It’s Déjà Vu All Over Again* — the U.S. Section 301 Investigation Targeting Digital Services Tax Efforts (Internet Tax Measures)

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On Friday, June 5, the Office of the U.S. Trade Representative (USTR) started another Section 301 investigation.[1] Section 301 is the same process that ultimately added tariffs against virtually all goods imported from China because of the theft of U.S. intellectual property.[2] It is also the tool used to add tariffs against many goods from Europe because of subsidies given Airbus, Boeing’s European competitor in the large civil aircraft market.[3] This time the U.S. is targeting tax measures proposed or implemented against U.S. technology firms, called a Digital Services Tax (DST).

USTR’s focus is on DST measures proposed or implemented in Austria, Brazil, the Czech Republic, the European Union, India, Indonesia, Italy, Spain, Turkey, and the United Kingdom. This relates to the spat last year between the U.S. and France, which was stayed until the end of 2020, pending completion of the Organization of Economic Cooperation and Development’s (OECD’s) work program called the BEPS 2.0 initiative.

It is unclear how COVID-19 will affect the BEPS 2.0 efforts to reach consensus. If it delays the project past 2020, France is teed up to levy a 3% tax against the likes of Google, Apple, Facebook, and Amazon (the “Gafa” entities, as France calls them). The countries named in this investigation are similarly exploring DST measures. Concerned about the unilateral imposition of DST measures against U.S. technology firms, the U.S. initiated the Section 301 investigation. USTR is accepting written comments, which must be submitted electronically and are due by July 15, 2020.

The DST Background

The OECD

Tax challenges arising from digitalization and cross-border issues surrounding perceived fairness in taxation are not new.[4] In 2013, the OECD started its Base Erosion and Profit Shifting (BEPS) project.[5] The BEPS project “motivated the adoption” of several anti-tax avoidance measures,[6] such as controlled foreign corporation (CFC) rules,[7] patent box nexus rules,[8] thin-capitalization rules,[9] transfer pricing regulations,[10] and cross-country reporting requirements.[11] In May 2019, the OECD released its work program to address challenges posed by digitalization.[12] Now referred to as “BEPS 2.0,” the expanded project has two pillars—(1) addressing the tax challenges of the digitalization of the economy (Pillar 1), and (2) addressing tax avoidance through a global minimum tax (Pillar 2).[13]

The French Measure

In 2019, around the time that the OECD was finalizing its work program on BEPS 2.0, France introduced a domestic digital services tax, the goal of which is to limit the ability of U.S. technology giants to avoid taxes.[14] The French legislation imposes a 3% levy directed at those companies with digital revenues of more than €750 million worldwide and €25 million in France, which includes those connecting customers and producers, retailers, or service providers, as well as advertising and the resale of personal data for advertising purposes.[15] Think Google, Apple, Facebook, and Amazon (Gafa). French legislators certainly did, openly calling it the "Gafa" tax.[16] The U.S. response was to launch a Section 301 investigation.[17] In January 2020, after threats of tariffs on sacrosanct French cheese and champagne,[18] Presidents Macron and Trump agreed to a détente.[19] The rapprochement is simple: France delays further collections until the end of 2020, pending the results of the BEPS 2.0 process. In turn, the U.S. holds off on additional tariffs.

COVID-19

With BEPS 2.0, as with most things, timing is everything.[20] Announced January 21, 2020, the U.S.-French agreement was a temporary truce that permitted the OECD to continue work on BEPS 2.0.[21] It is not surprising that less than ten days later the OECD "members reaffirm[ed] their commitment to bridge the remaining differences and reach agreement on a consensus-based solution by the end of 2020, noting that this agreement will depend on the further concurrent work that will be carried out on the two pillars. An important step will be its next meeting in early July, at which it is intended to reach agreement on the key policy features of the solution that would form the basis for a political agreement."[22] Then enter COVID-19. The world stops, and it is unclear whether the OECD will be able to finish its work on time. But with the toll on enforcement of the French legislation set to expire at the end of the year, the USTR is not waiting,[23] particularly as other countries are considering their own DST measures.[24] For instance, the day before USTR's DST 301 Notice, reportedly both Spain and Chile moved forward with DST measures.[25]

The Section 301 Investigation

Which Countries Are Affected

The USTR is focusing on the DST measures adopted or under consideration by Austria,[26] Brazil,[27] the Czech Republic,[28] the European Union,[29] India,[30] Indonesia,[31] Italy,[32] Spain,[33] Turkey,[34] and the United Kingdom.[35] It started the investigation to determine whether the policies adopted or under consideration by these countries are unreasonable or discriminatory and burden or restrict U.S. commerce. If it determines that any such policy is unfair and inequitable to U.S. companies—which the USTR found the French measure to be[36]—the USTR must determine what action to take, which likely will be additional tariffs on products from that particular country.

What the USTR Is Investigating

The investigation initially will focus on the following concerns with DSTs: discrimination against U.S. companies; retroactivity; and possibly unreasonable tax policy. With respect to tax policy, the DSTs may diverge from norms reflected in the U.S. tax system and the international tax system in several respects. These departures may include extraterritoriality; taxing revenue not income; and a purpose of penalizing particular technology companies for their commercial success. In addition to these areas of concern with DSTs, the USTR is inviting comments on any other aspect that may warrant a finding that one or more of the covered DSTs are actionable under Section 301.

How to Influence the Investigation

The USTR is accepting written comments, which must be submitted electronically and are due by July 15, 2020. In particular, the USTR invites comments with respect to:

- Concerns with one or more of the DSTs adopted or under consideration by the jurisdictions covered in these investigations;
- Whether one or more of the covered DSTs is unreasonable or discriminatory;
- The extent to which one or more of the covered DSTs burdens or restricts U.S. commerce;
- Whether one or more of the covered DSTs is inconsistent with obligations under the WTO Agreement or any other international agreement; and
- The determinations required under section 304 of the Trade Act, including what action, if any, should be taken.[37]

Given continued public health concerns arising from COVID-19, the USTR does not plan to have a public hearing regarding these investigations. If that changes, the USTR will issue another notice.

Who Should Care

If you are a U.S. technology company affected by the DST measures; a U.S. company competing with imports from Brazil, the Czech Republic, the European Union, India, Indonesia, Turkey, or the United Kingdom; or a company (U.S. or foreign) that imports or exports goods to the United States that are manufactured in a country whose DST measures are being examined, you should pay close attention to the Section 301 investigation and consider strongly whether to submit written comments.

Venable International Tax Alert Forthcoming

In the near future, Venable's International Tax Team plans to publish a client alert or article that explains how DSTs work, explores the issues multinational enterprises should be considering, and focuses on the jurisdictions considering and implementing such tax regimes. Given the game-changing aspect of DSTs—that they are a gross tax similar to a VAT/GST—it is expected that this will have a substantial impact on how technology companies will launch their go-to-market strategies. Given the substantial movement of DST measures in various jurisdictions and the impact of COVID-19 of delaying the OECD's work on BEPS 2.0, that work plan may be secondary and have a very different impact than BEPS 1.0, where the OECD led the charge. Stay tuned for more DST guidance and insight.

In the interim, please contact us if you need help submitting written comments to the Section 301 investigation or have any questions.

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[*] The phrase is attributed to Yogi Berra. See Listing of "Yogi-isms"—the unique and witty observations Mr. Berra became famous for which became etched into the American language—at the Yogi Berra Museum and Learning Center, available at: https://yogiberramuseum.org/about-yogi/yogisms/.

[1] Initiation of Section 301 Investigations of Digital Services Taxes, 85 *Fed. Reg*. 34709 (June 5, 2020) (DST 301 Notice), available at https://www.govinfo.gov/content/pkg/FR-2020-06-05/pdf/2020-12216.pdf.

[2] Notice of Determination and Request for Public Comment Concerning Proposed Determination of Action Pursuant to Section 301: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation, 83 *Fed. Reg*. 14906 (April 6, 2018) (List 1), available at https://www.govinfo.gov/content/pkg/FR-2018-04-06/pdf/2018-07119.pdf; Notice of Action and Request for Public Comment Concerning Proposed Determination of Action Pursuant to Section 301: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation, 83 *Fed. Reg*. 28710 (June 20, 2018) (List 2), available at https://ustr.gov/sites/default/files/2018-13248.pdf; Request for Comments Concerning Proposed Modification of Action Pursuant to Section 301: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation, 83 *Fed. Reg*. 33608 (July 17, 2018) (List 3), available at https://www.govinfo.gov/content/pkg/FR-2018-07-17/pdf/2018-15090.pdf; and Request for Comments Concerning Proposed Modification of Action Pursuant to Section 301: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation, 84 *Fed. Reg*. 22564 (May 17, 2019) (List 4), available at https://ustr.gov/sites/default/files/enforcement/301Investigations/84_FR_22564.pdf.

[3] Initiation of Investigation; Notice of Hearing and Request for Public, Comments: Enforcement of U.S. WTO Rights in Large Civil Aircraft Dispute, 84 *Fed. Reg*. 15028-29 (April 12, 2019) ("In order to enforce U.S. WTO rights in connection with the *Large Civil Aircraft* dispute, the Trade Representative is initiating a section 301 investigation of the subsidies provided by the EU and certain member States on the manufacture of large civil aircraft."), available at https://www.govinfo.gov/content/pkg/FR-2019-04-12/pdf/2019-07267.pdf.

[4] Action 1: Tax Challenges Arising from Digitalisation, OECD, available at https://www.oecd.org/tax/beps/beps-actions/action1/.

[5] *See* Action Plan on Base Erosion and Profit Shifting, OECD (2013) (describes multilateral process to review and address multinational businesses using tax planning practices to pay very low or no tax on income), available at https://www.oecd.org/ctp/BEPSActionPlan.pdf.

[6] Elke Asen, What is the OECD BEPS project and what is its main objective? *Tax Foundation* (January 30, 2020), available at https://taxfoundation.org/oecd-beps-digital-tax/#11.

[7] Action 3: Controlled Foreign Company, OECD, available at http://www.oecd.org/tax/beps/beps-actions/action3/ (responding to the risk that taxpayers can strip the tax base of their country of residence by shifting income into a foreign company that is controlled by the taxpayer).

[8] Action 5: Harmful Tax Practices, OECD, available at http://www.oecd.org/tax/beps/beps-actions/action5/; *see also,* e.g., Harmful Tax Practices—2018 Progress Report on Preferential Regimes, OECD (January 29, 2019), available at https://www.oecd-ilibrary.org/docserver/9789264311480-en.pdf?expires=1591554344&id=id&accname=guest&checksum=1FF96B8810C2CBF1D93300A3B52C5056.

[9] Action 4: Limitation on Interest Deductions, OECD, available at http://www.oecd.org/tax/beps/beps-actions/action4/.

[10] Action 8-10: Transfer Pricing, OECD, available at http://www.oecd.org/tax/beps/beps-actions/action8-10/.

[11] Action 13: Country-By-Country Reporting, OECD, available at http://www.oecd.org/tax/beps/beps-actions/action13/.

[12] Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy, OECD (May 28-29, 2019), available at https://www.oecd.org/tax/beps/programme-of-work-to-develop-a-consensus-solution-to-the-tax-challenges-arising-from-the-digitalisation-of-the-economy.pdf.

[13] *See,* e.g., Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy, OECD/G20 Base Erosion and Profit Shifting Project Statement by the OECD/G20 (as approved on January 29-30, 2020), available at https://www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-beps-january-2020.pdf.

[14] France agrees to delay new tax on tech giants, *BBC News* (January 21, 2020), available at https://www.bbc.com/news/business-51192369.

[15] Liz Alderman, France Moves to Tax Tech Giants, Stoking Fight With White House, *New York Times* (July 11, 2019), available at https://www.nytimes.com/2019/07/11/business/france-digital-tax-tech-giants.html.

[16] France Hits Back at US Over Tax On Digital Giants, *The Guardian* (July 11, 2019), available at https://www.theguardian.com/world/2019/jul/11/france-us-tax-big-digital-companies-donald-trump-amazon-facebook.

[17] Initiation of a Section 301 Investigation of France's Digital Services Tax, 84 *Fed. Reg*. 34042 (July 16, 2009), available at https://www.govinfo.gov/content/pkg/FR-2019-07-16/pdf/2019-15081.pdf. ("On March 6, 2019, the Government of France released a proposal for a 3% levy on revenues that certain companies generate from providing certain digital services to, or aimed at, French users (the Digital Services Tax, or the DST). On June 26, a joint committee of the two houses of the French Parliament agreed to a joint committee DST bill. On July 4, the French National Assembly passed the DST bill. The French Senate is expected to take up the bill on July 11."). The bill was signed by President Macron on July 24, 2019, and published in the official gazette on July 25, 2019.

[18] Notice of Determination and Request for Comments Concerning Action Pursuant to Section 301: France's Digital Services Tax, 84 *Fed. Reg*. 66956 (December 6, 2019) (proposing additional duties of up to 100 percent "to be drawn from the preliminary list in the Annex to this notice"), available at https://www.govinfo.gov/content/pkg/FR-2019-12-06/pdf/2019-26325.pdf.

[19] France agrees to delay new tax on tech giants, *BBC News* (January 21, 2020) ("Payments were already collected in November for 2019 on revenues from July. Those are still subject to final adjustments but will not be refunded under this agreement."), available at https://www.bbc.com/news/business-51192369.

[20] Robert Goulder, Overtaken by Events: Should the OECD Delay Taxing the Digital Economy? *Forbes* (April 22, 2020), available at https://www.forbes.com/sites/taxnotes/2020/04/22/overtaken-by-events-should-the-oecd-delay-taxing-the-digital-economy/#65462ae7613d.

[21] Liz Alderman, Jim Tankersley, and Ana Swanson, France and U.S. Move Toward Temporary Truce in Trade War, *New York Times* (January 21, 2020) ("A deal between the two countries would buy time for the development of an international framework Negotiations are continuing at

the [OECD], but the slow pace of the talks has frustrated European officials — and especially the French government, which has insisted that digital businesses must pay "fair taxes."), available at https://www.nytimes.com/2020/01/21/business/france-US-digital-tax.html.

[22] Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy, OECD/G20 Base Erosion and Profit Shifting Project Statement by the OECD/G20 (as approved on January 29-30, 2020) at 5, available at https://www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-beps-january-2020.pdf.

[23] Josh Zumbrun, U.S. Weighs Tariffs Against Nations Seeking to Tax Internet Firms, *Wall Street Journal* (June 2, 2020).

[24] *See* DST 301 Notice at 34709 ("Over the past two years, various jurisdictions have taken under consideration or adopted [DST] taxes"); *see also* Letter from the U.S. Department of the Treasury to the U.S. Senate Finance Committee, July 11, 2019 ("If France unilaterally adopts a DST and the United States does not respond, other countries may impose similar unilateral measures"), available at https://www.finance.senate.gov/imo/media/doc/7.11.19%20-%20Chairman%20Grassley%20-%20DST.pdf.

[25] Sam Edward, Spain Moves Forward with Digital Tax Despite U.S. Tariff Threat, *Daily Tax Report*, Bureau of National Affairs, Inc. (June 4, 2020); Tom Azzopardi, Chile Launches Digital Tax Despite Concerns From Mastercard (2), *Daily Tax Report*, Bureau of National Affairs, Inc. (June 4, 2020).

[26] DST 301 Notice at 34709-710 ("In October 2019, Austria adopted a DST that applies a 5% tax to revenues from online advertising services. The law went into force on January 1, 2020. The tax applies only to companies with at least €750 million in annual global revenues for all services and €25 million in in-country revenues for covered digital services.").

[27] DST 301 Notice at 34710 ("Brazil is considering a legislative proposal entitled the 'Contribution for Intervention in the Economic Domain' or CIDE. If adopted, CIDE would apply to the gross revenue derived from digital services provided by large technology companies.").

[28] DST 301 Notice at 34710 ("The Parliament of the Czech Republic is considering a draft law that would apply a 7% DST to revenues from targeted advertising and digital interface services. The tax would apply only to companies generating €750 million in annual global revenues for all services and CZK 50 million in in-country revenues for covered digital services.").

[29] DST 301 Notice at 34710 ("The European Commission is considering a DST as part of the financing package for its proposed COVID-19 recovery plan. The EU DST is based on a 2018 DST proposal that was not adopted. The 2018 EU proposal included a 3% tax on revenues from targeted advertising and digital interface services, and would have applied only to companies generating at least €750 million in global revenues from covered digital services and at least €50 million in EU-wide revenues for covered digital services.").

[30] DST 301 Notice at 34710 ("In March 2020, India adopted a 2% DST. The tax applies only to non-resident companies, and covers online sales of goods and services to, or aimed at, persons in India. The tax applies only to companies with annual revenues in excess of approximately Rs. 20 million (approximately U.S. $267,000). The tax went into effect on April 1, 2020.").

[31] DST 301 Notice at 34710 ("Earlier this year, Indonesia adopted an electronic transaction tax that targets cross-border, digital transactions. Further implementing measures are required for the new tax to go into effect.").

[32] DST 301 Notice at 34710 ("Italy has adopted a DST. The measure includes a 3% tax on revenues from targeted advertising and digital interface services. This tax applies only to companies generating at least €750 million in global revenues for all services and €5.5 million in in-country revenues for covered digital services. The tax applies as of January 1, 2020.").

[33] DST 301 Notice at 34710 ("Spain is considering a draft DST. The measure would apply a 3% tax to revenues from targeted advertising and digital interface services. This tax would apply only to companies generating at least €750 million in global revenues for all services and €3 million in in-country revenues for covered digital services.").

[34] DST Notice at 34710 ("Turkey has adopted a DST. The measure applies a 7.5% tax to revenues from targeted advertising, social media and digital interface services. The tax applies only to companies generating €750 million in global revenues from covered digital services and TL20 million in in-country revenues from covered digital services. The Turkish President has authority to increase the tax rate up to 15%. The law went into effect on March 1, 2020.").

[35] DST Notice at 34710 ("The United Kingdom is considering a DST proposal as part of its Finance Bill 2020. The measure would apply a 2% tax on revenues above £25 million to internet search engines, social media, and online marketplaces. The tax applies only to companies generating at least £500 million in global revenues from covered digital services and £25 million in in-country revenues from covered digital services. The bill is in the final stages of adoption by Parliament, and if passed, payments would be due from affected companies in 2021.").

[36] Notice of Determination and Request for Comments Concerning Action Pursuant to Section 301: France's Digital Services Tax, 84 *Fed. Reg*. 66956, 66957 (December 6, 2019) (proposing additional duties of up to 100 percent "to be drawn from the preliminary list in the Annex to this notice"), available at https://www.govinfo.gov/content/pkg/FR-2019-12-06/pdf/2019-26325.pdf. ("The act, policy, or practice covered in the investigation, namely the French DST, is unreasonable or discriminatory and burdens or restricts U.S. commerce.").

[37] *See* 19 U.S.C. § 2411 (2020) (Actions by United States Trade Representative).