The Daily Dish

Let’s (Un)Make a Deal

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The New York Times reports that the president is prepared to rip up the trade deal he negotiated with the European Union:

> *President Trump threatened to scrap a just-finalized trade deal with the European Union on Friday, saying that any country that levies a digital services tax would be hit immediately with a 100 percent tariff on all exports to the United States.*

No deal is ever really done (see: peace deal, Iran) with this administration. But at least this action is for a good cause. Digital services taxes (DSTs) are a common form of inefficient, unfair money grab by foreign governments.

DSTs are taxes imposed on multinational firms — usually large, successful American firms — on the basis of their digital activities in a particular jurisdiction. So, for example, a French DST would be a percent of the gross revenue (above a certain threshold) earned in France by digital intermediaries (e.g. Amazon). (The precise definition of the tax base differs from jurisdiction to jurisdiction.) But what does it mean to be earned “in France?” After all, the point of digital activities is to have them be location-free. The answer is that it is usually based on the number of French users.

This is a problem. The prevailing norms in international taxation typically preclude taxing foreign firms without a permanent presence or “nexus” in a given tax authority’s jurisdiction. Under the usual rules, a U.S. digital entity would have its net income taxed in the United States. There is no nexus in France. Even worse, if a U.S. firm pays income tax in France, it receives $1 of tax credit in the U.S. for every $1 in tax paid to France. There is no double-taxation. In contrast, there is no credit for a DST (it’s not an income tax), so it is currently open season for double taxation of U.S. firms via DST.

President Trump used the threat of dropping trade negotiations to get Canada to stop its DST before implementing it. (The Canadian proposal was especially egregious because it included two years of retroactive taxation.) Obviously, the hope here is that any European country toying with the idea of a DST will drop its plans.

In economics, however, there are no freebies. The price of this strategy to nix DSTs is more tariff uncertainty and, maybe, even more tariffs. Which one depends entirely on the Europeans.