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Conflict between European Union countries and large digital platforms over digital tax

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ABSTRACT: *The digitalisation of both the economy and society at large poses new tax policy challenges. In particular, some European nations find that large digital platforms operating in their territories are able to use their unique features to their advantage, as countries watch large sums of tax fleeing their countries. Despite ongoing multilateral negotiations, some of these countries have decided to move ahead with unilateral measures to tax the digital economy. Because these taxes mainly impact US companies and are thus perceived as discriminatory, the United States has responded with retaliatory threats. As a result of their great power, large digital platforms are also able circumvent unilateral measures by shifting the tax burden to consumers.*

The aim of this paper is to assert whether a common solution adopted by all EU countries would be most beneficial than a strictly unilateral approach. To do so, we describe the common solutions proposed by the OECD and the EU to date, we outline the different economic and political perspectives among EU countries regarding the digital tax issue and analyse the current paradigm in order to assert the most suitable path to follow. The topic is relevant in order to understand whether EU countries should continue to impose unilateral measures while waiting for a common solution, which is being worked on at the negotiation table.

Key words: Digital tax conflict, Digital economy, Digital platforms, GAFAM, European Union, OECD tax.

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Abbreviations and Acronyms

AI: Artificial Intelligence

BEPS : Base Erosion Profit Shifting

CCCTB: Common Consolidated Corporate Tax Base

DST: Digital Service Tax

EU: European Union

EC: European Commission

ECIPE: European Center for International Political Economy

G20 : Group of Twenty

GAFAM : Google, Apple, Facebook, Amazon, Microsoft

IoT: Internet of Things

OECD: Organization of Economic Cooperation and Development

PE: Permanent Establishment

SDP : Significant Digital Presence

TFEU: Treaty on the Functioning of the European Union

US: United States

VAT: value-added tax

1. Introduction

1.1 Purpose and research question

The Fourth Industrial Revolution is characterized by 'a range of new technologies impacting all disciplines, economies and industries' that blur the boundaries between the physical, digital and biological worlds. The fusion of advances in artificial intelligence (AI), robotics, the Internet of Things (IoT), 3D printing, genetic engineering, quantum computing, and other technologies has radically changed the way of doing business and the relationship between consumers and producers.

These changes have occasioned the coexistence of traditional business models, also addressed as 'brick-and mortar' businesses who rely heavily on physical presence and new digital businesses. The latter are based on several distinctive features. They generally place greater importance on intangible property (licenses, brands, trademarks, copyrights), most of their activities rely on the use of technology (cloud, analytics, algorithms, smart machines) and their digital goods and services are highly mobile. For that reason, the physical presence of these companies in the countries they operate in is often not needed.

Further, the COVID-19 pandemic has accelerated the digitalisation of the economy, bringing about digital changes that were predicted to come in years in just a few months. Added to their reliance on mobile assets, the pandemic has exacerbated the use of large digital platforms and has consolidated them as leaders in their respective sectors. Amazon, for instance, is expected to obtain between $100.0 billion and $106.0 billion in net sales on the first quarter of 2021, which results in growth between 33% and 40% compared to first quarter 2020. (Amazon, 2021) As digital platforms such as Uber, Amazon, Google and Facebook to name a few have become the dominant force in the digital economy, an increasing number of political bodies and government authorities have voiced complaints about their business practices.

This is particularly relevant for the European Union. Whereas only one tech company qualified for the top 20 list in Europe by market capitalisation in 2006 with a share of 7%, 9 digital companies led by US tech giants were in the top 20 with a 54 % portion of the market in 2017. (Brookings Institute, 2017) Today, the largest European tech companies put together are worth about 30% of any one of the top 4 American companies. The largest

European tech company by far is SAP, worth about 14% of Amazon or Microsoft. (Bloomberg, 2018)

Both the OECD and the European Commission came up with a series of recommendations to follow a common approach regarding digital tax, given the pressing issues concerning taxation of the largest digital platforms.

The OECD agreed to conduct a comprehensive study published in 2019 and was supposed to set the guidelines to achieve definitive consensus on digital tax for all OECD members by 2020. The main objective would have been to avoid the implementation of unilateral proposals that would be detrimental to the relationship among governments, particularly the EU and the US. In fact, it is important to highlight that during COVID, the work to build effective tax systems has proved to be of the utmost importance.

However, due to the few advancements made during G20 meetings and after the US pulled out of talks in June due to the COVID-19 pandemic there has been no further progress on the matter. The last OECD meeting for tax base erosion and profit shifting (BEPS) to date was held in February 2021. It consisted of a reaffirmation of what had been previously elaborated and it served as a renewal of the commitment to reach a common agreement, but nothing definitive was brought to the discussion table. Members have postponed the deadline for an agreement to mid-2021. (Voa News, 2020)

Considering political and economic pressures in the Union countries, a “quest for fairness” regarding digital tax was justified by the EU Tax Commissioner Pierre Moscovici as he claimed that digital companies pay an average of 9% effective tax rate in the EU compared to other firms that pay 21%. (EU Commission, 2018) Yet, this affirmation is based on distorted premises, as shown by the European Centre for International Political Economy, an independent and non-profit policy research think tank based in Brussels. (ECIPE, 2018)

We may find dissenting attitudes among EU countries regarding digital tax. Supporters of total or partial reform of the tax system, such as the governments of the UK and France, argue that companies operating in the digital arena should pay additional taxes to the ones already in place. Others, such as the governments of Ireland and Luxembourg, worry that tax reform could lead to double taxation and higher prices.

While all EU country members agree on the salient features of digital business models and find it necessary to address them within the current tax system, they differ in how to do so. To find a joint approach has proved to be difficult considering that individual members of the Union have jurisdiction over digital tax matters within their individual territories. (European Commission, 2018) Despite this, there is a shared common interest in maintaining a single set of relevant and coherent international tax rules, in order to promote economic efficiency and global welfare.

In the context of this discussion, we find relevant to answer the following question. Is a common tax approach in the European Union a more appropriate way forward than strictly national tax policies to tax digital platforms?

The relevance of this topic resides in two matters. First, the fact that smart data incentivized by AI and machine learning together with large data volumes will likely foster the creation of new businesses that we cannot envision today. (KPMG, 2016) This is why it is of great importance to find the best long-term approach to tackle current and future digital tax issues.

Second, the EU is not the only one considering tax policy reforms for the digital economy. Numerous countries around the world, as well as major international bodies such as the aforementioned OECD, participate in the discussion to address tax of the digital economy. Indeed, issues related to rules such as “permanent establishment” (PE) of digital companies go beyond the EU borders. Perhaps the EU may find a suitable path to tax the digital economy that may be followed by other regions around the world.

1.2 Objective

The main objective of this paper is to analyse the progress that has been made to tackle digital tax within the European Union countries. We will assess if a common solution for a digital tax, particularly with regard to large digital platforms, is the answer to both intra-European constraints, which include the tax difference that makes some countries in direct competition with others among the Union, as well as external political pressures, taking into account the different perspectives among EU countries. Ultimately, we would like to know if a common tax approach at the level of the Union would be more beneficial for member countries, EU citizens and digital platforms at large.

Secondary objectives will be the following:

- To analyse the main challenges of the digital economy and understand discrepancies with regard to value creation.
- To outline the progress made by the OECD and the EU Commission, as well as the limitations of their proposals.
- To address the conflict between the EU and the US, as well as the Union's conflict with large platforms regarding digital tax and its general consequences.
- To briefly assert the EU's path towards tax harmonisation as to be able to outline future lines of research with regard to digital tax in the EU.

1.3 Methodology

This work is essentially descriptive-explanatory. In the first phase we will review several economic and legislative documents published by EU institutions in order to understand the features of the digital economy and the Union's perspectives on digital tax. The following primary sources will be used: European Commission, European Union, Eurostat, OECD, various ministries related to the topics covered, as well as specialized research centres, such as Statista.

In a second phase, we will review works and reports published by banking institutions, consulting and auditing firms, as well as technology companies in order to assess the current progress on digital tax. Once the data has been compiled, it will be processed in order to identify the different existing trends among EU members and tackle potential issues raised by external actors.

Finally, we will briefly outline the obstacles and the political discussion on EU's progress towards tax harmonisation through official reports by the European Union and external entities such as Wolters Kluwer, a reputed Dutch-American information services company.

1.4 Structure

In order to perform a detailed analysis of the impact of large digital platforms on EU country members, several steps will be followed. First, we will address the problem over digital tax from a theoretical point of view. We will cover the particular features of large digital platforms, their business model, how they generate value and why it becomes so difficult to measure. We will also analyse the standard features of a tax system in order to understand what the ideal taxation system for these platforms would look like, taking into account current established parameters.

Second, we will go through the OECD and EU proposed approaches. Although they are temporary and no definite final solution has been published yet, many countries have adopted interim unilateral measures these organisations suggested in order to start collecting taxes from large digital platforms.

Thirdly, we will cover current national taxation schemes for large digital platforms in the EU. We will address the three main trends among EU countries and their conflict with large digital platforms and other states, namely the US.

Finally, having analysed the issue in depth, we will gather the key points on the discussion previously considered along the paper and would make a number of recommendations about what a fair and appropriate common system might look like for the EU.

2. The conflict over digital tax

2.1 Digital taxation of the digital economy: Main challenges

The specific features of the digital economy bring about new and existing challenges for tax policy. The main tax challenges of the digital economy are the following. (OECD, 2019)

The first would be the lack of nexus or physical presence. Unlike traditional companies whose profits are taxed at value creation, digital technology companies conduct most transactions electronically, which allows them to reduce costs on physical infrastructure. (European Parliament, 2019) On the other hand, assets and activities of digital businesses can easily move across jurisdictions in order to avoid taxable presence in a high-tax jurisdiction, which is commonly known as BEPS. (OECD, 2019)

Nevertheless, the concept of BEPS is not new nor unique to the digital sector, as cross-border transactions of, for instance, delivery companies, pose similar issues regarding the determination of the taxing jurisdiction. Another typical example, this time regarding intangible value that moves across countries, is the case of consulting services that flow from a low-tax jurisdiction country within the EU to other countries with higher-tax jurisdiction. (European Parliament, 2019)

Tightly linked to the first feature is digital platforms' reliance on intangibles (licenses, brands, trademarks and copyrights) and the use of technological innovations (cloud, analytics, algorithms, smart machines). This gives rise to difficulties around the principle of value creation in which tax systems are based. There is currently no consensus among national authorities on how income from digital platforms' value creation activities should be identified, measured and allocated amongst different parts of multinational groups.

Finally, the third challenge is digital platforms' management of data and user-generated content.

One consequence of the digitalization of the economy is the massive increase of volumes of data. Data collection is doubling every year, and combined with advances in data analytics and technology diffusion it is providing the insights necessary to transform and shape the way people behave and organisations operate.

Then again, extensive use of data and user-generated content raises the question on whether the users contribute to value creation by providing their data to platforms in exchange for free access (which is then sold to online advertisers by platforms) in addition to enlarging the user base of the platform and enhancing its reputation through network effects. (European Parliament, 2019)

2020's Netflix documentary "The Social Dilemma" explains how digital platforms' main source of income is data and user-generated content, which is difficult to measure and regulate. (Netflix, 2020) While the topic of data privacy will not be covered in this paper, the fact that large digital platforms may have access and use citizens' data for profit purposes has become increasingly polemic and it is a great challenge for political authorities.

All in all, we find that digital platforms generate revenue from user's data, which is not contemplated under the current tax framework and consequently not charged with VAT.

2.2 Business model of digital platforms

Traditionally, economies have been driven by companies selling products or providing services. Today, companies like Google, Facebook, Uber and Amazon are defining new monetisation strategies for the 21st Century and shaping new business models.

The platform economy, formerly known as collaborative economy, is a vast digital ecosystem that interconnects cloud technology, big data and mobile apps. It encompasses, for instance, food delivery services such as Deliveroo, video streaming services such as YouTube, ride-hailing apps such as Uber and Lyft and tourism services like Airbnb and Booking, among others. (Kyocera, 2018) In the digital economy, value is created from a combination of algorithms, user data, sales functions and knowledge. Digital platforms mainly focus on value creation through the establishment of digital marketplaces that connect users and facilitate digital transactions, in addition to the traditional offer of goods and services.

Business models vary across platforms. For many digital enterprises, the main objective is to build large platforms as to benefit from network effects. This is the case for social media networks like TikTok, Instagram or Facebook, who also profit from the introduction of advertisements that are relevant to the user. More recent is the hyper-personalization of ads for the user, which is possible due to the data these platforms obtain from their consumers.

A second type of digital companies offer their own products or services directly, such as Google or Amazon. Some of them build their business models around transaction costs, meaning that their revenues are directly determined by the volume of sales in their network. Uber, for example, charges a variable booking fee of around 20% of the transaction, while Airbnb charges its customers between 5% and 15% plus management fees. (Kyocera, 2018) If these platforms are undersized, costs and profitability drop.

A third type of digital platforms opt to use subscription models, based on a free service for users with the option of a premium upgrade, such as Netflix or Spotify. The possibility to combine several of these business models is more and more common, which is why digital platforms increasingly adopt a combination of several business models.

2.3 Value creation in the digital era: Where do digital platforms pay taxes?

This section has two main purposes. First, we analyse value creation of digital platforms as assessed by the OECD Report for BEPS Action 1 *Addressing the Tax Challenges of the Digital Economy*. Published in 2015, this initial report has been updated by the OECD/G20 Inclusive Framework on BEPS in recent years and includes advancements in public consultations up until 2021. Second, we assert where large digital platforms ultimately pay their taxes within the EU.

First, the OECD Report distinguishes between the value chain, the value network and the value shop. (OECD, 2019) The Report explains how it is widely believed that the value chain analysis for digital platforms does not differ greatly from the traditional analysis. Rather, it is novelties surrounding digital platforms' primary activities in their network and shop that give rise to dissenting views.

Second, the document analyses the data value cycle. While data-driven decision-making is where most economic value resides, other sources such as personal data may also be a great source of revenue. The current lack of regulation regarding the compilation and use of data generates value yet to be calculated for digital platforms. (European Commission, 2018)

Third, the OECD Report addresses the spectrum of user participation, which may be active or passive. On the one hand, active participation of users may be measured through content generation (e.g. media posts) or ratings and reviews that build a trust mechanism, which is a fundamental component of value generation. On the other hand, passive participation takes into account more unassertive actions, like users downloading an app.

These contributions make digital platforms profit from indirect network effects. To illustrate this with an example, in the media industry, a digital business model will entail that a higher tax rate on revenues from selling media content will result in a lower price for the media content and a higher number of readers. This is contrary to the standard tax response, which entails a higher price and a lower number of users. (Köthenbürger, 2020) As a result, we have positive indirect network effects. A higher number of readers makes the platform more attractive for advertisers and generates significant amounts of advertising income. (Köthenbürger, 2020)

The degree of importance of user participation differs across businesses. For example, user participation is key for social networks such as Facebook, but perhaps not as important for search engines like Google. For digital activities surrounding manufacturing, for instance, user participation is practically useless. (OECD, 2019)

As a result, user participation has non-conventional implications for the evaluation of taxes and the design of tax policies. The degree of importance of user participation will widely determine the difficulty of analysing value creation.

Fourth, the Report identifies problems regarding nexus. Digital platforms' business model allows them to be present in multiple jurisdictions (or physical nexus) that are subject to different taxes. In these environments, the aforementioned indirect network effects modify the way the platform responds to taxes. Thus, tax avoidance takes the form of shifting revenues from the more heavily taxed side to the less heavily taxed side of the platform via quantity increases on the more heavily taxed side. In other words, digital companies tend to stablish their Permanent Establishment (PE) in low-tax jurisdictions and operate from there to offer services in higher-tax jurisdictions.

Another example is how, in digital business models, the profits are not necessarily taxed in the country of the user (or viewer of the advert), but rather in the country where the advertising algorithms have been developed. This means that the user contribution to the profits is not taken into account when the company is taxed. (European Commission, 2018)

Nexus problems commonly result in Base Erosion and Profit Shifting (BEPS) practices. As explained in the Report, these are concerning for several reasons. First, they distort competition. Second, BEPS may lead to inefficient allocation of resources by distorting investment decisions. Third, a legal practice to avoid income tax undermines voluntary compliance by all taxpayers within the tax system. (OECD, 2019) The issues mentioned in the OECD Report raise questions as to whether the current rules to determine nexus with a jurisdiction for tax purposes are appropriate.

Moving forward, we may identify different perspectives surrounding value generation on digital services.

We may distinguish upon those countries who believe that no major change is needed within the current system, as BEPS and other measures already in place are sufficient to act on all types of existent businesses. Another group of authorities calls for a fundamental change in the tax system to reflect issues arising from globalisation. Nevertheless, they find that no additional measures regarding digital businesses specifically are needed. Finally, the last group of nations believes in the establishment of a novel framework that contemplates the impact of technology on digital enterprises, including new business models and the issue of value creation. (PwC, 2018)

All in all, the OECD Report suggests that there is no consensus on the relevance of key features and their importance to the location of value creation and the identity of the value creator. (OECD, 2019) Particularly, as there is no current agreement as how to assert value of certain digital activities, to assert where they generate value becomes increasingly difficult. Both the OECD and the EU Commission have different perspectives on the matter. However, all parties agree that further study on the matter is needed for future decisions regarding digital tax.

On the other hand, we need to consider where these large digital platforms pay their taxes.

As we mentioned, digital platforms will look for low-tax jurisdictions to stablish their reduced physical presence. Examples of this in the European Union would be Dublin in Ireland, Amsterdam in the Netherlands or Tallinn in Estonia, which have been successful in attracting leading technology companies to base their headquarters in Europe due to their low-tax jurisdictions. (Business Insider, 2020)

2.4 Main traits of a general tax system. How do they apply to digital platforms?

The conflict described in this paper arises because the general features of a traditional tax system do not apply to the digital platform economy. We will now analyse what those characteristics would be and how they would ideally apply to digital platforms.

The general features of an effective tax system are the following. A tax system determines the amount that constitutes an obligation for taxpayers, must be established by law and must be proportional, equitable and progressive. (Wolters Kluwer, 2019) The tax will have to take into account the amount to be collected and the collection expectation in order to ensure the adequacy of the tax system. Further, it should be based on principles of fairness and equity in all taxes, stability and neutrality. (Martín Queralt, 2020)

For one thing, taxes on digital platforms should be proportional. Each entity should pay a fixed, non-progressive percentage of their income. In addition, taxes should be predictable in the sense that they should not be set arbitrarily, avoiding exemptions and deductions established depending on the source of income or other factors. The current system should not create incentives to avoid taxes (BEPS) and should be simple to minimize the cost of collection. (Tax Foundation, 2021)

A good system would also be characterized by a tax burden that does not discourage job creation and investment. In fact, investment in R&D by large technology companies totalled USD 100 billion in the first quarter of 2018. (Cinco Días, 2018) Higher tax burdens on digital companies could exacerbate the challenges that tech firms face in building out their infrastructure in Europe.

Stability is another important feature for the taxation of large digital platforms, which means that fiscal policy should be consistent in the long term. This is the reason why the OECD and the EU are taking the time to analyse in depth the current tax framework.

Digital entities should be able to trust the legislation in force so as to avoid trade wars among countries. This is particularly important for EU consumers, who are the great losers of commercial disputes and are deeply affected by retaliation. The tax system should have broad tax bases so that tax rates can be moderate and, lastly, foster cooperation and understanding among nations as to avoid restricting free trade. Ideally, the taxation of digital platforms would be based on a common and harmonized system for all countries.

Finally, tax implementation should be fair and neutral. This condition is relevant as for national actors not to discriminate digital companies as a consequence of its origin.

2.5 Features of large digital platforms

The peculiarities of large digital platforms in relation to taxation are the following.

Firstly, the largest digital platforms, also addressed as GAFAM (Google, Apple, Facebook, Amazon and Microsoft) are American. SAP, Spotify and Skype, respectively originated in Germany, Sweden and Estonia, are examples of large European digital companies in 2021. However, they are far behind from great American and Asian corporations. (European Parliament, 2019)

Secondly, these platforms are currently quasi-monopolistic in their respective markets, namely e-commerce, online advertising and cloud computing, which is translated into extraordinary profits that countries around the world want to benefit from. Network and scale effects, the potential to differentiate from competitors and multi-sided platforms are the reason why digital businesses have a tendency towards monopolisation.

A good example of this would be Google. On December 2020, the platform was accused of overcharging publishers for ads showed across the web and limiting the entrance of rival search engines who tried to challenge the company’s dominance. (Techcrunch, 2020)

Admittedly, these markets are volatile and seemingly contestable by disruptive newcomers, as barriers of entry and exit appear to be low. In fact, Google defended itself by alleging that its competitive advantage resides in its ability to provide the best quality results for every user, which allows the company to outperform other search engines. However, it is also true that strong network effects cause barriers of entry to rise. Social networks such as Facebook or Twitter, for instance, largely depend on their popularity, as their main objective is to connect the user with a great number of people. The fact that the use of a social network is less widespread may in turn limit its use by other users.

A direct consequence of the quasi-monopolistic nature of large digital platforms is that they have the economic, political and social power to negotiate with national governments and even take them on directly in court. (Medium, 2019) In fact, large digital platforms' size and influence make them a potential adversary of national governments, even more so of EU member states as a result of platforms' high level of activity in the region. Overall, the EU is an attractive market for digital platforms. However, member countries of the EU individually would find it more difficult to negotiate tax terms on their own due to their relatively small size.

Thirdly, digital platforms' reliance on intangibles and their lack of physical presence makes them particularly mobile. Hence, digital companies are more able to structure themselves as to minimise their tax liabilities and makes it more difficult for tax authorities to assess how income from such assets should be identified, valued and allocated amongst different parts of multinational groups.

3. Institutional framework

3.1 OECD and EU approaches. Limitations and problems

The following chapter will describe the EU and OECD approaches to digital tax concerns, which were both published in March 2018. We will outline long-term proposals and interim measures the EU has set in place in order for individual members of the Union to start collecting digital taxes right away.

Long-term solutions

In recent years national authorities in the EU have been facing increasing political and media pressure that called for a European solution to address digital tax. In fact, a survey conducted in 2018 among EU citizens showed that 74 % of respondents believed that current taxation rules allow digital business models to pay lower taxes, at the same time that 82% of them believed that action to address this matter should be taken. (European Commission, 2018)

As a result, the EU Commission made a long-term legislative proposal, also addressed as Significant Digital Presence. Its goal is to reform corporate tax rules and would aim to address *what* and *where* companies and services should be taxed.

A common EU proposal would be justified under the TFEU, the Treaty on the Functioning of the European Union, Art. 116. "*Where the Commission finds that a difference between the provisions laid down by law, regulation or administrative action in Member States is distorting the conditions of competition in the internal market and that the resultant distortion needs to be eliminated, it shall consult the Member States concerned.*

If such consultation does not result in an agreement eliminating the distortion in question, the European, Parliament and the Council, acting in accordance with the ordinary legislative procedure, shall issue the necessary directives. Any other appropriate measures provided for in the Treaties may be adopted." (Official Journal of the European Union, 2016)

Under the Significant Digital Presence proposal, a digital platform has taxable 'digital presence' or a virtual permanent establishment (PE) in a European Union country if it fulfils only one of the following criteria: (European Commission, 2018)

- It generates an annual revenue of more than €7 million in a European Union country.
- It has more than 100,000 users in a European Union country per taxable year.
- It creates more than 3000 business contracts for digital services with business users per taxable year.

With this proposal the EU Commission aims to tax profits from user data, services connecting users as well as other digital services, such as platform subscriptions. In the Commission's view, the proposal will contribute to put an end to BEPS practices arising from technological changes in the tax system, will guarantee a minimum level of tax paid by multinational platforms and will also level the playing field between traditional 'brick and mortar' and digital companies. (ECIPE, 2018)

The aim of these standards is to affect large digital platforms exclusively (which are American, quasi-monopolistic and very mobile) and to avoid limiting the growth of European start-ups, most of which rely heavily on digital services. (European Commission, 2018)

However, it has been argued that with this proposal the EU Commission seems to be moving away from trying to value and tax the use of data as such. The critiques range in content from countries arguing that the proposals affect national sovereignty of EU member countries over tax policy to questioning the logic behind the proposals themselves. (Tax Foundation, 2018) In fact, proposals may create a tax charge in the EU member country or Source State even where there is no or relatively little use of customer data, or where there is no creation of intangible assets. (KPMG, 2018)

On the other hand, the OECD Report published in March 2018 highlights the need to tax *only* where value is created, and to understand the impact that digitalization may have had on business models and value creation as described in section 2.3. The organisation has called for further work to examine existing international tax rules on nexus, or if digital platforms should be taxed in a country where generates value but does not have a physical presence, and how to allocate profit on the basis of such nexus.

Given the lack of consensus among EU countries, the DST and SDP proposals are blocked since 2019.

Interim measures

As a result of the lack of agreement on the common implementation of the Significant Digital Presence, the European Commission proposed the ‘Digital Service Tax’ (DST). It consists of a proposed national tax which covers the main digital activities that escaped tax altogether in the EU, such as advertising, digital platforms and sale of data. (European Commission, 2018) Arguably, this proposal does not constitute a long-term solution, as although it may appear to be targeted towards large businesses exclusively, current smaller digital businesses’ growth might be compromised in the future. Hence, the DST constitutes a temporary unilateral measure.

However, the proposed and implemented DST differ significantly in amount and structure across EU countries. Regarding the amount, the EU stablished a standard rate measure of 3% per taxable year on the largest digital companies, which would allegedly generate an estimated amount of €5 billion per fiscal year for member states. (European Commission, 2018) Implemented tax rates currently ranges from 1.5% in Poland to 7.5 % in Hungary (although Hungary's tax rate is temporarily reduced to 0 percent).

Concerning the structure, some examples are the following. Austria or Hungary only tax revenues from online advertising, whereas France's tax base is much broader, including revenues from the provision of a digital interface, targeted advertising, and the transmission of data collected about users for advertising purposes. (Tax Foundation, 2020)

As we explain on the following section 4.1, about half of all European OECD countries have either announced, proposed, or implemented a 'Digital Services Tax' unilaterally. Their justification resides in alleged political and economic needs. (KPMG, 2019) Others have decided to wait for a long-term common approach to be established by the OECD and EU, in fear of retaliation by both the US government and large digital platforms.

Nevertheless, the unilateral approach among EU countries does not come without consequences.

First, unilateral measures raise significant concerns regarding potential double taxation, increased administrative burden and uncertainty. (Tax Journal, 2018) This in turn threatens the attractiveness of investment on countries that adopt them.

Second, unilateral measures lead to economic distortions and an unhealthy tax competition between higher and lower-tax jurisdictions. This may give raise to political tensions among EU countries.

Third, the one-sided approach has an impact on consumers within the EU, as independent reforms may lead to uncertainties and changes in prices. Further, large platforms' power and scope is such that they are able to avoid unilateral measures and shift the burden of taxation to consumers. Given that digital users make daily use of digital platforms in order to meet their professional and personal demands, they ultimately have no choice but to pay the additional difference imposed by large platforms.

Finally, we need to take into account external reactions. Considering the most relevant digital platforms are American, some have argued that unilateral measures may lead to a "hostile work environment" for US businesses. (Brookings Institute, 2017) This results in the rise of tensions between individual European countries and one relevant strategic partner for the Union such as the US, which may in turn affect other areas of economic activity through retaliatory measures. (European Parliament, 2019)

All in all, unilateral measures with regard to digital tax generate a significant risk of double or multiple taxation. They raise the number of cross-border disputes and political tensions within the EU and among the Union and other countries, which may result in trade wars and economic protectionism. Ultimately, the unilateral tax does not accomplish its original purpose, as the tax burden ends up being paid by the Union consumers.

As for the OECD, the 2018 Report notes that there is no consensus on the need or the merit of introducing interim measures, which is why the organization has not introduced any. An important downside of this decision has been that many OECD members have implemented an interim tax under their own standards, which has provoked the same results than the DST. (KPMG, 2021)

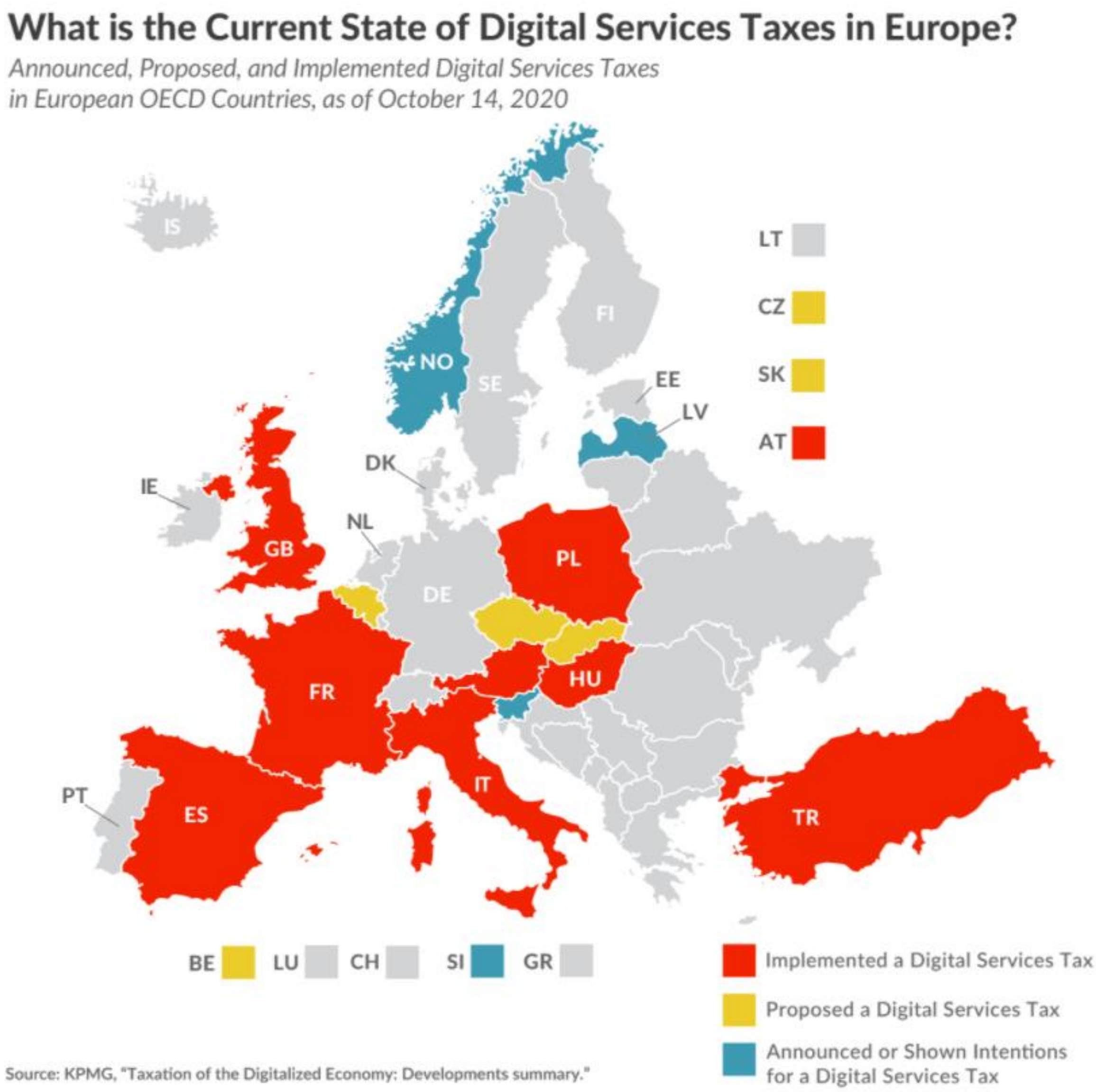
4. Current national taxation schemes for large digital platforms

4.1 Digital tax at EU member state level

In this section we describe national taxation schemes of large platforms in the EU. We particularly focus on countries relevant to the topic, which either constitute a large market for large platforms or are those where platforms have set up their tax residences.

We may identify three main trends among EU countries with regard to digital tax. The first group of countries are those who have already introduced new digital tax laws, namely the interim DST proposed by the European Commission. They are represented in red in the map. The second group involves those who plan to add digital taxes in the near future (yellow and blue) and the third group is formed by those who do not see the need to introduce new taxes in addition to those already in place (grey, excluding those who are not EU members).

The following map shows the enactment of the interim measure DST in Europe up until the 14th of October 2020. However, we are able to make an analysis of interim measures due to the report *Taxation of the digital economy*, published by KPMG and updated up until 15th January 2021.



Source: KPMG (2021); Tax Foundation (2020)

First, we will focus on EU countries which have introduced DST or other digital tax measures, which are represented in red. Each country has decided to implement the measure in accordance to their needs, as to benefit national companies in detriment of large foreign platforms. In fact, the large majority of these countries are currently being investigated by the Office of the United States Trade Representative (USTR) under the view that the digital services taxes EU countries have adopted are discriminating against US companies. (KPMG, 2021)

The most hard-line approach in the EU would be the held by Austria or Hungary, with respective taxes of 5% and 7%, for revenues from advertising services on digital interfaces or any type of software or websites used within their territories.

A more flexible yet polemic approach within this first group would be the case for France, Italy, Spain. These markets are some of the most important in the EU for their large number of consumers, which is why the decision has had more impact and has exacerbated a media response and the conflict with the US.

As European leader of the general discussion, France introduced the same tax but addresses it as “French digital presence”, the collection of which was delayed to the end of 2020 for political motives.

Italy and Spain introduced the DST proposal of the European Commission, which constitutes a 3% of gross revenue from online advertising services, the sale of online advertising and the sale of user-data. In Spain, DST receives the name of ‘Google tax’. (Reuters, 2021)

To this group we may also add Poland, who passed in July 2020 a 1.5% tax on revenue of on-demand provider resulting from access to audio-visual media services and audio-visual commercial communications.

Further, although the UK is no longer part of the EU, we find relevant to include it in the discussion for its introduction of the DST, with a 2% on revenue in excess of 25 million pounds derived from social media platforms, internet search engines and online marketplaces. (KPMG, 2018)

In the UK’s government position paper ‘Corporate tax and the digital economy’ published in 2017, the general assessment of the country was to exclusively tax value driven by user participation. Hence, the approach would consist on targeting pure user participation business models (i.e where revenue is generated through advertising or intermediation), and not retail businesses selling goods through online platforms. (Tax Journal, 2018) This would have excluded platforms like Google or Amazon, at least with regard to revenues generated from their online marketplaces. However, given that they acknowledged it to be a long-term objective that requires broad international consensus and adoption, the UK decided to enact unilateral interim measures for multiple large digital platforms operating in the country.

Moving on to the second group, we analyse countries represented in yellow and blue, who have shown intentions of imposing the DST or other alternatives that may suit national interests. In the majority of these countries, the national finance minister has announced the implementation of digital tax measures and has urged to come up with a solution by 2020. However, as political parties in power changed none put forward digital tax as their priority agenda and, consequently, no further steps have been taken to implement the proposals. (KPMG, 2018) This has been the case for Belgium, Slovenia, Slovakia and Latvia, among others.

The most noteworthy case for its high tax proposal is Czech Republic. In 2020, the country introduced a 7% DST proposal, which was later on reduced to 5%. Although it was expected to be enacted by 2021, there have been no further signs of the adoption of the tax. (Deloitte, 2021)

In this second group we also need to include those who have shifted their position in the EU conversation over digital tax. A distinct case is Denmark. In 2018, the Finance Ministers of several Nordic countries such as Denmark, Finland, and Sweden released a joint statement indicating that the digital economy should be taxed where value is created. The statement advocated for a consensus-based solution shaped by the OECD, as a result of which rejected the EU DST proposal. (Reuters, 2018) However, in January 2020 the Danish Prime Minister announced Denmark's support to an EU-wide agreement on the DST controversy in case a global consensus was not reached. (Bloomberg, 2020)

We have observed that the decision whether or not to impose DST in EU countries often depends exclusively on the political line of the government in question. In particular, countries with more left-wing governments tend to defend the tax imposed on large digital platforms, while more liberal governments opt to wait for a joint approach supported by the OECD. (KPMG, 2021) For the time being, therefore, the enactment of DST is a political choice driven by particular interests of the administrations in power.

Finally, in the third group we find Portugal, Ireland, the Netherlands, Luxemburg, Germany, the Nordic countries and certain Eastern countries, who have decided to wait for a common solution arranged in global negotiations. We have noted different attitudes among this group. Some, like Germany or the Nordic countries, understand and to a certain extent agree with countries who have already imposed DST, but have preferred to avoid direct conflict with an important trading partner. Instead, they advocate for an integrating solution that satisfies all parties. As an example, while Germany held the EU Presidency from July 2020 to December 2020, tax attaché at the German Embassy in Washington Sandy Radmanesh stated that “Germany will strive to get everybody on board under their presidency for a global agreement, and explore all options to prevent the OECD negotiations from failing.” (Diginomica, 2020)

A third group, such as Ireland or Estonia, assert that the particular features of large digital platforms are already contemplated under the current tax framework. These are tax residencies of many digital platforms that in turn attract others to create a digital hub. Hence, it is in their current interest to maintain the established tax system so as to safeguard their inward investment.

4.2 External conflicts of the European Union

4.2.1 Conflict with the US

In this section we comment on the evolution of the digital tax conflict between the US and the European Union, the underlying reasons of both parties and the general consequences of the dispute.

We will first address the evolution of the conflict. Perhaps the most well-known episode of the digital tax conflict was impersonated by the Trump administration and President Emmanuel Macron from France.

Back in 2018, France aimed to lead a heavy-handed campaign to gather all EU countries behind a common European digital tax proposal, which failed as a result of self-interested motivations of individual countries. As a result, France decided in July 2019 to apply a 3% unilateral tax measure on digital platforms with more than 25 million euros France and 750 million euros worldwide. (Harvard Business Review, 2019)

In response, the US threatened to impose trade tariffs on French Champagne, handbags and other goods on the grounds that the tax unfairly targeted US internet companies, a claim Paris dismissed. (CNBC, 2020)

But the conflict only aggravated the following year. On the 12th of June 2020, US Treasury Secretary Mr. Mnunchin addressed a letter to the finance ministers of France, Italy, Spain, and the UK in which he called upon the OECD to pause negotiations of the digital tax discussion, with a view towards resuming them later on that year. The withdrawal occurred on the basis of US' opposition to unilateral imposition of digital taxes. In his letter, the US Secretary threatened to respond with "appropriate commensurate measures." (KPMG, 2021)

Shortly after, on the 22nd July 2020, the Office of the US Trade Representative (USTR) announced that investigations were being carried out for trading partners of the United States who adopted or were considering to adopt unilateral tax measures. These included the EU, Austria, Czech Republic, Italy, Spain and the UK. (Office of the United States Trade Representative, 2021) Additionally, the institution announced the imposition of additional customs duties of 25% on $1.3 billion of French products imported into the United States. However, these were suspended until the 6th of January, 2021.

On 1st September 2020, the House of Representatives introduced a resolution (H.RES. 1097) expressing strong opposition to the imposition of digital services taxes by other countries that discriminate against US companies.

Since Joe Biden's election on November 2020, there has been further hope to reach an agreement on digital tax that proved to be difficult under the Trump administration.

In fact, at the time of writing, a global tax proposed by his administration is under serious discussion. The new corporate tax would aim to target the world's largest companies with revenues over $20 billion, which would not only affect large digital platforms, but also powerful companies based on "brick-and-mortar" business models. (Politico, 2021) This action moves the discussion away from European countries' discrimination of US digital companies and focuses on large consumer-facing businesses. The proposal has been sent to the OECD and will be considered along with their current independent work on the matter.

However, there have been substantial critics of this proposal. European experts argue that a new corporate tax shifts away from the digital focus and does not fundamentally solve the problem of reforming the OECD transfer pricing framework. Further, some in Europe warn that the Biden administration proposal will still resist imposing a tax exclusively on technology companies, as his approach has always been pro-GAFA. (Voa News, 2020)

More recently, in April 2021, both the Union and the US set the 30th of June as deadline to get a deal over the digital tax issue. It is noticeable that the Biden administration is more open to negotiate. However, the US has not yet returned to the OECD negotiating table of the Global Digital Tax talks.

As the date draws closer, we have witnessed a change of attitude in European counterparties. This may be exemplified through a comment made by EU Commissioner for Internal Market Thierry Breton, who explained that "Europe is not naive anymore in its partnership with the US. (…) If all other countries agree but the United States is unwilling to cooperate, Europe will take its responsibilities and will unilaterally impose a tax". (Politico, 2021)

To fully understand the conflict, we need to find the underlying reasons of the parties.

The US argues the following. The DST and other tax measures proposed by the EU Commission, as well as the language of the EU administration "we aim to maintain our digital sovereignty" back in 2018, (Diginomica, 2020) are viewed as discriminating against US companies.

Some in the US argue that the tax framework should not limit digital platforms' growth by imposing additional taxes. However, not every American institution feels this is a fair approach. In fact, it is important to highlight that even within the US there are different approaches at federal and state level. While US federal tax has argued against separate rules for the digital economy, the individual states have resorted to acting unilaterally in an attempt to solve their digital economy tax problems.

As for the EU perspective, France argued that its digital tax would ensure that the world's technology giants paid the appropriate taxes for transactions even in countries where they have no major physical presence. (Financial Times, 2020) Hence, they do not consider these measures as discriminatory to their partner and argue that it constitutes a matter of fairness and equity.

Even so, it is important to highlight that although the EU has clearly taken a position of leadership in terms of digital policy, there has been a bit of a laggard in tech development. (CNBC, 2020) As a result, some argue that the position of the Union might not have been the same if the technology giants had been European.

We also need to analyse the economic and political reasons of individual EU countries. We find that some countries have not joined France and others in their fight for DST for self-interested reasons. Germany, for instance, resists to damage their car industry. Cars and car parts make up about \$60bn of the \$800bn of goods traded between the US and EU each year. Hence, Germany would be particularly vulnerable to retaliatory measures, as motor vehicles are an important part of their export mix. (Deutsche Bundesbank, 2019)

Low-tax jurisdictions in the Union, such as Ireland and some Nordic countries, agree that a collective approach is the most suitable to tackle digital tax challenges. However, there is no agreement as to assert the amount of an EU digital tax, as they do not want to take an action that would put their export-led economies at a disadvantage.

Further, there is a general sentiment among EU countries of French politicians' tendency to grandstand to their home crowd, which does not make France an ideal candidate to lead the digital tax discussion. (Diginomica, 2020)

The consequences of this conflict are the following. A study made by Politico has estimated that the revenue collected by countries implementing the DST would be limited. (Politico, 2021) The amount would consist on a few billions, which represents a mere rounding error to the trillions of dollars that governments around the world have collectively destinated to COVID-19 recovery funds over the last 12 months. It would represent a substantial amount for large digital platforms, but does not represent a storm they could not weather.

However, the cost of unilateral action may be devastating. The OECD warned that tensions over a digital tax could trigger a trade war that could wipe out one percent of global growth every year. (OECD, 2020) Further, the organisation asserted that "The absence of a consensus-based solution … could lead to a proliferation of unilateral digital services taxes and an increase in damaging tax and trade disputes, which would undermine tax certainty and investment.” (CNBC, 2020)

All in all, we may conclude that further from being an economic conflict, the matter is deeply political. While gains of unilateral measures would be economically insignificant, loses in a trade war might be great.

4.2.2 Conflict with large digital platforms

The EU insists that large digital platforms have been the most benefited during the pandemic. While other businesses suffered economic consequences of lockdowns, digital platforms have emerged more powerful and resilient than before.

The power of large digital platforms is such that they may generate a response and an effect to digital tax measures, being EU consumers the most affected by their actions.

The reasons for the conflict are the following. EU proposals build on the assumption that digital companies should be taxed differently than other firms because their reliance on intangibles allows them to generate an extra value that is currently not contemplated under the current framework. However, as we have been discussing the OECD Report points out that there is no clear consensus on the principle of value creation.

As a result, national politicians and representatives in the Union have asserted that digital companies pay less taxes than traditional businesses. But in fact, digital companies already face comparable levels of tax under corporate taxes. This is shown in the study carried out by the economist Matthias Bauer at the European Centre for International Political Economy, who showed that digital companies have roughly similar tax burdens than other industries. (ECIPE, 2018) (Tax Foundation, 2018)

Nevertheless, the study does confirm that, as a result of tax incentives to invest in R&D, digital companies are granted tax preferences across the Union countries. Hence, it is the Union countries themselves who promote the digitalization of the economy.

The consequences of the conflict are the following. Since the implementation of the DST across various EU countries in mid-2020, there has been a backlash of large digital companies to avoid suffering losses.

Apple announced that it will increase its charges for app developers in Apple Store. However, Apple also said that some of its latest price adjustments were taking place due to changes in VAT rates. (CNBC, 2020)

In August, Amazon also said the company was increasing charges on sellers after the UK government approved its digital tax. Later on in November, Google Ads' fees were updated to reflect the new digital levies in the UK and Austria. (Reuters, 2021)

The digital tax war between the European Union and large digital platforms is to the ultimate detriment of EU consumers. Given that private individuals and organisations increasingly depend on digital platforms, they ultimately have no choice but to pay the additional difference imposed by these platforms.

On the one hand, instead of focusing on where value is generated, EU proposals are based on consumption tax systems that are meant to tax consumption at the place of the buyer. On the other hand, as a consequence of the quasi-monopolistic nature of large digital platforms and the increasing reliance of users on digital products and services, EU users ultimately have no choice but to pay the imposed tax.

4.3 EU path towards tax harmonisation

In this section we briefly consider where the EU is in terms of tax harmonization. We comment on the main obstacles for tax harmonization and the general political discussion around the topic.

The obstacles for tax harmonization are the following. First, a unanimous agreement of all members of the European Council is necessary to adopt any legislative measures in the field of taxation. (Wolters Kluwer, 2019)

Second, national governments are reluctant to lose sovereignty to supranational entities in the area of direct taxation, preferring to maintain the ability to introduce regulatory changes. (Wolters Kluwer, 2019) This grants European countries greater control over their individual territory and the power to make changes to the tax system when economic difficulties arise. It is also a great national political asset, since while some parties favour a minimal tax system, other parties believe that a large tax system benefits the national population.

Third, European tax harmonisation has developed unevenly, with evident progress in the area of indirect taxation (VAT) and rather localized progress in the area of direct taxation. (Wolters Kluwer, 2019) The reason for this is that while indirect taxes are closely linked to trade, direct taxes are more associated with the national tax structure, which in turn is largely linked to political decisions.

As for the political discussion on tax harmonisation, the fundamental problem is that there is a lack of agreement among EU countries as for the amount of a minimum tax base or what it would consist on. In fact, national EU members have different tax systems and different political conceptions regarding what these should or should not cover.

To sum up, European tax harmonisation efforts are limited. The variety of tax regimes within the Union, the defence of these regimes by national governments who do not want to give up their sovereignty, as well as the requirement that any reform must be approved unanimously, have made it very difficult to reach any kind of agreement with regard to taxation in the EU. Yet, there has been remarkable progress in some fields of tax harmonisation, particularly in the area of indirect taxation.

5. Conclusions

In this section we will gather the key points of the discussion and will offer some guidelines as to which should be the appropriate course of action, based on our own reflections on the matter.

First, we will make a brief summary of what has been mentioned in previous chapters.

There is a current lack of global consensus as to how to tax the digital economy. Particularly, there is a worldwide conflict with large digital platforms, which are

American, quasi-monopolistic and highly mobile, who have been strengthened by the effects of the pandemic because of the users' increasing dependence on them.

There are three main areas that are relevant for large digital platforms' business model, namely value creation, data and user participation. The main conflict arises as to where large digital platforms pay their taxes, as their highly mobile nature and reliance on intangibles allows them to have their taxable presence in low-tax jurisdictions. This issue receives the name of BEPS and is a matter subject to constant updates.

Unilateral and inconsistent measures to tax the digital economy are being considered and widely implemented at country level. A consensus-based solution has proved difficult as a result of the pandemic, as it prevented face-to-face meetings and also because the US pulled out of the discussion table at the OECD last June, 2020. Instead, the OECD is now aiming to reach a deal by mid-2021.

Given the economic and political pressures in European Union countries, the European Commission enacted several proposals to respond to national members' needs. As it did not consist on a compulsory joint approach, some countries implemented the digital tax measures unilaterally.

This has occasioned a response from both the US central government and large digital platforms, namely GAFAM, in the form of retaliation or additional tax. As a result, it is European consumers who are most affected by the digital tax conflict.

Further, the sum collected by EU countries is infimal in comparison to the losses that may arise from a trade war, which leads us to believe that the conflict is mainly political.

As for the EU, the European Commission is currently working on a common approach within its territory. If no agreement is reached by mid-June 2021, which is when countries have self-imposed a deadline in the OECD discussion table, the EU will try to implement its own measures. However, the Union is at risk of finding itself divided between those who will implement new digital taxes and those who will refuse to do so.

The most suitable solution in the case of the EU would be the pursuit of a common approach. As we have seen, tax harmonisation within the Union has great obstacles ahead, which are mainly political.

Second, we aim to provide some guidance as to what the EU should do with regard to digital taxation of large platforms.

In a time of trade wars and war against globalization, there is a need to remember the gains from trade. The challenge of international cooperation in a context of distrust and competition has raised the prospect of a possible new Bretton Woods moment for the digital age. (IMF Finance & Development, 2019)

Just as Bretton Woods led nations towards a new monetary order after two world wars, increasing protectionism and the Great Depression, international cooperation on digital issues could also seek consensus around general principles and common institutions to solve problems such as those we have been commenting on, and help create a predictable and open framework for international trade.

With regard to the conflict over taxation of digital platforms, this paper argues in favour of a common taxation system for all countries agreed under the OECD. Ideally, every country in the world would follow the same approach. However, we are aware of the particularities and needs of different nations around the globe. Even so, we find it relevant to maintain a coherent and fair taxation system for the digital economy.

For that reason, we advocate for joint resolution for all EU countries that follows the guidelines of the OECD proposal that will most likely be published by the end of June 2021. Although we have outlined the complications of analysing value creation to date, we believe that further study is needed in order to find a suitable long-term solution. We insist that political demands should not interfere with a common solution that may be beneficial for every country in the long run.

To attain a common approach, we believe that the Union must find a middle ground which considers sensibilities of all countries, without giving in to national political interests that will eventually create an inconsistent tax framework. For that reason, the EC should consider external recommendations and pay special attention to critics such as the ECIPE so as to avoid taxing unfairly, which would eventually compromise European digital companies' growth.

In a worst-case scenario, if no agreement was reached during the OECD discussions, the EU must carefully consider how it aims to proceed as to avoid a trade war that would ultimately affect EU consumers.

In this paper we concur with the view expressed by the Irish finance minister Paschal Donohoe in his interview for CNBC. Donohoe was elected President of the Eurogroup in July 2020, an informal body in which ministers of the euro area Member States discuss matters of common interest relating to economic policy coordination. While we firmly defend the need to change the way we tax the digital economy, we find even more important to preserve international relations after the pandemic, which has hugely affected European Union countries.

We acknowledge that the development of a fair and coherent digital tax system is a long process that will take years to forge, so no immediate solution will be beneficial. Hence, it is necessary to avoid rushed unilateral action that will further destabilize trade and detract economic recovery.

Finally, a common approach within the European Union to tackle digital taxation would be of great benefit. However, there is still work to be done within and outside the EU to achieve this.

The limitations of our study are the following. First, we are currently unaware of the consequences of the usage and monetisation of user data by digital platforms, which compromises users' data privacy. This is a very relevant issue of great concern for the EU, which needs to be addressed and goes hand in hand with the issue of taxation. Second, we have not taken into account the final decision made during the multilateral discussion of digital taxation nor the extensive analysis promised by the OECD, which, if issued, will be published in mid-June 2021. The findings or conclusions of that discussion could give a new perspective to this work.

In line with this final note, we have identified the following legislative developments to find a solution to the digital tax conflict.

First, there is a need to make advancements in the area of value creation and nexus as to be able to reach appropriate and timely innovations for the current tax framework.

Second, given that wholistic tax harmonisation at the EU level seems like a distant goal, a possible solution would be to further enhance the EU Commission's harmonisation proposals such as the Common Consolidated Corporate Tax Base (CCCTB). This proposal might be an answer for the Union members' economic and political demands, as to affect the largest companies operating in Europe.

Third, it would be useful to obtain more information and demand transparency to large digital platforms, as they have access to a large amount of data that can be beneficial to solve this issue. In fact, EU legislators have recently enacted DAC7 in order to increase the standard of tax transparency.

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