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# Mission Recovery

How Big Tech's Tax Bill could  
kickstart a fairer economy

Report May 2021

# Contents

Introduction	3
Difficulties in taxing the Digital Economy	5
Why does this matter now?	8
Initial recommendations	10
What can countries do to tax big tech companies in the absence of a global tax deal?	11
Many urgent tax measures could help fund a post-Covid recovery	13
Tax on profits	14
Formulary Alternative Minimum Tax	14
Fractional Apportionment	15
Excess profit tax	17
Taxes on transactions	18
Withholding Tax on Digital Transactions	18
Digital Service Taxes	19
Conclusions and recommendations	21
Annex I: Methodology	22

Cover Image:

Orji is an unpaid nurse and midwife in a local hospital with no water source, no electricity and no government funding. Nigeria.

Photograph: Tom Saater/ActionAid

# Mission Recovery: How Big Tech's Tax Bill could kickstart a fairer economy

New research by ActionAid shows that G20 countries may be losing as much as US\$32bn annually in taxes from just five of the world's largest tech companies. That could have paid for a full two-dose Covid-19 vaccination for every human on earth.<sup>1</sup>

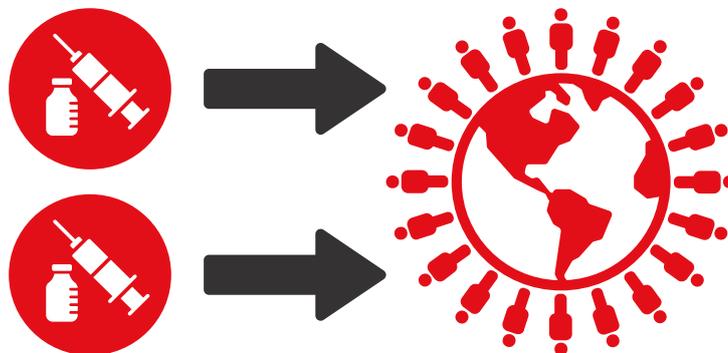
Alternatively it could have paid for hundreds of thousands of teachers and nurses in G20 countries, or millions of teachers and nurses in developing countries. More than US\$20bn of these potential tax losses are in G7 countries.

With public budgets under severe strain globally from the double whammy of increased spending during the Covid-19 pandemic and decreased tax receipts due to the economic downturn, it is more important for governments to ensure big tech companies pay their fair share of corporate income taxes. Big Tech companies and their owners have profited enormously during the ongoing pandemic, with the world's richest billionaires-many of whom have made their millions from tech companies – adding hundreds of billions of US dollars to their personal wealth since the crisis started.

ActionAid's research examined five of the world's largest tech companies (Alphabet, Amazon, Apple, Facebook and Microsoft) and the potential tax revenue that their market activity could generate, if the tax regime and resulting corporation tax bills better reflected these companies' economic presence worldwide. We do know that they pay some corporate income tax in some countries, but as these companies do not publicly report their exact tax payments in each jurisdiction, we do not know how much tax they actually pay and where they pay it. However, we do also know these companies are reportedly avoiding taxes in many countries.<sup>2</sup>

Taxes lost from five of the world's largest tech companies could have paid for

**two doses of  
Covid vaccination**  
for every human on Earth



<sup>1</sup> This is used to give a sense of the scale of resources involved in taxing big tech companies. In practice, vaccine provision should not need to be financed like this: agreeing a waiver of Trade Related Intellectual Property Rights (TRIPS) would be a much better way to ensure equitable access to vaccines worldwide

<sup>2</sup> See e.g. story about how Apple managed to make €110bn worth of income 'stateless' for tax purposes, i.e. no state has the right to tax it: <https://www.theguardian.com/commentisfree/2020/jul/16/eu-tax-avoidance-big-companies-ireland-apple-state-aid#:~:text=Apple%20was%20simply%20exploiting%20a,overturned%20the%20European%20commission%20ruling.>

Our research therefore shows the potential rather than the actual tax losses. At a time when governments are desperately looking for revenue to fund Covid-19 response expenses, not leveraging this potential tax resource is a missed opportunity.

If the companies covered by our research wish to publish details of any corporate income tax they actually do pay on a country-by-country basis we would very much welcome it.

### Potential tax losses from 5 of the world's largest tech companies<sup>3</sup>

#### Groups of countries

G20	US\$31.99bn
OECD	US\$27.97bn
G7	US\$20.77bn
EU27	US\$7.92bn

#### Other major economies

India	US\$1.54bn
Brazil	US\$1.57bn
China	US\$2.33bn
Russia	US\$838m
Indonesia	US\$810m

In terms of individual companies, the potential tax losses are:

Company	Groups of countries			
	G20	OECD	G7	EU27
Alphabet	US\$6.47bn	US\$4.11bn	US\$5.70bn	US\$1.81bn
Amazon	US\$2.12bn	US\$1.61bn	US\$2.10bn	US\$0.52bn
Apple	US\$8.38bn	US\$6.28bn	US\$7.59bn	US\$1.54bn
Facebook	US\$5.19bn	US\$3.26bn	US\$4.81bn	US\$1.45bn
Microsoft	US\$9.83bn	US\$5.51bn	US\$7.77bn	US\$2.60bn

<sup>3</sup> Potential tax loss calculated on the assumption that the companies are not paying any taxes.

# Difficulties in taxing the Digital Economy

The digital economy is difficult to tax for many reasons, including the difficulties in establishing exactly where profits are made.

Current global tax rules, already containing loopholes and provisions that make it possible for companies to shift profits and avoid taxes, were largely designed before the digital economy emerged and are badly equipped to deal with tax challenges in the 21st century. Through the so-called BEPS (base erosion and profit shifting) process at the OECD,<sup>4</sup> rich country governments have been trying to agree on ways to improve taxation of the digital economy and they are due to announce towards mid-2021 what the new rules for taxing the digital economy will be.

Early drafts of the new rules show that these rules won't do much to change the status quo or help governments raise substantially more revenue from the digital giants. This is disappointing, especially as our research

shows that OECD countries themselves may be missing out on as much as US\$28bn a year in tax revenues from the big five tech companies analysed in this report alone. It is not only rich countries that are missing out on revenue. Our research shows that proper taxation of the digital economy could raise substantial amounts of revenue in developing countries where additional funds are desperately needed to meet the financing needs of Covid responses.

Below is a selection of developing countries and the potential tax losses. While these numbers are generally smaller than those in OECD countries, this potential tax revenue would make a significant difference if invested in gender responsive public services as part of the post Covid-19 recovery.

## Potential tax losses from 5 of the world's largest tech companies

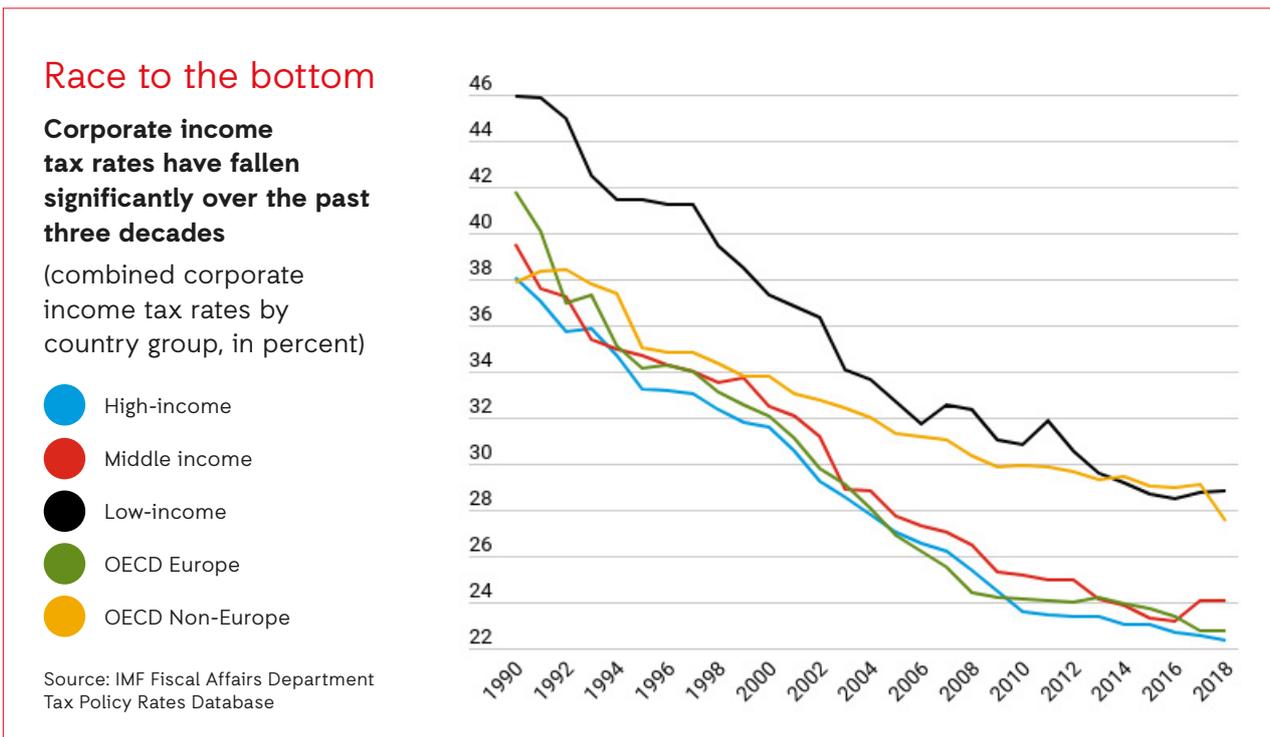
Country	Loss
Bangladesh	US\$49.3m
Ghana	US\$13.6m
Kenya	US\$18.5m
Nigeria	US\$103.2m
Senegal	US\$5.8m
Tanzania	US\$7.2m
Zambia	US\$3.5m
Zimbabwe	US\$2.4m

In 2021, largely as a response to the need for additional public funding to respond to the Covid-19 crisis, governments across the world have recognised that corporate income taxes are an important part of the funding mix for governments. For example, the UK has announced that corporate income taxes will increase in the coming years<sup>5</sup> to raise more revenue, as has the US, whose increase from 21% to 28% is hoped to raise an additional US\$2tn over the coming 15 years.<sup>6</sup> There has also been increased global consensus that a global minimum corporate income tax is needed. In April 2021, IMF's chief economist stated that 'we are very much in favor of a global minimum corporate tax,'<sup>7</sup> a sentiment echoed by the US Treasury Secretary Janet Yellen.<sup>8</sup>

This is in stark contrast to the prevailing narrative and policies over the past decades which has portrayed reductions in corporate income tax rates as necessary for stimulating economic growth with drastic decreases in rates in the last 30 years (See chart from the IMF below).<sup>9</sup>

A global minimum tax rate would apply to companies' overseas profits. Therefore, if countries agree on a global minimum, governments could still set their own corporate income tax rate. However, if companies pay a lower rate in another jurisdiction, their home governments could "top-up" their taxes to the agreed minimum rate. This could in theory decrease incentives for companies to shift profits to tax havens as they would have to pay the agreed minimum tax rate in their home country anyway.

The OECD negotiations have so far discussed a 12.5% minimum global rate, while the US has proposed introducing a 21% minimum global rate. While the US plan has been estimated to raise as much as US\$50bn extra in revenue,<sup>10</sup> this is money that would be raised for the US. A global minimum corporate income tax would not change the basic structure of taxing rights globally – i.e. that it is essentially the country where a company is headquartered that gets to tax its profits – and it would not tackle the specific challenges of the digital economy.



<sup>5</sup> See e.g. <https://www.cnbc.com/2021/03/03/uk-hikes-corporation-tax-to-25percent-as-pandemic-supports-hits-407-billion.html>

<sup>6</sup> See e.g. <https://www.reuters.com/article/us-usa-biden-taxes-factbox-idUSKBN2BN3NU>

<sup>7</sup> See <https://www.reuters.com/article/us-imf-world-bank-idUSKBN2BT1NG>

<sup>8</sup> See <https://www.cnbc.com/2021/04/05/yellen-to-push-for-global-minimum-tax-on-corporations.html>

<sup>9</sup> See <https://blogs.imf.org/2019/07/15/corporate-tax-rates-how-low-can-you-go/>

<sup>10</sup> See e.g. <https://www.taxpolicycenter.org/taxvox/oecd-pillar-2-provides-good-model-biden-us-worldwide-tax>

This means that highly profitable companies in the digital economy would not necessarily pay more tax outside the country where they are headquartered, for example in developing countries where they operate and make money as a result of a global minimum corporate income tax.

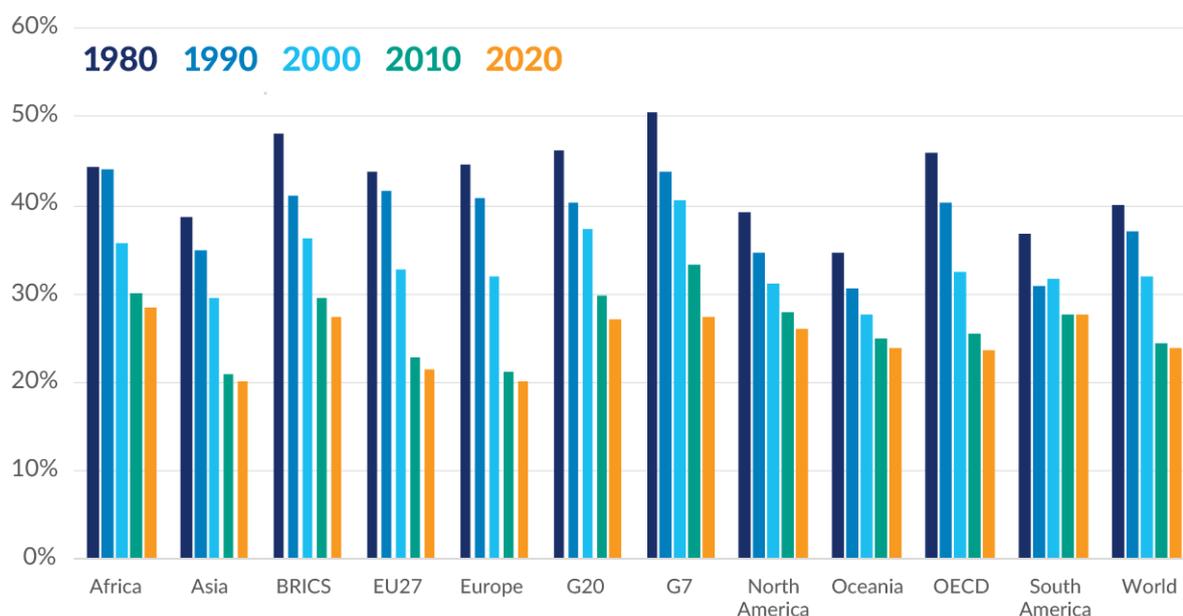
The 12.5% rate under discussion and even the 21% rate are also too low. A minimum global rate risks quickly becoming a de facto rate that countries around the world adjust to, meaning that corporate income tax rates could in some countries end up being lowered as a result of such reforms. ActionAid recommends a minimum rate of at least 25% to ensure that a policy meant to raise more revenue does not end up actually raising less revenue in some countries.

This minimum rate is widely agreed on by for example leading economists as part of the Independent Commission for the Reform of International Corporate Taxation (ICRICT).<sup>11</sup> It is also worth noting that up until a few decades ago, corporate tax rates of more than 30% and sometimes even 40% were the norm (see chart below from the Tax Foundation).<sup>12</sup>

Whilst we welcome an increased focus on reversing a race to the bottom on corporate income tax rates through the introduction of a global minimum rate, we maintain that this is not the silver bullet to addressing the challenges of taxing the digital economy and raising much needed additional revenue in developing countries.

## Corporate Tax Rates Have Declined in Every Region over Time

Average Statutory Corporate Income Tax Rate by Region and Decade



Note: The number of countries included in calculated averages varies by decade due to missing corporate tax rates for years prior to 2020; that is, the 1980 average includes statutory corporate income tax rates of 74 jurisdictions, compared to 177 jurisdictions in 2020. Source: Statutory corporate income tax rates were compiled from various sources. Tax Foundation.

<sup>11</sup> See p. 3 <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5ee79779c63e0b7d057437f8/1592235907012/ICRICT+Global+pandemic+and+international+taxation.pdf>

<sup>12</sup> See <https://taxfoundation.org/publications/corporate-tax-rates-around-the-world/#Trends> for more information

# Why does this matter now?

Taxing the digital economy is difficult in part due to how hard it can be to assess where profits should be taxed, and in part because international tax rules were designed a long time ago, before the digital economy took off. So action to ensure that the companies in the digital economy, and especially big tech companies, pay fair tax, is much overdue.

Many big tech companies have actively tried paying as little tax as they can, stretching laws and regulations to their limit to do so. In 2016, the European Commission concluded that Apple had used complicated corporate structures to make €110bn worth of sales 'stateless' for tax purposes, i.e. no country had the right to tax that income.<sup>13</sup> Meanwhile, in 2020 the US tax authorities sued Facebook for US\$9bn in unpaid taxes based on the way the company shifted profits around the world to minimise tax bills.<sup>14</sup>

The ongoing Covid-19 crisis has also highlighted the need for additional public funds. In fact, our research shows that the potential tax losses in G7 countries could have paid for tens and thousands of additional key public sector workers in those countries.

The Covid-19 crisis has hit women and girls particularly hard. The economic crisis has hit frontline public workers and those with low job security – predominantly women – particularly



The Covid-19 crisis has hit women and girls particularly hard. Anjana works as an agricultural laborer. When the lockdown was implemented, there was no work, which means no earning for the family. 'I cannot think of anything I could do. I cannot even buy a packet of biscuit for my children.'

Photograph: Sabin Shrestha/ActionAid Nepal

<sup>13</sup> See <https://www.theguardian.com/commentisfree/2020/jul/16/eu-tax-avoidance-big-companies-ireland-apple-state-aid#:~:text=Apple%20was%20simply%20exploiting%20a,overturned%20the%20European%20commission%20ruling.>

<sup>14</sup> See <https://www.theverge.com/2020/2/19/21144291/facebook-irs-lawsuit-9-billion-taxes>

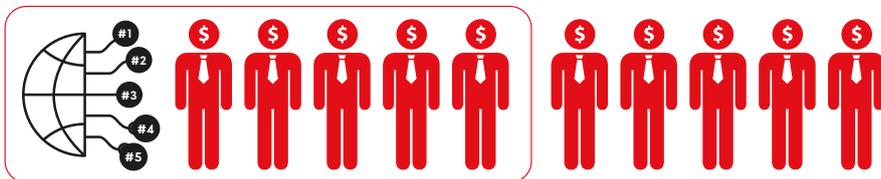


Students returning to school in Kampong Thom, Cambodia, after Covid lockdowns. 'During Corona pandemic, my school was closed and I did miss everyone at school. Now, I am so happy to resume school to meet teacher and classmates.' Chita  
 Photograph: Mr. Sokin Chhuoy & Ms. Tom Mao/ActionAid

hard. The temporary or long-term closure of schools in up to 192 countries<sup>15</sup> placed additional care burdens on women around the world and girls are less likely than boys to ever return to school, owing to domestic pressures, child labour, early marriage or early pregnancy.<sup>16</sup>

During the Covid-19 crisis, inequality has also widened, with those profiting from the Big Tech companies drastically increasing their wealth.

According to the Forbes billionaire list for 2021,<sup>17</sup> the top 10 richest people in the world are all men and five of them have made their fortunes primarily from the five big tech companies covered by this briefing. It is clear that the Covid-19 crisis is hitting different segments of society very differently, and this only increases the urgency of ensuring big tech companies, and companies operating in the digital economy more widely, pay their fair share of tax.



According to the Forbes billionaire list for 2021, **the top 10 richest people in the world are all men** and five of them have made their fortune primarily from the five largest tech companies

<sup>15</sup> UNICEF UNICEF Executive Director Henrietta Fore's remarks at a press conference on new updated guidance on school-related public health measures in the context of COVID-19

<sup>16</sup> Girls hardest hit by Covid-19 school closures – as teachers report spike in early marriage and teen pregnancies | ActionAid International

<sup>17</sup> See <https://www.forbes.com/billionaires/> (retrieved May 2021)

# Initial recommendations

ActionAid supports a global minimum corporate tax rate of at least 25% but believes that specific measures are needed to ensure that companies operating in the digital economy, especially the big tax giants, pay their fair share of tax.



Mona Desir is a nurse in Haiti who gives free treatment to those in need. Haiti. *Photograph Fabbienne Douce/ActionAid*

We also believe that many of the problems that countries have today in ensuring that the tech giants, but also multinational companies in general, pay their fair share of taxes and do not engage in tax avoidance could be solved by a more unitary approach to taxing companies, treating big multinationals as one unit rather than a group of separate entities, and allocating taxing rights based on where economic activity takes place, rather than where companies choose to book their profits.

However, whilst a satisfactory multilateral solution would be better – preferably one negotiated at the UN with all countries participating on an equal footing – developing countries in particular but also richer countries need to act swiftly to ensure that companies in the digital economy pay their fair share of taxes in their jurisdictions – particularly in the context of the economic crisis triggered by Covid-19.

Our specific recommendations are:

- For a global minimum corporate tax rate of no less than 25% to be introduced, without loopholes that would allow companies to have a lower effective tax rate;
- For countries to introduce unilateral measures to ensure that companies operating in the digital economy pay their fair share of tax in the absence of a satisfactory multilateral deal (see next section for specific options for such unilateral measures);
- For countries to generally take a more unitary approach to taxing multinational companies, including big tech companies (see page 12 for more details on unitary taxation);
- For discussions and negotiations regarding international tax rules and regulations to be moved to a truly global forum such as the UN.

# What can countries do to tax big tech companies in the absence of a global tax deal?

Each year, hundreds of billions of US dollars are lost to tax avoidance. For example, a study by the Tax Justice Network in late 2020 estimated that around US\$245bn are lost annually to tax abuses,<sup>18</sup> while an IMF study has estimated that revenue losses to corporate tax abuses could be up to US\$600bn a year.<sup>19</sup> The five companies we have studied are thus just a part of an overall picture of the global tax gap that needs to be rectified.

While some efforts are being made at national and international levels to address the legal frameworks that make it possible for companies to avoid paying their taxes, it has proved particularly difficult to address tax avoidance within the digital economy. In fact, EU figures show that digital companies' effective tax rate at 9.5% compared to 23.2% for companies with traditional business models.<sup>20</sup>

The latest proposals in the so-called "BEPS 2.0" process which focuses mainly on taxing the digital economy<sup>21</sup> do contain some positive elements including finally proposing at least a partial formulary apportionment and recognizing the need for a minimum global corporate income tax rate, but it does not go far enough to make a significant difference, especially for developing countries. It is also uncertain whether even the proposals currently on the table will get sign off from OECD members.

The process leading to the current proposals has been flawed. While the OECD/G20 Inclusive Framework on BEPS is open for all countries to participate in, the conditions of joining and the practical participation made it hard for lower income countries to participate on a truly equal footing and many low-income countries did not take part in the process.

This emphasises the need for global tax reform processes to take place under the auspices of the UN.

Ideally, countries will – under the auspices of the UN and with all countries participating on an equal footing – be able to agree on a global deal to address tax avoidance within the digital economy and provide clear rules for how to tax the digital economy which provides both certainty and ultimately revenue for governments. Such a deal is unlikely in the short run, and given the Covid-19 pandemic and economic crisis that it has induced, countries cannot wait any longer to start collecting their fair share of tax from multinationals, especially from the digital giants. There are various measures that countries can apply unilaterally or in regional blocks to collect more tax from multinationals in the absence of a fairly negotiated global deal. None of them are perfect and they will not replace a global solution, but in the meantime, they can provide revenue for countries and increase the impetus for countries to co-operate to find a good global solution.

**It has proved particularly difficult to address tax avoidance within the digital economy**

<sup>18</sup> See [https://taxjustice.net/wp-content/uploads/2020/11/The\\_State\\_of\\_Tax\\_Justice\\_2020\\_ENGLISH.pdf](https://taxjustice.net/wp-content/uploads/2020/11/The_State_of_Tax_Justice_2020_ENGLISH.pdf)

<sup>19</sup> See e.g. <https://www.ictd.ac/blog/estimating-tax-avoidance-new-findings-new-questions/>

<sup>20</sup> See e.g. [https://ec.europa.eu/taxation\\_customs/sites/taxation/files/factsheet\\_digital\\_taxation\\_21032018\\_en.pdf](https://ec.europa.eu/taxation_customs/sites/taxation/files/factsheet_digital_taxation_21032018_en.pdf)

<sup>21</sup> See e.g. <https://www.oecd.org/tax/beps/beps-actions/action1/>

## Unitary taxation

Under a unitary tax approach, governments treat a multinational corporation as a group made up of all its local branches, instead of treating each local branch as an individual entity separated from the global chain of companies. The company is treated like a unit, thus the name 'unitary' taxation.

The profits that the multinational corporation declares as a group would then be apportioned to each jurisdiction where it operates based on how much of its real economic activity took place in that country. Real economic activity can be based on economic factors such as e.g. sales, users, assets, staff numbers etc.

Unitary taxation is beneficial to both tax authorities and business. Once the factors to take into account when deciding where profits should be taxed are agreed upon, it is easy to calculate how much tax should be paid where. This provides companies with greater certainty and would remove the incentive to spend money and resources on shifting profits around between subsidiaries to avoid paying tax in particular countries.

The removal of incentives to shift profits and avoid paying taxes would also greatly benefit tax authorities, which would get a more predictable stream of revenues and, overall, tax revenues would also increase in the countries where economic activity actually takes place.

# Many urgent tax measures could help fund a post-Covid recovery

There are many different models for how countries can ensure that tech giants and the digital economy are properly taxed. Some are already in place in some countries, while others provide new solutions to the problem at hand.

The fact that many countries have already taken unilateral measures and that, for example, the EU is exploring a digital levy to complement whatever deal is struck at the OECD, shows that there is scope for countries to consider and ultimately to implement unilateral measures.

The measures discussed in this briefing vary in terms of ease of use, their revenue generation potential, their impact on developing countries and how difficult they would be to introduce legally and politically. This report offers a brief overview and assessment of some of the main policy options that countries have for taking unilateral measures to tax the digital economy, however it is worth noting that there are also other options that countries could consider.

ActionAid does not necessarily favour one or another, but rather recommends that countries consider what works best in their particular context, keeping in mind that measures should: raise more revenue; protect small businesses; be designed to restrict companies' ability to easily pass on additional costs to consumers; and also make tax avoidance harder. Long-term, we would like to see a convergence of measures, accompanied by a global deal.

## Measures should:

- Raise more revenue,
- Protect small businesses,
- Restrict companies' ability to easily pass on additional costs to consumers,
- Make tax avoidance more difficult for companies

The measures outlined below can broadly be divided into two categories – those that tax profits, and those that tax transactions.

The advantage of the proposed taxes that target profits is that they do not impact on unprofitable businesses, including start-ups or fast-growing innovative companies that are yet to turn a profit. However, as companies have developed sophisticated strategies to shift profits between jurisdictions and in some cases even managed to create 'stateless income,' and as the digital economy provides ample opportunity for moving and hiding profits compared with the traditional economy, introducing unilateral profit taxes could have shortcomings.

Transaction taxes on the other hand risk bluntly targeting all businesses regardless of size and profitability, and depending on how the tax is designed, the cost burden could be passed on by companies in the digital economy to consumers. These taxes are however generally easier to administer and provide a more predictable revenue stream for governments. Neither unilateral profit nor transaction taxes are therefore ideal in taxing the digital economy, but in the absence of a satisfactory global deal and as long as multinationals continue to engage in tax avoidance, they are the best option on the table for countries in the short to medium term.



# Tax on profits

## Formulary Alternative Minimum Tax

A Formulary Alternative Minimum Tax (FAM Tax) uses formulary apportionment<sup>22</sup> to allocate a portion of the total group profits to group members located in a specific country which applies the FAM Tax. The FAM Tax would be based on a formula incorporating key factors reflecting economic activity (such as sales revenue, employment and assets). The minimum tax could be set at e.g. 80% of the regular corporation tax rate and would be payable if it exceeds the jurisdiction's regular corporation tax payable based on the MNE's local income as determined under conventional arm's-length transfer pricing methods.<sup>23</sup>

Such an alternative minimum tax regime could be enacted as domestic legislation without impacting existing multilateral agreements and commitments to the arm's-length principle,<sup>24</sup> including the OECD transfer pricing guidelines. Moreover, it would contribute towards moving to a more unitary global taxation system.

### Formulary Alternative Minimum Tax

To what extent does it address tax avoidance?	If applied unilaterally, the FAM Tax does not address the root causes of base erosion and profit shifting. If however applied more widely on a regional or even global level, it could play an important role in ensuring that tax is paid where real economic activity takes place.
What is the impact on developing countries?	As most assets and employment is not located in developing countries, they would mainly benefit from the sales part of the formulary apportionment. This might limit how much would be payable under the FAM Tax, unless a substantial amount of back end services were performed in the developing country, thus attracting a greater share of the company's total profits.
What is the revenue potential?	The revenue potential is biggest in developed economies where big tech companies have their assets and with big consumer/user markets.  The revenue potential is more limited in developing countries but could nevertheless raise some extra revenue and discourage tax avoidance.
How feasible is it to introduce technically, politically, legally and socially?	A FAM tax could be enacted as domestic legislation without the affecting existing multilateral agreements and commitments.  It might however cause double taxation if applied unilaterally unless appropriate tax credits are recognised.

<sup>22</sup> Formulary apportionment is a method of allocating profit earned (or loss incurred) by a corporation or corporate group to a particular tax jurisdiction in which the corporation or group has a taxable presence. Under formulary apportionment, a multinational corporation would thus locate its profits across countries based on e.g. its sales, payroll, and capital base in each jurisdiction.

<sup>23</sup> <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5a78e6909140b73efc08eab6/1517872798080/ICRICT+Unitary+Taxation+Eng+Feb2018.pdf> p12

<sup>24</sup> The arm's length principle means that the price charged in a transaction between two related parties (such as two subsidiaries within the same multinational company) should be the same as the price charged in a comparable transaction between two unrelated parties

## Fractional Apportionment

Fractional Apportionment is one of the options that have been advanced by the OECD in their work on taxing the digital economy.<sup>25</sup>

Fractional apportionment attempts to share all of the MNCs group profits amongst eligible jurisdictions. The fractional apportionment method involves the determination of the amount of profits subject to digital taxes without making any distinction between routine and non-routine profit.

In taxing digital businesses, fractional apportionment would consider the following steps:

1. Determining the profit (tax base) to be allocated.
2. Selecting the appropriate allocation key, including capturing remote digital activity to decide how much of the profit should be allocated to each jurisdiction for tax purposes<sup>26</sup>
3. Once the overall tax bases has been established and apportioned between jurisdictions, the relevant tax rates in that jurisdiction will be applied.

Fractional Apportionment	
To what extent does it address tax avoidance?	In theory, a sales-based formula for apportioning taxing rights is less likely to result in tax planning strategies as e.g. customers are less mobile than companies.  Depending on the way each country designs its apportionment formula (provided it is not designed and implemented in a uniform manner globally), companies may still have incentives to move activities to a jurisdiction where the apportionment between e.g. sales, revenue, staff numbers etc is more favourable to that particular business.
What is the impact on developing countries?	Determining allocation key and apportionment formula is a challenge of the fractional apportionment method. Different sectors or types of companies, depending on their characteristics, might require different formulas. This means that depending on the formula chosen and the size of different economic sectors in a developing country, the net impact on revenues might be very uneven.
What is the revenue potential?	The revenue potential is greatest in richer countries with larger consumer markets and where a lot of companies currently have assets and staff based. The revenue potential in developing countries is more limited.
How feasible is it to introduce technically, politically, legally and socially?	Fractional apportionment would be compatible with most tax treaties, but nevertheless attention would need to be paid to avoiding double taxation. It is however reliant on the assumption that information on the allocation keys is reliable and accurate.

<sup>25</sup> See e.g. <https://www.oecd.org/tax/beps/programme-of-work-to-develop-a-consensus-solution-to-the-tax-challenges-arising-from-the-digitalisation-of-the-economy.pdf>

<sup>26</sup> Selecting an allocation key entails allocating costs of a service provider among other related entities including those with the most remote areas for the purposes of computing the arm's length fee under the cost-plus method using an indirect charge approach. The allocation key may be a quantity such as turnover, employee numbers, working hours.

## Case study: India Significant Economic Presence Rule and Consequent Formulary Apportionment

Through its Finance Act of 2018,<sup>27</sup> India introduced the concept of Significant Economic Presence (SEP), which entails taxing Multi-National Corporations that do not have a physical presence in India yet have significant economic activity there. The SEP is based on two alternative threshold elements: the number of users and the amount of revenue generated in India above specific thresholds. If either of these elements are met, India asserts its right to tax the company operating in the digital economy.

A 2019 report by India's Central Board of Direct Taxes suggested a 'fractional apportionment' method to tax MNCs. In the proposed method, the Indian profits are arrived at by multiplying

the MNC's Indian revenue with its global operating profit margin. If the MNC makes a loss at global level, the global profit margin is deemed at 2%.

The allocation keys selected in India's Fractional apportionment include sales, assets, employees and users. This was arrived at considering both supply and demand factors affecting the profitability of businesses. The proposed weightings differ depending on the 'user intensity' of the business models while users are assigned a weight of 10% in cases of low and medium user intensity, while each of the other three factors should be assigned a weight of 30%.<sup>28</sup>

<sup>27</sup> See <http://egazette.nic.in/writereaddata/2018/184302.pdf/>

<sup>28</sup> See [https://www.incometaxindia.gov.in/news/public\\_consultation\\_notice\\_18\\_4\\_19.pdf](https://www.incometaxindia.gov.in/news/public_consultation_notice_18_4_19.pdf)

## Excess Profit Tax

Excess profit taxes are, as the name suggests, taxes on the “excess” profits of large companies, i.e. profits that are for some reason abnormal and above what could be expected by companies in certain sectors at certain times.

It can be applied to the profits above a certain threshold, e.g. a certain rate of return or average profits in non-crisis years. This type of tax was applied in the UK and US during the first world war and similar measures were introduced during and after the second world war in these and some other countries. During the ongoing Covid crisis, certain companies have made huge profits<sup>29</sup> which combined with the dire

need for additional government funding has once again made the issue of excess profits relevant. There is however a question about how countries should attribute these excess profits and the resulting tax revenues. One option is to use a formulary approach, based on e.g. sales, employees, assets etc.

The tax would affect only very profitable companies, not affecting their routine profits or other companies. It would be a progressive tax and would only affect companies that can genuinely afford to pay it, as opposed to e.g. revenue taxes that would affect all companies, regardless of profitability.

Excess Profit Tax	
To what extent does it address tax avoidance?	This tax would not directly address tax avoidance as it does not affect routine profits, though a formulary apportionment approach to assigning taxing rights could go some way towards discouraging companies from booking their excess profits in tax havens.
What is the impact on developing countries?	As most companies that would likely be affected by an excess profit tax are resident in richer countries, developing countries would only benefit properly if a formulary apportionment approach was adopted. As routine profits are not affected, the overall allocation of taxing rights would also remain largely unaffected.
What is the revenue potential?	In certain countries, including the US, the revenue potential is huge.
How feasible is it to introduce technically, politically, legally and socially?	When applied unilaterally, it could lead to double taxation. If applied only in one or few countries, might encourage relocation of companies to countries without such a tax.

<sup>29</sup> See e.g. <https://www.brookings.edu/blog/the-avenue/2020/12/22/amazon-and-walmart-have-raked-in-billions-in-additional-profits-during-the-pandemic-and-shared-almost-none-of-it-with-their-workers/>

# Taxes on transactions

## Withholding Tax on Digital Transactions

Withholding taxes on digital transactions are one of the short to medium-term options for taxing the digital economy that has been introduced or considered by a number of countries such as India,<sup>30</sup> Kenya,<sup>31</sup> Vietnam<sup>32</sup> and Pakistan. They vary widely in the scope of their taxable base and who is liable to make the payment across countries.

Withholding taxes<sup>33</sup> on digital transactions are typically imposed on income from services delivered electronically. Withholding taxes are accompanied by source country<sup>34</sup> rules that clarify what economic activity is considered to take place within that jurisdiction and is therefore taxable within that jurisdiction. While most of what is targeted is advertising, other services that are sometimes covered include website maintenance, online movies, online music, online games etc. The responsibility for withholding the tax is usually on the consumer directly

or on the financial institution facilitating the transaction. For example, India introduced a form of Withholding Tax on digital transactions in 2016 through the Equalization Levy at 6% on certain online advertising and related services with a threshold of 100,000 rupees (around US\$1380), for non-resident companies. The Finance Act 2020 amended the Finance Act 2016, to expand the scope of the Equalization levy introducing a 2% tax on income received/receivable by an e-commerce operator from the supply of e-commerce services. Considering the threshold of 20 million rupees (around US\$260,000), all large global e-commerce platforms catering to Indian customers are likely to be covered (unless transacting through a tax resident entity in India or a permanent establishment in India).<sup>35</sup>

The Equalization levy of 6% is thought to have raised over US\$551 million in taxes from 2016 to end of 2020.<sup>36</sup>

### Withholding Tax on Digital Transactions

To what extent does it address tax avoidance?	It doesn't address tax avoidance as such, rather it ensures that companies and/consumers pay a certain amount of tax regardless of whether they try to avoid taxes or not. The burden of withholding taxes are easily passed on to customers.
What is the impact on developing countries?	This tax could help raise more money for developing countries if they apply it. However, as it is effectively a revenue tax rather than a profit tax, it may negatively impact on new and smaller businesses in developing countries that are not yet profitable, while global tech giants would more easily be able to absorb the additional costs, or pass them on to customers. One solution to this is to introduce thresholds so at least smaller businesses are not affected by this tax. That doesn't however solve the problem of larger businesses that are not profitable being affected by this tax. There is also a risk that the extra cost to the companies are simply passed on to customers through price rises, which could negatively impact access to technology and information plus raise the general cost of living for people in developing countries.
What is the revenue potential?	Depending on how the tax is designed and which transactions it applies to, this tax has a significant revenue potential.
How feasible is it to introduce technically, politically, legally and socially?	There is a risk of double taxation if credits of corporate tax are not available.

<sup>30</sup> See e.g. India Pushes Digital Taxes Amid the Coronavirus Crisis | Tax Foundation

<sup>31</sup> See e.g. Kenya Sets The Stage For Implementation Of The Digital Services Tax – Tax – Kenya (mondaq.com)

<sup>32</sup> See e.g. Vietnam implements taxation of digital transactions | EY – Global

<sup>33</sup> A withholding tax is a deduction (from e.g. wages, fees, or dividends) levied at a source of income as advance payment on income tax

<sup>34</sup> A source country is generally where income is earned and economic activity takes place, while a residence country is the country where a company is resident for tax purposes

<sup>35</sup> See Equalisation Levy | EY <https://cleartax.in/s/equalisation-levy>

<sup>36</sup> See India collected Rs 4,000 crore 'Google Tax' since 2016 | Business Times <https://www.businesstoday.in/current/economy-politics/india-collected-rs-4000-crore-google-tax-since-2016-rs-1100-crore-in-fy20/story/410545.html>

## Digital Service Taxes

The OECD estimates that there are currently over 40 countries that are considering or have put in place a Digital Services Tax as a form of unilateral measure to tax the digital economy.<sup>37</sup> Digital Services Taxes (DST) are taxes that are imposed on gross revenues of businesses selling eligible digital services to consumers located within a specific jurisdiction. The definition of eligible digital services varies across jurisdictions. Common taxable services include video streaming, search engines, online advertising, digital marketplaces and booking platforms.

Implementation of digital service taxes generally, differs amongst countries, while some restrict them to cross border transactions, others widen them to both national and cross border transactions. In cases where thresholds for domestic and global minimum revenues are defined, the DST is charged on the gross revenue of companies.

Below are some of the examples of how digital service taxes are implemented in different countries (all figures in US dollars based on early 2021 conversion rates)

Country	Tax Rate	Scope	Global Revenue Threshold	Domestic Revenue Threshold
France	3%	<ul style="list-style-type: none"> <li>Provision of a digital interface</li> <li>Advertising services based on users' data</li> </ul>	US\$840m	US\$28m
Spain	3%	<ul style="list-style-type: none"> <li>Online advertising services</li> <li>Sale of online advertising</li> <li>Sale of user data</li> </ul>	US\$840m	US\$3m
United Kingdom <sup>38</sup>	2%	<ul style="list-style-type: none"> <li>Social media platforms</li> <li>Internet search engine</li> <li>Online marketplace</li> </ul>	US\$638m	US\$32m <sup>39</sup>
Kenya <sup>40</sup>	1.5%	Income accruing through a "digital marketplace", being a platform that enables the direct interaction between buyers and sellers of goods and services through electronic means	Not specified	Not specified
Nigeria <sup>41</sup>	30% <sup>42</sup>	<ul style="list-style-type: none"> <li>Streaming and downloading of digital content to anyone in Nigeria;</li> <li>transmission of data collected about users in Nigeria;</li> <li>goods or services directly or indirectly through a digital platform</li> <li>provision of intermediation services via digital platforms, websites, or other online applications that link suppliers and customers</li> </ul>	Not specified	US\$65K <sup>43</sup>
Zimbabwe <sup>44</sup>	5%	Gross income from satellite broadcasting services in respect of the provision or delivery of television or radio programs, and on e-commerce operators providing or delivering goods or services to persons resident in Zimbabwe.	Not specified	Revenue in excess of US\$500K
Sierra Leone <sup>45</sup>	1.5%	digital and electronic transactions and sales on the universal income derived by a resident taxpayer in Sierra Leone	Not specified	Not specified

<sup>37</sup> 11th Meeting of the OECD/G20 Inclusive Framework on BEPS(Day 1) [Video file]. Retrieved from <https://www.youtube.com/watch?v=hEJqRHkLQa8/>

<sup>38</sup> <https://www.bdo.global/en-gb/microsites/digital-services-taxation/taxation-of-the-digital-economy/>

<sup>39</sup> <https://kra.go.ke/en/helping-tax-payers/faqs/digital-service-tax-dst>

<sup>40</sup> <https://www.taxathand.com/article/15137/Egypt/2020/Digital-services-tax-in-AfricaThe-journey-so-far>

<sup>41</sup> Included in gross income for CIT purposes

<sup>42</sup> This is the threshold defined for having significant economic presence in the Companies Income Tax (Significant Economic Presence) Order 2020 (SEP Order)

<sup>43</sup> <https://www.taxathand.com/article/15137/Egypt/2020/Digital-services-tax-in-AfricaThe-journey-so-far>

<sup>44</sup> <https://mof.gov.sl/wp-content/uploads/2021/01/The-Finance-Act-2021.pdf>

Digital Service Taxes	
To what extent does it address tax avoidance?	This tax does not directly address tax avoidance but rather ensures that companies pay tax regardless of their tax strategies.
What is the impact on developing countries?	This tax could have a positive impact on developing country revenues. Without thresholds, it could however also create barriers to entry for new and growing businesses from developing countries that are not yet profitable but are liable to pay the tax nonetheless. For instance the DST introduced in Sierra Leone in 2021 charges 1.5% on all sales to resident taxpayers regardless of the size of the sales and profitability.
What is the revenue potential?	The revenue potential is highly dependent on how the tax is designed. High thresholds will ensure only the largest businesses will be affected, but will also limit revenues. Similarly, lower rates will lower the risks of disadvantaging companies with no or low profits who are less able to absorb the extra costs but will also limit the revenue potential.
How feasible is it to introduce technically, politically, legally and socially?	Without proper tax credits, there are risks of double taxation.

# Conclusions and recommendations

It is clear that a global reform of international corporate taxation is needed, one which has been negotiated by all countries on an equal footing and which fully addresses the realities of the digital economy to ensure that all types of tax avoidance are addressed. However, as such a deal is unlikely in the short-term, countries should consider taking unilateral measures to avoid tax avoidance, especially in the digital economy, until a comprehensive, fair and effective global deal has been reached.

Such measures could be introduced rapidly and could constitute one of the key ways for countries to both recover revenue lost owing to Covid-19 and to finance a comprehensive response to the economic impact of the pandemic in the coming years.

As multilateralism is generally the preferred option when addressing international tax issues to avoid tax competition, countries should also consider, where possible, applying measures in regional blocks.

Tax justice is a key to reduce inequalities between countries and within countries. Making the highly profitable digital sector pay its fair share is a key challenge. However, equally important is that countries also ensure a fair distribution of revenue from such taxes, paying particular attention to ambitious investments in gender responsive public services and social protection, especially as women are among the hardest hit by the ongoing pandemic, as they are more likely to be in low paid, precarious jobs and face increased unpaid care work, domestic chores and home-schooling during extended lockdowns.

**Tax justice is a key to reduce inequalities between countries and within countries. Making the highly profitable digital sector pay its fair share is a key challenge.**

## Recommendations:

- In the absence of a satisfactory global deal negotiated multilaterally with all countries participating on an equal footing, all countries should consider introducing unilateral measures to tax the digital economy.
- Unilateral measures to tax the digital economy should:
  - raise more revenue from the digital economy;
  - protect small businesses, for example through thresholds that ensure smaller businesses are not adversely affected;
  - Restrict companies' ability to easily pass on not be designed in a way so that companies can easily pass on the additional cost to consumers;
  - Make it harder for companies to avoid paying their taxes.
- Unilateral measures should preferably have some element of unitary taxation underpinning them. Countries should also consider applying a unitary approach to taxation of all multinational companies regardless of whether they are operating in the digital economy or not.
- In the medium to long term, countries should act together on an equal footing under the auspices of the UN to reach a multilateral deal for taxing the digital economy.

# Annex I: Methodology

In this section we will outline how we calculated the potential tax gap owed by tech giants if they were being tax fairly at a global level and provide an outline of the underlying assumptions. Let us first be clear about the fact that these are potential tax losses, rather than actual tax losses. That does not mean that the numbers are either an overestimation or an underestimation of the actual figures, it just means that we have used the best publicly available data and made reasonable assumptions about the companies' economic presence in different jurisdictions. The best way for companies to give their account of their tax contributions in the various countries where they operate is to publish public country-by-country reports. Such reports – which detail sales, number of staff, revenues, assets, taxes paid etc in different jurisdictions – are already filed confidentially with tax authorities.

## Data sources

- We used each company's 10k<sup>46</sup> report for 2020 (filed with the US Securities and Exchange Commission and available online) to get data on global profits.
- We then apportioned profits to each country according to the number of technology users in each country,<sup>47</sup> scaled by GDP per capita relative to the global average.<sup>48</sup>
- Because Facebook and Google are blocked in China, we assumed that revenue there were zero. A similar assumption was made for Amazon as it does not sell directly to customers there.

## Calculating corporate tax avoided in each country

To calculate the amount of tax that is potentially avoided in each country we used a two stage calculation:

**Step 1:** We took the headline corporate tax rate in each country

**Step 2:** To estimate the effective tax rate in each country we used data from the US Internal Revenue Service on the actual rate of tax paid by multinational corporations in the information sector in the US compared to the headline (federal+state+local) corporate tax rate in the US (<https://www.irs.gov/statistics/soi-tax-stats-country-by-country-report>). The IRS statistics show that the effective tax rate is on average 83% of the headline rate. The headline tax rate for each country in this study is multiplied by a factor of 0.83, on the assumption that the relationship between headline and effective tax rates for multinationals will be similar (on average) in the countries featured in the study to the pattern that exists in the US.

The final formula for calculating potential tax losses is therefore:

**Apportioned profits<sup>49</sup> x Headline corporate tax rate x 0.83**

We have then assumed that the companies analysed do not currently pay any corporate income tax.

<sup>46</sup> A 10-K is a comprehensive report filed annually by public companies about their financial performance. The report is required by the U.S. Securities and Exchange Commission (SEC) and is far more detailed than the annual report. Information in the 10-K includes corporate history, financial statements, earnings per share, and any other relevant data.

<sup>47</sup> Alphabet: number of internet users (using internet use as a proxy for Google search use). As a check I also used number of people with Android smartphones as an alternative user base given that Alphabet owns Android – this produced very similar results to using the number of internet users as the user base.

Facebook: number of Facebook users

Microsoft: number of people accessing the internet using desktop computers (as a proxy for Microsoft Windows/Office use)

Apple: number of people with iOS smartphones

Amazon: total value of consumer ecommerce market in each country (as a proxy for Amazon sales in each country).

<sup>48</sup> Users are a key indicator of sales for big tech companies and indeed user data is probably the most valuable asset for these companies – that they can use in a multitude of ways. Normally, we would argue for apportioning profits based on a wider range of factors including sales, assets and employment. For big tech companies it makes sense to follow a different approach as they have very few employees relative to their profits and users are a fair starting point for determining sales and assets. Indeed, we believe that users are a reasonable proxy for economic presence which we can use for companies of this type in the absence of publicly available data on profits, taxes paid and other key information from country-by-country reporting by these companies. However, we stop short of suggesting that user numbers or sales should be the sole basis for design of actual taxes, as any apportionment formula should consider other factors, ensuring a fair allocation of profits. Our research only aims to illustrate the scale of potential tax revenue that is at stake, if companies' tax bills better reflected their genuine economic presence.

<sup>49</sup> Based on taking total global profits and apportioning it by country based on the number of technology users in a country scaled by GDP per capita relative to the global average

As none of the companies provide any public country-by-country breakdown of current corporate tax payments it is impossible to know for sure what their tax liabilities are in any of the featured countries. They are however likely to pay some corporation tax in some jurisdictions which is why we make it clear that these are potential rather than actual tax losses.

Because of the lack of public country-by-country reporting by these companies, we refer to the findings of our calculations as potential tax losses rather than actual tax losses. To help us improve the calculations, the big tech companies analysed in this report can publish country-by-country breakdown of their tax payments, revenue, sales, number of staff etc.

## Estimating the number of Covid vaccinations and courses that could be funded with the avoided tax

This analysis uses data from the World Health Organization (WHO) on the average cost of a Covid-19 vaccination (\$1.66 per shot) and the average cost of a 2-shot vaccination course for a person (\$3.70 per shot, allowing for administration and wastage).

These figures are used to estimate the number of Covid vaccinations and courses of vaccinations that could be purchased with the avoided tax.

## Estimating the number of public service workers that could be funded with the avoided tax

Data from the **OECD statistical database** was used to provide salary information for key public service workers (hospital nurses and primary school teachers) in OECD countries. The OECD has complete data on teachers' starting salaries for OECD countries but the data on nurses' salaries is missing for some countries (Belgium, Chile, Korea and Sweden).

For G20 countries outside the OECD, the only salary information available from the OECD database was for teachers in Brazil.

The number of public service workers that could be funded with the avoided tax for each country was then calculated straightforwardly as "total potential avoided tax / salary".

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