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# *Could the Global Digital Service Providers be Persuaded to Pay Their Share?*

**SUMMARY:** The emergence, rapid expansion, and globalization of digital services have significantly reshaped the world-economy. The rise of global digital service providers, i.e. multinational companies providing digital services in many countries around the world, is also a new challenge in terms of equitable public burden bearing. Under current tax rules, physical presence provides the legal basis for the exercise of each country's taxing power. However, digital services do not require a physical presence. Taking advantage of this, global digital service providers do not tax their profits where they produce, but where the tax conditions are most favourable. As a result, they contribute much less to public burdens in proportion to their profits than traditional economic actors, and most of the countries concerned lose significant tax revenues. Many international organizations are looking for a solution to this inequitable situation, but no agreement has yet been reached. The solution is complicated by determining where profit-generating value creation occurs geographically. This article reviews the answers to these questions.<sup>1</sup>

**KEY WORDS:** digitalization, equitable public burden bearing, digital value creation

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**H**ow would you feel if the labourers harvesting wheat in your field transferred the produce through a pipeline to a neighbour's field agreeing to pay a higher price, taking advantage of the fact that they work there as well? You would obviously be outraged and consider it unfair and unjust, or indeed, an outright theft. Nevertheless, this phenomenon is not at all uncommon in today's global economy. As a matter of fact, it is not crop but the profit, not the fields but the countries, and not the labourers but the multinational

companies responsible for this act of turpitude. It should be noted that in contemporary common language the Hungarian equivalent of turpitude (*turpisság*) means mischief or trickery. However, the Hungarian word comes from the Latin *turpis*, and originally means foul, wicked or immoral. In this case the original meaning should prevail due to the fact that it is no mischief but a foul and immoral act to rechannel profits from one county to another for the sake of paying less tax. Many international organisations, including the OECD consider this commonly used practice inequitable. In 2013 the OECD launched a

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project dedicated to combating base erosion and profit shifting (BEPS). This was due to multinational enterprises exploiting gaps and mismatches between different countries' tax systems to shift profits from one country where underlying economic activity and value creation takes place to another country offering more favourable tax conditions. It contradicts the principle by which, as a rule, corporate tax (income tax) should be paid in the country where profit-generating value creations occurs physically.

Currently the rise of global digital service providers poses a new challenge in terms of equitable public burden sharing due to lack of physical presence. It provides an opportunity for these multinational companies to pay tax in a country where the tax conditions are most favourable without particular accounting challenges. They simply need to set up or relocate sites in countries with minimum levels of taxation. These naturally include tax havens with very low rates of taxation, but also some other countries with otherwise adequate income tax levels that offer special tailor-made benefits to attract digital multinational enterprises. Hence, these companies are exempted from corporate tax payment in the countries whose citizens and businesses receive their services, with the specific countries losing out on tax revenues. Naturally, the countries offering physical location are not exactly deprived due to substantial tax revenues generated by rechannelling huge profits from other places. According to the OECD's 2018 estimate, for all countries in the world, the annual loss of government revenue in 2015 was at least USD 100–240 billion, equivalent to 4–9 percent of global corporate tax revenue.

Returning to the initial question, comparing global digital services to harvesting wheat is nevertheless inappropriate due to the fact that the provision of services does not seem to

require a specific place as it is done by using satellites high above the earth. Indeed, when talking about digital services 'rain' would make a more useful analogy. In this case the question we need to ask is: How would you feel if the rainwater fallen on you land was channelled to a reservoir on a neighbour's field in order for him to be able to use it in the dry season? Many would not call it stealing; after all, the rain has soaked your field and the unabsorbed rainwater would be of little consequence. Meanwhile, the shrewd neighbour would benefit from your indifference. As we will see, this example appears to be similar to the situation with digital services. Unless prohibited, global digital services are received in every country. But this alone is not necessarily considered enough. What if the profit from the new value created for, or even through the consumers of a specific country could be shared too? This, however, is not likely to work by itself. Similar to channelling rainwater into reservoirs, sharing the profits of the digital service providers also requires additional effort. But here is the catch. In order to collect the rainwater fallen on your field you need to build reservoirs. Yet, there will be no return on the investment if the rainwater fallen on your land can still be channelled to the neighbour's reservoir, no matter how much you disagree.

For this reason the equitable taxation of global digital services poses a dual challenge. On the one hand, the particular share of global digital service value<sup>2</sup> associated with a country should be made tangible. On the other hand, a system should be developed and safeguarded to ensure that the global digital service providers pay tax on the profits resulting from new value to the country that can be associated with the creation of such value. Clearly, building a system of this level of complexity would require international cooperation and understanding. The good

news is that not only complex solutions would suffice, as the individual countries are also capable to identify a tangible share of the value created by the global digital service providers that can be associated with them, and to impose and collect appropriate taxes using a high level of creativity and persistence. The advertisement tax introduced in Hungary is a good example, requiring also the global digital service providers to pay huge taxes based on the value of adverts ordered in Hungary.

## THE BOUNDARIES OF DIGITAL SPACE

The rise in digitalization was the result of the digital revolution which began in the second half of the 20th century. The breakthrough in economic digitalization was brought about by personal computers developed and manufactured with a high level of efficiency, as well as multimedia devices allowing digitization of data. Economy as a concept had to be redefined as a result of extensive digitalization. The transformation into a digital economy took place with the appearance of digital products and services. New businesses emerged, offering entirely digital products and services based on existence and communication with consumers in the digital space.

The international literature provides multiple definitions for the digital economy. Based on the approach taken by *Ostrom et al.* (2016) the digital economy is huge due to the fact that digital information and data can be used by various actors ranging from agriculture to R&D. The research carried out by Ostrom et al. in 2016 found that for example the Dutch companies with online presence accounted for 87 percent of business sector turnover and 86 percent of employment in 2015. In a narrower sense, the internet related businesses (webstores, online and

ICT services) represented a share of only 7.7 percent and 4.4 percent in terms of turnover and employment, respectively. According to a narrower approach taken by some IMF experts (2018) the digital economy can be identified by the existing online platforms and their activities, but based on a wider approach, any activity that relies on digital data should be considered as a part of the digital economy. In the modern world, it practically means the entire economy. Digital economic activity can be characteristic for the automotive industry just as much as for agriculture, depending on the level of development and the degree of digitization. According to *Ahmad and Ribarsky* (2018) the accounting and other records prevailing at the time made the tracking and tracing of the digital economy rather difficult. The fundamental problem was that the systems used back then had been essentially designed for the pre-digital age.

The definition of the digital economy fundamentally influences the estimation of its size, as digitalization penetrates the entire economy to a certain degree, although the measurements should be focused on the actual fields of economic activity concerned with digitization. In 2018, due to the ambiguity of the concept and content of digital economy, the IMF experts established the concept of digital sector as a starting point for measurements, based on the sector's size identifiable by basic activities.

Within the digital economy, the digital sector incorporates the businesses that provide digital products and services with a unique process of value creation based on direct consent by the consumers. The activities of the digital sector typically include information and communications technology (mobile applications) and online platform based (social media) services. The relationships between the three elements of the business sector are shown in *Figure 1*.

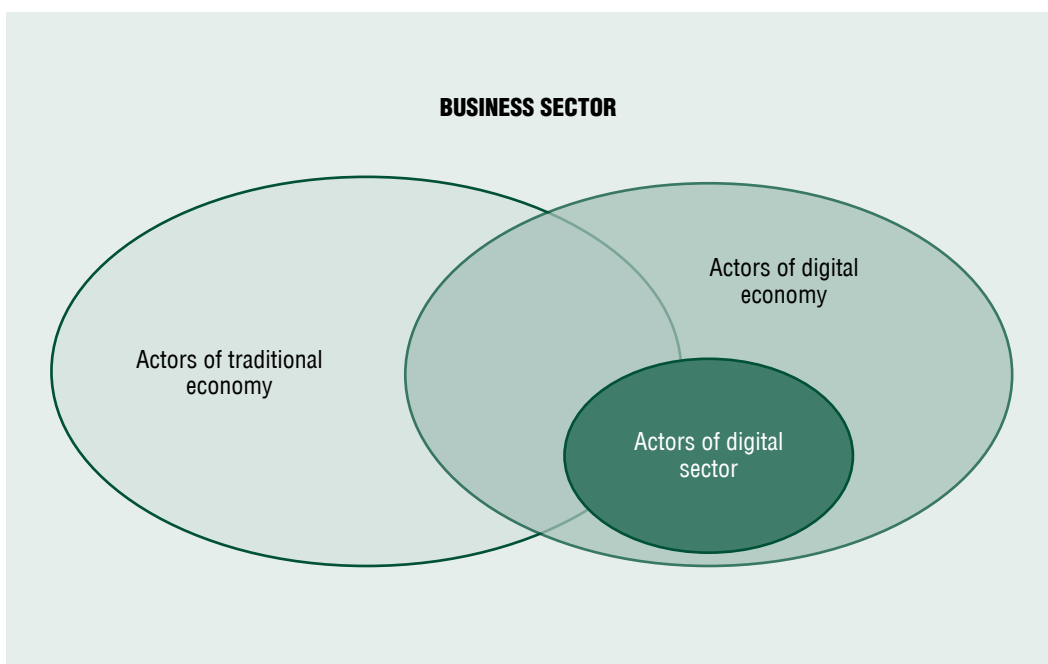
The growth of the digital economy, including the digital sector, is more dynamic than the growth of the traditional economy. Therefore, the proportions shown in Figure 1 are constantly changing. The economic actors providing services in the digital space represent an increasing share due to new entrants as well as the growing scale of digital activities performed by the traditional business sector companies. As the above processes are widely known, this article will address these changes from the aspect of equitable taxation in the digital sector, with particular focus on fair burden sharing by the global DSPs. The global digital service providers are companies that provide digital services for the citizens and businesses of numerous countries around the world.

## DEFINITION OF EQUITABLE TAXATION

*‘The criticisms of tax systems tend to draw attention to the unfairness of taxation. However, it is not easy to determine exactly what is fair and what is not fair. Two concepts of fair tax treatment have emerged: horizontal equity and vertical equity. ... The tax system is horizontally fair if it treats the same taxpayers equally in all relevant respects. ... In accordance with the principle of vertical equity, some taxpayers are able to bear more tax burdens than others and actually have to pay more taxes.’ (Stiglitz, 2000, pp. 410–411). Consequently, based on the principle of horizontal equity, the global digital service providers should be taxed on the profits generated by value creating activity that can be associated with specific countries to the*

Figure 1

### TRADITIONAL AND DIGITAL ECONOMIC ACTORS IN THE BUSINESS SECTOR



Source: Teski et al. (2020, page 10)

same extent as the companies actually located in those countries.

The requirement of equitable taxation should not be influenced by the different legal situation of the global DSPs as opposed to established companies for having no registered sites in the majority of the countries where the value creating activities take place.

The difference between equity and (legal) justice was explored by *Aristotle* as well, with an attempt to clearly distinguish between the two. In *Aristotle's Nicomachean Ethics* (Book V, Section 1137b) equity and justice are compared in a separate chapter. In his view the two are not entirely the same, but not generally different either. Comparing the two, justice and equity are both good, but equity is superior. *'The source of the difficulty is that equity, though just, is not legal justice, but a rectification of legal justice. (...) law is always a general statement, yet there are cases which it is not possible to cover in a general statement (...), the law takes into consideration the majority of cases, although it is not unaware of the error this involves. And this does not make it a wrong law; for the error is not in the law nor in the lawgiver, but in the nature of the case: the material of conduct is essentially irregular. (...) This is the essential nature of the equitable: it is a rectification of law where law is defective because of its generality.'* (*Aristotle*, 350 BC, 1137b).

Also, we could take the position that, based on tax-bearing capacity, the global digital service providers should not be considered identical to the established companies in all material aspects. Therefore, adopting the principle of vertical equity, the global digital service providers should not be taxed in the same way and to the same extent, but rather in an equitable manner adjusted to their specific characteristics and actual tax-bearing capacity. We will see that it represents a different approach to the desired taxation equity.

On a theoretical level, the principle of horizontal equity should be applied, excluding the possibility of tax optimization resulting from free choice of location. *'All tax optimizations are, in essence, manipulation, more strictly "fraud", as the taxpayer does not account for revenues and expenses at the place where they are incurred, using fictitious, distracted, deliberately shaped prices.'* (*Kocziszky, Kardkovács* 2019, p. 178). In respect of global digital services this situation is nuanced by the free choice of location for incurring revenues and expenses, which should be regulated so as to apply the principle of horizontal equity in practice. This, however, requires international consensus as to the content and level of equitable taxation.

According to the most common definition, equity is *'an objective that is related to the sharing or distribution of resources among individuals'*.<sup>3</sup> The above definition is interesting for two reasons. For one, the definition is focused not on the content, i.e. the purpose of equity itself but on the actual effort of setting objectives in the course of sharing and distributing resources. Therefore, this concept comes into the equation when the level of taxation is determined not only by balance of power but by higher purposes. The other interesting factor is that equity is determined in the light of the objective, which is necessary to decide whether or not the distribution of resources occurred equitably. *'It would be appropriate to supplement the above definition with the acceptance of the objective by the specific community, somehow like this: equity is an objective accepted by a community to be just in relation to the sharing or distribution of resources among individuals. This addition is in line with the widely accepted view that the concepts of equity and social justice are synonymous.'*<sup>4</sup> *According to this view, what society accepts as just, that is, it meets society's sense of justice, can be considered equitable. Of*

*course, the question remains what society and its individual communities consider to be just, as this can change significantly in space and time as well.'* (Pulay, 2017, p. 418)

Overall, it can be said that the equitable taxation of global DSPs requires solutions for two problems. First, the rules for connecting digital service revenues and expenses with the relevant countries should be developed. Second, it requires international consensus to establish the level of taxation to be applied to the profits of global digital service providers that can be distributed among these countries in an equitable manner. In the first case the distribution of expenses across countries can pose a bigger challenge therefore, as the second best solution, it is suggested that the global DSPs should pay a special tax in proportion to the revenues associated with the particular countries, which would more or less exempt them from income tax liability.

## WHY IS FAIR BURDEN SHARING A NEW CHALLENGE IN THE DIGITAL SECTOR?

The countries' problems experienced in realizing tax revenues are nothing new, but globalization and the rise of the digital economy pose a new challenge in combating tax avoidance. In the traditional economies with fixed geographical borders taxes are collected according to strictly defined rules and fairly accurate estimation of tax revenues. Budget spending is planned with relatively high precision based on the tax revenues of the traditional economy. The first challenge is globalization due to the natural state borders becoming blurred, making way for profit transfers among countries for tax optimization purposes, and base erosion in the national economies. The second challenge is due to the rise of global digital services, which require no specific location and therefore can be supplied

to numerous countries from any given site. Consequently, it requires no shifting of profits among multiple countries and locations either. For the sake of tax optimization these providers only need to select a site in a country that offers the most favourable tax conditions.

Therefore, in order to enforce a fair burden sharing for global DSPs the tax strategies and tax planning processes should be fundamentally reviewed including tax residency status, taxable entity, subject of taxation and calculation of tax base.

For the global digital service providers the world's countries are essentially divided into three categories according to their role in the international tax structure. The first category includes the 'market countries' where the customers of the global DSPs are located. The 'intermediate countries' are the ones whose taxation systems are used by the global digital service providers for tax optimization purposes. The third category includes the countries in which the ultimate parent companies of the global DSPs have tax residency status. All three types are important in the global DSP structure with the ultimate result that, on a global scale, these providers pay very low taxes on the profits generated (Varga, 2020). The real advantage of the global DSPs is due to the applied aggressive tax planning techniques which exploit the gaps in the different countries' tax systems to artificially reduce taxable income, or they shift profits to other countries offering very low tax rates where no or hardly any actual economic activity takes place (Erdős, 2019).

According to *Ahmad and Ribarsky* (2018) the emergence of global DSPs creates a new situation in taxation and makes it necessary to reinterpret the tax rules originally designed to business models based on physical presence. As *Erdős* (2019) explains, the global DSPs have developed an international tax structure in which taxable presence (physical sites) can be



avoided. It is in line with the view of Ahmad and Ribarsky (2018) by which both the clientele and the created economic value are typically in those countries where the global DSPs are not physically present. Due to lack of physical presence and income typically generated through intangible assets the global digital service providers fail to pay their share in most cases. Determining the place of taxable value creation, and interpreting and measuring the actual value of digital activity represent additional problems (Jakurty, 2017). Next, the above will be discussed in more detail.

## VALUE CREATION IN THE DIGITAL SECTOR

Unlike in the traditional economy, value creation by the global digital service providers is quite unique. As the activities of the global DSPs require no physical presence, the boundaries between providers and consumers become blurred. Discussing the process of value creation in the digital space, *Olbert and Spengel* (2019) argue that the levels of value creation are hard to identify due to the fact that value in the digital sector is generally created by a combination of algorithms, user data, functions and knowledge. Data represent a key element of the digital sector, though not all the collected data contribute to value creation. The process of value creation is based on the use and analysis of data and data quality. *Olbert and Spengel* (2019) defined this type of data analysis method as data mining. The actors of the digital sector generate income or profit by means of data mining. *Figure 2* shows that the process is based on the emergence of raw data from which the global digital service providers identify the relevant data for value creation purposes. This stage is followed by preprocessing and transformation in order to gain data that can be used for subsequent

analysis. The analysis of the transformed data can reveal patterns and models to be evaluated in order to achieve the ultimate goal, that is the knowledge of user preferences. The global digital service providers rely on this knowledge to sell services and realize profits.

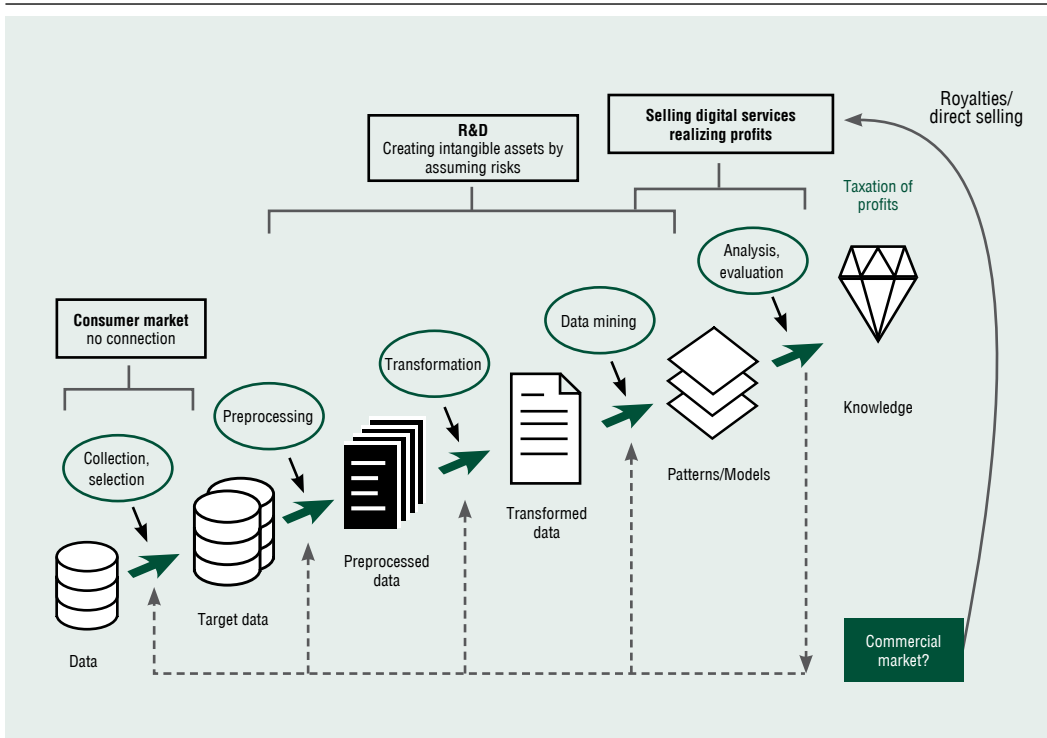
In respect of user preference knowledge and the resulting value creation and profits, *Vestager* (2019) expressed her view as *'we can get a lot of valuable online services free of charge, but there's no such thing as a free lunch.'*<sup>5</sup> *Vestager's* opinion refers to the fact that even the use of online services advertised as free can create substantial value for the DSPs. In exchange for these services we pay, if not in cash, then by means of our data and preferences.

This was recognized by the Hungarian Competition Authority (HCA) in December 2019 when it found that Facebook Ireland Ltd., as a global digital service provider, acted wrongfully by advertising services as free due to the fact that the consumers, although not required to pay any fees, ultimately generated profit for the company by means of user activity and data sharing, as a form of payment. In an article published on the case the HCA's view was that *'the essence of Facebook's (so-called zero-price) business model is to attract consumers with shared content on the site, whose interests, behaviour and shopping habits are ultimately collected. With this information, it sells targeted advertising to its business customers and delivers the ads to consumers by placing them between posts.'*<sup>6</sup> According to the position adopted by the HCA the messages displayed on the registration page, such as *'Free and anyone can join', 'It's free and always will be'* distracted consumer attention from the sort of compensation undertaken by registration and its consequences. As a result, the HCA imposed its highest ever penalty, HUF 1.2 billion on Facebook for consumer law infringement.

Consequently, as a new method of creating income for the global DSPs, the users of the

Figure 2

**PROCESS OF VALUE CREATION IN THE DIGITAL SECTOR THROUGH DATA MINING**



Source: Teski et al. (2020, page 12)

digital platforms provide their contribution by sharing preferences through social media. As for the profit generated in this manner, it does not necessarily materialise in burden bearing at the place of sharing, or where the advertising algorithms have been presumably developed. This means that the global digital service providers fail to recognise the users' contribution to profit (value creation) in tax payment.

In terms of public burden sharing the problem is further aggravated by the fact that the digital value creation processes can vary according to the given user preferences and the providers' business models, occurring in completely different ways. Some of the providers collect data after which the actual sale takes place, while others collect, select,

process and transform the user data for internal use and develop services using the information gained from them. Then again, some providers use the data mining process for developing products, therefore it is through these products that value is created and revenue is realized. Others use the entire data mining process to gain knowledge which they sell, rather than build into the products to earn profits. Taking all this into account, in order to enforce burden sharing the applied business models and the entire data mining processes of these providers need to be analysed and evaluated individually to establish the actual value created through activities. Burden sharing can be enforced after that (Olbert, Spengel, 2019).

The global digital service providers create data links through hardware devices, software



and technology (see Figure 3). The information gained by analysing them can be used as a basis for selling products and services. Links with the partner companies can generate turnover with revenues that can provide a base for value added taxation. In case of overall profitability, a tax on profits should be applied too.

### INTERNATIONAL PROPOSALS FOR TAXING THE DIGITAL ECONOMY

Due to uncertainty as to interpreting value, establishing the place of value creation and its measurement for tax base purposes, the global DSPs relatively pay much less tax on profits than the actors of the traditional economy, in addition to the fact that tax is not necessarily paid at the place of value creation. Therefore,

it means loss of tax revenue for numerous countries and competitive disadvantage for the actors of the traditional economy. As a consequence, these countries share an interest in preventing the possible tax avoidance of the global digital service provider companies.

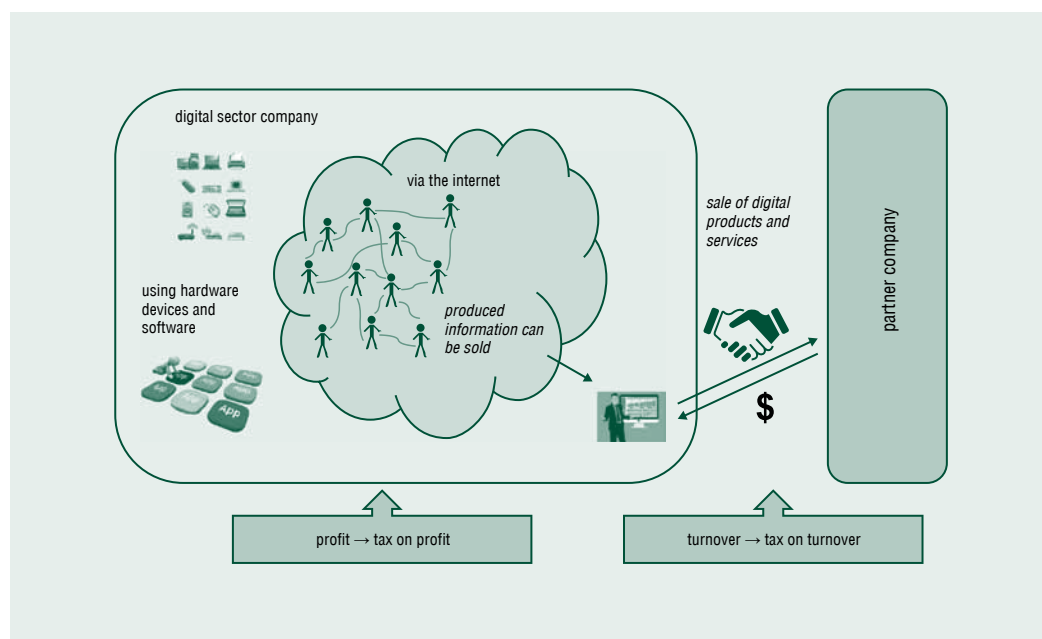
The OECD and the European Union, among others, raised a number of proposals in order to ensure fair competition and burden sharing.

### OECD PROPOSALS FOR TAXING DIGITAL SERVICES

The OECD project launched in 2013 on base erosion and profit shifting (BEPS) particularly focused on the challenges of taxing the digital economy. The OECD Ac-

Figure 3

#### VALUE CREATION IN THE DIGITAL SECTOR BASED ON SHARED USER PREFERENCE



Source: Teski et al. (2020, page 13)

tion Plan on Base Erosion and Profit Shifting consists of 15 actions essentially based on three main pillars:

- Improve the coherence of national rules relating to cross-border activities,
- Ensure taxation of value generated by economic activity according to place of value creation, and
- Improve transparency for businesses and governments.

Of the 15 actions set out in the project, Action 1 discusses the tax challenges of the digital economy. Based on the OECD proposals published in October 2015 the challenges of taxing global digital services can and should be addressed in the framework of Action 1, particularly by changing and harmonizing the rules relating to place of business, transfer pricing and controlled foreign companies. As regards place of business, a prohibition was proposed, among others, to avoid fragmentation of operations among multiple group entities to qualify for the exceptions to permanent establishment status for preparatory and ancillary activities. The proposed changes to transfer pricing rules aim, in particular, to prevent disproportionate allocation of profit via transfer of intellectual property and related rights. As for the rules relating to controlled foreign companies, they should cover also the income related to digital services. Although Action 1 addresses the specific problems identified so far, the global DSPs can easily change their structures in a way to avoid tighter regulation. The OECD is of the view that for the BEPS project to be really effective it is necessary to ensure collaboration and transparency for the tax administrations, as well as regular revision of the proposals (Varga, 2020).

In 2018 the OECD established the three main characteristics of highly digitized businesses that can pose the biggest challenge to international tax principles:

- Significant presence without actual physical presence in a specific country,
- Intangible assets typically represent a high percentage among the fixed assets of digital sector companies with increasing impact on value creation and the ability of the companies to determine their location across countries in a flexible way, potentially influencing the place of taxation,
- Data and user involvement are highly important: by extensive use of data the products and services of the businesses can be significantly improved; meanwhile, collection and analysis of user data creates profit.

In 2020 the OECD published a revised package of proposals to promote global consensus, essentially based on two pillars.

The first pillar aims to change the distribution of taxing rights in a way to assign profits partially to the market countries. Accordingly, taxing rights would be distributed based on three aspects:

- place of actual activity,
- place of operational management of marketing and technical functions,
- actual location of consumers.

The second pillar aims to introduce a global minimum tax to prevent tax avoidance by relocating certain activities to low-tax countries.

The proposal is likely to target global revenues exceeding EUR 750 million. The minimum tax rate is expected to be around 12.5 percent (OECD, 2020).

## ANALYSES AND PROPOSALS OF THE EUROPEAN UNION FOR TAXING THE DIGITAL ECONOMY

According to the position of the European Commission put forward in 2018 the mismatches between the Member States' tax

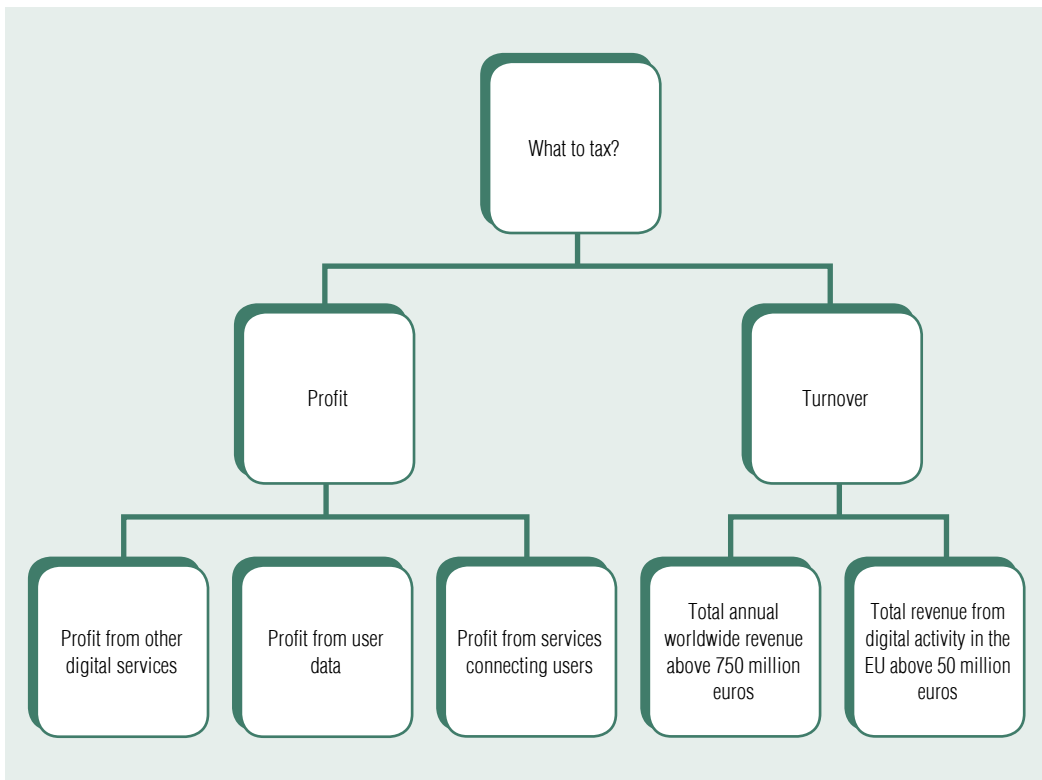
systems combined with the mobile, virtual nature of digital companies could reduce tax revenues even more than expected. Based on the principle supported by the EU, fair taxation should be an essential element of the European social and economic model. Loss of tax revenue and tax avoidance pose a risk to Member State functions, distort competition and undermine the relationship between citizens and state. As a further challenge, the tax competition among the Member States without harmonizing the digital sector taxation policies could harm the whole EU economy. Therefore, the European Commission developed two proposals: the first one for a common reform of the EU's corporate tax rules (profits), and the second

one to introduce interim tax on certain digital activities (turnover) (see Figure 4).

Proposal 1 would enable Member States to tax profits that are generated in their territory, even if a company does not have a physical presence there. The aim was to introduce the concept of 'significant digital presence or digital site' into the tax rules, and thereby to influence and change the definition of taxpayer. Based on the proposal a digital platform would be deemed to have a taxable digital presence in a Member State if it fulfils one of the following criteria: it exceeds a threshold of EUR 7 million in annual revenues in a Member State; it has more than 100,000 users in a Member State;<sup>7</sup> or it has over 3,000 business contracts

Figure 4

**PROPOSALS OF THE EUROPEAN COMMISSION CONCERNING FOCUS OF TAXATION**



Source: Self-edited based on the proposal of the European Commission for fair taxation of the digital economy (2018)

for digital services established in a taxable year (Varga, 2020).

The other proposal of the European Commission (2018) aimed to introduce an interim tax on certain revenues for digital activity. This would apply to services where user involvement in the digital activity provides a fundamental input. The tax would be based on revenues from the following services:

- Placement of digital adverts aimed at platform users;
- Sale of collected user data, or utilization of such data for business purposes;
- Provision of digital intermediary services which allow users to interact with other users and which can facilitate the sale of goods and services between them.

To be considered a taxable entity, the service provider should meet the following criteria:

- Total revenue reported for the last full financial year exceeding 750 million euros,
- Total taxable revenue in the EU for the fiscal year exceeding 50 million euros.

The tax rate for digital services was set at 3 percent which, based on calculations of the European Commission (2018), could generate additional EUR 5 billion in revenues annually.

The draft was hoped to be accepted before December 2018, but during the ECOFIN meeting in November it was rejected by several Member States. Tax decisions in the EU require unanimity of the Member States (Varga, 2020). According to the Council of the European Union (2020) digital taxation should preferably be addressed at international level in order to prevent fragmentation and unilateral measures.

## INDIVIDUAL SOLUTIONS INTRODUCED BY THE MEMBER STATES

The OECD's purpose in setting forth the above two pillars was to ensure a consensus by the end of 2020 aiming to transform the

global tax system, but it failed. The Member States of the EU exercise increasing pressure toward a solution. Individual efforts already have been made by some of the countries. The Member States deciding to take independent action typically focused on the proposal made by the European Commission for taxing digital services.

Italy and Austria introduced tax on digital services from 1 January 2020. In both Member States the tax applies to digital companies and company groups with worldwide revenues reaching 750 million euros. The practices of the two countries differ in terms of national level revenue and tax rate. The revenue threshold for digital companies and company groups is minimum 5.5 million euros in Italy, and minimum 25 million euros in Austria realized at national level. The tax rates applied in Italy and Austria are 3 percent and 5 percent, respectively. In Italy the scope of taxable activities covers digital advertising, running digital platforms based on social sharing, and transmitting user data collected from digital platforms. Austria applies a narrower scope, specifically targeting online advertising companies, but no other forms of digital services (Varga, 2020).

France re-introduced digital tax at the end of 2020, originally imposed on digital services in 2019 and suspended in January 2020 as a result of negotiations with the United States. The French solution fundamentally echoes the proposal of the European Commission, in line with the practices of Italy and Austria. In France the taxable entities include companies with a total revenue of EUR 750 million from digital services and EUR 25 million realized at national level. The applied tax rate is 3 percent. The scope of taxable activities includes digital services with provision of online advertising platforms as well as digital platforms facilitating user interaction in order to sell products and services.

Table 1

**ARGUMENTS FOR AND AGAINST DIGITAL TAXATION**

Arguments for introducing digital tax	Arguments against introducing digital tax
<ul style="list-style-type: none"> <li>▶ Current tax rules rendered obsolete in the digital environment.</li> <li>▶ Government revenues to increase.</li> <li>▶ Tax avoidance by global digital actors is less likely.</li> <li>▶ The competitive disadvantage of companies typically providing digital services locally would decrease.</li> <li>▶ Fair from the point of view of traditional economic players.</li> <li>▶ Sustainability of tax rules to improve.</li> </ul>	<ul style="list-style-type: none"> <li>▶ Tax competition due to individually introduced tax measures can be harmful.</li> <li>▶ Parent countries may consider countermeasures due to regulations adversely impacting their companies.</li> <li>▶ As for introducing tax on global DSPs independently, there are no indicators to support enforceability.</li> <li>▶ Increase in administrative burdens for both taxpayers and tax collectors out of proportion to expected initial tax revenues.</li> <li>▶ Tax enforcement requires continuous monitoring.</li> <li>▶ International agreement likely to be reached, no need to put effort into national solutions.</li> </ul>

Source: self-edited

In addition to the above listed Member States, the Czech Republic has a similar solution under way. Again, the Czech proposal sets forth a total revenue exceeding EUR 750 million (KPMG, 2019). However, the decision as to national level revenue and tax rate has not been reached yet. The threshold for national level revenue is expected to be around 5 million euros, and the tax rate between 5-7 percent. The new tax is likely to be introduced in July 2021 at the earliest (USTR, 2020).

**THE ASPECTS OF FAIR BURDEN SHARING BY GLOBAL DIGITAL SERVICE PROVIDERS IN RELATION TO HUNGARY**

The Member States introducing their own versions of the solution proposed by the European Commission typically plan to abandon them as soon as an agreement on digital burden sharing is reached at EU or OECD

level. Meanwhile, Hungary should also consider a national solution for taxing global digital services.

In that case it should be decided whether to focus on combating base erosion and profit shifting in general, or rather to introduce tax on digital services specifically. Moreover, the arguments for and against digital taxation, and the potential advantages and disadvantages should also be considered. *Table 1* provides a summary of the arguments for and against national level taxation to be introduced for global digital services.

**SUMMARY AND CONCLUSION**

In summary, it seems fitting to quote Aristotle once again: '(...) *This is the essential nature of the equitable: it is a rectification of law where law is defective because of its generality.*' (Aristotle, 350 BC, 1137b). Therefore, in

Aristotle's view, the laws applied generally are unfit to take into account specific instances, hence the need for equity, that is to extend the general rules in order to rectify legislative shortcomings. We agree. At the same time, if the instances not covered by law increase in number and become typical the law itself should be changed in a way to establish fair rules reflecting the principles of horizontal and vertical equity. The rise in global digital services has created a situation where the laws (international tax principles) should be changed by reinterpreting the concept of physical presence for these companies. The

issues discussed in this article make it clear that it is not an easy task, and it seriously harms the interest of the situation's current beneficiaries. However, the majority are interested not in this, but in a situation where the global digital service providers pay their share in proportion to the realized profits just like the traditional economic players, taxed in the country where the underlying value is created. The increasing contribution of the global digital service providers to world economic performance makes it even more urgent to change the current unfair taxation system.

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#### NOTES

- <sup>1</sup> This article is based on the authors' analysis prepared for and published at the website of the Hungarian State Audit Office; however, the article reflects the opinion of the authors.
- <sup>2</sup> In this context value means the measurable performance that ultimately generates profit.
- <sup>3</sup> Barr, N (2009), p. 583
- <sup>4</sup> Barr N. (2009) provides a brief summary of the different political and economic theory perspectives relating to social justice (Chapters 3-5). An excellent overview of the philosophical and economic interpretations of equity is given by Eszter Megyeri (2012).
- <sup>5</sup> Internets of the World Conference, Copenhagen, 5 December 2019, quote from Margrethe Vestager, Executive Vice President of the European Commission for A Europe Fit for the Digital Age.
- <sup>6</sup> [https://www.gvh.hu/en/press\\_room/press\\_releases/press\\_releases\\_2019/gvh-imposed-a-fine-of-eur-3.6-m-on-facebook](https://www.gvh.hu/en/press_room/press_releases/press_releases_2019/gvh-imposed-a-fine-of-eur-3.6-m-on-facebook) (downloaded: 20 March 2021, 14:51)
- <sup>7</sup> For a user to be considered as such in a given territory it should use a device to access a digital platform necessary for the provision of digital services in a specific tax territory and taxable period.

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