

# **Taxing the Digital Economy. Is the DST the Right Solution?**

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## **Abstract**

This paper examines the current income tax challenges of the Digital Economy, and the current proposals to tax digital firms where the users of their products or services are located. Building on law and economic literature, the paper firstly reviews the theory on corporate taxation, paying attention to the evidence on tax avoidance and profit shifting of multinational firms. The paper then argues that introducing a new tax on digital businesses could prove ineffective and lead to several distortions on corporate decision-making, especially in the case of unilateral and uncoordinated implementation.

**Keywords:** tax policy, digital services tax, multinational firms, digital economy.

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## 1. Introduction

In the recent years, new digital business models have arisen, which have shown how the traditional criteria to identify a taxable presence in a certain jurisdiction – i.e., residence and permanent establishment (“PE”) – are outdated, as they imply a physical nexus to the source country. Both businesses and certain jurisdictions have had a strong interest in taking advantage of loopholes in the current international legal framework. Many multinational enterprises (“MNEs”) have in fact designed their supply chains in such a way that limits the taxable presence in high-tax countries.<sup>2</sup> Relatedly, the latter have enacted and granted MNEs extremely favorable tax treatments – especially through advance rulings.<sup>3</sup>

All of this has resulted in a significant base erosion and profit shifting (“BEPS”) from high-tax countries (i.e., the source countries of most of the digital businesses) to low-tax jurisdictions, where MNEs decided to place their tax residence.<sup>4</sup> To cope with the growing importance of the Digital Economy and its related tax challenges, most industrialized OECD countries have tried to develop responses to preserve or re-establish their taxing power.

In particular, over the last decade, the tax policy-making discussion, at both domestic and international level, has centered on two main sets of countermeasures, which, in principle, contradict each other. On the one hand, a restructuring of the existing international corporate income tax legal framework is urged, whereas, on the other hand, the development of a completely new legal framework to tax the Digital Economy is advocated.

## 2. What to do next? Reforming the Existing International Tax Framework or Implementing a New Paradigm?

### *2.1 Reforming the Existing International Tax Legal Framework: The concept of Virtual PE*

The first option would implement substantial adjustments to the existing corporate income tax framework. Such adjustments should enable source countries to exercise their taxing powers over multinational companies that have a significant market presence within their territory. Therefore, such changes would re-align the taxable presence to the market presence, without ring-fencing multinational digital firms from other traditional businesses. To achieve the realignment of taxable and market presence, some have advocated the persistency of the corporate income tax with the introduction of a new concept of virtual PE, which would apply whenever there exists a significant digital presence in the source country.

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<sup>2</sup> Allevato, G. (2019): ‘Multinational enterprises and design of a tax-aligned global supply chain’, *Legal Business World*, 2 (available at <https://www.legalbusinessworld.com/single-post/2019/04/04/Multinational-enterprises-and-design-of-a-tax-aligned-global-supply-chain>). See, also, Desai, M. (2008): ‘The Decentering of the Global firm’, *Harvard Business School working paper 09-054*.

<sup>3</sup> Houlder, V. (2014), ‘Leak reveals scale of corporate tax deals with Luxembourg’, *Financial Times*.

<sup>4</sup> For a review, see Dharmapala, D. (2014): ‘What do we know about Base Erosion and Profit Shifting? A Review of the Empirical Literature’, *Fiscal Studies*, 35(4), 42-448.

Prominent scholars firstly advanced the proposal for a virtual PE to solve the BEPS issue.<sup>5</sup> In 2018, the OECD also discussed it in its Interim Report<sup>6</sup> and, most importantly, since then it has been the subject of an EU Commission's directive proposal.<sup>7</sup> All these proposals maintain that source countries should be entitled to tax cross-border business income anytime a foreign enterprise has a significant digital presence within their territory.<sup>8</sup> By now, the EU Commission's proposal represents the most advanced and structured attempt to incorporate the concept of a virtual PE into the international income tax legal framework. Specifically, a foreign enterprise should be deemed to have a "significant digital presence" in the source country anytime it, alternatively: (i) generates over €7 million annual revenues from digital services; or (ii) has more than 100,000 users accessing their digital services; or (iii) concludes over 3,000 business contracts for digital services in the member country.

Theoretically, the introduction of the virtual PE concept should provide source countries with more taxing rights over the income generated therein by multinationals that have a market presence without having a qualified physical presence therein. Furthermore, the adoption of the virtual PE would allow taxing income where, according to several commentators, an important part of value creation takes place, which for the Digital Economy corresponds to where the users are located. However, this proposal encounters two feasibility problems. On the one hand, the introduction of the virtual PE requires unanimous consensus to be effective, at least among all the jurisdictions that are part of a certain economic and geographical region, which, in the case of the EU Commission's directive proposal, includes all EU member countries. Otherwise, the effectiveness of the virtual PE would vanish or be weakened, similar to the amendments to the treaty concept of PE in the Multilateral Instrument ("MLI"),<sup>9</sup> which are currently impaired by the fact that certain key-jurisdictions, such as the United States, have not signed it or made reservations on certain measures. On the other hand, the significant digital presence threshold would not apply to European-sourced income derived by corporations that are resident of an extra-EU country with which the EU source country has entered into a DTT. Indeed, in such a case the traditional PE threshold would keep applying. However, given that, in most instances, the ultimate residence of the foreign enterprise is outside Europe (e.g., the United States for the largest multinationals), the problem appears to be still open. To address it, the EU Commission has recommended the EU member countries to negotiate bilaterally with the relevant non-EU country the inclusion of the significant digital presence clause in their existing DTTs. Surely, though, the renegotiation of DTTs will be time-consuming and, certainly, not a quick fix.

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<sup>5</sup> See Collin, P., and Colin, N. (2013): 'Task Force on Taxation of the Digital Economy' (available at [https://www.hldataprotection.com/files/2013/06/Taxation\\_Digital\\_Economy.pdf](https://www.hldataprotection.com/files/2013/06/Taxation_Digital_Economy.pdf)).

<sup>6</sup> OECD (2018): *Tax Challenges Arising from Digitalization – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project*, OECD Publishing.

<sup>7</sup> EU Commission, *Proposal for a Council Directive laying down rules relating to the corporate taxation of a significant digital presence*, COM/2018/0147, March 2018.

<sup>8</sup> For an in-dept analysis of the EU Proposal for the introduction of the "significant digital presence" concept, please see Escribano, E., 'A Preliminary Assessment of the EU Proposal on Significant Digital Presence: A Brave Attempt That Requires and Deserves Further Analysis', in "Combating Tax Avoidance in the European Union: Harmonization and Cooperation in Direct Taxation" (Ed. J.M. Almudí, J.A. Ferreras Gutiérrez, P. Hernández González-Barreda), Wolters Kluwer, (2018), 559-599.

<sup>9</sup> Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, available at <https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm>.

## 2.2 Implementing a New Tax Paradigm

As it emerges from the paragraphs above, although the adoption of the virtual PE can theoretically represent a technically appropriate systematic solution to the BEPS issue, its practical implementation could actually prove ineffective and, in any case, extremely time consuming to adopt. The question thus revolves around what can be done in the meantime. An increasing number of scholars, policy makers, governments, are currently considering implementing new types of taxes, which would enable source countries to collect tax revenues based on where the users of the digital firms are located.<sup>10</sup> In this regard, the public debate has reached an advanced stage, with some countries having already implemented their own new taxes: the “diverted profit tax” and the “digital service tax”.

### 2.2.1 The Diverted Profit Tax

The first country to introduce the diverted profit tax (“DPT”) has been the UK in 2015, followed by Australia in 2017.<sup>11</sup> The DPT is a special tax for “avoided permanent establishments”, that is, on profits that are diverted through artificial schemes from the UK or Australia as source jurisdictions. Its scope covers the UK or Australian-sourced profits of non-resident multinationals that have a significant digital presence in the source country, whose supply chain structure allows not having a PE and, thus, a taxable presence pursuant to the DTTs, therein. The DPT also applies on outbound payments made from UK or Australian resident business entities that lack economic substance, or directed to foreign entities established in low tax jurisdictions without economic substance.

The rate of the DPT is equal to 25% in the UK and to 40% in Australia, both of which are higher than the statutory corporate income tax rate (i.e., 19% in the UK and 30% in Australia). However, in order for the DPT to apply, a significant economic presence threshold is required, which amounts to £10 million or more of UK-related sales for the UK DPT, and to an annual global income of A\$1 billion or more for the Australian DPT.

While the DPT might seem appealing from a revenue perspective, it also faces compatibility issues with the DTTs. Specifically, it is not yet clear whether the DPT falls under the umbrella of income taxes and, as such, under the scope of the DTTs, and whether its application is in violation of the DTTs.

With respect to the former issue, the problem lies in the nature of the DPT. If the DPT qualifies as an income tax, then its payment should entitle the taxpayer to claim the credit against the corporate income tax due in its country of residence, as provided under Article 7 and Article 23 of the DTTs. On the contrary, if the DPT does not qualify as an income tax, then the taxpayer would not be entitled to claim the treaty benefit (i.e., the foreign tax credit), thereby exposing the taxpayer to double taxation. So far, most observers seem

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<sup>10</sup> Kofler, G. W., Mayr, G., and Schlager, C. (2017): ‘Taxation of the Digital Economy: “Quick Fixes” or Long-Term Solution?’, *European Taxation*, 523-32; Báez M., Brauner, A. (2015): ‘Withholding taxes in the service of BEPS action 1’, *WU International Taxation Research Paper Series*.

<sup>11</sup> See Kofler, G. W., Mayr, G., and Schlager, C., *supra* note 43, at 526. Wagh, S.: (2016): ‘The Taxation of Digital Transactions in India: The New Equalization Levy’, *Bulletin of International Taxation*, (70)9, p. 543 et seq. UK: Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015, No. 170, 2015; UK: Finance Act 2015, sec. 77 et seq. and the detailed Guidance of the HMRC (available at <https://www.gov.uk/government/publications/diverted-profits-tax-guidance>).

to favor the qualification of the DPT as an income tax, provided that it applies on profits, and not on gross revenues.

Regarding the latter issue, there exists a legitimacy problem of the DPT with the DTT under Article 7. Namely, determining unilaterally a significant economic presence, which entitles the source country to exercise its taxing power on the profit of a foreign corporation, could conflict with the current connecting factor (i.e., the PE) provided and agreed upon by the UK and Australia under the DTT. Such position is grounded on solid arguments. Indeed, the significant economic presence rests on presumptive quantitative elements (i.e., aggregated revenues and annual global income); thereby deviating from the qualitative PE threshold under Article 7 and Article 5 of the DTTs. Therefore, the DPT is not just out of the scope of the DTTs but it is actually in violation of them. However, against such argument, some claim the compatibility of the DPT with DTTs as allowing the implementation, by contracting countries, of measures aimed at preserving their taxable bases from tax avoidance schemes.<sup>12</sup>

### 2.2.2 *The Digital Service Tax*

The other type of tax targeting Digital Economy's multinational businesses is the digital service tax ("DST"). Such tax belongs to the category of taxes defined as "equalization levies", since, as stated by the OECD in the BEPS Action 1's Final Report, this levy represents a type of excise tax on digital transactions aiming at compensating for the "lost" profit taxes, which is payable by taxpayers with a significant economic presence.<sup>13</sup> Similar to the DPT, the aim of the DST is to tax non-resident large taxpayers, which have a significant economic and market presence in a source country but do not meet the PE threshold. This requirement aims to avoid undue compliance burden on small and medium enterprises.

It is worth highlighting two main differences between the DPT and the DST. First, while the DPT applies to the profits of foreign multinationals, the tax base of the DST is the gross sales. Crucially, this difference makes the equalization levy an indirect tax, likely an excise tax. Second, the equalization tax only applies to digital transactions, whereas the DPT applies to all profits generated of a foreign multinational in the source country, regardless of the transactions those profits originated from. Furthermore, the digital transactions falling within the scope of application of the DST depend on the policy priorities of the source country. As pointed out by the OECD, if the aim is to tax remote sales transactions, then the scope of application of the levy should encompass all transactions concluded remotely with in-country customers. On the contrary, if the priority is to tax the value directly attributed to local users and customers, then the levy should apply to every transaction implying or requiring the gathering of data from in-country customers and users.

Currently, the only country having unilaterally adopted and implemented the DST is India. Such a levy, which corresponds to a 6% tax rate applicable to revenues from digital transactions, is a withholding tax on payments to foreign companies for online advertising services provided to Indian businesses, or to PEs of other non-resident enterprises.<sup>14</sup>

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<sup>12</sup> Tomazela Santos, R. (2016), 'The United Kingdom's Diverted Profit Tax and Tax Treaties: An Evaluation', *Bulletin for International Taxation*, 399-405, at 400.

<sup>13</sup> *Supra* note 5.

<sup>14</sup> Such tax was introduced in 2016. For more details, please see Wagh, S., *supra* note 43, at 543 et seq.

Being a withholding tax, it poses a significant compliance burden on the Indian client, although the actual taxpayer is the non-resident advertiser. The significant economic presence threshold for the application of the equalization tax is met if the annual aggregated value of the payments exceeds USD 15,000.

On March 2018, the EU Commission released a directive proposal for a 3% EU-wide DTS<sup>15</sup> along with the already-mentioned directive proposal for the adoption of a significant digital presence concept. Both proposals are part of a plan of the EU institutions to cope with the tax challenges of the Digital Economy. As it will be illustrated, after the EU Commission released its proposal, several EU Member States have taken action to enact their a DST.

### 2.2.2.1 Structural Criticalities of the DST

Several structural criticalities surround the implementation, at either domestic or multinational level, of a DST.

The first structural criticality is related to the circumstance that a DST apply, by definition, only to digital service transactions. This may go against the economic concept of tax neutrality<sup>16</sup> and would thus ring fence the Digital Economy industry. This may end up unduly favoring firms operating in other industries, i.e. those whose core business does not fall under the umbrella of the Digital Economy. Indeed, as some rightly argue, nowadays, even traditional business rely on intangible assets, data collection, and digital platforms to offer their products and services. It is therefore unclear why only digital businesses' transactions should be tax liable.<sup>17</sup>

An additional element which may affect the effectiveness of equalization levies is whether the burden of such a levy would be borne by the service provider or actually by other weaker subjects, such as consumers or employees. Indeed, the fact that large businesses will legally be subject to the tax does not necessarily implies that such tax will ultimately be borne by them or by their shareholders. There is plenty of evidence showing that firms with strong market power – which is the case for the large MNEs targeted by

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<sup>15</sup> EU Commission (2018): *Proposal for a Council Directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services*, 148 final 2018/0073 (CNS) (available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018PC0148&from=EN>).

<sup>16</sup> A central theme in the design of corporate tax systems is the neutrality of taxes with respect to investment decisions (i.e., tangible and intangible assets). See, Sandmo, A. (1974): 'Investment incentives and the corporate income tax', *Journal of Political Economy*, 82, pp. 287-302. Boadway, R., and Bruce, N. (1984): 'A general proposition on the design of a neutral business tax'. *Journal of Public Economics*, 24, pp. 231-239. Auerbach, A. J., Devereux, M. P., and Simpson, H. (2008): 'Taxing corporate income', *NBER working paper no. 14494*.

<sup>17</sup> Olbert & Spengel, *supra* note 24, at 16.

the DST – pass on the tax burden to consumers.<sup>18</sup> Recently, some authors have even warned that part of the tax burden can be borne by suppliers<sup>19</sup> or employees.<sup>20</sup>

Another issue is represented by the fact that, since the DST applies to gross revenues, loss-making firms are in principles would also subject to the payment of the tax. However, if loss-making businesses were tax liable without any relief (i.e., tax losses carryforward or tax losses carryback), this could distort investment,<sup>21</sup> put at disadvantage start-up firms and discourage entrepreneurship,<sup>22</sup> and even create additional profit shifting incentives.<sup>23</sup>

Many policy-makers that such levy should be paid only in regard to services rendered by businesses having a significant economic presence: for example, in its proposal for the implementation of a EU-wide DST, the EU Commission has established that the tax is due only by those businesses which, in a given fiscal year, have reached at least € 750 million of total annual worldwide revenues and €50 million of annual intra EU revenues arising from the digital transactions. While such thresholds provide firms with certainty about the applicability of the DST, they could also provide firms with incentives to report or manipulate revenues and locate closely below the thresholds triggering the tax. Such strategic behavior (i.e., the so-called “bunching”) would not be surprising – since firms respond to incentives – and it has extensively documented in the prior literature.<sup>24</sup> Such threshold issue even exacerbates when MNEs, which by definition operate in multiple jurisdictions, report their financial information using different accounting standards.<sup>25</sup>

According to proponents of the DST, the only cost which should be deductible from its taxable base is the VAT. As such, no other business expenses would be tax deductible from the gross revenues. Such feature may trigger cascade effects of the DSTs not just on

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<sup>18</sup> As Fullerton and Metcalf write “the standard assumption about the corporate income tax that the burden falls 100% on capital it is commonly believed to be false.” Fullerton, D., Metcalf, G. (2002): ‘Tax incidence’, in Alan J. Auerbach & Martin Feldstein (Eds.), “Handbook of Public Economics”, Vol. 4, 1788–1872, at 1842.

<sup>19</sup> Dyreng, S., Jacob, M., and Xu, J., and Maximilian, M. A. (2019): ‘Tax Incidence and Tax Avoidance’ (available at SSRN: <https://ssrn.com/abstract=3070239>).

<sup>20</sup> Fuest, C., Peichl, A., and Siegloch, S. (2017): ‘Do higher corporate taxes reduce wages? Micro Evidence from Germany’, *American Economic Review*, 108(2), 393-418.

<sup>21</sup> Bethmann, I., Jacob, M., and Müller, M. A. (2018): ‘Tax Loss Carrybacks: Investment Stimulus versus Misallocation’, *The Accounting Review*, 93(4), 101-125.

<sup>22</sup> Cullen, J. B., and Gordon, R. H.: (2007): ‘Taxes and entrepreneurial risk-taking: theory and evidence for the U.S.’, *Journal of Public Economics*, 9(7), pp. 1479-505. EU Commission (2018): *Literature review on taxation, entrepreneurship and collaborative economy. Final Report TAXUD/2016/DE/315 FWC No. TAXUD/2015/CC/131*.

<sup>23</sup> De Simone, L., Klassen, K., and Seidman, J. K. (2017): ‘Unprofitable affiliates and income shifting behavior’, *The Accounting Review*, 92(3), pp. 113–136. Hopland, A. O., Lisowsky, P., Mardan, M., and Schindler, D. (2018): ‘Flexibility in income shifting under losses’, *The Accounting Review*, 93(3), 163–183.

<sup>24</sup> Almunia, M., Lopez-Rodriguez, D. (2018): ‘Under the Radar: The Effects of Monitoring Firms on Tax Compliance’, *American Economic Journal: Economic Policy*, 10(1), 1–38. Kleven, H. J. (2016): ‘Bunching’, *Annual Review of Economics*, 8(1), 435-464. Kleven, H. J. and Waseem, M. (2013): Using Notches to Uncover Optimization Frictions and Structural Elasticities: Theory and Evidence from Pakistan. *The Quarterly Journal of Economics*, 128(2), 669-723. Tennant, S. N., Tracey, M. R. (2019): ‘Corporate profitability and effective tax rate: the enforcement effect of large taxpayer units’, *Accounting and Business Research*, 49(3), 342–361.

<sup>25</sup> Balakrishnan, K., Blouin, J. L., Wayne, R. Guay (2019): ‘Tax Aggressiveness and Corporate Transparency’. *The Accounting Review*, 94(1), 45-69.

intra-group transactions, but also on transactions between independent platforms.<sup>26</sup> Therefore, appropriate mechanisms should be set forth to prevent such risk.

Finally, to date, it is still unclear whether the DST should follow cash or accrual accounting to identify when the tax is due. Choosing one rather than the other method may have significant practical implications.

#### 2.2.2.2 Policy Questions

Besides the above described structural issues, several policy questions concerning the design of an equalization levy arise. As highlighted by certain commentators, such policy questions center on the scope, the rate, the technical implementation, and its enforcement.<sup>27</sup>

With respect to the scope of application, the first issue is whether such tax should apply only to cross-border transactions or whether it should also apply to purely domestic transactions. As argued so far, it appears clear that the ultimate target of such a tax should be to tax cross-border digital transactions due to the misalignment between the market presence and the taxable presence of MNEs in the source countries. However, narrowing down the scope of application of an equalization levy to the revenues arising from cross-border digital transactions would likely raise WTO law and EU law issues because of a discriminatory nature of such a choice.<sup>28</sup> Closely related to this, other sensitive aspects entail the definition of “digital transactions” and the criteria to determine the threshold for the application of the tax, i.e., the significant economic presence.

As for the tax rate, the main issue is represented by the risk that countries may start competing with each other by setting lower tax rates. Indeed, prior experience with the corporate income tax and literature have extensively documented that countries compete with each other over mobile tax bases by setting lower tax rates.<sup>29</sup> It follows that countries could even engage in tax competition over the equalization tax, and this would raise tax arbitrage and base erosion issues.

With respect to the practical implementation and its enforcement, the main question lies in whether countries adopting such a levy should rely on the client of the digital services to act as a withholding agent, similar to the Indian equalization tax, or whether the compliance burden should be placed on the service provider. Choosing one option over the other is particularly relevant for cross-border transactions. With the withholding mechanism, the source country would collect the tax, which is in line with the policy rationale of the equalization levy. This approach would also avoid apportionment issues among countries. However, it would impose a compliance burden on the client of the digital services, which could be particularly burdensome for business-to-customer (thereafter, “B2C”) transactions. On the contrary, placing the compliance burden directly on the service provider would relieve the clients but it would also require tax revenue apportionments among countries, which could prove extremely complex and could require significant monitoring activities by several countries involved. Either way, since

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<sup>26</sup> Di Tanno, T., and Marchetti, F. (2019), (Eds.): ‘La tassazione dell’economia digitale’ (available at <http://www.fondazionebrunovisentini.eu/>), at 74.

<sup>27</sup> See Kofler, G.W., Mayr, G., and Schlager, C., *supra* note 43, at 530-531.

<sup>28</sup> See Kofler, G.W., Mayr, G., and Schlager, C., *supra* note 43, at 531.

<sup>29</sup> Devereux, M. P., and Loretz, S. (2013): ‘What do we know about corporate tax competition?’, *National Tax Journal*, 66(3), 745-774.

the policy rationale of the equalization tax is to re-establish the taxing power of the source countries over digital transactions, the application of an equalization tax will always require putting forth clear rules to determine where a service takes place.

Finally, the general concern among scholars is the characterization of the equalization tax. Although the aim is to re-establish source countries' taxing power over business income generated within their territories and compensate for corporate income tax revenue losses, there seems to be consensus that such a tax would not qualify as an income tax because the taxable base is based on gross revenues rather than profits. Such treatment would place the equalization tax outside of the scope of the existing tax treaties. From a policy perspective, the advantage would be that the application of such a tax could not be in violation of the DTTs (i.e., Article 7 or Article 5 of DTTs). The disadvantage would be that countries of residence of multinationals would not have a duty to grant a relief (i.e., tax credit or a deduction) for the equalization tax paid in the source countries. This would constitute an issue if the equalization tax were to be levy on taxpayers resident in high-tax countries.<sup>30</sup>

### 3. Final Remarks

Due to the mounting opposition of Ireland and the Nordic Member States (e.g., Sweden) in the ECOFIN meeting of May 2019, the EU Commission's project for the implementation of a EU-wide DST is currently on hold and, most likely, will not conclude anytime soon. Hence, the scenario is fragmented with some Member States willing to implement the DST, even unilaterally (i.e., Italy and France, which already have passed law introducing such a levy,<sup>31,32</sup> or Austria, the UK<sup>33</sup>, and Spain<sup>34</sup>), and some others refusing to take any action in such regard. Such a scenario is very detrimental, because, as the EU Commission argues, "divergent national approaches within the EU can fragment the Single Market, increase tax uncertainty, destabilize the level playing field and open new loopholes for tax abuse."<sup>35</sup> In this regard, a longstanding literature on tax competition dating back to the seminal works of Wilson<sup>36</sup> and of Zodrow and Mieszkowski,<sup>37</sup> along with the policy recommendations of the EU and the OECD against

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<sup>30</sup> The OECD has suggested that the levy be structured "to apply only to situations in which the income would otherwise be untaxed or subject only to a very low rate of tax". However, the OECD does not provide detail as to how such an alignment between the corporate income tax and the equalization tax should be concretely achieved. See, OECD, *supra* note 5, paras. 115 and 364.

<sup>31</sup> Bonichi, F., Cesetti, E., (2019): 'New Italian Web Tax and the EU Directive', *Bloomberg Tax* (available at: <https://news.bloombergtax.com/daily-tax-report-international/insight-new-italian-web-tax-and-the-eu-directive>).

<sup>32</sup> What is France's Digital Service Tax?, Euronews, 11 July 2019, available at <https://www.euronews.com/2019/07/11/what-is-france-s-new-digital-tax>

<sup>33</sup> Tidey, A. (2019): 'Austria is latest EU country to unveil tax targeting digital giants', *Euronews* (available at: <https://www.euronews.com/2019/04/03/austria-is-latest-eu-country-to-unveil-tax-targeting-digital-giants>).

<sup>34</sup> Mount, I. (2019): 'Spain takes another step towards Google Tax', *Financial Times* (available at: <https://www.ft.com/content/2020e052-1b45-11e9-9e64-d150b3105d21>).

<sup>35</sup> European Commission, Fact Sheet (2017): *Questions and Answers on the Communication on a Fair and Efficient Tax System in the EU for the Digital Single Market*, MEMO/17/3341 (available at [http://europa.eu/rapid/press-release\\_MEMO-17-3341\\_en.htm](http://europa.eu/rapid/press-release_MEMO-17-3341_en.htm)).

<sup>36</sup> Wilson, J. D. (1986): 'A Theory of Interregional Tax Competition', *Journal of Urban Economics*, 19(3), 296-315.

<sup>37</sup> Zodrow, G. R., Mieszkowski, P. (1986): 'Pigou, Tiebout, Property Taxation and the Underprovision of Local Public Goods', *Journal of Urban Economics*, 19(3), 356-370.

the “harmful tax competition” (i.e., the so-called “race to the bottom”), show that countries strategically compete over mobile tax bases,<sup>38</sup> and this eventually raises tax arbitrage and base erosion issues. All of this goes on top of the structural and policy issues that have been analyzed in the previous paragraphs.

In light of such an inauspicious scenario, the latest and reinvigorated resolution by the international community (specifically, the 129 members of the OECD/G20 Inclusive Framework on BEPS, which joint together for their plenary meeting in on May 28-29) to continue working towards a consensus-based long-term solution must be welcome.<sup>39</sup> In particular, the international community agreed on a Programme of Work leading to the enactment of substantial, although not disruptive, adjustments to the current international tax legal framework, aimed at resolving the tax challenges arising from the digitalization of the economy. The Programme of Work is based on two pillars:

1. the revision of the profit allocation and nexus rules, in order to achieve an apportionment of taxing powers between the jurisdictions involved by the MNEs’ businesses which could be deemed to be more consistent with the actual digital and economic presence and the value creation.
2. the design of a system aimed at ensuring that MNEs – in the Digital Economy and beyond – pay a minimum level of tax.<sup>40</sup>

For both the Pillars, the OECD has released consultation documents advancing technical solutions,<sup>41</sup> which imply coordinated changes to domestic law and tax treaties. Such Programme of Work clearly seems to return to the idea of cooperative multilateral actions aimed at revitalizing the effectiveness of the corporate income tax and the achievement of its revenue-raising, redistributive and regulatory purposes on a global scale, rather than shifting to a new international tax paradigm and framework based on new taxes.

Hence, large European countries considering introducing the DST unilaterally and with varying tax rates could even lose out or, at best, collect less than expected tax revenues. In this vein, we warmly welcome the very recent agreement of the OECD/G20 members of the BEPS Inclusive Framework to continue cooperating to achieve a long-term structural solution to the tax challenges arising from the Digital Economy.

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<sup>38</sup> EU Commission (1997): *Harmful Tax Competition. A Code of Conduct* (available at: [https://ec.europa.eu/taxation\\_customs/business/company-tax/harmful-tax-competition\\_en](https://ec.europa.eu/taxation_customs/business/company-tax/harmful-tax-competition_en)). OECD (1998): *Harmful Tax Competition. An Emerging Global Issue*. OECD Publishing.

<sup>39</sup> OECD (2019): *International community agrees on a road map for resolving the tax challenges arising from digitalization of the economy* (available at: <http://www.oecd.org/tax/international-community-agrees-on-a-road-map-for-resolving-the-tax-challenges-arising-from-digitalisation-of-the-economy.htm>).

<sup>40</sup> OECD (2019), *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy*, OECD/G20 Inclusive Framework on BEPS, OECD, Paris, (available at [www.oecd.org/tax/beps/programme-of-work-to-develop-a-consensus-solution-to-the-tax-challenges-arising-from-the-digitalisation-of-the-economy.htm](http://www.oecd.org/tax/beps/programme-of-work-to-develop-a-consensus-solution-to-the-tax-challenges-arising-from-the-digitalisation-of-the-economy.htm)).

<sup>41</sup> “OECD invites public input on the Secretariat Proposal for a “Unified Approach” under Pillar One”, available at <https://www.oecd.org/tax/oecd-invites-public-input-on-the-secretariat-proposal-for-a-unified-approach-under-pillar-one.htm>; “OECD secretariat invites public input on the Global Anti-Base Erosion (GloBE) Proposal under Pillar Two”, available at <https://www.oecd.org/tax/oecd-secretariat-invites-public-input-on-the-global-anti-base-erosion-proposal-pillar-two.htm>