

COMBATting BASE EROSION AND PROFIT SHIFTING: IS A DIGITAL SERVICE TAX ON REVENUE THE RIGHT PATH TOWARD EQUITABLE INTERNATIONAL TAXATION?

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I. INTRODUCTION

Social media and digital platforms have increased the interconnectedness of the world by allowing for a level of communication unseen before, but it has exacerbated a variety of societal problems. Everything from unfair taxation practices and promotion of gambling in children¹ to creation of black markets for stolen relics has been increased by digital platforms.² This note seeks to first shed light on the issues surrounding base erosion and profit shifting and subsequently advocate for the recognition of “user created value” to combat it. Base erosion and profit shifting allow large tech companies to pay little to nothing in taxes in countries where they conduct business.

Base erosion and profit shifting are tax planning strategies that exploit gaps in tax rules.³ These strategies allow businesses that operate in multiple countries the ability to shift their profits from high-tax jurisdictions to low-tax jurisdictions.⁴ Essentially, a company like Facebook will keep their labor in a high tax jurisdiction like the United States but move all of their profitable intellectual property to a low tax country like Ireland. Effectively, the higher U.S. payroll tax is countered by the lower tax rate of the profits from the intellectual property and allows Facebook to pay virtually nothing in either jurisdiction. This is a simplified version of the problem, but it highlights the main issues.

Every year, base erosion and profit shifting costs countries between \$100 to \$240 billion in lost revenue.⁵ Multinational Companies (MNCs) like Google, Amazon, Facebook, and Apple, disguise their income through profit shifting schemes that reduce the effective tax rate imposed on their cross-border income. Tech MNCs do this easily because their income derived from intangible assets like patents, algorithms, and trademarks are registered in

1. *See generally*, Ara Aghakhanian, Video Game Microtransactions Featuring Loot Boxes: Not Gambling, but Similar Enough to Warrant Regulation (February 2020) (unpublished note, Southwestern Law School) (on file with the Southwestern Law School Library).

2. *See generally*, Alexandra Figueroa, Applying Transnational Anti-Trafficking Legal Regimes to Digital Platforms in Order to Preserve Global Cultural Heritage (Dec. 19, 2019) (unpublished note, Southwestern Law School) (on file with the Southwestern Law School Library).

3. *What is BEPS?*, ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT [OECD], <https://www.oecd.org/tax/beps/about/> (last visited Dec. 14, 2021).

4. DANIEL BUNN, SUMMARY AND ANALYSIS OF THE OECD’S WORK PROGRAM FOR BEPS 2.0, TAX FOUND. 3 (2019), <https://files.taxfoundation.org/20190617125254/Summary-and-Analysis-of-the-OECDs-Work-Program-for-BEPS-2.0-FF-660.pdf>.

5. OECD, *supra* note 3.

shell corporations in low tax countries. In 2017, for example, Amazon paid one tenth of one percent in taxes on its \$2.2 billion revenue in the United Kingdom by disguising its profits using a holding company in Luxembourg.⁶

Many European Union (EU) countries agree that base erosion and profit shifting are a problem, but they cannot agree on a uniform solution. The European Commission released its digital service tax proposal in March 2018.⁷ This tax would apply to companies with total annual worldwide revenues of \$868 million and total EU revenues of \$58 million.⁸ This proposal could only be passed with unanimous support of all EU members. As a result, it has not been implemented.⁹ Ireland, Luxembourg, Malta and the Netherlands are skeptical of a digital service tax, fearing it will make them less competitive as low-tax havens for tech MNCs.¹⁰

Refusing to wait for EU cooperation, France enacted a three percent digital service tax on tech MNCs' revenues in July 2019.¹¹ The United States immediately launched investigations as it found the tax discriminatory against U.S. companies.¹² By August 2019, both countries reached an agreement hinging on the Organization for Economic Cooperation and Development's (OECD) tax guidelines set to be released by the end of 2020.¹³ However, other EU countries are considering passing digital service taxes on MNCs' revenue.¹⁴ Canada has also declared that it will enact a three percent tax on targeted advertising services.¹⁵

6. *France Tech Tax: What's Being Done to Make Internet Giants Pay More?*, BBC NEWS (July 11, 2019), <https://www.bbc.com/news/business-48928782>.

7. DANIEL BUNN, A SUMMARY OF CRITICISMS OF THE EU DIGITAL TAX, TAX FOUND. 2 (2018), <https://files.taxfoundation.org/20181022090015/Tax-Foundation-FF618.pdf>.

8. *Id.* at 3.

9. *Id.*

10. Andrew Thompson & Louis D.C. Grandjouan, *Digital Economy Taxation: The OECD's Report and European Commission's Draft Directives*, 35 J. TAX'N INVESTMENT 23 (2018), LEXIS.

11. *France Passes Tax on Tech Giants Despite US Threats*, BBC News (July 11, 2019), <https://www.bbc.com/news/world-europe-48947922>.

12. Lilian V. Faulhaber, *Beware. Other Nations Will Follow France with Their Own Digital Tax*, N.Y. TIMES (July 15, 2019), <https://www.nytimes.com/2019/07/15/opinion/france-internet-tax.html>.

13. Jim Tankersley & Alan Rappoport, *As Nations Look to Tax Tech Firms, U.S. Scrambles to Broker a Deal*, N.Y. TIMES (July 12, 2019), <https://www.nytimes.com/2019/07/12/business/economy/tech-company-taxes.html>.

14. Elke Asen, *Announced, Proposed, and Implemented Digital Services Taxes in Europe*, TAX FOUND. (Oct. 25, 2019), <https://taxfoundation.org/digital-taxes-europe-2019/>.

15. Alexander Panetta *POLITICO Pro Canada: Liberal Platform Vows French-style Digital Tax*, POLITICO (Sept. 30, 2019, 10:01 AM), <https://www.politico.com/news/2019/09/30/politico-pro-canada-liberal-platform-vows-french-style-digital-tax-011564>.

In December 2019, the investigation's findings were announced. The U.S. Trade Representative determined that the French digital services tax unfairly discriminates against U.S. companies, conflicts with international tax principles, and intends to penalize Google, Apple, Facebook, and Amazon.¹⁶ France's digital service tax will affect only a small number of large companies. The tax will apply to companies with worldwide revenues of at least \$868 million and at least \$28 million of French "qualifying" revenues.¹⁷ A few Chinese, British, and Indian companies, and one French firm fit into this revenue category; the rest of the companies affected are U.S. based.¹⁸ Although the tax is not directly aimed at the United States, all the leading tech MNCs are American.

France's decision to tax only the highest earning tech MNCs shows its desire not to impede competition in the tech sector, but rather ensures MNCs are contributing their fair share. Further, France's negotiations with the United States show it is willing to end the tax once a solution is created. The tax is discriminatory, but only because the United States has the highest-earning companies in the tech sector. France's willingness to cooperate once a worldwide tax solution is achieved shows a diplomatic restraint the country should be commended for. It also creates an adaptable framework, which other countries seeking to tax tech MNCs can use. This law and its flexibility will push the OECD to make changes sooner.

Traditionally, taxing a corporation requires a fixed, "physical presence" within the country.¹⁹ The French law creates an "economic presence" criteria by establishing the above income thresholds for companies profiting from the French people and the data they provide to the companies.²⁰ Critics argue this is unfair because users do not create value through using a free service.²¹ Furthermore, a social networking company may have no employees, servers,

16. Douglas J. Heffner & Richard P. Ferrin, *U.S. Trade Representative Announces Results of Section 301 Investigation of French Digital Services Tax*, NAT'L L. REV. (Dec. 4, 2019), <https://www.natlawreview.com/article/us-trade-representative-announces-results-section-301-investigation-french-digital>.

17. Jessie Gaston, *Tax Alert: French Digital Services Tax ("DST")*, DENTONS (July 15, 2019), <https://www.jdsupra.com/legalnews/tax-alert-french-digital-services-tax-24392/>; *see generally*, Loi 2019-759 du 24 juillet 2019 portant création d'une taxe sur les services numériques et modification de la trajectoire de baisse de l'impôt sur les sociétés [Law 2019-759 of July 25, 2019 on the creation of a tax on digital services and modification of the downward trajectory of corporate tax], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [Official Gazette of France], July 25, 2019, https://www.legifrance.gouv.fr/download/pdf?id=vQhycwR0pIwjxQK8QpQMgIstvrVw7vibSIX3L_C8eE=.

18. BBC NEWS, *supra* note 6.

19. SEAN LOWRY, CONG. RSCH. SERV., R45532, DIGITAL SERVICE TAXES (DSTs): POLICY AND ECONOMIC ANALYSIS 2 (2019).

20. *Id.* at 4; Law 2019-759 of July 25, 2019 (Fr.).

21. BUNN, *supra* note 4 at 5-6.

or even sales agents in France and still be taxed.²² In reality, user-created data is highly valuable because advertisers pay for users' personalized attention which is only possible through collecting and analyzing personal data.²³ These steps serve to check the power of tech MNCs and increase competition in the digital sector. As more and more countries begin implementing their own digital service taxes, tech MNCs will be forced to change their practices.

This note aims to further Professor Wei Cui's assertion that users do in fact create value simply by using a social media platform.²⁴ Using the French law's "economic presence" theory, it can be shown that tech MNCs are profiting from their applications' mere usage in a foreign jurisdiction. However, this note counters other scholars' assertion that users of social media platforms should be compensated for their labor. Data is highly valuable, but tech MNCs still provide a costly service by allowing access to their applications for free or little cost. With the advances in data mining in the coming years, it may be possible that users will start selling their data to tech companies, but that subject goes beyond the scope of this note.

Digital Service Taxes (DST) are the next step in creating equitable taxation worldwide. As the economy becomes digitized, more income can be generated without a company's physical presence within a country. Tech MNCs have taken advantage of this through base erosion and profit shifting. Section II addresses the French tax and explains how it set this movement in motion. Section III discusses how the tax should be implemented by recognizing that users create value for tech companies and seeking a global shift toward recognizing economic presence criteria. Finally, Section IV will respond to critics of the tax demonstrating the strategic value of implementing a DST.

II. THE CIRCUMSTANCES LEADING TO THE CREATION OF FRENCH LAW NO. 2019-759

Following the EU's failure to make a decision on how to tax tech MNCs, France enacted its digital services tax law on July 25, 2019.²⁵ Recognizing the need to combat base erosion and profiting, the OECD adopted a plan to

22. *Id.*

23. Le Monde avec AFP, *Le Parlement adopte définitivement la « taxe GAFA », contestée par les Etats-Unis* [Parliament Finally Adopts "GAFA Tax", Challenged by the United States], LE MONDE (July 12, 2019, 6:25 AM), https://www.lemonde.fr/economie/article/2019/07/11/le-parlement-francais-adopte-definitivement-la-taxe-gafa-contestee-par-les-etats-unis_5488135_3234.html.

24. Wei Cui, *The Digital Services Tax: A Conceptual Defense*, 73 TAX L. REV. 69, 84 (2019).

25. Law 2019-759 of July 25, 2019 (Fr.).

address these issues in September 2013.²⁶ With over 120 member countries involved, progress is slow, but the OECD has promised to publish a plan by the end of 2020.²⁷

Many countries are concerned that tech MNCs are failing to pay their “fair share” in taxes. Unafraid of the repercussions, frustrated with the slow progress, and supported by President Emmanuel Macron, the French parliament passed France’s DST primarily to “break any impasse at the OECD level and push countries to reach an international solution.”²⁸ The legislation taxes revenue, generated by (i) selling personalized digital advertising, (ii) providing intermediation services, and (iii) online market places, at a flat rate of three percent.²⁹ This is generally the same as the European Commission’s digital services tax proposal.³⁰ However, it differs greatly from traditional tax bases that only tax profits.³¹

The biggest differences are in the thresholds of who is taxed. As stated previously, France will impose the same threshold for a yearly total revenue of \$868 million but will drop the in-country revenue from the European Commission’s \$58 million to \$28 million.³² U.S. companies fit squarely in these thresholds, yet the French will tax those with lower revenues in country.³³ This means the French version of the tax actually encompasses more non-U.S. companies than the European Commission’s proposal. Following France’s lead many others have begun moving toward a digital services tax. Since October of 2019, Austria approved a DST; the Czech

26. OECD, OECD/G20 Base Erosion and Profit Shifting Project, *Harmful Tax Practices - 2018 Progress Report on Preferential Regimes: Inclusive Framework on BEPS: Action 5*, at 3 (2019), <https://www.oecd.org/tax/beps/harmful-tax-practices-2018-progress-report-on-preferential-regimes-9789264311480-en.htm>.

27. James Ross, *INSIGHT: U.K.’s Digital Service Tax—Where Are We?*, BLOOMBERG TAX (Oct. 21, 2019, 12:01 AM), <https://news.bloombergtax.com/daily-tax-report-international/insight-u-k-s-digital-services-tax-where-are-we>.

28. Lilian Faulhaber, *France’s Digital Services Tax a Sign of Things to Come*, LAW 360 (Aug. 30, 2019, 12:07 PM), <https://www.law360.com/articles/1194303/france-s-digital-services-tax-a-sign-of-things-to-come>.

29. Julien Pellefigue, *The French Digital Service Tax: An Economic Impact Assessment*, DELOITTE TAJ (Mar. 22, 2019), <https://taj-strategie.fr/content/uploads/2020/03/dst-impact-assessment-march-2019.pdf>.

30. European Commission, Proposal for a Council Directive on the Common System of a Digital Services Tax on Revenues Resulting from the Provision of Certain Digital Services, COM (2018) 148 final (Mar. 21, 2018), <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2018:148:FIN> [hereinafter EC DST].

31. Faulhaber, *supra* note 28.

32. See EC DST, *supra* note 30; Law 2019-759 of July 25, 2019 (Fr.).

33. See Faulhaber, *supra* note 28.

Republic published a revised draft of their DST; and Italy, Uganda, and Turkey plan to implement a DST.³⁴

A. *Base Erosion, Profit Shifting and the OECD*

Since 2012, the OECD's Base Erosion and Profit Shifting project has been working to create a solution to inequitable global tax in conjunction with G20 countries.³⁵ The G20 is an international forum for global economic cooperation made up of a variety of countries with robust economies.³⁶ It includes the EU, the United Kingdom, the United States, Mexico, Canada, and Argentina to name a few.³⁷ By the end of 2015, the OECD began to implement their new changes to combat base erosion and profit shifting.³⁸ The OECD's goal is to prevent the incentive of shifting intellectual property profits to low-tax jurisdictions while keeping labor and costly expenses in high tax jurisdictions. It has been fairly successful in doing so, touting that practically every jurisdiction involved in negotiations has begun to implement their directives to create more transparency.³⁹ Nonetheless, it points out that tax changes worldwide continue to make their work difficult, especially the United States' recent "Tax Cuts and Jobs Act."⁴⁰

The slow progress of the OECD has pushed countries to implement their own DSTs. Due to base erosion, the EU only receives nine percent of taxes owed by tech MNCs, while traditional businesses pay twenty four percent.⁴¹ All EU members are affected, but France was the first to act. Corporate tax rates worldwide have also dropped seven percentage points since 2000, and the United States cut rates in 2018 to the worldwide average of twenty-one percent.⁴² This is another factor that likely increases the amount of money tech MNCs hide because it suggests a worldwide tendency of lax taxation for large corporations.

34. Asen, *supra* note 14.

35. See e.g., *The Latest on BEPS-2019 Midyear Review*, ERNST & YOUNG (July 30, 2019), <https://globaltaxnews.ey.com/news/2019-5951-the-latest-on-beps-2019-mid-year-review?uAlertID=fzxxkRx9St40PMYLOPBYQA%3d%3d>.

36. *The G20*, AUSTRALIAN GOV'T DEP'T OF FOREIGN AFFS. & TRADE, <https://dfat.gov.au/trade/organisations/g20/Pages/g20.aspx>.

37. *Id.*

38. ERNST & YOUNG, *supra* note 35.

39. *Id.*

40. *Id.*

41. Eléa Pommiers, *Taxation des GAFAs : la France peut-elle faire cavalier seul ? [Taxation of GAFAs, Can France Go It Alone?]*, L'EXPRESS (Apr. 1, 2019, 18:46), https://expansion.lexpress.fr/actualite-economique/taxation-des-gafa-la-france-peut-elle-faire-cavalier-seul_2055669.amp.html.

42. See Tankersely & Rappeport, *supra* note 13.

Perhaps due to these tax cuts or their strong control of markets, tech MNCs revenues have surged worldwide.⁴³ With the increased revenues of tech MNCs, France realized the OECD was not working fast enough. Although the United States has responded negatively to the tax, France's DST may push countries to move more quickly in reaching a multilateral solution.

At the moment, it seems that more unilateral moves are being made as more countries implement their forms of the DST. One can speculate that these pushes may be to force the United States to do something about the U.S. companies that are primarily causing the great inequities in foreign tax. The United States would benefit from a treaty pushing legislators to research these taxation issues and to reach an agreement between the countries that have implemented DSTs.

B. Impact in the United States

Much criticism is targeted at France, although many countries, including the United States, have been seeking to collect taxes from large tech MNCs. The U.S. Supreme Court has overruled prior decisions allowing only domestic businesses with physical presence in a state to be taxed.⁴⁴ Now, a company dealing in "e-commerce" may be taxed in any state where it substantially engages in business, thus no longer requiring an actual storefront, office, or employees in state.⁴⁵ The current international tax system was established at a time when international trade involved tangible assets and physical locations for companies to sell goods or services.⁴⁶ Thus, changes must be made to keep up with evolving technology in order to maintain competitive and equitable markets.

Understandably, the United States does not want its companies discriminated against by international taxation. However, profit shifting and base erosion have allowed many companies, including Netflix and Amazon, to pay no taxes in the United States in 2018.⁴⁷ Furthermore, Congress is launching a bipartisan investigation into the tech industry regarding the "anti-competitive conduct" of tech MNCs like Facebook, Google, and Amazon in

43. *Id.*

44. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2085 (2018).

45. *Id.* at 2099.

46. *See* Faulhaber, *supra* note 28.

47. 60 Fortune 500 Companies Avoided All Federal Income Tax in 2018 Under New Tax Law, INST. ON TAX'N & ECON. POL'Y (Apr. 11, 2019), <https://itep.org/60-fortune-500-companies-avoided-all-federal-income-tax-in-2018-under-new-tax-law/>.

the United States.⁴⁸ This note does not examine the possible monopolies existing in big tech, but this is a serious concern within the realm of taxation and tech MNCs.

U.S. scholars, tax experts, and attorneys continue to criticize the implementation of digital services taxes, but more countries continue to implement them. In particular, critics allege that France's DST's tax burden will be borne by customers and lead to high administrative costs in determining who owes what.⁴⁹ This perceived burden to be carried by consumers is addressed later in this note.

It is important to note that the United States is not content with the passing of DSTs. In 2019, U.S. President Trump threatened to impose tariffs upon French wine and luxury goods in response to this "discriminatory" tax;⁵⁰ however, both countries quickly reached a compromise. France agreed to tax tech MNCs for differences in the digital tax and whatever changes arise from the OECD's upcoming global mechanism for taxation.⁵¹ French President Macron believes that an international solution is necessary⁵² and the United States has agreed, in principle, to implement a tax change sanctioned by the OECD.⁵³ Many are unhappy with the slow rate of progress the OECD is making. Even if a plan is created in 2020, it will take years to implement.⁵⁴ Thus, France's stance, although opposed by the United States, is a push in the right direction. More countries are deciding to not standby idly as tech MNCs fail to pay their fair share. Hopefully, this will push the OECD to make changes sooner or lead to a U.S. sponsored treaty.

It seems the OECD is struggling because of the three classes of countries that are at odds. The United States is one type of class where the tech MNCs are headquartered and founded. France, a majority of the EU, Canada and most countries that acknowledged tech MNCs are not paying enough are

48. Vivian Ho, *Tech Monopoly? Facebook, Google and Amazon Face Increased Scrutiny*, GUARDIAN (June 3, 2019), <https://www.theguardian.com/technology/2019/jun/03/tech-monopoly-congress-increases-antitrust-scrutiny-on-facebook-google-amazon>; see Press Release, Off. Of Pub. Affs., Dep't of Just., Justice Department Reviewing the Practices of Market-Leading Online Platforms (July 23, 2019), <https://www.justice.gov/opa/pr/justice-department-reviewing-practices-market-leading-online-platforms> [<https://perma.cc/3J6A-9CZ3>].

49. Pellefigue, *supra* note 29.

50. Hadas Gold, *US and France Reach Compromise on Digital Tax*, CNN (Aug. 26, 2019, 1:59 PM), <https://www.cnn.com/2019/08/26/business/digital-tax-france-us/index.html>.

51. *Id.*

52. *Id.*

53. Sean J. Brennan, *The Digital Service Tax: A Big Gun in International Tech Company Tax Wars*, PA. INST. OF CERTIFIED PUB. ACCTS. (Aug. 21, 2019), <https://www.picpa.org/articles/cpa-now-blog/cpa-now/2019/08/21/digital-service-tax-big-gun-in-international-tech-company-tax-wars>.

54. See Gold, *supra* note 50.

another class. Finally, the third class includes countries like Ireland and Luxembourg that benefit from attracting tech MNCs to set up shop in their countries due to low-tax rates.

Rather than be at odds with each other, the first- and second-class countries should bind together and propose a treaty. The United States feels its companies are being discriminated against, yet the United States is also losing out on valuable tax revenue just like France and the others. These conflicts likely prevent the OECD from making quicker decisions in the international taxation realm. A treaty or executive agreement between the United States and similarly positioned countries may be a solid step forward. Until then, U.S. companies may incur more and more DSTs.

III. ACKNOWLEDGING THAT MNCs DO NOT NEED A PHYSICAL PRESENCE AND VALUE IS CREATED BY DIGITAL TECHNOLOGY USERS

The French DST recognizes the need to adapt the current tax laws for the changing landscape of tech businesses. As imposed, the DST recognizes two important factors: some companies without a physical presence should be taxed and users on tech platforms create value.⁵⁵ Both of these factors go hand-in-hand because substantial profits are earned in countries where companies have no physical presence. Tech MNCs mine tons of data from their users in particular countries, and subsequently sell that data to advertisers or use that data themselves to develop how to target users. Thus, the users of the social media or online marketplace essentially become the product that the MNCs sell.

A. *The Problem with a “Physical Presence” Framework*

The recognition that users create value, although using a free service, is a critically important component of the DST. As legislators accept this reality the fair taxation of tech MNCs will become increasingly possible. The problem stems again from the idea that a company should only be taxed if it has physical presence described in a country. The Supreme Court has recognized this problem domestically;⁵⁶ now it is time the rest of the world realizes that it can work to tax those companies who take from their countries without giving back. The OECD has recognized that tech MNCs can create

55. Law 2019-759 of July 25, 2019 (Fr.).

56. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018).

great value for themselves but are immune to taxes under the current international tax laws.⁵⁷

A simple example of the untaxed value stemming from a company with no physical presence in a jurisdiction occurs when an advertiser exists in one country, the tech MNC in another, and the users in multiple countries. Based on traditional taxation laws, only the country where the advertiser and MNC are located would be allowed to tax any profit the two made advertising to others. Under a DST, the country where the user interacted with the ad would also levy a tax because a user's online behavior generates the data and metadata needed to enable and personalize online advertising.⁵⁸ Without this data, advertisers and tech MNCs alike can neither predict what products will sell and what features are performing well nor can data collectors continue to be profitable, because they will have no data to sell advertisers.

As it stands, domestic tax laws and international agreements provide the first right to tax where a company owns an asset.⁵⁹ The location of the corporation's customers does not matter.⁶⁰ Thus, there needs to be a shift where the nexus is tied to the customers or users of the platform. This concept was a significant portion of the European Commission's proposal in March 2018.⁶¹ The Commission's stance has changed drastically since 2014, when an initial group of experts explicitly stated that they did not believe the collection of data via electronic means in a country should in itself create a taxable presence in that country.⁶²

The latest proposal shows a support for taxing tech MNCs for the revenue they take in from use of their platforms. One proposal the European Commission agreed with was expanding the permanent establishment or the physical presence definition.⁶³ This would allow a company with a significant economic activity through its "digital presence" to be taxed by either: (i) exceeding a threshold of seven million euros in annual revenue in

57. *Addressing the Tax Challenges of the Digitalisation of the Economy*, OECD (Mar. 6, 2019), <https://www.oecd.org/tax/beps/public-consultation-document-addressing-the-tax-challenges-of-the-digitalisation-of-the-economy.pdf>.

58. CHRISTIAN FUCHS, *THE ONLINE ADVERTISING TAX AS THE FOUNDATION OF A PUBLIC SERVICE INTERNET* 60 (2018).

59. LOWRY, *supra* note 19, at 8.

60. *Id.*

61. See Press Release, European Commission, Digital Taxation: Commission Proposes New Measures to Ensure That All Companies Pay Fair Tax in the EU, IP/18/2041 (Mar. 21, 2018), https://ec.europa.eu/commission/presscorner/detail/en/IP_18_2041.

62. *Report of the Commission Expert Group on Taxation of the Digital Economy*, at 7 (May 28, 2014), https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/gen_info/good_governance_matters/digital/report_digital_economy.pdf.

63. Press Release, *supra* note 61.

a EU member state, (ii) having over 100,000 users in a taxable year, or (iii) having over 3,000 business contracts for digital services business users in a taxable year.⁶⁴

The other proposal, after which the French modeled their DST, involves a three percent interim tax on digital activities.⁶⁵ These activities include selling online advertising, online market-place generated data, and data generated from user-provided information.⁶⁶ The EU as a whole has realized it is time to take charge of its taxing rights as individual sovereign nations. Although not every country is on board, France has led the push.

B. *The Case for “User Created Value”*

The main critique of “user created value” is that innovations and assets of the tech MNCs create the value, not their users.⁶⁷ This criticism is misguided because tech MNCs are multisided businesses, meaning one side of users cares about the other side of users, most importantly obtaining a large number of them.⁶⁸ Essentially, a tech MNC’s application is nothing without a wide user base and the interactions created by users drive the demand for new users to use the application. Advertisers are “one side of users” and recreational users of Instagram or Facebook are “the other side.” Advertisers are only willing to pay Facebook for ad space if it generates many users. Most users will only create a profile if it is free to do so. Thus, Facebook cannot profit unless it attracts many users, and those users create a community, which in turn puts more eyes on the ads Facebook sells.⁶⁹ Although an MNC’s intellectual property is what drove people to use or ignore a website, it is the number of people on the site that attracted the advertisers. This is critical and shows that value is created by users, an important concept the French recognized and implemented in support of their law.

Data is collected in three ways and used to sell ad space. A platform’s users are the product that is sold.⁷⁰ Volunteered data is the information users provide freely such as their names, addresses, birthdays, and activities or businesses they “like.”⁷¹ Observed data is the information gathered by GPS tracking, monitoring flash-cookies, and by digging through the history of

64. *Id.*

65. *Id.*

66. *Id.*

67. LOWRY, *supra* note 19, at 13.

68. Cui, *supra* note 24.

69. *Id.* at 85.

70. Adam B. Thimmesch, *Transacting in Data: Tax, Privacy, and the New Economy*, 94 DENV. L. REV. 145, 151 (2016).

71. *Id.* at 152.

pages browsed.⁷² Inferred data is the information gathered from searches and purchases to determine information, such as, a user who may be pregnant or an avid soccer fan.⁷³ All this data combined allows companies a thorough look into a user's habits, lifestyle, and career. In turn, such data can be used to market specific products to a person and influence their political beliefs or purchasing habits. Thus, the "free" access the digital platforms provide is not truly "free" of cost.

Conversely, the user receives access to a highly valued product through exchanging data for services. The use of digital platforms is arguably necessary to be a fully engaged member of society.⁷⁴ However, at some point, a line must be drawn because consumers are handing over a lot of personalized data in exchange for information and entertainment.⁷⁵ Consumers are not completely giving away free labor, but there is a disconnect in the privacy they are losing and the services they are receiving. In addition, companies that mine the data are making large profits from privacy breaches.

Some scholars have argued that consumers should own their data and have the choice to decide whether to sell it or not. For example, U.S. presidential candidate, Andrew Yang, has proposed treating data as a property right.⁷⁶ This is important as he brought user-created value into the U.S. zeitgeist. In the United States, data gathering and marketing is a \$198 billion industry, and Yang believes Americans have not received enough in return for their data and loss of privacy.⁷⁷ Others have suggested viewing data creation as labor because so many jobs will soon be lost to automation in the coming decades.⁷⁸ Furthermore, artificial intelligence needs the constant input of others in order to become better.⁷⁹ It is of note that the users who input the data needed for better digital platforms create the value. Viewing data as property that can be sold is a radical approach that may one day be applicable. For now, governments must realize that users create value for tech MNCs, and this value must be taxed.

72. *Id.*

73. *Id.*

74. *Id.* at 155.

75. *Id.* at 160.

76. Tyler Sonnemaker, *Andrew Yang Wants You to Make Money on Your Data by Making It Your Personal Property*, MKTS. INSIDER (Nov. 14, 2019, 4:19 PM), <https://markets.businessinsider.com/news/stocks/andrew-yang-data-ownership-property-right-policy-2019-11-1028691103>.

77. *Id.*

78. Imanol Arrieta Ibarra et al., *Should We Treat Data as Labor? Moving Beyond "Free,"* 108 AM. ECON. ASS'N PAPERS & PROC. 38, 42 (2018).

79. *Id.* at 40.

The first step in pushing tech companies to be equitably taxed requires the understanding that users are creating value. Many recognize this and France is making the salient moves needed to center these values. Considering data input as labor may reach too far, but recognizing value is created by data mined from users is not. This value can be determined through annual reports by the tech MNCs that take into account the ad revenue generated in various parts of the world. Finally, if the users create value that means profits are being made simply from interactions with the social media platform inside the country. This would allow the tech MNCs to be taxed because they are actually profiting a tangible amount of money from that particular country.

C. Understanding the Value of Data and the Tech Marketplace

The market inhabited by tech MNCs is much different than the previous international businesses. Professor Wei Cui explains how Facebook in France offers free social media services to users all over the world as well as advertising services to advertisers for untaxed profit.⁸⁰ U.S. companies then purchase advertisements targeting French consumers, and Facebook profits from the American company, receiving payment in the United States.⁸¹ If Facebook had a permanent establishment (PE) in France, there would be no reason to attribute the profits it earns from American advertisers to the French PE.⁸² However, Facebook's profit from the ads targeted at the French is based on value created in France. American companies pay Facebook only because they expect the ads will boost sales in France, and sales do not increase unless French consumers use the social media platform. Although Facebook creates the technology outside France's jurisdiction, the users create the value because without them, advertisers would not pay for ad space on the platform that is unique to France.⁸³ Therefore, Facebook's profits from ads targeted at the French is earned from users in France.⁸⁴

This differs from yesteryear's business model. Previously, through television or radio, consumers received free programming in exchange for listening to or viewing ads.⁸⁵ Before, someone may see a good commercial and tell a friend about a particular blender. The friend could then go to the store and buy the blender based on word of mouth but tracking the

80. Wei Cui, *The Superiority of The Digital Services Tax Over Significant Digital Presence Proposals*, 72 NAT'L TAX J. 839, 848-49 (2019).

81. *Id.* at 848.

82. *Id.*

83. *Id.*

84. *Id.*

85. LOWRY, *supra* note 19, at 13.

commercial that caused the friend to buy would be difficult. Now, every click made on a website shows the consumer trends of a country.

Consumers today are not stagnant. Consumers create content which drives demand for others to join the social media platform. These people are “prosumers,” meaning they are producing consumers.⁸⁶ These prosumers are the ones that drive people to sites like Instagram to keep up with the constant photos the prosumer shares. France estimates 150 million posts are uploaded daily in the EU and that value, which is user created, goes into the pockets of tech MNCs.⁸⁷ Tech MNCs depend on a developing, active, and engaged user base. The larger the base, the more market power an MNC can wield.⁸⁸

Tech MNCs are aware that users create value. The volume and quality of the content created by users is key in a tech MNC’s ability to generate revenue from other users or paid-for advertising targeted at those users.⁸⁹ Many users realize this and become influencers, users who create value through advertising products, and yet Instagram is beginning to slow the progress these influencers have made. Under the guise of mental health, Instagram allowed users to remove “likes,” a numerical indicator that shows how much attention a post is getting, but in reality they want to turn around and sell the analytics of “likes” to users.⁹⁰ Millions of dollars pass from brands to influencers weekly, while Facebook (Instagram’s parent company) does not get a share.⁹¹ To combat this, Instagram is removing analytics, such as “likes,” and then turning around to sell a service to brands which shows the traffic a post gets.⁹²

This may be a bad move as social media business models are based on encouraging users to proactively contribute content and spend time on the platform. Instagram may now find itself losing users, which in turn would mean losing profits as users switch to a platform that allows them to capitalize from their contributions.

Netflix is also aware that its users create value through the data gathered from them. At its core, Netflix is a data driven company focused on collecting

86. FUCHS, *supra* note 58, at 62.

87. *Projet de loi relatif à la taxation des grandes entreprises du numérique*, MINISTÈRE DE L’ÉCONOMIE ET DES FINANCES 4 (Mar. 6, 2019), <https://www.economie.gouv.fr/files/files/2019/dp-tax-gafa-v11.pdf>.

88. OECD, *supra* note 57, at 9.

89. *Id.*

90. Olivia Ovenden, *Why Is Instagram Removing Likes? It’s Probably Not to Help Your Mental Health*, ESQUIRE (Nov. 12, 2019), <https://www.esquire.com/uk/design/a29768558/instagram-removing-likes-facebook/>.

91. *Id.*

92. *Id.*

information from its large user base.⁹³ It uses the data to analyze what shows to commit to. For example, without even seeing a pilot, Netflix invested \$100 million into two seasons of “House of Cards.”⁹⁴ Unlike other platforms, Netflix is ad-free and, although it charges a monthly subscription, it has had a negative cash flow throughout the majority of its existence—\$3 billion in 2018 alone.⁹⁵ Many speculate that this is because of their extreme data collection and that soon they will profit by selling off all of this data.⁹⁶ This data would be worth a fortune to marketers, political campaigns, and advertisers.⁹⁷

User data is worth a lot to tech MNCs, some even operate at a loss to continue to mine user data. The previous view that users of internet platforms do not create value is wrong. Existing international taxation is too focused on the physical activities of tech MNCs to determine where they can be taxed.⁹⁸ France is taking sound steps by realizing remote participation in a domestic economy without a taxable physical presence must be addressed.⁹⁹

D. DST Costs Will Be Passed Onto Consumers

Users create value when using the search engines and social media platforms of tech MNCs. The passing of a new tax, especially on businesses conducting business on an international scale, will be hard to trace. Some costs will rise in the implementation of the new tax, but ultimately the costs will balance out as France begins to collect the revenue from the tax. There is also the chance that the frustration caused by the tax and the concurrently implemented DSTs by other nations will push the OECD to move quickly in creating an international solution to base erosion and profit shifting.

A conundrum exists with increasing the taxes tech MNCs pay because it allegedly will increase costs on consumers. However, that again shows a misunderstanding of the tech business model. If all costs are passed onto individual users, it may drive down usage, which would drive down

93. Harsha Hedge, *Netflix and Its Revolutionary Use of Big Data*, DATAECONOMY (Sept. 22, 2014), <https://dataconomy.com/2014/09/netflix-and-its-revolutionary-use-of-big-data/>.

94. *Id.*

95. Jason Mittell, *Gold Mine: Will Netflix Eventually Monetise Its User Data?*, THE WIRE (Apr. 24, 2019), <https://thewire.in/the-arts/netflix-user-data-finances>.

96. *Id.*

97. *Id.*

98. OECD, *supra* note 57, at 10.

99. *Projet de loi relatif à la taxation des grandes entreprises du numérique*, *supra* note 87, at 3.

advertisers' desire to pay for ad space and diminish a platform's market power.¹⁰⁰

Costs will rise, but that cost may not be transferred onto the consumer in certain areas. For example, due to increased taxation, a newspaper may lower, rather than raise, the price of a subscription in order to increase circulation and attract more advertisers.¹⁰¹ The advertising profits go up and compensate readers for the increase in advertisement with a lower subscription price.¹⁰² Now, in applying this to Facebook or Google, it would be best for these firms to absorb the costs or risk losing advertisers.¹⁰³ The more advertisers either of these sites lose, the less profitable it becomes to maintain the platform, unless the firm operates on the rare "Netflix" model of running at a deficit without ads.

The shifting of costs onto consumers may be different for sites that sell products, rather than social media providers. In response to the DST, Amazon has passed the cost onto vendors.¹⁰⁴ Legally, Amazon is the one who pays the tax, but this does not stop them from passing that tax along as the economic incidence of the DST.¹⁰⁵ As of October 1, 2019, Amazon has increased the commission rate it takes from businesses selling in the French marketplace by three percent.¹⁰⁶ The vendors will likely pass this on to the consumers by raising the prices of the goods sold.¹⁰⁷ In fact, the Tax Foundation argues that the DST will pass fifty five percent of the burden onto consumers, forty percent onto online vendors and only five percent onto the targeted digital companies.¹⁰⁸ In this case, the French may have overstepped by applying the tax to interfaces on which the sales of goods and services take place. However, if prices continue to rise, it can spur the creation of a French marketplace, or influence vendors to sell using different platforms. Amazon should tread lightly in how much it intends to raise costs as many customers may leave.

100. Cui, *supra* note 24, at 106.

101. *Id.*

102. *Id.* at 28.

103. *Id.* at 27-28.

104. Elke Asen & Daniel Bunn, *Amazon Passes France's Digital Services Tax on to Vendors*, TAX FOUND. (Aug. 6, 2019), <https://taxfoundation.org/amazon-france-digital-tax/>.

105. *Id.*

106. *Id.*

107. *Id.*

108. *Id.*

IV. THE POLITICAL UNDERPINNINGS OF THE DIGITAL SERVICES TAX

As global barriers are lessened through the advancement of technology, many disparities become more apparent. Social media, through all of its collection of data, has provided a window into the affairs of other countries. It has even allowed for meddling in the political affairs of other countries. DSTs may serve to get tech MNCs to pay their share, but also to increase responsibility for the actions they take. As the OECD makes clear, base erosion and profiting have become a huge global problem.¹⁰⁹ They have allowed tech MNCs to take control of sovereign nations through the manipulation of government elections and failure to pay taxes.

France's decision to implement the DST was due in part to social unrest throughout the country.¹¹⁰ The country erupted in protests after President Macron implemented anti-labor policy such as cutting taxes for the wealthy and large corporations.¹¹¹ Seeing the deteriorating conditions of his approval, Macron made concessions, including increasing the minimum wage, allowing for tax exemptions on overtime pay, and raising retiree social security.¹¹² These concessions are set to cost the French government approximately \$11.3 billion, which the DST will help to finance.¹¹³ The government aims to collect \$5.5 million annually from the proposed DST.¹¹⁴ Although the DST alone will not solve France's budget issues, it will address the issue of tech MNCs not paying taxes and show the public that Macron is ready to tackle larger issues.

Critics see this desire to equitably tax firms as "populist responses to demonize tech."¹¹⁵ This may be true considering the United Kingdom will

109. *What is BEPS?*, *supra* note 3.

110. Liz Alderman, *France Moves to Tax Tech Giants, Stoking Fight with White House*, N.Y. TIMES (July 11, 2019), <https://www.nytimes.com/2019/07/11/business/france-digital-tax-tech-giants.html>.

111. Alissa J. Rubin, *France's Yellow Vests Confront Macron with a New Reality*, N.Y. TIMES (Dec. 17, 2018), <https://www.nytimes.com/2018/12/17/world/europe/macron-yellow-vests-france.html?module=inline>.

112. Alissa J. Rubin, *Macron's Proposal to Mollify Yellow Vest Protesters Fails to Impress*, N.Y. TIMES (Dec. 11, 2018), <https://www.nytimes.com/2018/12/11/world/europe/yellow-vests-france-macron.html?module=inline>.

113. *Id.*; see also Liz Alderman, *France, Not Waiting for European Union, to Tax U.S. Tech Firms as '19 Starts*, N.Y. TIMES (Dec. 18, 2018), <https://www.nytimes.com/2018/12/18/technology/france-tax-tech-companies.html>.

114. LOWRY, *supra* note 19, at 7-8.

115. Gillian Tans, *Why Global Taxation Is Needed for the Success of the Digital Age*, WORLD ECON. F. (Jan. 21, 2019), <https://www.weforum.org/agenda/2019/01/why-global-taxation-is-needed-for-the-success-of-the-digital-age>.

begin a two percent DST as of April 2020,¹¹⁶ and seeing that France agreed to end the tax as soon as the OECD reaches a resolution.¹¹⁷ However, the whole world, including the United States, seems to have had it with tech MNCs and their failure to pay their fair share of taxes.

An internationally coordinated approach through the OECD is likely the best option to address this issue. Continuous unilateral decisions make it difficult to assure there is no double taxation or burdensome administrative costs in determining where taxes are owed. All countries are affected by the harms of base erosion and profit shifting. As the leader in tech, the United States should push for a treaty to make arrangements to receive taxes until the OECD can reach an agreement.

V. CONCLUSION

In 2019, Google's ex-CEO, Eric Schmidt, stated that he was comfortable with Google's tax avoidance practices. He emphasized that everything they did was ethical, and that if countries desperately wanted more money, they should change their tax laws.¹¹⁸ The French DST is the first set of tax laws to push Google and others to pay its share of tax around the world. In a short time, Schmidt may regret his statement as more than ten countries plan to implement DSTs in one form or another.

The French DST will serve to increase competition and push corporations to pay their fair share in taxes. The actual revenue collected by each tax may be low, but the frustrations it will cause tech MNCs will help sovereign states and people take back their power. Recognizing that users create value will serve to show tech MNCs that they truly need individual input for continued success. Furthermore, states need taxes to operate effectively and tech MNCs should not be allowed to flourish without giving back. If the taxes do become too burdensome and force vendors and advertisers to leave the site, then it will increase competition and innovation.

The French Digital Services Tax is a solid start in combatting base erosion and profit shifting to make corporations more responsible. Through acknowledging that users create value, the tax effectively captures profits earned by tech MNCs. Furthermore, France's widening of the scope of MNCs that are subject to the tax, by setting the in country threshold at \$28

116. Chris Jewers, *UK Presses Ahead with Digital Services Tax*, ACCT. AGE (July 12, 2019), <https://www.accountancyage.com/2019/07/12/uk-presses-ahead-with-digital-services-tax/>.

117. Faulhaber, *supra* note 28.

118. Paul Hill, *Eric Schmidt Is 'Comfortable' with Google's Tax Avoidance Practices*, NEOWIN (May 14, 2019, 1:08 PM), <https://www.neowin.net/news/eric-schmidt-is-comfortable-with-googles-tax-avoidance-practices/>.

million, shows a desire to tax more than just American tech MNCs.¹¹⁹ In truly combatting base erosion and profit shifting, the DST is not the best, but serves as a testing ground for eventually finding a way to stop all industries from artificially moving and keeping money tax free.¹²⁰

Many other countries have followed France's bold move, although U.S. scholars and companies continue to argue that the DST is disastrous. It may be disastrous to large MNCs, but perhaps it will create more competition and in turn, more innovation in the tech industry. Rather than fall behind, the United States must get ahead of this growing problem and agree on a treaty to deal with these taxation issues.

The main takeaway is recognizing that users of social media platforms create value. U.S. legislators must understand this and begin to move forward in creative ways to adhere to that principle. This is the first wave in the regulation of the complex digital economy that has been created by social media. It is best that larger countries with more resources lay the foundation for new tax schemes or be forced to adhere to small, complex taxes throughout the world. Tech MNCs have made it known that they have no problem with gaming the loopholes in the current taxation system. Thus, a justly taxed world will not come about unless countries are willing to push back.

119. Alderman, *supra* note 110.

120. See generally Christine Kim, *Weekly SSRN Tax Article Review and Roundup: Kim Reviews Cui's The Digital Services Tax: A Conceptual Defense*, TAXPROF BLOG (May 17, 2019), https://taxprof.typepad.com/taxprof_blog/2019/05/weekly-ssrn-tax-article-review-and-roundup-kim-reviews-cuis-the-digital-services-tax-a-conceptual-de.html.