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U.K. Chancellor Announces New Digital Service Tax

By David Fang, J.D. Candidate 2021 | November 3, 2018

European governments grow increasingly concerned that major tech companies are not paying enough taxes to the countries they operate in. Critics argue that because revenue for tech companies is recorded based on where those services are created rather than where they are consumed, tech companies like Amazon, Facebook, and Google benefit from the European market without paying European taxes. For example, in 2017, Amazon earned £1.98B in revenue and £72.37M in profit in the U.K., but only paid £1.7 million in taxes, a 2.35% tax rate.

In response, recently the U.K. announced a 2% tax on digital services starting April 2020. Under the new provision, tech companies will be taxed if they have global revenues of at least £500M and are profitable. The U.K. was not the first to explore a digital services tax. The European Commission and the Organization for Economic Co-operation and Development (OECD) have been working on a uniform and long-term solution. They proposed a two pronged approach, first an interim digital service tax, and second, a long-term solution of taxes based on significant digital presence in a country. However, progress has been slow so the U.K. decided to act first.

Opponents of these new taxes argue that it will result in double taxation of revenue, a slowdown of international trade and development, and hurt smaller firms. They further argue that these digital service taxes come at a bad time with increasing global trade tensions and protectionist policies. Because mostly large U.S. tech companies will be affected by the U.K. tax, the U.S. government might interpret these new taxes as tariffs on American companies, which could spark retaliation. In addition, the more a U.S. company's profit is taxed in Europe, the smaller the taxable base in the U.S is. Ironically, these higher taxes may help U.S. tech companies establish stronger market positions in Europe by increasing the barrier to entry for competitors.

In a digital economy where borders are not a significant barrier for tech companies to operate and scale, technology is pushing governments to change what and how they tax. Therefore, it is important to revamp old assumptions such as where revenue is recognized and where a sale occurs to create effective taxation structures without driving away beneficial tech services.