Thank you for the opportunity to provide comments on the Section 301 Investigation. These comments summarize the discriminatory nature of Digital Services Taxes (DSTs) which arise from their design. These comments also provide some details on the policies targeted by the Section 301 investigation including the unique features of the various policies.

**DSTs and their Discriminatory Features**

**Scope**

- DSTs effectively ring-fence the digital economy by limiting the tax to certain revenue streams of digital businesses, discriminating in favor of more traditional sectors of the economy.

- Within sectors, digital businesses are at a relative disadvantage to non-digital businesses—e.g., online vs. traditional advertising.

A tax policy that singles out specific sectors for special treatment is likely to create distortions in market behavior. In the case of DSTs, that targeted treatment will create disadvantages for digital businesses relative to other sectors that provide similar services. For instance, a business that provides online advertising services may compete with a business that provides advertising services in print or other media. Under a DST that covers online advertising, the online advertising business would be put at a disadvantage relative to that other business.
Revenue Thresholds

- DSTs are discriminatory in terms of firm size. The domestic and worldwide revenue thresholds result in the tax being solely applied to large multinationals. While this can ease the overall administrative burden, it also provides a relative advantage for businesses below the threshold and creates an incentive for businesses operating near the threshold to alter their behavior.

Just as the scope definition creates differential treatment between digital and non-digital firms, the revenue threshold creates differential treatment based on firm size. This is particularly important for countries that may have few domestic businesses that are both within the scope and above the revenue threshold.

Turnover instead of profits tax

- Unlike corporate income taxes, DSTs are levied on revenues rather than profits, not taking into account profitability. Seemingly low tax rates of such turnover taxes can translate into high tax burdens. For instance, a business with $100 in revenue and $85 in costs has a profit margin of $15—or 15 percent. A DST rate of 3 percent means the business is required to pay $3 in revenue tax (3 percent of $100 revenue), corresponding to a profit tax of 20 percent ($3 tax divided by $15 profit). This implies that the corresponding effective profit tax rates vary by profitability, disproportionately harming businesses with lower profit margins.

- Due to the issues outlined above and to enhance the functioning of the European cross-border market, Europe replaced its turnover taxes with VATs in the 1960s. The emergence of DSTs reintroduces the negative economic consequences of turnover taxes—a step back in terms of sound tax policy.

Though policymakers sometimes suggest that DSTs are designed to equalize treatment of foreign digital businesses and local companies, the design of DSTs as a turnover tax turns this argument on its head. Local businesses are commonly taxed on their profits or net income. A turnover tax applies to gross revenues and thus differs significantly from a profits tax. A foreign company with a 5 percent profit margin in a country with a 5 percent DST would have the entirety of those profits taxed away, effectively a 100 percent profits tax. No country taxes profits of domestic companies that heavily.

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Summary of Policies

DSTs are taxes on selected gross revenue streams of large digital businesses. Their tax base typically includes revenues either derived from a specific set of digital goods or services or based on the number of digital users within a country. Relatively high domestic and global revenue thresholds limit the tax to large multinationals.

In 2018, the European Commission proposed a DST at a rate of 3 percent on revenues derived from online advertising services, online marketplaces, and sales of user collected data. Businesses with annual worldwide revenues of €750 million (US $868 million) and total EU revenues of €50 million ($56 million) would be subject to the tax. Although the proposal was rejected at the EU level, several European—and non-European—countries have modeled their DSTs after the EU proposal.

Some of the proposed and implemented DSTs have unique features that differ from the EU proposal. Austria and Hungary’s DSTs are limited to online advertising, narrowing the tax base relative to other DSTs. India expanded its DST to all nonresident e-commerce operators, making it a much broader tax than any other DST. The UK’s DST—unlike other proposals—includes an exemption for the first £25 million ($31.9 million) of taxable revenues and provides an alternative DST calculation for businesses with low profit margins on in-scope activities.

Austria

Effective January 2020, Austria implemented a DST. The new digital advertising tax applies at a 5 percent rate on revenue from online advertising provided by businesses that have worldwide revenues exceeding €750 million ($840 million) and Austrian revenues exceeding €25 million ($28 million). As Austria’s DST is only levied on online advertising, its scope is narrower than, for example, France’s or the UK’s DST.

The Austrian DST applies to:

- Banner advertising on web sites
- Search engine advertising
- Other comparable advertising services

To comply with the DST, businesses are required to withhold the tax monthly and pay the balance as part of their 2020 tax return in September.

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Traditional advertising is subject to a special 5 percent advertising tax in Austria. If a business sells an ad for €100, the business would first pay the 5 percent advertising tax (€5) which would be included in the tax base for purposes of calculating value-added tax liability.

One can argue that the DST thus levels the playing field between traditional and digital advertisement. However, the DST’s global and domestic revenue thresholds effectively exclude most domestic providers of digital advertisement, creating new distortions. In early 2019, when discussing an earlier, similar proposal, Austria’s Chancellor Sebastian Kurz told reporters that no Austrian companies would be hit by the tax.

Adding to the argument for unequal treatment, a portion of the revenues (€15 million ($17 million)) from the DST will be used to support the digitalization of Austrian media companies.

Brazil

The digital tax policy in Brazil has not yet been adopted or implemented. Because of this, some details on the policy are currently unclear. The proposal is a draft law which was put forward in the Brazilian House of Representatives in May 2020.

The proposal targets the following activities:

- Advertising to Brazilian users
- Digital platforms facilitating goods and services among users where at least one user is Brazilian
- Transfer of data on Brazilian users

The policy applies to businesses with more than R$3 billion ($760 million) in global revenues and R$100 million ($25 million) revenues from Brazil.

The tax is on gross revenues rather than net income and higher rates apply to businesses with higher levels of revenue from the targeted sectors.

<table>
<thead>
<tr>
<th>TABLE 1</th>
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</thead>
<tbody>
<tr>
<td>Brazil’s Proposed Digital Services Tax Rate Structure</td>
</tr>
<tr>
<td>Rate</td>
</tr>
<tr>
<td>1%</td>
</tr>
<tr>
<td>3%</td>
</tr>
<tr>
<td>5%</td>
</tr>
</tbody>
</table>


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For instance, a business with R$500 million in taxable revenues under the proposal would owe R$16 million. If that business has a combined 5 percent profit margin from those activities, the effective tax rate on those profits would be 64 percent, significantly higher than Brazil’s combined corporate tax rate of 34 percent.\(^8\)

The high revenue threshold and the structure of the tax alongside its targeted nature make the tax single out large digital businesses with a distinctly different tax policy relative to other businesses.

As with other DSTs, the policy would discriminate on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in Brazil. However, given that the policy is still being developed, these features could shift prior to adoption if indeed the policy reaches that point.

**Czech Republic**

The Czech Republic’s proposal for a DST has not yet been adopted. Like some other European DSTs, the policy has both a global and a domestic revenue threshold. The global threshold is €750 million ($840 million) while the domestic threshold is CZK 100 million ($4 million). The original proposed tax rate was 7 percent, although that has recently been changed to 5 percent. The tax base is gross revenues from targeted advertising, use of multilateral digital interfaces, and the provision of user data. It is expected that the tax would not be implemented until 2021.

The proposed DST has two unique features relative to other similar policies. First, businesses whose revenue from the targeted activities do not make up more than 10 percent of their total revenues in Europe would be excluded. Second, a separate domestic revenue threshold applies to the transmission of user data. That lower threshold is CZK 5 million ($0.2 million).\(^9\)

As with other DSTs, the policy would discriminate on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in the Czech Republic. However, given that the policy is still being developed, these features could shift prior to adoption if indeed the policy reaches that point.

**European Union**

The European Union proposed a 3 percent DST in 2018; however, it was ultimately not adopted after many months of negotiations. It is possible that a new digital tax will be proposed as part of the funding for the Next Generation EU.\(^10\)

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Though no details were provided, a document describing financing mechanisms for new EU budget proposals suggested a digital tax on companies with global annual turnover above €750 million ($840 million), which would raise €1.3 billion ($1.5 billion).\textsuperscript{11}

Currently, however, there is not a DST proposal that is pending at the EU level.

**Hungary**

Hungary imposes a DST on advertising revenue. The policy has been in place since July 2017. A 7.5 percent tax rate applies to revenues exceeding HUF 100 million ($344,000); a tax exemption applies to revenues below that threshold. Temporarily, the rate has been reduced to 0 percent from July 1, 2019 through December 31, 2022.\textsuperscript{12}

Unlike other countries, Hungary has only one revenue threshold rather than two separate global and domestic revenue thresholds.

As with other DSTs, the policy discriminates on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in Hungary.

**India**

Effective from June 2016, India introduced an “equalisation levy,” a 6 percent tax on gross revenues from online advertising services provided by nonresident businesses.\textsuperscript{13} As of April 2020, the equalisation levy expanded to apply a 2 percent tax on revenues of e-commerce operators\textsuperscript{14} that are nonresident businesses without a permanent establishment in India and are not subject to the already existing 6 percent equalisation levy. The annual revenue threshold is set at Rs. 2 crores ($284,115\textsuperscript{15}).\textsuperscript{16}

The recent change essentially expands the equalisation levy from online advertising to nearly all e-commerce done in India by businesses that do not have a taxable presence in India, making it a much broader tax than the European DSTs and explicitly exempting domestic businesses.

This makes the Indian approach one of the broadest and clearly discriminatory policies. This is due to the expansive application of the gross revenue tax and because it clearly applies to foreign and not domestic businesses.


\textsuperscript{12} KPMG, “Taxation of the Digitalized Economy.”


\textsuperscript{14} An “e-commerce operator” is defined as a nonresident that owns, operates, or manages a digital or electronic facility or platform for online sale of goods or the online provision of services.


As with other DSTs, the policy discriminates on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in India.

**Indonesia**

Indonesia has a two-part policy aimed at digital companies, with one contingent on the other. The first part is a permanent establishment definition for e-commerce businesses based on significant economic presence in Indonesia. The criteria, which have not yet been fully defined, rely on consolidated gross revenue, sales in Indonesia, and the size of active members in Indonesia. Nonresident e-commerce businesses that do not meet the thresholds for significant economic presence will be charged an “Electronic Transaction Tax.” The rate for that tax is currently undefined.

Because it is targeted at overseas sellers, the policy directly discriminates between domestic and foreign businesses. As with other DSTs, the policy discriminates on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in Indonesia. However, the current lack of details on the policy make it difficult to understand the full impacts of the policy.

**Italy**

The Italian DST is effective from January 1, 2020. Like some other European DSTs, the policy has both a global and a domestic revenue threshold. The global threshold is €750 million ($840 million) while the domestic threshold is €5.5 million ($6 million). The tax rate is 3 percent and the tax base is gross revenues from three targeted sectors:

- Advertising on a digital interface
- Multilateral digital interface that allows users to buy/sell goods and services
- Transmission of user data generated from using a digital interface

As with other DSTs, the policy discriminates on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in Italy.

**Spain**

The Spanish DST is being considered but has not yet been adopted. Like some other European DSTs, the policy has both a global and a domestic revenue threshold. The global threshold is €750 million ($840 million) while the domestic threshold is €3 million ($3 million).

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17 KPMG, “Taxation of the Digitalized Economy.”
18 Ibid.
The tax rate is 3 percent and the tax base is gross revenues from three targeted sectors:

- Online advertising services
- Sale of online advertising
- Sale of user data

As with other DSTs, the policy would discriminate on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in Spain. However, given that the policy has not yet been implemented, these features could shift prior to adoption if indeed the policy reaches that point.

Turkey

Turkey has adopted a DST that is similar to several other DSTs except for two main departures. Like some other countries, Turkey’s DST has both a global and a domestic revenue threshold. The global threshold is €750 million ($840 million) while the domestic threshold is TRY 20 million ($4 million).\(^{19}\)

The tax rate is 7.5 percent and the tax base is gross revenues from online services including advertisements, sales of content, and paid services on social media websites.

The two differences from other similar policies are the high rate of 7.5 percent and the fact that the president has authority to adjust the rate to as low as 1 percent or as high as 15 percent.

The 7.5 percent rate by itself increases the likelihood for the tax to tax away all profits of a digital business subject to the tax. Unless a business has profit margins in Turkey at or in excess of 7.5 percent, the policy would tax away all profits. The presidential option to increase the rate to 15 percent creates significant uncertainty in addition to the differential treatment of digital businesses.

As with other DSTs, the policy discriminates on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in Turkey.

United Kingdom

While it has not yet been fully implemented, the UK DST is expected to be adopted soon and would apply from April 1, 2020. Like some other European countries, the UK DST has both a global and a domestic revenue threshold. The global threshold is £500 million ($638 million)
while the domestic threshold is £25 million ($32 million).  

The tax rate is 2 percent and the tax base is gross revenues from three targeted sectors:

- Social media platforms
- Internet search engines
- Online marketplaces

The UK policy is unique in a few ways. First, the policy provides an alternative calculation that allows businesses with low profit margins to be taxed more lightly than businesses with higher profit margins. Second, the first £25 million ($32 million) of revenues are exempt from the DST. Third, the UK policy provides a 50 percent reduction in the tax for businesses that are taxed on their revenues by a DST in another country.

As with other DSTs, the policy discriminates on business size and sector, and is structured as a turnover tax. This makes it different in substance and application than the income taxes that apply to other businesses in the UK.

**Negative consequences of a tax and trade war**

The current investigation and previous tariff threats from the U.S. Trade Representative raise serious concerns about the possibility that this current investigation will lead to a harmful tax and trade war.

The negative impact of DSTs could be compounded by the negative impact that tariffs against these major trading partners could have on U.S. businesses, workers, and consumers. Those negative impacts would hurt the U.S. economy at a time of weakness, potentially delaying or derailing a recovery from the economic impacts of the current COVID-19 pandemic.

Both DSTs and tariffs are fundamentally flawed policies. They both disproportionately impact targeted sectors relative to other market players and burden international commerce. At a time when not just the U.S. economy but the entire global economy is weak, a tax and trade war could do real, long-term damage to long-term economic growth.

Tariffs have a direct impact on U.S. businesses and consumers. The Tax Foundation estimates that the total impact of imposed and announced tariffs will reduce long-run GDP in the U.S. by 0.5 percent. Simply put, this means lower wages and fewer jobs. Additional tariffs in retaliation to the DSTs currently being investigated would mean even more economic harm to the U.S.
Instead of adopting new barriers to commerce and trade, countries should focus their energies on multilateral discussions that aim to address the questions of digitalization and tax policy in the context of income taxes rather than resorting to turnover taxes. The features that make DSTs particularly problematic would not be true for policies that are broad-based and connected to net income calculations rather than gross revenues.

The USTR should be cautious in designing a response that could lead to harmful escalation in tax and trade barriers.
## Summary of Proposed and Implemented Digital Services Taxes Targeted in Section 301 Investigation, as of May 2020

<table>
<thead>
<tr>
<th>Country/Institution</th>
<th>Tax Rate</th>
<th>Scope</th>
<th>Global Revenue Threshold</th>
<th>Domestic Revenue Threshold</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>5%</td>
<td>Online advertising</td>
<td>€750 million (US $840 million)</td>
<td>€25 million ($28 million)</td>
<td>Implemented (Effective from January 2020)</td>
</tr>
</tbody>
</table>
| Brazil              | 1%-5%    | • Targeted online advertising  
• Use of digital interfaces  
• Transmission of user data generated from using a digital interface | R$3 billion ($760 million) | R$100 million ($25 million) | Proposed |
| Czech Republic      | 5%       | • Targeted advertising  
• Use of multilateral digital interfaces  
• Provision of user data (additional thresholds apply) | €750 million ($840 million) | CZK 100 million ($4 million) | Proposed (Delayed until 2021 to wait for agreement at the OECD level; government lowered the proposed tax rate from initially 7% to 5%) |
| European Union      | 3%       | • Digital advertising  
• Online Marketplaces  
• Sales of user data | €750 million ($840 million) | €50 million ($56 million) | Rejected |
| Hungary             | 7.5%     | Advertising revenue      | HUF 100 million ($344,000) | N/A | Implemented (As a temporary measure, the advertisement tax rate has been reduced to 0%, effective from July 1, 2019 through December 31, 2022) |
| India               | 6% and 2%| • Online advertising services (6%)  
• E-commerce operators (2%) | – | Rs. 2 crores ($284,000) | Implemented (India introduced its “equalisation levy” in 2016, a 6 percent tax on gross revenues from online advertising services provided by nonresident businesses; as of April 2020, the equalisation levy expanded to apply a 2 percent tax on revenues of nonresident e-commerce operators that are not subject to the already existing 6 percent equalisation levy) |
| Indonesia           | TBA      | TBA                      | TBA                       | TBA | Implemented (So-called “Electronic Transaction Tax” effective from March 2020; imposed on e-commerce sales when the digital PE cannot be applied due to the provision of a tax treaty; details TBA) |
| Italy               | 3%       | • Advertising on a digital interface  
• Multilateral digital interface that allows users to buy/sell goods and services  
• Transmission of user data generated from using a digital interface | €750 million ($840 million) | €5.5 million ($6 million) | Implemented (Effective from January 2020) |
| Spain               | 3%       | • Online advertising services  
• Sale of online advertising  
• Sale of user data | €750 million ($840 million) | €3 million ($3 million) | Proposed (The Spanish Parliament rejected the government’s proposed budget bill for 2019, which included the digital services tax; however, a new draft law for a DST was introduced this year) |
| Turkey              | 7.5%     | Online services including advertisements, sales of content, and paid services on social media websites | €750 million ($840 million) | TRY 20 million ($4 million) | Implemented (Effective from March 2020; the president can reduce the DST rate to 1% or increase it to 15%) |
| United Kingdom      | 2%       | • Social media platforms  
• Internet search engines  
• Online marketplaces | £500 million ($638 million) | £25 million ($32 million) | Implemented (The UK government stated in its Finance Bill 2020 that the DST would go into effect as of April 1, 2020; the Finance Bill is currently in Parliament and is expected to be enacted this summer) |