USTR's Probe into Digital Services Taxes

Why in News

Recently, the office of the **United States Trade Representative (USTR)** has initiated investigations into **taxes adopted or under consideration by 10 nations, including India,** on revenues of **American digital service companies** like **Netflix, Airbnb etc.**

Such taxes are known as **Digital Service Taxes.**

Key Points

- **The Office of the United States Trade Representative (USTR):**
  - It is responsible for developing and coordinating US international trade.
  - **The Section 301** gives the USTR **broad authority** to **investigate and respond to a foreign country's** action which may be unfair or discriminatory as well as negatively affect US commerce.
    - Adopted through the 1974 Trade act, the Section allows the US President to impose tariffs or other curbs on foreign nations.
  - However, the law mandates consultations with trading partners.
- **Digital Services Taxes (DSTs):**
  - These are the adopted taxes on revenues that certain companies generate from providing certain digital services. E.g. digital multinationals like Google, Amazon and Apple etc.
  - The **Organisation for Economic Cooperation and Development (OECD)** is currently hosting negotiations with over 130 countries that aim to adapt the international tax system. One goal is to address the tax challenges of the digitalization of the economy.
    - Some experts argue that a tax policy designed to target a single sector or activity is likely to be unfair and have complex consequences. The digital economy cannot be easily separated out from the rest of the global economy.

- **India's Tax on Digital Companies:**
    - The US is probing the **2% Digital Services Tax (DST)** that India adopted in March and which went into effect on April 1, 2020.
    - The tax applies only to **non-resident companies** with annual revenues over $267,000, and covers online sales of goods & services to persons in India.
    - Further, equalisation levy at 6% has been in force since 2016 on payment exceeding Rs. 1 lakh a year to a non-resident service provider for online advertisements.

        This is **applicable for e-commerce companies** that are sourcing revenue from Indian customers without having tangible presence in the particular country.
- **The US Stand:**
    - The US is concerned that many of its trading partners are adopting tax schemes designed to unfairly target US companies.

        Several countries in the world are adopting unilateral measures in the absence of a multilateral consensus spearheaded by OECD. US tech companies which have been phenomenally successful globally are facing the brunt of these unilateral measures and therefore this investigation.
    - It argued that **India's equalisation levy** is **complex and ambiguous** which includes the **possibility of double taxation of income** in absence of access to foreign tax credit as per tax treaties.
- **India's Chance to Respond:**
    - India will be given an opportunity to negotiate with the US and prevent the imposition of tariffs by reaching a comprehensive outcome, on the line of similar negotiations that are currently underway with France.
    - India is expected to argue that the levy is in compliance with India's commitments under the 1995 General Agreement on Trade in Services (Treaty under the World Trade Organization) and is applicable on all global companies, not just American ones.
    - In case when the goods and services are supplied to the resident, typically the **non-residents have been able to pass on the burden to the Indian consumers** and therefore indirectly the tax has been borne by the **Indian consumers.**

- **Concerns:**
    - In the backdrop of an improper functioning of the **World Trade Organization (WTO)**, the move could signal the start of more **unilateral action** by the US especially on the digital services front.
    - In India's case, the probe could potentially affect the **outcome of a bilateral trade deal** that India has been looking to forge with the US.
    - Further, **India continues to be on the 'Priority Watch List' of the United States Trade Representative (USTR)** for lack of adequate Intellectual Property (IP) rights protection and enforcement.

Way Forward

As India is racing towards becoming a digital giant, the 2% DST should be negotiated to avoid any hurdles in its implementation. Further, there needs to be international consensus on taxation on a digital economy.

Source: IE