Tax Reform, Past & Future: 
TCJA, OECD, Digital Taxes, & the Tech Industry

ABA Tax Section Fall Meeting 
Tax Policy & Simplification Committee 
October 4, 2019

Agenda

• TCJA – Background, Intent, Issues, Technical Corrections, Post-Enactment Reform Activities and Reports
• OECD Efforts to Build Consensus
• Digital Services Taxes (DST)
In the 1990’s Lawmakers Talked of Moving Tax Code into 21st Century

Need to "fundamentally rethink the tax code with a view to enhancing American competitiveness in the new global economy and helping the American workforce“

• Senator William Roth, chair Senate Finance Committee, 1998

What took so long? And ... Has the system moved into the 21st Century?
Treasury Tax Reform Work under President Bush

• 2007 - Treasury Department reports on business competitiveness:
  • Business Taxation and Global Competitiveness (7/23/07)
  • Approaches to Improve the Competitiveness of the U.S. Business Tax System for the 21st Century (12/07)
  • Looked at lower corporate rate, expensing of assets, int’l changes.

And more activity ...

• 2009 - President Obama's Tax Reform Task Force chaired by Paul Volcker
• 2010 - National Commission on Fiscal Responsibility and Reform (President Obama's Deficit Commission; Simpson-Bowles)
• 2011 State-of-the-Union – Pres. Obama calls for lower corporate rate
• Jan 2011 – HWM & SFC start series of hearings
  • Over 100 held since that time
• 2014 – Congressman Camp’s tax reform plan (HR 1, Tax Reform Act of 2014 (113rd Congress))
• 6/24/16 – House Republican’s “A Better Way” tax reform blueprint
Finally - the Tax Cuts and Jobs Act

H.R. 1 introduced 11/2/17
Enacted 12/22/17
via budget reconciliation process
Mostly effective 1/1/18
JCT Bluebook 12/20/18

Goals of TCJA

Per President Trump’s 1 pager
April 2017

Key – Improve Int’l Competitiveness by:
Reducing corporate rate
Moving corporate system to territorial

2017 Tax Reform for Economic Growth and American Jobs

The Biggest Individual And Business Tax Cut In American History

Goals For Tax Reform

- Grow the economy and create millions of jobs
- Simplify our burdensome tax code
- Provide tax relief to American families—especially middle-income families
- Lower the business tax rate from one of the highest in the world to one of the lowest

Individual Reform

- Tax relief for American families, especially middle-income families:
  - Reducing the 7 tax brackets to 3 tax brackets of 10%, 25%, and 35%
  - Doubling the standard deduction
  - Providing tax relief for families with child and dependent care expenses
- Simplification:
  - Eliminate targeted tax breaks that mainly benefit the wealthiest taxpayers
  - Protect the home ownership and charitable gift tax deductions
  - Repeal the Alternative Minimum Tax
  - Repeal the death tax
- Repeal the 3.8% Obamacare tax that hits small businesses and investment income

Business Reform

- 35% business tax rate
- Territorial tax system to level the playing field for American companies
- One-time tax on trillions of dollars held overseas
- Eliminate tax breaks for special interests
Business Changes Include ...

- Corporate rate reduction to flat 21%
  - tyba 2017
  - IRC §15 applies for fiscal year corps
  - QPSCs too
- Repeal of corporate AMT
- Special deduction for non-corporate business owners (new §199A) [2018 through 2025]
- Loss limitation for other than C corps (new §461(l)) [2018 through 2025]
- Repeal of §199
- Expensing of assets
  - Used and new
  - Only tangible property (see definition at §168(k) as amended)
  - Generally, after 9/27/17 and before 2023; phases down through 2026
  - Increases to §179 ($1 million and threshold $2.5 million) + certain lodging property + §280F changes
- Expanded accounting method exceptions for small business §§448, 263A, 471 & 460(e)
- No deduction for entertainment
- Changes to various fringe benefit deductions including qualified transportation and meals by employer
  - Transit fringes and meals generally still exempt to employee, but QTF no longer deductible by employer (de minimis meals and meals for convenience of employer 50% deductible, 0% after 2025)
  - Tax-exempts treat some benefits as UBTI.
- Qualified equity grant benefits for employees (§83(i))
- No c/b of NOL; can’t reduce taxable income by more than 80%; unlimited c/f
- Limitation on interest expense deduction for non-small businesses (over $26 million receipts); limited exceptions (§163(j))
- Partnership changes including repeal of technical termination rule.
- Corporate shift from worldwide to quasi-territorial system; can also affect some individual shareholders.

Were TCJA Goals Met?

- Lower tax rates
  - Lower corporate rate
  - Lowered individual rates (temporary)
  - Section 199A QBI deduction for non-corporations
  - Cut back or eliminated a few tax expenditures (tax preferences) to keep cost at $1.5 trillion over 10 years
- International tax reform
  - Moved to a quasi-territorial system for C corporations
  - Deemed repatriation at a low rate
  - Address some Base Erosion, Profit Shifting (BEPS) concerns
- Appropriate tax incentives for economy
  - Yes –
    - Kept research credit
  - No
    - Kept orphan drug credit, but reduced
    - R&D deduction turns to capitalization after 2021
    - 100% bonus depreciation is temporary and not for intangibles
Overlooked in TCJA

A. Lower tax rates with revenue neutrality
   • Individual changes mostly temporary
   • $1.5 trillion cost over ten years

B. Appropriate tax incentives for digital economy
   • Intangible assets, gig/freelance workforce (safety net, reporting and worker classification issues) not addressed.

C. Administrative reforms
   • Rules to reduce identity theft
   • Modernize compliance systems; IRS funding

D. Efforts to reduce the almost $400 billion annual tax gap.

E. Budget issues
   • No change to address growing levels of mandatory spending (including interest on debt).
   • No change to address Social Security and Medicare funding issues, as well as increasing health care costs.

“we must keep building off the momentum from last year’s tax reform to ensure our economy keeps booming. That’s why we’re here today to change the culture of Washington – from one that waits an entire generation to fix a broken tax code, to one that keeps our code ahead of the pack and the best in the world.” 9/13/18

Is Tax Reform 2.0 the answer?

3 bills passed in House Ways and Means Committee on 9/13/18
• **H.R. 6760**, Protecting Family and Small Business Tax Cuts Act of 2018—makes permanent certain provisions of the TCJA affecting individuals and small businesses. It also makes the higher estate tax exemption permanent.

• **H.R. 6757**, Family Savings Act of 2018—Includes several provisions to promote savings including pooled employer plans, repeal of the maximum age for traditional IRA contributions, universal savings accounts, expanded 529 education plans, and penalty-free withdrawals from retirement plans for costs of birth or adoption.

• **H.R. 6756**, American Innovation Act of 2018—Modifies §195 to allow a larger amount to be expensed in the first year ($20,000) with that amount not phasing down until total startup expenses exceed $120,000. The dollar amounts are adjusted annually for inflation.

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**Tax Reform 2.0 Challenges**

• Concern about increasing the debt and deficit.
  • But, since individual cuts don’t expire until after 2025, the earlier permanency is passed, the lower the cost in a 10-year projection period.

• Several states don’t like the $10,000 SALT cap.

• Democrats can highlight the tax breaks skewed to higher income individuals and higher health insurance costs due to repeal of mandate.

• Needs 60 votes in Senate.

• November 6, 2018 mid-term election, and the 2020 election.
Technical Corrections

JCT Bluebook on TCJA

• “A technical correction may be needed to carry out this intent.” This phrase or similar shows up ...

74 times!

https://www.jct.gov/publications.html?func=startdown&id=5152

Questions on economic effects

• Will economic growth cover the $1.5 trillion cost?
  • Short term versus long term effects likely to differ.
• What about extenders bill passed 6 weeks after TCJA?
  • P.L. 115-123 (2/9/18)
    • JCT cost estimate for mostly 1 year extension for 2017 = $15 billion
• What about existing and growing debt and deficit? --→
• Effect on group and non-group health insurance costs of mandate repeal starting in 2019
  • Note: California, NJ and Vermont have enacted federal mandate. Will other states do same?
• Effect of fewer itemizers on charitable donations.
• Effect of UBTI changes on charities.
TCJA Affect on Tax Revenues in Other Countries

- **Tax Spillovers from US Corporate Income Tax Reform**
  - IMF working paper, 7/13/18
  - 1.6% to 5.2% tax revenue decline on average
  - Reasons:
    - Increased investment in U.S. (so less elsewhere)
    - Profit shifting to U.S.
    - “Policy spillover” – law changes in response to U.S. corporate tax changes including lowering their country’s tax rate

Investment Growth and TCJA

• **U.S. Investment Since the Tax Cuts and Jobs Act of 2017**
  • IMF working paper, 5/31/19
  • Preliminary assessment with 2018 including comparing 2018 to what expectations were without the TCJA.
  • “We find that U.S. business investment since 2017 has grown strongly compared to pre-TCJA forecasts and that the overriding factor driving it has been the strength of expected aggregate demand. Investment has, so far, fallen short of predictions based on the postwar relation with tax cuts. Model simulations and firm-level data suggest that much of this weaker response reflects a lower sensitivity of investment to tax policy changes in the current environment of greater corporate market power. Economic policy uncertainty in 2018 also subdued investment growth, although to a lesser extent.”

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U.S. Treasury Department

[https://home.treasury.gov/TaxCutCutCut](https://home.treasury.gov/TaxCutCutCut)

In March 2018, the number of job openings reached **historic** levels, with 7.3 million jobs—enough for every unemployed American to go to work.[1]

- The Washington Post: “March [2018] marked the first time there has been a job opening for every unemployed person since the Labor Department began keeping track of job openings in 2000.”[2]

In November 2018, the **Unemployment Rate** reached a 50-year low of 3.7%. [3]

**Over six months later, the Unemployment Rate remains at 3.7% and in June 2019 the economy added 224,000 new jobs.**[4]

- CNBC reported: “Payroll growth rebounded sharply in June as the U.S. economy added 224,000 jobs, the best gain since January”[5]
- The New York Times reported: “A decade after the Great Recession released its grip on the American economy, the job market shows no sign of falling into another slump.”[6]
- The New York Times also reported: “[Workers are] benefiting from what is now, at least unofficially, the longest economic expansion on record.”
- The Wall Street Journal reported: “There are several pillars of strength for the U.S. economy beyond historically low unemployment and a record 105 straight months of job gains. American household spending and incomes both rose at solid rates in May, consumer confidence remains relatively strong and the stock market reached a record high this week.”[7]

**Business Optimism Has Hit Record Heights, With Job Creators Across America Expressing Confidence In The Future.**

- According to the National Federation of Independent Businesses (NFIB), tax reform is working, and the relief is driving record optimism about the economy among small and independent business owners.[8]
- In May, business optimism rose to a seven-month high as companies have the money to expand and invest in their workers.[9]

**Across America, workers are experiencing a blue collar boom.**
Figure 1. Growth in Real Gross Domestic Product, First Quarter 2013 Through Fourth Quarter 2018

Source: Table 1.1.1, Bureau of Economic Analysis, National Income and Product Accounts (NIPA).
Note: Seasonally adjusted at annual rates.

More from CRS report...

On the whole, the growth effects tend to show a relatively small (if any) first-year effect on the economy. Although examining the growth rates cannot indicate the effects of the tax cut on GDP, it does tend to rule out very large effects in the near term.

The data appear to indicate that not enough growth occurred in the first year to cause the tax cut to pay for itself. Assuming a tax rate of 18% (based on CBO estimates), and estimating the tax cut to reduce revenue in calendar year 2018 by about 1.2% of GDP, a 6.7% GDP increase due to the tax cuts alone would be required.16 Rather, the combination of projections and observed effects for 2018 suggests a feedback effect of 0.3% of GDP or less—5% or less of the growth needed to fully offset the revenue loss from the Act.
Use of Funds for Worker Bonuses and Share Repurchase

Increased funds, whether accessed from abroad or through tax cuts, could be used in several ways: investment, paying down debt, increasing wages, paying wage bonuses, paying dividends, or repurchasing shares.

During the passage of the tax revision and in the immediate aftermath, some argued that firms would use these funds to pay worker bonuses (as discussed in the previous section on wages). Subsequently, a number of firms announced bonuses, which in some cases they attributed to the tax cut. One organization that tracks these bonuses has reported a total of $4.4 billion. With US employment of 157 million, this amount is $28 per worker. This amount is 2% to 3% of the corporate tax cut, and a smaller share of repatriated funds. It is consistent with what most economists would expect that a small percentage of increased corporate profits or repatriated funds (if any) would be used to compensate workers, as economic theory indicates that firms would pay workers their marginal product, a result of fundamental supply and demand forces.

The bonus announcements could have reflected a desire to pay bonuses when they would be deducted at 35% rather than 21% (in late 2017 for firms with calendar tax years but in 2018 for firms with different tax years). Worker bonuses could also be a result of a tight labor market and attributed to the tax cut as a public relations move.

Much of these funds, the data indicate, has been used for a record-breaking amount of stock buybacks, with $1 trillion announced by the end of 2018. A similar share of repurchases happened in 2004, when a tax holiday allowed firms to voluntarily bring back earnings at a lower rate.

Despite the lower corporate tax rate, it is not clear that capital will be shifted into the United States from abroad; although a lower rate reduces the tax rate on equity-financed investments, it increases the subsidy to debt-financed investments. Whether the capital stock increases or decreases depends on the magnitude of the tax changes (which appear largely offsetting) and the international mobility of debt versus equity. It is also not clear whether the capital stock will be allocated more efficiently or in a way more optimal for U.S. welfare, although economic theory suggests that reducing the tax subsidy for debt is a clear improvement.

Although a territorial tax may make profit shifting more attractive, overall, given other elements of the new system, it appears to make profit shifting less important. GILTI and FDII bring the tax treatment of income from intangibles in the United States and abroad closer together, and BEAT and stricter thin capitalization rules (rules limiting interest deductions) also limit profit shifting, including shifting through leveraging.

The new system ends the penalties (except for portfolio investment in foreign firms) for repatriating earnings and thus eliminates the prior incentives to retain earnings abroad. A series of measures aimed at inversions appears to make inversions much less attractive.

Some of the measures may violate international agreements such as the World Trade Organization (WTO), bilateral tax treaties, and Organization for Economic Cooperation and Development (OECD) minimum standards to prevent harmful tax practices.

There have been a number of concerns about design features in the new regime, including the dividend deduction, GILTI, FDII, BEAT, and other features. A variety of options might be considered to address these issues.
A few more details ...

GILTI

GILTI has been criticized by some for being too harsh and by some as not capturing enough income.

Perhaps the major concern that GILTI is too harsh involves the foreign tax credit. The law retains the existing rules for the allocation of deductions for purposes of the foreign tax credit limit. These rules allocate interest, R&D spending, and overhead to a narrowed GILTI foreign tax credit basket (which excludes a variety of foreign-source income, including royalties that may be associated with domestic research and development). Allocating too many deductions to foreign-source income can cause GILTI to apply at a higher rate than 13.125%. In addition, there is no foreign tax credit carryback or carryforward, so that unused foreign tax credits are lost, and no credits are allowed for loss CFCs. CFCs with losses also lose the tangible asset return exclusion, as well as foreign tax credits, and foreign tax credits of other CFCs are reduced to the extent that the loss offsets another CFC’s income. Many critics note that GILTI income is not focused on intangible income but on any residual income not associated with tangible property, and thus captures excess profits, along with income from finance or insurance. ...

“The Effect of the Tax Cuts and Jobs Act (TCJA) of 2017 on Multinational Firms’ Capital Investment: Internal Market Frictions and Tax Incentives,” by Professor Mathis, et al

“It’s an unintended consequence,” Mathis said. “What we’re showing in this paper is the way they calculated this new tax (Tax Cut and Jobs Act of 2017) actually incentivizes foreign rather than domestic investment through both the GILTI (global intangible low-taxed income) inclusion and FDII (foreign-derived intangible income) deduction. By increasing their foreign capital expenditures and investments, U.S. firms can reduce the U.S. taxes they pay.”

Researchers compared corporate capital spending of 1,804 public companies in three quarters prior to the Tax Cut and Jobs Act to spending in the three quarters after the bill was passed.

Focusing on the bill’s effect on multinational corporations, researchers found an increase in capital investment of about 14 percent among firms that would have faced high repatriation costs under prior regulations. The paper reports, “Firms with repatriation costs in the top quartile increased their capital expenditures from 0.86 percent of assets to 0.98 percent of assets.” In contrast, “firms with zero repatriation costs kept their capital expenditures at 0.98% of assets.”

http://harbert.auburn.edu/news/Mathis%20research.php
Effect on Effective Tax Rates

• Generally, drop from 35% to 21% lowers reported corporate effective tax rates
• 2017 effects were variable (one-time effects)
  • Transition tax increased ETRs
  • Revaluation of “deferred tax liabilities” decreased ETRs
• 2018 and onward – generally lower rates
  • Pre-TCJA – 19-32%
  • Post-TCJA – 10-18%

OECD Efforts to Build Consensus

October 4, 2019
Notices

The following information is not intended to be “written advice concerning one or more Federal tax matters” subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230.

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

Why are we here?

TAX CHALLENGES

— Ability of MNEs to sell remotely without physical presence
— Concentration of residual profits in low-taxed jurisdictions
— Active users drive enterprise value without attracting a commensurate tax base to the jurisdiction of the users

Consensus unlikely without a general view of the Inclusive Framework that these issues have been satisfactorily resolved
Three key trends in global tax reform policy

Adoption of BEPS 1.0
- Coordinated action on international standards
  - County-by-country reporting, multilateral instrument, transfer pricing guidelines
- Domestic law adoption of BEPS recommendations
  - U.S. tax reform/EU Anti-Tax Avoidance Directive/other domestic reforms

Proliferation of unilateral measures
- U.K. and Australia diverted profits tax
- U.S. tax reform (BEAT/FDII)
- Digital services taxes (DSTs) and other unilateral measures to address taxation of the digital economy

OECD effort to reestablish consensus BEPS 2.0
- Reconsider balance between source- and residence-country taxation
- Address concerns spurred by consideration of challenges of taxation of digital economy without ring-fencing
- Strengthen and extend BEPS recommendations

OECD Programme of Work – Two pillars

1. New market-based taxing right
   - Modified Residual Profit Split
   - Fractional Apportionment
   - Distribution-based Approach

2. Extension of BEPS 1.0
   - CFC Income Inclusion Rule
   - Under-Taxed Payment Rule
   - Subject to Tax Rule
   - Switch-over Rule
Pillar I – New taxing right

Proposed profit allocation approaches

To address the “Digital Tax Problem,” Pillar I seeks to identify profits subject to reallocation from exporting jurisdictions to market jurisdictions.

Explore different approaches to
—Quantify the amount of profit subject to “new taxing right”
—Determine how to allocate the profit among market jurisdictions

Methods to be explored
—Modified Residual Profit Method
—Fractional Apportionment Method
—Distribution-based Approaches

Key design features
—Business line or regional segmentation
—Scoping limitations (e.g., size, industry)
—Treatment of losses

Step 1 – Determine total profit
Source of data?
Group-wide or segmented basis?
Statutory accounts?

Step 2 – Remove routine profit
Likely formulaic and simplified
Percentage of sales and/or assets?

Step 3 – Split the nonroutine
Identifying the profit subject to “new taxing right”
Simplicity vs. accuracy

Step 4 – Spread profit to market jurisdictions
Nexus not limited by physical presence
Factors – revenue? Market engagement factors?
Customer/user location identification, especially for B-to-B businesses
Safe harbor or “on top of” existing allocations?

Modified Residual Profit Split Method
Fractional Apportionment Method

Step 1 – Determine subject profits
- In-scope business models?
- Source of data?
- Group-wide or segmented basis?
- No routine/nonroutine distinction

Step 2 – Select the allocation factors
- Sales by user location?
- Employment? Assets?
- Same weights for all or differ by industry/business model?

Step 3 – Spread profit to market jurisdictions
- Replaces existing transfer pricing?

Distribution-based Approach

Step 1 – Determine base-line profits
- References group-wide and local profits
- Group-wide/entity-wide or segmented?

Step 2 – Adjustments based on economic factors
- Required local profit adjusted by group profitability?
- Local marketing effort?
- Local physical presences (employment/assets)?

Step 3 – Attribute returns to market jurisdictions
- Safe harbor for existing entities?
- Expanded nexus jurisdictions?
- Treatment of complex local business models (beyond distribution)?
### Pillar I critical design considerations

**Where do the “market profits” come from?**
- “Simple” on the front-end means “complex” on the back-end
- “Surrender country” deduction/exemption – Need for formulaic approach
- Approach inseparably connected to Pillar I approach adopted

**A new nexus rule**
- A novel concept reflecting the transformation of the modern economy
- Remote but sustained and significant business presence
  - Revenue thresholds, targeted marketing activities, digital engagement, etc.
- MNE group level

**Double taxation and dispute resolution**
- Examine the interaction between new and existing taxing rights
- Analyze the current dispute prevention and resolution procedures
- Explore options to modifying existing tax treaties – a new MLI?
- Effectiveness of current multi-lateral dispute resolution mechanisms (APAs, MAP, arbitration, etc.)
- Is near-universal binding arbitration possible?

### Pillar II – Minimum tax

**Design considerations**

**Parent’s perspective**
- **Income inclusion**
  - Top-up to minimum rate
  - Effective rate test vs. incentives, NOLs, etc.
  - Country-by-country
  - Substance and carve-outs

**Switch-over**
- Application of the credit method over exemption method

**Payer’s perspective**
- **Under-taxed payments**
  - Denial of deduction
  - Scope of payments covered
  - Addressing conduits
  - ETR test
  - Over taxation

**Subject-to-tax**
- Domestic law and treaty changes
- Focus on interest and royalties?
How does this affect me?

**Countries**

**Factors positively affecting tax base:**
- Significant HQ Cos that have centralized profits in low-taxed jurisdictions
- Large customer base for nondominant industries
- Dominant in largely domestic industries, etc.

**Factors negatively affecting tax base:**
- Significant proportion of the tax base consists of residual profits
- Share of residual profits > share of global customers, etc.

**Companies**

**Factors positively affecting ETR:**
- HQ in high-taxed jurisdictions with significant HQ DEMPE activities
- Less aggressive transfer pricing policies
- Significant domestic businesses

**Factors negatively affecting ETR:**
- Centralized DEMPE functions attracting large shares of tax-favored global residual profits
- More aggressive transfer pricing policies

Timeline

**Broad based agreement coming out of Japan G-20 meeting (but for a few hold out countries):**
- OECD work plan must adequately address DE tax challenges
- Must be finalized quickly

|-----------|---------------|-------------|-------------|-----------------|-------------|
Digital Services Taxes (DSTs)

October 4, 2019
Taxation of the digitalized economy

Direct Taxes (e.g., DST / WHT / Digital PE)

1. Australia
2. Austria
3. Belgium (DST / PE)
4. Canada
5. Chile
6. Czech Republic
7. Denmark
8. Finland
9. France
10. Germany (WHT)
11. Greece
12. Hungary
13. India (Equal.Tax / PE)
14. Indonesia
15. Israel (DST / PE)
16. Italy
17. Kenya
18. Malaysia
19. Mexico
20. New Zealand
21. Norway
22. Pakistan
23. Poland
24. Romania
25. Singapore
26. Slovenia (DST / PE)
27. Slovenia
28. South Korea
29. Spain
30. Sweden
31. Switzerland
32. Taiwan
33. Thailand
34. Turkey
35. United Kingdom
36. United States
37. Uruguay
38. Vietnam
39. Zimbabwe

13 Legislation Implemented
1 Draft Legislation / Public Consultations
7 Public Announcement / Intentions to Implement
8 Waiting for Global Solution
1 Rejection of a Public Announcement / Proposal

To learn more about Taxation of the digitalized economy read.kpmg.us/digital-economy

EU Member States remain concerned: unilateral actions

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<tr>
<th>EU DST</th>
<th>France</th>
<th>Italy</th>
<th>Spain</th>
<th>Czech Republic</th>
<th>UK</th>
<th>Austria</th>
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<td>€750/50m</td>
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<td>€750/2m</td>
<td>GBP500/25m</td>
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EU unilateral measures

Update on unilateral initiatives

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<td>Thresholds</td>
<td>—Global turnover more than €750 million</td>
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<td>—Domestic in scope turnover more than €25 million</td>
<td>—Domestic in scope turnover more than €10 million</td>
<td>—Domestic in scope turnover more than €5.5 million</td>
<td>—Domestic in scope turnover more than €3 million</td>
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<td>Effective</td>
<td>—1 January 2019</td>
<td>—2020 (at the latest)</td>
<td>—1 January 2021</td>
<td>—TBC (likely in 2020)</td>
</tr>
<tr>
<td>Levied on</td>
<td>—Revenue streams: digital interfaces (intermediation), advertising revenues, resale of private data</td>
<td>—Revenue streams: online advertising</td>
<td>—Revenue streams: digital advertising digital transmission of data, provision of digital interface</td>
<td>—Revenue streams: digital advertising digital transmission of data, provision of digital interface</td>
</tr>
</tbody>
</table>

Unilateral measures vs international law?

1. Unilateral DST vs EU Treaty Freedoms?
2. Unilateral DST vs EU State aid principles?
3. Unilateral DST vs double tax conventions?
4. Unilateral DST vs World Trade Organization (WTO) rules?
Overview of the French DST

According to the French Government, there is a mismatch between the place and way of taxation of profits resulting from certain digital activities and where and how this value is effectively generated.

The French Government believes that tech companies benefit from a clear advantage as the territorial tax system has not been designed taking into account the way that they create value but the way more “traditional” companies do with brick and mortar operations.

The Government also had in mind to put pressure on the multilateral negotiations.

3% tax on gross revenues derived from activities in which “users” are deemed to play a major role in value creation.

French DST will be levied on 2 types of services:

- provision of a digital interface;
- targeted advertising and transmission of data collected about users for advertising purposes.

Only large digital companies, i.e. companies receiving revenues in consideration of taxable services during the previous calendar year exceeding the following two thresholds will be subject to the DST:

- € 750m for taxable services supplied worldwide;
- € 25m for taxable services supplied in France.

These thresholds must be calculated at the consolidated group level.

The French Government has identified approximately 30 expected taxpayers.

Only large digital companies, i.e. companies receiving revenues in consideration of taxable services during the previous calendar year exceeding the following two thresholds will be subject to the DST:

- € 750m for taxable services supplied worldwide;
- € 25m for taxable services supplied in France.

The tax applies retroactively as from 1 January 2019.

Practical challenges on the application of the French DST

**Taxpayers**

**Taxpayers** are those with both:

1. Worldwide revenue* of €750M,
2. French revenue* of €25M

* From the provision of taxable services

**Taxable Services**

**Taxable Services** are:

1. Provision of a digital interface
2. Sale of Advertising Services & Related Services

**Tax Computation**

**Gross Revenues from Taxable Services (less VAT)**

\[
\text{Gross Revenues from Taxable Services (less VAT)} \times 3\% \text{ tax rate}
\]

**Tax Compliance**

Registration and Filing

1. VAT
2. Through tax office
3. Agent VAT return
4. AAA Representative

Group Filings

Payments
“The United States is very concerned that the [French] digital services tax . . . unfairly targets American companies. The President has directed that we investigate the effects of this legislation and determine whether it is discriminatory or unreasonable and burdens or restricts United States commerce.” Robert Lighthizer, US Trade Representative (July 10, 2019)

“The digital services tax that France and other European countries are pursuing is clearly protectionist and unfairly targets American companies in a way that will cost U.S. jobs and harm American workers. . . The United States would not need to pursue this path if other countries would abandon these unilateral actions and focus their energies on the multilateral process that is underway at the Organisation for Economic Cooperation and Development.” Senate Finance Committee Joint Committee, Sen. Chuck Grassley (R., Iowa) and Ron Wyden (D., Ore). (July 10, 2019).

Next?

1 A “deal”?

2 OECD process?

3 Other challenges?

4 Trade implications