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Prospects for Introducing a Digital Tax in the EU

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The European Commission (EC) wants to tax the digital sector in the EU. According to the Commission's calculations, companies operating on the virtual market pay much lower taxes than traditional enterprises. The aim is to tax U.S. corporations that record high revenues on the EU market but it will also affect European enterprises. The tax is supported by only a few Member States, which diminishes the likelihood of it being introduced quickly. Under pressure from France, Germany, and Spain, the EC is developing a new, narrower version of the proposed regulations, which would be beneficial for Poland.

In March 2018, the EC presented a package of two proposed directives on taxation of the digital economy: one, a "long-term project," and the second, a "temporary solution" that would apply until a permanent solution is reached either within the EU or in the Organisation for Economic Cooperation and Development (OECD) format. The proposal for a digital tax is based in the argument that existing regulations need to be adapted to current market challenges, which in the digital sector refers to those revenues generated by EU citizens interacting online with a company that is not established on a Member State's territory and are not taxable. By the end of 2018, however, discussions on the proposals had not rendered a common position between the Member States and the EC. At the December meeting of the Economic and Financial Affairs Council (ECOFIN), under pressure from France, Germany, and Spain, it was agreed that the EC would draft a new proposal by March this year, taking into account comments from the European Parliament (EP) and responding to doubts from states sceptical of the proposals.

EC Proposals. As part of its "long-term project" for a digital tax, companies in a given country would be subject to the tax if they meet at least one of the following criteria: revenues from digital services exceed €7 million, the number of users exceeds 100,000, or it has a minimum of 3,000 commercial contracts for digital services. On the one hand, such regulations would force companies that record high turnover in a given country to pay the tax and, on the other hand, they protect smaller entities from having to pay the tax, which otherwise might inhibit their development. In turn, the "temporary solution" concerns the taxation of revenues from the sale of online advertising and the sale of data generated from information provided by users. This applies only to companies with total global revenues above €750 million and revenues in the EU of €50 million.

Arguments for the Tax. The basic idea is the need to adapt regulations to cover these new types of services and other revenues not covered by applicable law. According to EU estimates, the lack of legal provisions to tax revenues derived from data obtained from the users of services results in an estimated outflow from the EU of up to €5 billion per year. France, with the support of Germany and Spain, is the main promoter of this idea and their view is dictated by internal conditions—these countries are large markets in which the turnover of technology companies is not subject to taxation. Another argument for the EU tax is the slow pace of work on analogous regulations at the OECD level. The introduction of temporarily binding standards in the EU likely would mobilise OECD members to complete work on legislation applicable to the 34 most-developed economies in the world, including the U.S. The tax is also an element of broader actions

organising the rules for how enterprises may function in the digital sector, especially those with a quasi-monopolistic position. In recent years, antitrust proceedings have been conducted against several of them (namely Amazon, Apple, Google, and Microsoft). The work also includes a draft directive on intellectual property rights and would impose charges on internet-based platforms (such as Facebook, Google, YouTube) for processing of copyrighted content (e.g., articles from newspapers, films). The political context is also important. The public's expectations regarding fair taxation of what are now some of the world's largest companies have been picked up by politicians who focus parts of their programmes on fighting inequality and protecting citizens' rights on the free market while seeking financing for costly social policies.

Impediments to Taxation of the Digital Economy. The main argument of states unwilling to tax the digital economy is based on the negative effect it might have on European businesses if introduced only in the EU. First, the estimated tax revenue to the EU budget would be only €1 per €1,000 if all the proposed taxes are collected. Second, the unilateral implementation of such regulations may hinder the development of European companies in the digital sector for which the EU is the main (and often only) area of activity. What's more, there are possible repercussions from the U.S. government, which *de facto* interprets the initiative as imposing duties on its corporations. Opponents of the idea argue that all work on digital taxation should be carried out only at the OECD level to prevent all these risks.

The discrepancy of interests and tax cultures between the Member States remains a brake on the introduction of the tax. The main opponents are countries where European subsidiaries of international corporations are registered—Ireland (the European headquarters of Facebook and Google), the Netherlands (Uber), Luxembourg (Amazon's EU headquarters), and the Czech Republic, which offers preferential tax rates.

Projects' Prospects. The need for a unanimous decision of the Member States means the prospects of introducing a digital tax at the EU level are low. The recent EC proposal to abolish the unanimity rule on tax issues has no chance of success. It serves only as a political manifesto ahead of elections to the European Parliament and the end of the current term. The scepticism by some states also reduces the chance of progress in implementing other tax projects at the European level (including the Common Consolidated Corporate Tax Base).

The most likely scenario is the unilateral introduction of various tax options by individual Member States: France has announced legislative work on the matter (and it may apply it retroactively to January 2019), as have the UK (from April 2020), Spain, and Austria. The introduction of national solutions would convince the next group of undecided states. However, for Ireland, the Netherlands, and Luxembourg, the economic calculation is that the net revenues of such taxes are a rather poor incentive if faced with the risk of the loss of the digital giants' headquarters in these countries.

An alternative being considered is the adoption of more ambitious provisions by selected countries under the "enhanced cooperation mechanism" (ECM). A solution that involves at least nine countries would differ from unilaterally introduced regulations by states in that it would take place using EU institutions and procedures. That could speed up reconciliation of the target solution at the OECD level. However, the chances of an ECM-level tax should be assessed as moderate due to the limited progress in introducing the financial transaction tax (FTT) in a similar format. The least likely option seems to be unanimous adoption of a very limited version of the tax proposal, for example, revenues from the sale of data generated by the users of websites in individual countries. Further, Ireland and Luxembourg see no reason to implement any solution at the EU level.

The EU digital tax is also important in relations with the U.S. Theoretically, such a tax could trigger retaliation in the form of duties on European goods. The ongoing U.S. rivalry with China over technology strengthens the American government's support for its corporations abroad but can also lead the administration to seek compromise in transatlantic relations as part of its wider competition with China.

For Poland, taxation of the digital economy and progress in other EU tax areas could be beneficial due to the potential revenues to the EU budget. Increased revenue could be spent on research and development of new technology. In addition, Poland, as the sixth (and after Brexit, fifth) largest Member State by population, is among those EU countries with the most potential budget revenue from such a tax (about PLN 500 million per year), based on services already provided on its territory. The consequence of the implementation of an EU tax project would, however, be the more problems in transatlantic relations in the economic dimension.