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EGDF response on the EU digital levy

About EGDF

1. **The European Games Developer Federation e.f. (EGDF)**[1] unites national trade associations representing game developer studios based in 19 European countries: Austria (PGDA), Belgium (FLEGA), Czechia (GDACZ), Denmark (Producentforeningen), Finland (Suomen pelinkehittäjät), France (SNJV), Germany (GAME), Italy (IIDEA), Malta (MVGSA), Netherlands (DGA), Norway (Produsentforeningen), Poland (PGA), Romania (RGDA), Serbia (SGA), Spain (DEV), Sweden (Spelplan-ASGD), Slovakia (SGDA), Turkey (TOGED) and the United Kingdom (TIGA). Altogether, through its members, EGDF represents more than 2 500 game developer studios, most of them SMEs, employing more than 35 000 people.

2. **The games industry** represents one of Europe's most compelling economic success stories, relying on a strong IP framework, and is a rapidly growing segment of the creative industries. The European digital single market area is the third-largest market for video games globally. In 2019, Europe's video games market was worth €21bn, and the industry has registered a growth rate of 55% over the past five years in key European markets[2]. All in all, there are around 5000 game developer studios and publishers in Europe, employing closer to 80 000 people.[3]

3. **Due to their key role in the digital value chain, games play a crucial role in implementing any taxation system based on user location.** On the other hand, consumer-facing businesses like the European games industry will have a critical role in collecting the location data from users for other companies in the value chain. This leads to significant data protection and privacy concerns and challenges. On the other hand, in the end, as advertisers and business users of digital distribution services, they are the ones

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[1] For more information, please visit www.egdf.eu
[2] ISFE Key Facts 2020 from GameTrack Data by Ipsos MORI and commissioned by ISFE https://www.isfe.eu/data-key-facts/
[3] European Games Industry in 2018: http://www.egdf.eu/wp-content/uploads/2020/08/European-Report-on-the-Game-Development-Industry-in-2018.pdf

carrying the burden of proposed taxes when ad networks and platforms push the increased costs in their prices.

The taxation challenges of a global and digital economy

Building a future proof taxation framework

4. In general, any digital taxation proposal should follow the following principles:

   - **The scope and definition of digital activities/transactions or companies subject to the initiative/levy:** A future proof taxation system is business model neutral and does not differentiate digital and non-digital businesses or business-to-business (B2B) and business-to-consumer (B2C) businesses. Digital taxation should be levied exclusively on profits and not target loss-making enterprises.

   - **Geographic scope:** The taxation of digital markets needs a system that works globally, not just in Europe. Any European digital tax has to respect the EU's and Member States' international obligations, including interaction with Double Taxation Conventions and WTO rules. Any new European digital proposal has to minimise the negative impact on European trade relations.

   - **Fairness:** Any digital tax proposal has to take into account the impact on SMEs, EU member states investing in R&D&I, European digital companies with a weak market position and European consumers of digital content or services

   - **Potential behavioural reactions:** Any digital taxation proposal has to be designed to mitigate incentives to avoid payment of the digital levy, especially by the companies located outside the EU.

   - **Forward-looking design**: Any digital taxation proposal has to encourage digitalisation of European society, secure competitiveness of European businesses, and consider the future evolution of the digital economy with a view to putting in place a sustainable tax framework and providing tax certainty for businesses.

   - **European fundamental rights:** The design of any new tax system has to follow principles of privacy by design and default in order to secure that location data collected for taxation purposes does undermine citizens' fundamental right for privacy. It is essential to remember that personal data should not be seen as an intangible tradable and taxable asset from the European perspective.

   - **Administrative burden and tax compliance costs:** The new rules should be so easy to understand that any SME can implement them and predict their impact on their business without consulting external tax consultants; otherwise, a threshold for SMEs is needed. The new rules should minimise the risk for double taxation and have clear and accessible redress mechanisms.

- **Holistic approach on taxation**: VAT and corporate taxation systems should not be seen as separate entities. Instead, they should be seen as a unified system, where each of them plays a significant but different role.

Uncertainty related to tax obligations when operating in different countries – the taxation of digital markets needs a system that works globally, not just in Europe

5. The current fragmented international tax framework creates significant taxation risks, for example, unexpected permanent establishments, for both SMEs and huge multinational enterprises operating on global digital markets.

6. EGDF underlines that in order to fight the fragmentation of global digital markets, global solutions are needed for digital taxation instead of regional, national or sub-national ones. In a worst-case situation, no international solution is achieved through OECD and overlapping national and international corporate taxation rules will form a significant barrier of entry to global digital markets. Consequently, in principle, EGDF strongly encourages the Commission to continue supporting OECD efforts to build a coherent global framework for corporate taxation. Only when it is clear that the OECD initiative will fail, the Commission should introduce a coordinated European approach. In any case, the EU should not build national or European digital corporate taxation frameworks on top of the OECD one.

Introducing privacy by principle and default into digital corporate taxation

7. From European game developer studios' perspective, tax regulation is only one of the different, and unfortunately sometimes conflicting, regulatory frameworks they have to follow while creating digital games. Consequently, EU and OECD countries must not develop their tax practices as an isolated field but consider their impact on other areas of digital regulation, especially on data protection regulation.

8. The right to privacy or private life is enshrined in the Universal Declaration of Human Rights (Article 12), the European Convention of Human Rights (Article 8) and the European Charter of Fundamental Rights (Article 7). After the General Data Protection Regulation entered into force in May 2018, it is now one of the key cornerstones of European regulation of digital markets.

9. During recent years, European game developer studios have taken action to minimise all their data flows to third parties like online marketplaces and digital advertisement networks. Now, the models discussed under digital levy are based on forcing European companies to provide their consumers' location data for big, usually non-European, conglomerates for taxation purposes.

10. The more companies are forced to collect sensitive location data from their users, the longer it has to be stored for accounting purposes. The more this data is moved from a tax authority to another for audit purposes, the bigger is the risk for highly harmful data breaches. Therefore, any digital taxation proposal based on the users' location creates a significant administrative burden and risks for data breaches and data protection rules violations.

11. Therefore, it is essential that the Commission closely follows the principle of data minimisation by minimising the data collection obligations. For example, only one piece of evidence on the

consumer's location and only aggregated country-level location data should be transferred to third parties in the value chain for taxation reasons.

Differentiated tax treatment of traditional and digital businesses – a future proof taxation system does not differentiate digital and non-digital businesses

12. For years, the European Commission has used digital businesses as a testbed for novel taxation solutions. For example, Mini One Stop Shop that was launched for cross border VAT reporting for electronically supplied services in 2015 will be widened to cover also e-commerce in July 2021.

13. Year by year, the line between traditional businesses and digital businesses is increasingly blurring, as more traditional products and services are enhanced with digital services and content. Indeed, digital value chains are often complex. However, the difficulties in establishing a company's tax liability in a digital value chain usually germinate from complex and arbitrary taxation rules, not from the complex value chain itself. If the reality does not fit in the taxation model, the reality should not be seen as the problem in the equation.

14. Now in the 21st century, the digital economy is increasingly becoming the economy itself. The digital economy is no longer a marginal curiosity. Instead, it is now a core part of the European economy itself. Consequently, the European Commission should abandon its efforts to arbitrary ring-fence digital economy from the rest of the economy for corporate taxation purposes.

15. Secondly, most European digital businesses are SMEs that do not have sufficient resources for hiring international corporate tax experts to optimise their international taxation. Therefore, although some multinational digital enterprises might be able to optimise their taxation to a lower level than traditional businesses, it does mean that all digital companies would enjoy a more friendly tax treatment. Therefore, the Commission should be careful not to hit European digital companies with significant administrative red tape and new taxes while building taxation instruments targeting large online platforms acting as gatekeepers in the digital markets.

Large profits of digital companies mean large tax income for countries that have invested in R&D&I support instruments – building a fair taxation system encouraging EU member states to invest in building a better future for humanity

16. As humanity's future is built through innovations, the Commission should be careful not to create disincentives for its member countries to invest in R&D&I, e.g. by allocating vast amounts of corporate tax income to the market countries instead of the countries where tech companies are established in or by reallocating corporate tax revenues from specific R&D&I focused sectors from member states to its own budget. It is crucial that the countries that have made the success of these companies possible by their public investment also receive the clear majority of the corporate tax income.

17. Similarly, significant tax uncertainty related to the use of novel technologies, digital artistic content or business models in digital businesses can easily create both a market access barrier for start-ups and an incentive for European companies to not invest in R&D&I.

Understanding the role of cross border personal data transfers in value creation

18. On the 14 of March 2017, European Data Protection Supervisor published a statement warning "against any new provision introducing the idea that people can pay with their data the same way as they do with money." Consequently, it is essential to remember that data itself should not be seen as an intangible taxable asset from the European perspective.

19. Secondly, data itself is rarely used as a tradable item. Instead, data is far more often used to enable other services like streaming online content that is already taxed through digital B2C VAT. Although digital companies can easily service customers across various markets without being located or a resident in those market jurisdictions, they are already paying digital VAT for all their B2C sales to those market jurisdictions.

Understanding the role of a user in value creation

20. The real value of digital games is the digital content, technology and business model that a game developer studios creates and supports. European game developers studios employ thousands and invest millions to create, support and improve their games. They, and not their users, are the ones that create the value.

COVID19 and the rise of some and fall of many digital companies

21. Some digital companies are emerging from the COVID19 health crisis more profitable and with larger market shares, but many are not. As the EGDF COVID19 survey demonstrates, many European digital SMEs are struggling due to the COVID19 outbreak. It has significantly hindered their access to risk capital, disrupted their B2B deal flow and made recruitment of new talents much more difficult.[4] Therefore, it is very difficult to understand why the Commission is considering targeting a whole sector with new corporate taxes just because some companies in the sector have been able to minimise the impacts of the COVID19 outbreak on their business.

Building digital-ready taxation services - better public services for paying and reporting international taxes leads to a stronger tax base

22. EU member states should provide sufficient financial resources for their tax authorities to advise businesses in implementing EU/OECD rules and participating in dispute resolution processes built for avoiding double taxation.

23. In the long run, companies should only need to register and pay taxes in one EU/OECD country, and the tax authority of that country would be the one taking care of transferring the tax payments to other countries based on the company's tax reports. A Mini One Stop Shop (MOSS) that was built for reporting B2C VAT payments demonstrates that a system like this can be built if there is enough political will to do so. Therefore, MOSS should be carefully benchmarked as an effective measure of the digital economy's taxation on the corporate taxation side.

24. In the short run, the Commission should secure that the process for tax dispute resolution is:

[4] http://www.egdf.eu/egdf-covid-19-survey/

- **As light as possible:** All disputes on paid taxes should be solved between national tax authorities instead of bilaterally between the company and each disagreeing tax authority.
- **Technologically and digitally competent:** It is not enough to just secure access to an effective dispute resolution process; it is equally essential to ensure that people involved in them have high enough technical expertise to understand how, for example, AI systems and digital value chain work.
- **Secure:** When EU/OECD tax authorities are auditing companies and transferring this information for the panel process, they have to invest in cutting-edge (data) security practices in order to avoid severe data breaches and any industry espionage.

Proposed measures

An increase in the current corporate income tax (top-up) for all companies conducting certain digital activities in the EU

25. This approach creates a significant risk of European digital levy being introduced as something additional to national digital levies. It would only increase the tax uncertainty and fragmentation of the digital single market area, as digital businesses would have to deal with the wide variety of corporate tax rates across Europe and the different definitions of income and relevant deductions. Therefore, in minimum, this proposal should include an explicit agreement that all existing and proposed unilateral national digital taxation measures are removed.

A new tax on revenues created by certain digital activities conducted in the EU

26. Only profits should be taxed under corporate taxation. A tax on revenues would continue the return of turnover taxes to Europe. Such taxes are regressive, taxing companies that are less profitable at higher effective rates than more profitable ones. Turnover taxes damage the economy because they do not take profitability into account, can result in disproportionate taxation, and leave less money available for re-investment in businesses, jobs, and growth. Thus any digital taxation system should be levied exclusively on profits and not target revenues of already loss-making enterprises.

27. In addition, it is likely that any tax on certain digital activities, e.g. advertisement, would easily lead to a situation where European SMEs relying on digital services and European consumers buying digital services will bear the added costs imposed by such measures through higher fees or prices.

A new tax on all digital business-to-business transactions conducted in the EU

28. EU member states already have a tax on business-to-business transactions: VAT.

29. Talking about the tax challenges of the digital economy without mentioning VAT is like fighting over who gets to eat leftovers without discussing who got to eat the cake in the first place. The current VAT system with 20-25% VAT rates automatically leads to a situation where the country a consumer is located in collects the majority of the taxes in a value chain. Typically, tax revenue from VAT is far more than the corporate tax revenue from the business profit. Therefore the country that collects the VAT from B2C transactions gets by far the biggest share of total tax revenue generated by each euro spent by a consumer.

30. EGDF finds it strange that due to bureaucratic administrative silos, VAT and corporate taxation are seen in the current debate as two almost entirely separate tax revenue sources. VAT and corporate taxation systems should not be seen as separate entities. Instead, they should be seen as a unified system, where each of them plays a significant but different role. The VAT system secures that the sales are taxed in the countries where purchases happen, and the corporate taxation system ensures that profits are taxed in the countries where the value is created.

31. In the games industry, value is created where the creation of IP is taking place. In general, this happens in the country where a company has its headquarters. This is also the country where the corporate taxes are paid to. Already now, game distribution platforms are paying the VAT on B2C transactions to the EU member states where the purchases are made.

32. Therefore, instead of building a new corporate taxation instrument, specifically increasing the cost of digitalisation, the Commission should explore the possibility of scaling up the already existing national B2B VAT system to the European level and possibly using the already existing tool for B2C VAT tax reporting to reallocate B2B VAT revenue to other member states or to the EU budget.

Scope of the new levy

Scope of the new levy

33. The Commission should avoid targeting specific digital sectors with the new levy. This creates arbitrary regulatory barriers in the digital value chain. Instead, the Commission should either support the OECD approach on a global level or consider introducing a system for cross border B2B VAT for all sectors at the European level.

34. If the commission is going to target specific sectors:

   - **Advertisement:** Games industry relies on both digital advertisement and the sale of games as a source of revenue. A targeted tax for digital advertisement combined with strict European data protection and privacy rules and current discussions for setting further limitations for advertisement under Digital Service Act are likely to decrease the games industry’s ability to boost digital growth and create digital jobs. Furthermore, this will make it difficult for game developer studios to continue to provide their content for free. Thus it would widen the digital gap between different socio-economic groups in the Union.

However, both EU and OECD have underlined that the business models, which generate revenue through the sales of advertisement, are the particularly problematic ones and the key focus of new digital taxes. This is also the area where current national proposals for digital taxation have been mainly focused on and, therefore, the risk of regulatory fragmentation is the highest and most urgent. Any digital tax on advertisement should always be collected and paid by business lines closest to a consumer, in this case, the advertisement networks.

- **Games:** The sales of copyrighted products like games are already effectively taxed through a digital VAT system. As there should not be additional taxation of businesses or transactions that are already effectively taxed, the Commission should leave all business lines based on sales of copyrighted products out of the scope of the proposed tax.

Revenue threshold

35. In minimum, a worldwide revenue threshold of EUR 750 million is needed. It would ensure that the new system does not bring an unproportionate administrative burden for the multinational enterprises (MNEs) or national tax administrations. Introducing a new taxation system is always a complex process that leads temporarily to significant administrative and regulatory uncertainty. Therefore, it would be better to introduce the new system step by step. The Commission should start from MNEs with global revenue above EUR 10 000 million and lower the threshold from there when the administrative capacity of national tax authorities and tax consulting companies in assisting MNEs in the implementation of the new system increases.

An SME threshold is needed – If SMEs are included in the scope of the proposal, the global corporate tax framework will create a significant barrier to entry into the global digital market

36. A clear threshold for SMEs is needed. Without it:

- Highly burdensome taxation requirements are likely to skyrocket the amount of private and public funding needed for starting a company targeting global digital consumer markets.
- European game industry SMEs are going to need a, usually non-European, publisher to access global markets. This would mean returning to a pre-digital value chain where a European developer receives about 20% of the revenue instead of the current 70%.
- Big global tax consulting companies would become significant gatekeepers for access to global digital markets.

Determining the place of taxation

37. The Commission should closely follow the GDPR data minimisation principle while drafting the new requirements. Only one piece of evidence on the geolocation of the consumer, chosen by the taxable person from a pre-established, list should be needed. Only aggregated country-level location data should be transferred to third parties in the value chain for taxation reasons.

38. The members of EGDF will be, in many cases, the ones providing that location data for the MNEs, as those MNEs are often acting as third-party services providers (e.g. advertisement networks, or cloud services) for game developer studios. While drafting the new rules, the commission must carefully address the privacy and data protection concerns of European data subjects whose personal location data should be distributed across a digital value chain for determining the place of taxation.

39. The commission should also clearly indicate the requirements, rights and responsibilities of both MNEs falling under the scope of the tax and third parties (often SMEs) that provide the location data of those MNEs through their digital services (e.g. games).

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