To the EU Commission – DG TAXUD

Public consultation on Digital Levy: MEDEF's comments

12 April 2021

MEDEF / Transparency Register identification number: 43763731235-75

Dear Sir/Madam,

We very much welcome the opportunity to participate in the public consultation on the Digital Levy and would like to share with you the following comments.

In our view, the main focus should be for the European Union (EU) to foster pro-growth tax policies. Taxation should not hinder EU business' recovery and growth, especially in the aftermath of the economic crisis.

As always, we stand ready to further discuss and explain our views.

Yours sincerely,

Tax Affairs - MEDEF

MEDEF (Mouvement des entreprises de France) is the largest representative business organisation in France, encompassing 173,000 member companies comprising 122 territorial organisations in continental France and in the overseas departments, 77 professional federations bringing together all business sectors (industry, services, construction, trade, etc.) and 14 associated organisations and partners. These represent 10.2 million employees (i.e. more than one-third of all French employees). Over 95 % of member companies are small- and medium-sized enterprises, with an average of 47 employees.[1]

[1] For more information of MEDEF's mandates, actions and membership, please visit our website at https://www.medef.com/en/who-are-we/overview.

General comments and key take-aways

1. The EU should champion pro-growth tax policies which foster competitiveness and the attractivity and economic sovereignty of the EU, while ensuring fair and effective competition in digital markets

One of the six headline ambitions of the European Commission's work program is a « *Europe fit for the digital age* » which includes an update of the new industrial strategy for Europe. Such an ambition implies supporting European digital champions that can compete against their giant competitors from the US and China which dominate the digital markets. The top-priority should be to strengthen the competitiveness of European companies, while not impeding their growth and development. What is at stake here is the EU's attractiveness and economic sovereignty.

It is crucial that tax policies fit within this wider economic agenda and do not hinder the economic growth and the competitiveness of European companies in any way. This is all the more important as we are currently facing an unprecedented economic crisis in recent history with many EU economic sectors struggling to survive. We therefore urge the EU not to rush ahead with a sector-specific tax system that may discriminate against EU businesses conducting tech activities or operating in the Digital field, in an already extremely competitive global industry. It is crucial that the tax rules implemented within the EU remain simple, fair and do not induce distorsions between EU and non-EU players (competitiveness issue).

2. A global agreement on the taxation of the digital economy should be favoured, simple and workable rules should be promoted

We believe that a globally-agreed approach on the reform of international tax rules to address the tax challenges of the digitalisation of the economy should be favoured as a harmonized and coordinated approach is key in order to avoid fragmentation of tax rules, double taxation and legal uncertainty as well as trade tensions.

We are extremely concerned that the Commission's initiative on the EU Digital Levy, as currently envisaged, will bring even more hurdles at a time when all stakeholders should be focusing on a global solution at the OECD. Despite the Commission's statement « *not to undermine the on-going discussions at the OECD, nor to fuel international trade tensions* », we struggle to understand how proposing a unilateral Digital Levy at EU level, at the same time as the expected mid-2021 OECD deadline, would not severely disrupt the international discussions and upset the already difficult negotiations within the OECD. We fear that this will fuel tensions and may lead to retaliation measures (e.g. trade tariffs) at the very moment when a reset of the transatlantic relationship with the United-States is a top-priority, and when positive signals are being voiced by US Secretary Yellen.

Another critical element for EU business is that any new rules relating to the digitalisation of the economy or any digital tax remain simple and workable. The Commission should promote simplification at international level, including in the discussions on Pillar 1 as the envisaged rules have reached overcomplexity in many areas.

3. Policy rationales and objectives of an EU Digital Levy are unclear and are not prioritized

As a preliminary observation, we would like to share our concerns about the policy rationale of the Digital Levy envisaged by the Commission as they lack clarity. As far as we understand, an EU Digital Tax would be justified by a number of different reasons:

- To ensure fairness in taxation: the digital tax aims at addressing the « *issue of fair taxation of the digital economy* ». It is « *of paramount importance to ensure that digital companies contribute their fair share to society, since a prolonged unequal distribution of rights and responsibilities undermines the social contract* »[2]. This « *initiative aims to make digital companies pay their fair contribution (…) as well as affect positively the (perceived) social fairness of the tax system* ».
- To solve ineffective taxation of companies engaging in the digital economy: the Commission mentions a number of concerns which are at the heart of the OECD's reflections on the so-called « Pillar 1» and which are the very reasons why a reform of the international tax system is called for by a number of States and stakeholders.[3]
- To fight against perceived abusive behaviours: one of the policy rationales for a Digital Levy seems to be countering abusive behaviours. For instance, the Commission mentions that "*unequal distribution of rights and responsibilities undermines the social contract* » and that digital companies can « *shift profits to certain jurisdictions more easily* ».
- To sustain public budgets in the midst of the current economic crisis: « *lower taxes, or even no taxes at all, paid by companies engaged in the digital economy weaken the sustainability of public finances. This is particularly blatant at a moment when the EU and Member States are facing a greater fiscal and debt burden as they tackle the COVID-19 crisis and support a recovery* ».[4]
- Own resources agenda: the Digital Levy is part of the « *Roadmap towards the introduction of new own resources* » in the Interinstitutional Agreement of 16 December 2020 between the Parliament, the Council and the Commission.[5] As such, the Commission is due to put forward a proposal on a Digital Levy by June 2021 (effective at the latest by 1 January 2023).

Given the number of different policy rationales that underpin the Commission's initiative for a Digital Levy, which do not appear to be prioritized, we fail to understand which of these is the main driver and whether the ultimate objective may simply be to push the own resources agenda. In our view, this is blurring the policy objectives as each of these policy rationales may call for a different policy response (some of the objectives might even be contradictory with each other).

Importantly, we believe that the Commission fails to explain whether the perceived shortcomings mainly relate to non-EU players and whether there are existing tax distortions between EU and non-

[2] See Inception impact assessment document : A fair & competitive digital economy – digital levy (europa.eu)

[3] Heavy reliance on intangible assets / companies able to generate large revenues by making particular use of and by monetising consumer and user data and user-created content / value created by users not captured by the current tax systems / place of value creation not aligned with the place of taxation / scale without mass and digital businesses not paying corporate taxes where they have a significant economic presence.

[4] See Inception impact assessment document : A fair & competitive digital economy – digital levy (europa.eu)

[5] Interinstitutional Agreement of 16 December 2020 between the Parliament, the Council and the Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management, as well as on new own resources. The Commission intends to accelerate its work and, following impact assessments launched in 2020, put forward proposals on a carbon border adjustment mechanism and on a digital levy as well as an accompanying proposal to introduce new own resources on that basis by June 2021 with a view to their introduction at the latest by 1 January 2023.

EU players in the Digital field. This is a major issue as policy responses may be tailored in a very different way if the main concerns mainly relate to non-EU players (please also see our comments below).

4. Avoid inefficient and counterproductive taxation in the EU

We would like to highlight a number of concerns that an EU Digital Levy raises. We call for the Commission to take these concerns into account when assessing the need and design of such a levy :

- **an EU-wide Digital Levy should not result in double or even multiple taxation for in-scope EU businesses** that already pay their corporate taxes in the EU (in particular while third country competitors would continue to benefit from extremely low corporate tax rates) and should not come « on top » of the OECD's Pillar 1. If an EU Digital Levy were to be adopted, it is crucial that the overall tax contribution of in-scope EU businesses be taken into account. Serious consideration should be given to make the Digital Levy offsetable against corporate income tax and a Pillar 1 liability in the EU Member State where the Digital Levy would be suffered.

- **an EU-wide Digital Levy should not lead to a fragmentation of 27 different taxes** (EU tech companies already face a number of national Digital Service Taxes within the EU, notably in Austria, France, Hungary, Italy and Spain).

- **an EU-wide Digital Levy should not be designed as a mean to « cover » the time period between the OECD's political agreement and its effective implementation,** as this would create major administrative costs and burdens for EU businesses (who would have to set up two tax systems within a short timespan, another source of competitive distorsion *vis-à-vis* third-country competitors). This would also lead to likely disputes with third countries, potential trade tariff retaliation measures, and thus increased uncertainty for businesses.

- **any Digital Levy should focus on taxing operating profits rather than turnover:** taxes that are based on gross revenue are know to be highly detrimental. They impact particularly companies that operate with low profit margins or loss-making companies (which is often the case when companies are in early phases of development). If such revenue-based taxes were considered, we would urge the Commission to consider safe harbour provisions, in order to exclude taxation when the operating margin of the in-scope activity is below a certain level. The structure of taxes on gross revenue also means the burden of the tax most likely falls on in-country consumers.

  For similar reasons, we also caution against any Digital Levy in the form of a taxation of production factors. We understand that the Commission strongly advises against taxes of production factors : we notably note its recommendation to France to remove inefficient taxes and to reduce taxes on production.[6]

- **we are concerned by the Commission's suggestion to tax B2B transactions :** the principle of neutrality is key in the area of indirect taxes and tax systems should be designed so as to avoid taxing business inputs (e.g. like in VAT). If the proposal rather relates to direct taxes, we fear that this would create much complexity in relation to corporate tax rules. Simplicity, neutrality and fairness are guiding principles of the Commission and we would caution against any distortive rule that would unduly target B2B transactions. Corporate taxes already borne by EU business

[6] See the Commission's recommendation nb 4 : https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020SC0509&from=EN).

(including on B2B transactions which are being considered) should be taken into account when assessing the relevance of targeting B2B transactions.

- **We are also concerned about a « top-up tax » approach** which would come « on top » of the corporate income tax liability as far as we understand. As mentioned in our comments in other sections, a number of EU tech companies and EU businesses operating in the Digital field are present across the EU through local affiliates and already pay corporate taxes in this respect. This should be carefully assessed and documented before any policy measure is decided upon. A top-up tax may be incompatible with the EU's aim of a striving EU Digital Single Market and a « *Europe fit for the digital age* », given its damaging impact on investment, workers and consumers. We would also underline that effective tax rates are already expected to rise following an agreement on Pillar 2 that the US administration supports.
- **The scope of an EU Digital Tax should be carefully assesed, SMEs should be excluded:** the scope of any Digital Levy should be carefully assessed as a poorly-tailored tax may entail unintended consequences that may stiffle competition in the digital sector. **We would strongly caution against an extensive scope of a Digital Levy which would include SMEs** and also mid-caps as the burden for them may clearly outweigh the expected benefits. Our current SMEs and mid-caps may become tomorrow's EU Digital champions. Any EU Digital Levy should be carefully designed so that taxation neither overly burdens the activities of EU businesses, not hinders their growth and develpment capacity. The activities in-scope are also a key issue, they should be carefully circumscribed.
- **Need for simple and workable rules :** as highlighted above, it is paramount that an EU Digital Tax be designed as a simple and workable set of rules. The complexity of existing digital taxes (and of the Pillar 1 rules envisaged), should be underlined as this creates challenges for businesses as well as for tax administrations: complexity creates uncertainty, which paves the way for disputes.
- **Cost of an Digital Levy being passed on end-users/final-consumers**: we note that a number of non-EU players have started passing on the cost of certain national digital taxes on end-users/final-consumers and would like to question how this emerging issue would be dealt with by the Commission.

5. Concerns about the public consultation on an EU Digital Levy

We would like to express our concerns about the risk of drawing conclusions before undertaking a thorough public consultation and impact assessment in regard of an EU Digital Levy. In particular, we worry that a number of statements and questions[7] in the public consultation documents may lead to biased responses. We note that there is no quantitative data nor academic research date in these documents to support any of these statements. For example, the Commission states, without providing supporting evidence, that a « *fairer contribution of companies in the digital sector will support the economic recovery* », while ignoring the potential impact of a Digital Levy on investment in the sector. Another example is the statement in the Roadmap - Inception impact assessment document, under « Likely social impacts » : « *The initiative aims to make digital companies pay their fair contribution, and will therefore support revenue generation and help the sustainability of Member States' public finances, as well as affect positively the (perceived) social fairness of the tax ».* [8]

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[7] For example, question 20 of the questionnaire : « *Many digital companies do not pay their fair share of taxes* ».

[8] See A fair & competitive digital economy – digital levy (europa.eu).

We refer to the Commission's « Better Regulation Toolbox » ('Tool 54')[9] whereby public consultation document questionnaires should be "relevant, short and simple and designed in a neutral manner". This is essential for a transparent and balanced public debate.

We also emphasize the need for a robust impact assessment which should notably take into account the current total tax contribution that in-scope EU businesses already bear. With respect to perceived potential abuses by EU digital companies, we note that there is no mention in the public consultation documents of the impact of the recent EU's Anti-Tax Avoidance Directives (ATAD), which have changed the EU's tax landscape considerably. We regret that the Commission may already be questioning their impact at such an early stage. It is crucial that (mis)perceptions be assessed against facts and data.

Finally, as already mentioned earlier, we believe that the public consultation documents fail to present the issue of the potential distorsions between EU and non-EU players, which would be an important element in the public debate.

Annex: additional comments on certain questions of the questionnaire [to be inserted directly in the questionnaire]

Question 22:

We would like to highlight the issue of potential distorsions between EU and non-EU players so that it be taken into account in the public debate and carefully assessed: a number of EU tech companies have chosen to maintain their research and innovation structures within the EU in a context where third country giant competitors attract most of the talent and capital. A number of EU businesses operating in the Digital field also choose to operate though local presence (affiliates in the countries where the end-users are located), one feature that may clearly differentiate them from some other non-EU digital players. This means that corporate taxation may already occur in the right jurisdiction.

Fighting against a perceived under-taxation of a number of non-EU digital players should not end up being detrimental for EU businesses. These businesses may already bear a higher level of taxation, including through a number of DSTs but also due to taxes other than corporate income tax (such as taxes on production factors). It is also noteworthy that EU businesses are subject to the ATAD directives implemented in the EU: we call for the Commission to assess the results of these directives before drawing any conclusions as regards the level of taxation of EU tech companies and EU digital players.

A major challenge for EU business is the proliferation of digital taxes/digital services taxes (or similar taxes) across the EU but also in third countries, including at sub-national level (e.g. State digital taxes in the US). The complexity of such taxes, which are all different, should be underlined as this creates challenges for businesses as well as for tax administrations (complexity creates uncertainty, which paves the way for disputes).

Comments - Question 27:

We would like to emphasize the need for all stakeholders to focus on a global solution at international level and to not disrupt the on-going negociations in view of a political deal in mid-2021.

We note that measures taken by EU countries at national level to tax the digital economy are very recent and it is uneasy to assess their impact at this juncture.

[9] https://ec.europa.eu/info/sites/info/files/file_import/better-regulation-toolbox-54_en_0.pdf