Information Technology Industry Council (ITI) Testimony
"France's Digital Service Tax" Docket No. USTR 2019-0009
Submitted by Jennifer McCloskey, Vice President, Policy
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Thank you for the opportunity to testify today in regard to the Section 301 investigation of the digital services tax recently adopted by France. My name is Jennifer McCloskey and I am a Vice President for Policy at the Information Technology Industry Council (ITI) where I oversee both tax and trade issues.

ITI represents the world's leading information and communications technology (ICT) companies. We are the global voice of the tech sector and the premier advocate and thought leader around the world for the ICT industry.

The recent enactment of France's unilateral digital services tax represents a troubling precedent, unnecessarily departs from progress toward stable long-lasting international tax policies and may disproportionately impact U.S.-headquartered companies. While we support the United States Trade Representative's (USTR) efforts to fully investigate the trade implications of France's unilateral action, our ultimate goal is an outcome in which all parties remain committed to a multilateral solution on appropriate international tax reforms. We encourage countries to work together to achieve workable solutions and we offer our comments in that spirit.

France is the first jurisdiction to enact a digital services tax, which, for these purposes, refers to a retroactive, gross-revenue based tax on a narrowly defined set of digital services. However, similar policies have been in discussion for some time, particularly in the European Union, where numerous member states have proposed or are considering similar unilateral measures. The European Commission proposed a digital services tax last year which was not agreed by European Finance Ministers. The French policy borrows heavily in scope and design from that effort. As we have shared with the French government, the European Union and other policymakers contemplating such measures, each of these approaches share concerning characteristics.

Section 301 defines "discriminatory" to include any act, policy and practice which denies national or most-favored nation treatment to U.S. goods, services or investment, and an "unreasonable" act, policy, or practice as one that is otherwise unfair and inequitable. The French digital services tax appears to meet both of these standards.

In response to the questions contained in the Federal Register notice, we would flag several key concerns with the French measure.

First, the limited range of business activities in scope raises questions around both selectivity and policy rationale. France argues that its digital services tax is consistent with the principle that tax should be applied where value is created because customers of digital companies participate in the

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creation of value. Even if one were to accept this premise, the narrow focus on a subset of digital companies appears to be designed to single out just a small number of companies – and a fraction of business models – despite the fact that all businesses derive value from their customers. Revenue thresholds do not have any bearing on the extent to which a company derives value from user participation. In short, there does not appear to be a legitimate, principled basis for drawing these distinctions in the French measure.

Second, as suggested earlier, the French tax includes two revenue thresholds that operate to limit the scope to a small subset of the largest highly digitized companies. Indeed, analysis underpinning the European Commission's proposed digital services tax, which served as a template for the French measure, suggests that revenue thresholds set by the law minimize impact on European firms while limiting government exposure to claims of selectivity.

Language used by French policymakers in advancing this measure puts a finer point on political intent. The tax has been widely referred to as the "GAFA" tax, which stands for Google, Apple, Facebook and Amazon. Key officials have remarked that "It's time for these companies to pay the taxes they owe[1]," and that the tax "should not sanction the European actors[2]."

A key assertion underpinning the policy rationale for France's and other unilateral tax measures is that certain companies are not paying their fair share in taxes. We recognize that international tax rules need updating to address widespread digitalization and the changes it has wrought. However, there are significant issues with these assertions. All companies currently operate under an agreed-upon, longstanding policy framework where tax is applied using an established set of rules dictating where value is created. The predictability afforded by this system has supported the ability of companies to conduct business globally for decades.

Beyond the fact that the digital services tax based on revenue challenges longstanding international income taxation principles, it could also disproportionately target low-margin, high-investment business models. Given its design, there is a high likelihood that the cost of the tax will be passed down the supply chain. The business models targeted, which provide key digital services, have enabled significant growth, including through the provision of free-of-charge services to consumers, increases in productivity, and the expansion of markets for thousands of small and medium-sized businesses. In this regard, the French tax – and similar digital services taxes – could greatly impact many businesses outside the 30 companies in scope.

Further, the propagation of unilateral digital tax proposals raises broader concerns around global fragmentation in the tax space. The imposition of individual country, gross revenue-based measures targeting different subsets of the "digital economy" will give rise to a complex and convoluted patchwork approach to international taxation. Such digital taxes will also set a problematic precedent for the ability of governments to single out specific sectors, and even specific business models – whether deemed digital or non-digital – for the purposes of taxation. As today's hearing suggests,

[1] Alderman, Liz. "France, Not Waiting for European Union, to Tax U.S. Tech Firms as '19 Starts", New York Times, New York. December 18, 2018.
[2] Pommiers, Eléa. "Taxation des GAFA: la France peut-elle faire cavalier seul?", l'Express, Paris. Jan. 3, 2019.

these features in turn raise significant concerns in the context of global trade relations and existing international agreements.

For those businesses directly in scope, there are also substantial administrative burdens resulting both in terms of compliance costs and a heightened degree of uncertainty. Companies will need to engage in significant re-engineering of their internal business and financial reporting systems to ensure that they can accurately capture required information and comply with the digital services tax. Companies will also need to include new filing and audit components on French accounts. We estimate associated costs to be in the millions for those in scope. Further, there will be very high audit uncertainty, which will lead to additional disputes and subsequent costs.

Throughout our engagement on this issue, policymakers have largely conceded that digital services taxes are imperfect solutions to address outdated rules governing the international tax system. We agree that these issues must be identified, and countries need to work together to negotiate agreeable changes to the international tax system that is income tax based, treaty compliant, fosters economic growth and investment, minimizes double taxation, and does not discriminate against any particular industry or business. Fortunately, that effort is underway at the Organisation for Economic Co-operation and Development (OECD), where the United States, France and more than 130 other nations in the Inclusive Framework are working to reach consensus on workable reform of the international tax system. That is the proper forum to address these issues and ITI supports this multilateral approach.

Today's hearing is about more than the French digital services tax. It is about preventing widescale application of unilateral excise taxes. The United States should continue to lead on a consensus-based approach to address the tax and trade angles to increasing digitalization of the global economy. We support the U.S. government's efforts to investigate these complex trade issues but urge it to pursue the 301 investigation in a spirit of international cooperation and without using tariffs as a remedy. We also again call on France and other countries considering unilateral actions to withdraw individual measures and recommit to the ongoing, multilateral OECD process.

Thank you for your time. We appreciate USTR's efforts in identifying these trends early and reviewing through a more critical lens. We look forward to answering any follow up questions you may have.