems across the EU, to including varying tax rates and deductions. Second, **the tax on revenues will lead to double taxation. Introducing a tax on revenues**, which have already been subject to a corporate income tax in a country where the users and merchants are based, amounts to levying an additional value added tax or excise duty. Tax on revenue can be also harmful to less profitable European businesses. Generating revenue is not equal to generating profit, hence such tax is discriminatory towards companies with smaller margins as they will bear a greater burden of the tax. Third, the tax on digital business-to-business transactions is likely to create negative effects for all market participants – digital companies selling within the EU, SMEs and consumers in particular. It is important to keep in mind there is a number of reforms in the field of digital B2B transitions already underway and putting forward digital levy would further complicate the system.

In brief, the EU should support reaching a globally agreed solution at the OECD to reform the international tax framework. A proposal for a European digital tax should be put forward only in case if the OECD negotiations break down. In that event, the proposal should include solutions proposed on the OECD level as to minimize any potential tensions. Alternatively, when a consensus on the OECD level is reached, Member States, which have implemented digital taxes, should withdraw then as to prevent a fragmented and multilayered taxation. Finally, we suggest a holistic approach to the digital levy. Not only ongoing OECD works but also existing tax rules related to online activities (inc. eCommerce VAT Directive and Proposal for DAC 7 Directive, currently finalized) should be taken into account.

[5] https://www.copenhageneconomics.com/publications/publication/the-impact-of-an-eu-digital-service-tax-on-german-businesses

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