PUBLIC SERVICES INTERNATIONAL

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Centre for International Corporate Tax Accountability and Research

SPECIAL BRIEF

SPECIAL BRIEF ENGLISH

Digital Profits Tax

EFFECTIVE TAXATION OF EXCESS PROFITS OF GLOBAL TECH GIANTS: REVENUE FOR RECOVERY & MOMENTUM FOR GLOBAL REFORM

POLITICAL MOMENTUM FOR ACTION

Despite years of promises from the Organisation for Economic Cooperation and Development (OECD) to limit multinational tax avoidance, the growing scale of tax dodging by tech giants such as Google, Amazon, Facebook, Apple and other multinationals has driven public outrage and forced governments to take action. Funding for public health and economic recovery from the coronavirus crisis is urgently needed, and new revenue measures are being considered and implemented across the world.

Ending corporate tax avoidance requires a range of actions including greater transparency, a global minimum tax, a global approach to unitary taxation and taxing excess profits. PSI's eight-part briefing series outlines them in detail (here). A unilateral digital profits tax can be consistent with these broader solutions.

KEY POINT:

TRADE UNIONS SHOULD CALL ON GOVERNMENTS TO:

IMPLEMENT A UNILATERALLY APPLIED DIGITAL PROFITS TAX WHILE CONTINUING TO PURSUE A MULTILATERAL AGREEMENT FOR REFORM OF THE ENTIRE GLOBAL CORPORATE TAX SYSTEM.

Since the pandemic began, public budgets have been squeezed and working people are making immense sacrifices, but the already obscene wealth of tech billionaires has increased dramatically. Jeff Bezos, the CEO of Amazon, has increased his wealth by US$73.2bn in the first six months of the pandemic. Facebook's Mark Zuckerberg has increased his wealth by US$45bn and Google's Larry Page by US$18bn.

Public outrage, combined with COVID related budget pressure, has moved more and more governments to impose, or consider, digital service taxes (DSTs). DSTs directly tax certain revenue streams of large digital companies. The UK and France have both developed DSTs, although France has delayed their implementation after retaliatory trade threats by the US. The European Union may revive its proposed regionwide digital tax if the OECD process fails and many other countries have proposed or implemented DSTs across Europe, Asia, Latin America and Africa. DSTs are a reaction to the failure of multilateral discussions and have gained momentum across the political spectrum. Despite popular appeal, DSTs are limited in scope and only apply to tech giants with global annual revenues above €750m (US$840m) and cover narrow digital revenue streams, such as online advertising. Tax rates range from 2% to 7.5% of selected revenue streams. As a tax on revenue (rather than profit), costs are much more likely to be passed on to consumers and allow global tech giants to continue to flout the obligation to pay tax on profits where they are generated.

SUMMARY

- **The best way to effectively tax the global tech giants is through a multilateral agreement for reform of the entire global corporate tax system.**
- **However, current efforts to achieve this are failing. In response, governments are adopting unilateral approaches, based on directly taxing certain revenue streams (rather than profits) of large digital companies.**
- **Unilateral action is necessary, but these approaches will raise relatively little tax and are not the way forward. Furthermore, they are regressive as costs will be passed onto consumers. They will be difficult to implement, subject to legal challenges and trade retaliation and may undermine political and public support for more fundamental reform in future.**
- **A different form of unilateral action is needed based on countries taxing an allocated proportion of the global profits, dependent on genuine economic activity in each country. A unilaterally applied digital profits tax can achieve this.**

Unfortunately, DSTs are regressive, will raise relatively little tax and move us further away from needed international solutions to effectively tax the excess profits of global tech giants. Poorly designed DSTs could create a false impression that they have ended tax dodging or, alternatively, be used by lobbyists to argue that tax changes are ineffective. This would undermine the public support and political will needed for genuine reforms to ensure that all global corporations pay a fair share.

DIFFERENT SOLUTIONS NEEDED

Tax dodging is not a new problem, nor is it unique to global tech companies. What is really required is comprehensive reform of the tax system that would ensure that multinationals are taxed on global profits. Tax revenues would be allocated to countries based on the location of real economic activity, not artificially shifted to where profits are taxed the least, or not at all, in a destructive race to the bottom. Proposals from the OECD's current 'inclusive framework' discussions, involving nearly 140 countries, take genuine steps in acknowledging multinationals as single entities to be taxed at the global level.

The application of a 'unitary' principle for taxation of multinational profits at the global level is essential. However, current OECD proposals also have significant conceptual and practical flaws and deliver very little revenue - especially to countries which need it most. Additionally, US demands that its corporations, some of which are the largest tax dodgers, are able to opt out has killed the prospect of any meaningful global agreement through the OECD in the near future.

Well designed, unilateral measures to tax global tech companies could increase income for governments to help respond to the immediate crisis and will also increase the pressure on corporations and governments for meaningful global reform. The more countries or regional bodies adopt effective unilateral approaches to taxing global tech giants, the faster a global agreement – and a pathway to broader reforms – will become feasible in the future.

GLOBAL DIGITAL PROFITS TAXES (DPTS)

A BETTER, BROADER, NATIONAL APPROACH

A more effective approach than the current crop of DSTs for achieving increased revenues and pressure for global reform would be for countries to impose a form of digital profits tax. Digital profits taxes are simply taxes on the global profits of a company that allocate a proportion of revenue to individual countries based on actual economic activity in that country. This makes it impossible to avoid tax by shifting profits to tax havens, since they will still be taxed elsewhere, regardless of to where profits are artificially shifted. The percentage of the global profits allocated in each country could depend on different factors including sales, workers, users, data collection and physical assets in that country.

Governments can harness the current momentum behind DSTs to introduce a tax on a portion of global profits allocated to genuine economic activity at the national level. This approach would be more aligned with proposals put forward at the global level, including by the G24 group of countries at the OECD and by India at the UN. Such an approach could ultimately be used for all multinationals, but immediately applied to global tech giants, widely acknowledged to exploit a lack of physical presence to avoid tax where profits are generated. The OECD's definition of automated digital services, which covers a number of business models including the use of social media platforms, online intermediary platforms and online advertising, amongst others, is a possible starting point for determining the inclusion of multinationals within a digital profits tax.

A national allocation of the global profits of multinationals directly tackles the widespread abuse of the current defective and outdated international tax rules, which allows profits to be shifted to where they are taxed the least, or not at all. This would make the widespread abuse of tax havens largely irrelevant, and fully reflects the principle of treating multinationals as single entities and taxing profits where real activities take place, making a strong foundation for longer term global tax reform.

In addition, the use of a digital profits tax would:

• Collect more revenue than DSTs, especially for countries that need it most

• Work within the current tax treaty framework and be less open to trade retaliation

• Be progressive, transparent, simple, fair, and easier to implement for all countries

• Be far less likely to be shifted onto consumers and would level the playing field for all businesses

• Ensure that corporations that do not make profits don't pay taxes – but corporations that make profits are taxed fairly

Minimum tax rates could be applied and progressively increased based on the scale of a multinational's digital platform, monopoly power and global profits. Digital profits taxes would be a fair and transparent way to calculate and collect corporate income tax payments owed by the largest global tech giants.

As public health and government budgets are crippled by the coronavirus crisis, there has never been a better time to push forward with fundamental changes to stop the fastest growing corporations from evading obligations to fund public services.