CLIENT ALERT

Digital Services Taxes in UK and France

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2019 has seen considerable focus on the taxation of the digitalised economy. Recent OECD proposals - the pillar one "unified approach" to profit allocation and nexus and introduction under pillar two of a globally-agreed minimum standard on direct tax matters – has the potential to fundamentally alter the international tax regime.

Building towards a consensus on the pillar one and pillar two OECD proposals is a significant challenge. Pending this, an increasing number of countries are taking unilateral action. This continues to attract attention. Just recently, the Trump administration made headlines by proposing the imposition of 100% tariffs on French cheese and champagne, in response to the recently introduced French digital services tax ("**DST**") that it considers is unfairly discriminating against American-headed multinational technology companies. The UK has also adopted a DST to take effect from April 2020. This has not, as yet, attracted quite the same criticism from the US. Boris Johnson has reaffirmed his commitment to this, but it remains to be seen whether, depending on the outcome of the UK election, this could be a bargaining chip in US/UK trade negotiations in a post-Brexit UK.

Ed Denny and **Bertrand Dussert** consider and compare both the UK and French proposals below. Ed and Bertrand both joined the Winston & Strawn global tax team in 2019 as partners based in London and Paris.

<u>The underlying issue</u>

Broadly, the issue relates to an observation, identified by the OECD in its 2015 BEPS Action 1 report, that current profit allocation rules, which focus on the right for countries to tax an enterprise where this has a physical presence in their jurisdiction, are ill-suited to a modern digitalised economy. This has led to a concern that multinational enterprises are increasingly able to shift profits to low or no tax jurisdictions.

In 2018, the European Union conceptualised an interim solution that would see a 3% DST applied on revenues derived from the sale of advertising space, digital intermediary activities such as online market places, and sales of user collected data.

Consistent with this type of approach, the pillar one proposals from the OECD focus on all "consumer-facing businesses" (not just "digital" businesses) and would broadly allocate more taxing rights to market jurisdictions, where customers and users are based. If a multinational enterprise "has a sustained and significant involvement in the economy of a market jurisdiction", for example through consumer interaction and engagement, this may be sufficient to establish taxable nexus without a physical presence. Once a relevant nexus has been established (whether physical or by virtue of significant involvement), the rules would rewrite the profit allocation rules to determine how the profits of multinational enterprises should be allocated to different countries.

The outlines of a unified global approach, based on these proposals and the corresponding consultation, are expected by January 2020.

Interim solutions in the UK and France

In the absence of immediate measures taxing digital services at an international level, countries such as the UK and France have adopted unilateral tax measures, which are expected to be revoked upon emergence of international consensus.

An overview of each DST's main features is set out below:

	UK	FRANCE
Date of effect	Affecting all qualifying revenue earned from 1 April 2020. Subject to review by the UK government in 2025 (there is no formal mechanism that effects revocation upon international agreement)	Application from July 2019, with retrospective effect to apply to all digital services revenue as of 1 January 2019. To apply until international agreement reached.
Tax rate	**2%**	**3%**
Affected enterprises – business activities that are in scope	Specific digital business models whose revenue is linked to the participation of UK users. This includes: 1. **search engines**; 2. **social media platforms**; 3. **online marketplaces**; and 4. any **associated online advertising** business.	Digital activities in which French users are involved in value creation. This includes: 1. **Intermediary services** – sums paid by users of an interface for the purposes of access to/use thereof. Permits users to interact with each other, mainly for the purpose of exchanging goods/services. 2. **Advertising services based on users' data** – sale of advertising space and digital data.

	UK	FRANCE
Excluded types of business / activity	Financial and payment services providers do not fall within the definition of online market places. The tax is not on online sale of goods, but rather the revenue earned from the action of intermediating sales.	Banking and financial services are not included, nor are services provided between related entities. Intermediary services do not include services only used to provide digital content, communication services, interfaces to enable the purchase or sale of services aimed at advertising, or payment services.
Size restrictions	1. Minimum £500million (US$ 469.7million) **global turnover** of corporate group from relevant digital activities; and 2. More than £25million (US$ 23.5million) of these revenues are **derived from UK users**.	1. **Worldwide revenues** of minimum €750million (US$ 826.7million) at consolidated group level; and 2. **French qualifying revenues** of at least €25million (US$ 27.6million at consolidated group level.
Relevant tax base	Revenues	Revenues
Relevant revenues	Revenues of in scope activities which derive value from UK users, as a result of these using the relevant platform. Participation of a UK user depends on the activity: 1. online marketplace transactions – if at least one of the parties is UK based; 2. advertising revenues – where the advert is intended for UK audiences. Includes any revenues earned by the corporate group, which are connected to the relevant business activity.	Revenues generated by relevant services which are deemed to be made, or supplied in France. The portion of revenues attributable to France is calculated by taking a percentage of worldwide revenues from qualifying digital service activities, based on the number of French users. This includes users located in France and accounts allowing access to the services which were opened in France.

	UK	FRANCE
Interaction with other taxes	Deductible from corporate income tax where qualifies as an expense.	Deductible from corporate income tax
Other significant features	The first £25million of revenues derived from UK users are not taxable. Reduced tax liability where the user is normally located in a country that operates a similar tax. Relief for low-margin businesses.	Due on 31 December of each year, but two advance payments fall due which must be at least equal to the amount of tax due the previous year. Different rules applied for 2019.

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