Expert Round Table:

“Online Impact of EU’s Digital Taxation Proposal on European SMEs”

SME Connect, EPP, Brussels, 19 February 2019
What is #FairTaxation?

Domestic digitalised business models are subject to an effective tax rate of only 9%. This is less than half compared to traditional business models facing an effective tax rate of 21%.

We will tackle this issue at the #FairTaxation roundtable today.
The European Commission’s political statement


- “Failure to address these situations will lead to [...] erosion of the social budgets, and it will destabilise the level playing field for businesses.”

- “This puts at risk EU competitiveness, fair taxation and the sustainability of Member States’ budgets.”
European Commission numbers: effective tax rates of hypothetical companies

“The study does not calculate EATRs [Effective Average Corporate Tax Rates] using tax information for actual companies or sectors; more importantly, the study cannot be used to compare the tax burdens of ‘digital’ and ‘traditional’ companies. In interviews with Bloomberg, Law360, and Disco, Prof. Spengel of ZEW made clear that the study does not support conclusions that the digital sector is undertaxed. In summary, the ZEW-PwC study enables a comparison of the relative attractiveness of certain countries’ tax regimes for intangible assets developed through R&D, but does not analyze the effective tax rates of actual enterprises or allow conclusions to be drawn regarding corporate taxes paid by the ‘digital sector’.” (PWC 2018)
Effective tax rates, US-based digital corporations vs. average effective tax rates large EU-based companies

- Spain (IBEX35)
- Germany (DAX30)
- MSCI World Technology
- Alphabet (Google, US-based)
- Facebook (US-based)
- MSCI World Software & Services
- Microsoft (US-based)
- France (CAC40)
- United States (DJIA)
- Italy (MIB40)
- Amazon (US-based)

Corporate tax rate United States (6Y average): 33.9%
Corporate tax rate France (6Y average): 28.7%
Corporate tax rate Italy (6Y average): 29.1%
Corporate tax rate Germany (6Y average): 27.8%
Corporate tax rate Spain (6Y average): 24.6%

Corporate tax rate United States (3Y average): 33.3%
Corporate tax rate France (3Y average): 29.3%
Corporate tax rate Italy (3Y average): 30.3%
Corporate tax rate Germany (3Y average): 28.2%
Corporate tax rate Spain (3Y average): 29.0%

- Effective corporate tax rate, 6Y average for 2012-2017
- Effective corporate tax rate, 3Y average for 2015-2017
## Differences in ECTRs, Renault vs. Alphabet (Google)

<table>
<thead>
<tr>
<th></th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Renault</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pre-tax income</td>
<td>1.96</td>
<td>2.96</td>
<td>3.3</td>
</tr>
<tr>
<td>Fiscal year is January-December. All values in billion EUR. Total income tax</td>
<td>0.366</td>
<td>1.06</td>
<td>0.891</td>
</tr>
<tr>
<td>Income Tax - Current Domestic</td>
<td>0.527</td>
<td>0.728</td>
<td>0.634</td>
</tr>
<tr>
<td>Income Tax - Current Foreign</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income Tax - Deferred Domestic</td>
<td>-0.161</td>
<td>0.327</td>
<td>0.257</td>
</tr>
<tr>
<td>Income Tax - Deferred Foreign</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income Tax Credits</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ECTR total</td>
<td>18.7%</td>
<td>35.8%</td>
<td>27.0%</td>
</tr>
<tr>
<td>3Y average 2015 - 2017, ECTR total</td>
<td>28.2%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ECTR current</td>
<td>26.9%</td>
<td>24.6%</td>
<td>19.2%</td>
</tr>
<tr>
<td>3Y average 2015 - 2017, ECTR current</td>
<td></td>
<td>23.0%</td>
<td></td>
</tr>
<tr>
<td><strong>Alphabet (Google)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pre-tax income</td>
<td>19.65</td>
<td>24.15</td>
<td>27.19</td>
</tr>
<tr>
<td>Total income tax</td>
<td>3.3</td>
<td>4.67</td>
<td>14.53</td>
</tr>
<tr>
<td>Income Tax - Current Domestic</td>
<td>2.84</td>
<td>3.83</td>
<td>12.61</td>
</tr>
<tr>
<td>Income Tax - Current Foreign</td>
<td>0.723</td>
<td>0.966</td>
<td>1.75</td>
</tr>
<tr>
<td>Income Tax - Deferred Domestic</td>
<td>-0.241</td>
<td>-0.07</td>
<td>0.22</td>
</tr>
<tr>
<td>Income Tax - Deferred Foreign</td>
<td>0.017</td>
<td>-0.05</td>
<td>-0.043</td>
</tr>
<tr>
<td>Income Tax Credits</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ECTR total</td>
<td>16.8%</td>
<td>19.3%</td>
<td>53.4%</td>
</tr>
<tr>
<td>3Y average 2015 - 2017, ECTR total</td>
<td>31.7%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ECTR current</td>
<td>18.1%</td>
<td>19.9%</td>
<td>52.8%</td>
</tr>
<tr>
<td>3Y average 2015 - 2017, ECTR current</td>
<td></td>
<td>32.0%</td>
<td></td>
</tr>
</tbody>
</table>
Distribution of effective corporate tax rates, 6Y averages, 2012-2017

France (CAC40; statutory corporate tax rate 2017: 33.3%)

- <10%: 1
- 10%-15%: -
- 15%-20%: 3
- 20%-25%: 10
- 25%-30%: 7
- 30%-35%: 10
- >35%: 5

Germany (DAX30; statutory corporate tax rate 2017: 29.7%)

- <10%: 2
- 10%-15%: 1
- 15%-20%: 2
- 20%-25%: 9
- 25%-30%: 6
- 30%-35%: 5
- >35%: 1

Spain (IBEX35; statutory corporate tax rate 2017: 25%)

- <10%: 1
- 10%-15%: 2
- 15%-20%: 4
- 20%-25%: 4
- 25%-30%: 2
- 30%-35%: 2
- >35%: -

United States (DJIA; statutory corporate tax rate 2017: 40.0%)

- <10%: -
- 10%-15%: 1
- 15%-20%: 1
- 20%-25%: 4
- 25%-30%: 9
- 30%-35%: 7
- >35%: 5
Fairness in the distribution of effective corporate tax rates

France (CAC40; statutory corporate tax rate 2017: 33.3%)

Fair?

<10% 10%-15% 15%-20% 20%-25%
1 3 10

25%-30% 30%-35% >35%
7 10 5

Germany (DAX30; statutory corporate tax rate 2017: 29.7%)

Fair?

<10% 10%-15% 15%-20% 20%-25%
2 1 2

25%-30% 30%-35% >35%
6 5 1

Spain (IBEX35; statutory corporate tax rate 2017: 25%)

Fair?

<10% 10%-15% 15%-20% 20%-25%
1 2 4

25%-30% 30%-35% >35%
4 2 2

United States (DJIA; statutory corporate tax rate 2017: 40.0%)

Fair?

<10% 10%-15% 15%-20% 20%-25%
- 1 1

25%-30% 30%-35% >35%
9 7 5
ECTRs of selected companies headquartered in Large EU Member States vs. large US-based “digital companies”, 2012 – 2017 and 2015 - 2017

**Fa?**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Microsoft, US, (Digital) Technology</td>
<td>28.2%</td>
<td>32.0%</td>
<td>27.7%</td>
<td>24.1%</td>
</tr>
<tr>
<td>Facebook, US, Online Advertisement</td>
<td>26.8%</td>
<td>31.7%</td>
<td>26.8%</td>
<td>24.1%</td>
</tr>
<tr>
<td>Alphabet, US, Online Search and Advertisement</td>
<td>23.2%</td>
<td>21.5%</td>
<td>21.3%</td>
<td>19.9%</td>
</tr>
<tr>
<td>Amazon, US, Technology, Online Retail, Advertisement</td>
<td>17.5%</td>
<td>15.0%</td>
<td>15.0%</td>
<td>13.7%</td>
</tr>
<tr>
<td>International Consolidated Airlines, Spain, Air Transport Services</td>
<td>13.1%</td>
<td>17.5%</td>
<td>17.5%</td>
<td>15.0%</td>
</tr>
<tr>
<td>Bankia, Spain, Banking and Financial Services</td>
<td>12.5%</td>
<td>23.2%</td>
<td>23.2%</td>
<td>21.5%</td>
</tr>
<tr>
<td>Brembo, Italy, Transport Equipment</td>
<td>19.9%</td>
<td>21.5%</td>
<td>20.5%</td>
<td>19.1%</td>
</tr>
<tr>
<td>Volkswagen, Germany, Automobile</td>
<td>14.9%</td>
<td>19.1%</td>
<td>19.1%</td>
<td>18.5%</td>
</tr>
<tr>
<td>Deutsche Telekom, Germany, Telecommunications</td>
<td>14.9%</td>
<td>19.1%</td>
<td>19.1%</td>
<td>18.5%</td>
</tr>
<tr>
<td>Deutsche Post, Germany, Logistics</td>
<td>13.7%</td>
<td>19.5%</td>
<td>19.5%</td>
<td>17.6%</td>
</tr>
<tr>
<td>Valeo, France, Transport Equipment</td>
<td>16.5%</td>
<td>16.5%</td>
<td>16.5%</td>
<td>14.9%</td>
</tr>
<tr>
<td>Renault, France, Automobile</td>
<td>19.5%</td>
<td>18.5%</td>
<td>17.6%</td>
<td>15.0%</td>
</tr>
</tbody>
</table>
Impact on SMEs (impact assessments available for Germany and Spain)

– The majority of the tax cost will be borne by SMEs using digital platforms, i.e. restaurants, brick-and-mortar retailers, online shops
– Increase in the cost of sales and online advertising
– Reduction of margin and the ability to communicate with customers
– Drop in sales, in case of transferring the cost to the price
– Relative reduction in productivity and competitiveness
– Advantage of the offline channel versus the online one, reducing the digitalisation level
Impact on SMEs (impact assessments available for Germany and Spain)

- Distorting tax on the digital infrastructure that businesses (most notably SMEs) rely upon to reach more customers at lower costs
- Individual countries: disadvantage of national digitalised exporters and advantage of foreign exporters over domestic ones
- Less diffusion of digital technologies among European SMEs
- Lower productivity, less entrepreneurship, R&D and innovation (business model innovation; technological innovation)
Tax incidence: Who’s really going to pay?

Companies (GAFA + Uber + AirBnb + ...)

Formally required to pay

Consumers (B2B, B2C, final consumers)

Effectively bearing the burden of the tax

Workers (directly, indirectly, 50-70% of burden)

Owners (shareholders)
Place of headquarter of constituent companies of MSCI World Technology and MSCI World Software and Services indices
Retaliation of third-country governments (US, ...)

The retaliatory trickling-down effect of an EU tax on selected digital services

European Commission and EU Member States (first-mover outside OECD-mediated process)

Introduction of special taxes on imports of selected digital services, as proposed by the European Commission on 21 March 2018

a) a special tax on online advertisement services

b) a special tax on online intermediation services

Retaliating governments of non-EU countries

Introduction of special taxes on imports of selected goods and non-digital services

Physical goods and intermediary products (e.g. cars, chemical products, special machinery, foodstuff and agricultural commodities)

Non-digital services (e.g. business and technical services, legal services, architecture services)
Impact of a 3% tax on gross revenues – Fair?

Corporate tax rate equivalent, in per cent

Level of (pre-tax) corporate profit margin

Source: ECIPE calculations.
Tax code complexity out of control; impact of DST ignored by certain policymakers

– Commission numbers are for “hypothetical” companies, not for real ones
– Survey quoted (and commissioned by?) Paul Tang (S&D): “[t]he most important finding is that over 80 per cent of all citizen in Denmark, Sweden, France, The Netherlands, Germany and Austria (strongly) agree with introducing a tax on tech companies, particularly when confronted with the low level currently paid and the possibilities of tax evasion.” (Kieskompas 2018, p. 3)
– New special taxes on digital services = another complex layer of tax code on an overly complex corporate tax system
– Detrimental to SMEs, consumers and increase of unfairness in taxation
– Corporate tax code effectively out of control of elected lawmakers