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## DIGITAL SERVICES TAX REGULATION AND WTO NON-DISCRIMINATION PRINCIPLE: IS THE DECK STACKED?

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# DIGITAL SERVICES TAX REGULATION AND WTO NON-DISCRIMINATION PRINCIPLE: IS THE DECK STACKED?

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## Abstract

*A growing debate on the imposition of digital services tax emerged as one of the latest trade war battlegrounds. Indonesia and the European Union (EU) are among the countries that have taken unilateral actions to implement digital services tax. This paper examines (i) digital services tax regulation in Indonesia and the EU and (ii) whether the digital services tax regulation violates the non-discrimination principles of WTO according to the GATS. By comparing the statutory and practice of digital services tax in Indonesia and the EU, this work concludes that firstly, digital services tax in Indonesia is regulated by law, which implements significant economic presence (SEP) criteria. In the EU, digital services tax is regulated through the Council Directives and implements ring-fencing method as well as SEP criteria. Secondly, the non-discrimination principles in the GATS are promulgated in Article II concerning Most-Favored Nation Treatment and Article XVII concerning National Treatment as well as relevant jurisprudence of WTO case laws. Indonesia and the EU's digital services tax regulation are not discriminatory, because based on existing indicators, the existence of both de jure and de facto discrimination is not proven. This paper suggests that in the event that there are member states who decide to challenge the measures to the WTO, Indonesia and the EU should provide evidence that shows the absence of unfavorable treatment of certain WTO member states in digital services tax practices by Indonesia and the EU.*

**Keywords** : digital services tax, non-discrimination principle, ring-fencing, significant economic presence.

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## I. INTRODUCTION

Trade in digital goods and services via the internet is growing rapidly. The Cisco Annual Internet Report for 2020 reveals that approximately 12% of global merchandise trade is conducted via the internet.<sup>1</sup> Based on the press release of the United Nations Conference on Trade and Development published in 2020, the estimated value of global e-commerce sales is \$ 25.6 trillion in 2018, valued at 30% of the world's Gross Domestic Product (GDP) in that year.<sup>2</sup> Despite making a significant contribution to the global economy,

<sup>1</sup> "Cisco Annual Internet Report," Cisco Systems, accessed 15 September 2020, <https://www.cisco.com/c/en/us/solutions/collateral/executive-perspectives/annual-internet-report/white-paper-c11-741490.pdf>.

<sup>2</sup> "Global e-Commerce hits \$25.6 trillion," United Nations Conference on Trade and Development, 27 April

the digital economy is a major challenge to international trade, particularly in the implementation of taxes on services.<sup>3</sup>

This is due to the defiance to the traditional principles of international tax law which require a permanent establishment or physical presence to tax the company's income or profits from the sale of the country.<sup>4</sup> Permanent establishment is recognized as a tax requirement in the traditional principle of international tax law, namely that there must be a substantial relationship between a country and a company's activities to build a nexus in that country, so that the country is allowed to impose taxes on the company's income or profits obtained from sales in the country.<sup>5</sup> Notwithstanding, nowadays multinational companies can earn income from local residents of a country without making a permanent establishment in that jurisdiction.<sup>6</sup> Permanent establishment based on physical relationships is made non-existent in digital activity over the internet because the internet is not physically located in one country, but rather a global computer network.<sup>7</sup> Digital services eliminate the need for a physical presence or corporate intermediaries to have access to service users.

In response to the phenomenon of profit creation through digital services, various countries and intergovernmental organizations have tried to propose a modified definition and interpretation of the permanent establishment rules to include the criteria for digital existence, which the Organisation for Economic Cooperation and Development (OECD) introduced as a significant economic presence.<sup>8</sup> Significant Economic Presence (SEP) is a taxation approach in which the presence of tax in a jurisdiction will appear when a non-resident

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2020, accessed 29 Agustus 2020, <https://unctad.org/en/Pages/PressRelease.aspx?OriginalVersionID=552>.

<sup>3</sup> Andrew D. Mitchell, Tania Voon and Jarrod Hepburn, "Taxing Tech: Risks of an Australian Digital Services Tax under International Economic Law," *Melbourne Journal of International Law* 20, no.1 (2019): 88.

<sup>4</sup> "Understanding Sales Tax Nexus," Tax Connex, 28 April 2020, accessed 15 September 2020, <https://www.taxconnex.com/blog/understanding-sales-tax-nexus>.

<sup>5</sup> Nexus by the OECD in Tax Challenges Arising from Digitalisation – Interim Report 2018 is defined as "(that which) identifies the profits that are taxable by a country by reference to their relationship to a Permanent Establishment." It is written that pursuant to Article 7 of the OECD and UN Model Convention, the nexus rule means that business profits obtained by a company can be taxed exclusively by the country where it is located unless the company does business in another country through a permanent establishment.

<sup>6</sup> "Addressing the Tax Challenges of The Digital Economy," Organisation for Economic Co-operation and Development, accessed 15 September 2020, <https://www.oecd-ilibrary.org/docserver/9789264218789-10en.pdf?expires=1600341374&id=id&accname=guest&checksum=552193BE9856F2A6615D73966A66FC50>.

<sup>7</sup> Marcin Szczepanski, "Corporate taxation of a significant digital presence," European Parliamentary Research Service, December 2018, accessed 7 October 2020, [https://www.europarl.europa.eu/RegData/etudes/BRIE/2018/623571/EPRS\\_BRI\(2018\)623571\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/BRIE/2018/623571/EPRS_BRI(2018)623571_EN.pdf), accessed 7 October 2020.

<sup>8</sup> Annabelle Bailleul-Mirabaud, Céline Pasquier and William Hamon, "Google Has Won Second Round Against the French Tax Authorities," Bloomberg Tax, 29 May 2019, accessed 8 October 2020, <https://news.bloombergtax.com/daily-tax-report-international/insight-google-has-won-second-round-against-the-french-tax-authorities>.

company has an economic presence that meets the criteria determined based on income-based factors, digital factors, and user-based factors.<sup>9</sup>

Significant economic presence criteria are applied in digital service taxation. Digital Services Tax is defined as taxes on income or profits that a company generates from providing certain digital services to, or intended for, users in those jurisdictions.<sup>10</sup> However, certain design features of digital services taxes can potentially create unfair treatment. For instance, the minimum income threshold in the criterion for economic significance could be set in such a way that a large proportion of foreign multinationals from a particular member state are taxed. In addition, there are ring-fencing methods that can unfairly exclude certain types of services.<sup>11</sup> Ring-fencing in taxation is defined as a form of regulation that differentiates the application of taxes to certain taxpayers, one of which is the exemption of taxpayers in certain sectors from tax implementation.<sup>12</sup>

Currently, there has not been a global consensus on the imposition of digital services tax. However, several countries have implemented digital services tax as a unilateral measure. The United States believes that the implementation of digital services tax is possibly disproportionate to companies originating from the United States, including Google LLC, Facebook, Inc., and Amazon.com, Inc.<sup>13</sup> Therefore, the enforcement of this tax has triggered allegations of discrimination that violate the principles of Most-Favored Nation and National Treatment in Article II and Article XVII of the GATS. The United States is conducting a series of new investigations against five countries that have adopted several forms of digital service tax, one of which is Indonesia.<sup>14</sup>

Indonesia decided to impose an Electronic Transaction Tax (*Pajak Transaksi Elektronik* or *PTE*) on digital companies in April 2020 due to surging sales amid the Covid-19 outbreak.<sup>15</sup> Now the electronic transaction

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<sup>9</sup> Organisation for Economic Co-operation and Development, “Addressing the Tax Challenges of The Digital Economy,” 16.

<sup>10</sup> OECD, “The 2015 BEPS Action 1 Report – Tax Challenges of the Digital Economy”

<sup>11</sup> Daniel Bunn, Elke Asen and Cristina Enache, “Digital Taxation Around The World,” <https://taxfoundation.org/digital-tax/>, accessed 12 October 2020.

<sup>12</sup> Organisation for Economic Co-operation and Development, “OECD/G20 Base Erosion and Profit Shifting Project,” 54.

<sup>13</sup> R. Herjuno Wahyu Aji, “Implikasi Pajak Transaksi Elektronik terhadap Perjanjian Perdagangan,” <https://news.ddtc.co.id/implikasi-pajak-transaksi-elektronik-terhadap-perjanjian-perdagangan-20805>, accessed 31 August 2020.

<sup>14</sup> Silvia Amaro, “A new trade war? U.S. opens new investigations into countries planning digital taxes,” <https://www.cnn.com/2020/06/03/us-probes-uk-india-brazil-the-eu-and-others-for-digital-tax-plans.html>, accessed 15 September 2020.

<sup>15</sup> Firman Hidranto, “Trafik Melonjak Pedagang Online Kena Pajak [Increased Traffic, Online Seller should pay tax],” <https://indonesia.go.id/narasi/indonesia-dalam-angka/ekonomi/trafik-melonjak-pedagang-online-kena-pajak>, accessed 30 August 2020.

tax regulations are listed, among others, in Government Regulations in Lieu of Law of the Republic of Indonesia (Perppu) No. 1 of 2020 concerning State Financial Policy and Financial System Stability for Handling Pandemic Corona Virus Disease 2019 (Covid-19) and / or in the Context of Facing Threats Endangering the National Economy and / or Financial System Stability, which was approved as law through Law No. 2 of 2020.

Prior to the investigation on Indonesia, in July 2019 the United States Trade Representative (USTR) conducted an investigation into the European Union DST implemented by France.<sup>16</sup> The European Union regulates the Digital Services Tax in the Council Directives issued by the European Commission in 2018. In Section 301 of Investigation - Report on France's Digital Service Tax by USTR dated December 2, 2019, it is stated that there is evidence that the European Union's DST is aimed at digital companies from the United States.<sup>17</sup> USTR then proposed to the United States parliament to impose trade restrictions and tariffs as an act of retaliation or retaliation, namely in the form of an increase in import duty rates of up to 100% on imported luxury goods from France.<sup>18</sup> This allegation of discrimination underlies the selection of the EU digital services tax arrangement to be compared with the Indonesian arrangement in this study.

Based on the explanation above, it can be seen that digital service tax as a unilateral policy in several countries has led to allegations of discriminatory practices that violate the WTO agreement, in particular Article II of the GATS concerning the principles of Most-Favored Nation and Article XVII of the GATS concerning the principles of National Treatment. Therefore, it is necessary to examine more deeply whether the accusation is justified.

In this study, three approaches will be utilized, namely statutory approach, case study approach, and comparative approach. Statutory approach is carried out by reviewing relevant laws and regulations,<sup>19</sup> and case study approach<sup>20</sup> will evaluate the jurisprudence of the application of the WTO agreement

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<sup>16</sup> "Conclusion of USTR's Investigation Under Section 301 into France's Digital Services Tax," Office of the United States Trade Representative, accessed 14 September 2020, <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/december/conclusion-ustr%E2%80%99s-investigation>.

<sup>17</sup> William A. Reinsch, Jack Caporal, and Carlota Martinez-Don, "What's Behind USTR's New Digital Services Tax Investigation?" Center for Strategic and International Studies, 19 June 2020, accessed 14 September 2020, <https://www.csis.org/analysis/whats-behind-ustrs-new-digital-services-tax-investigation>.

<sup>18</sup> Red Whitten and Sarah F. Ben-Moussa, "Potential Impact of U.S.-France Trade Tension on U.S. Imports of French Products and Luxury Goods," National Law Review, accessed 14 September 2020, <https://www.natlawreview.com/article/potential-impact-us-france-trade-tension-us-imports-french-products-and-luxury-goods>.

<sup>19</sup> Soerjono Soekanto, *Pengantar Penelitian Hukum [Introduction of Legal Research]* (Jakarta: Badan Penerbit Universitas Indonesia, 2007), 83.

<sup>20</sup> Peter Mahmud Marzuki, *Penelitian Hukum, Edisi Revisi [Legal Research]* (Jakarta: Kencana, 2014), 134.

through relevant disputes. Comparative approach<sup>21</sup> is carried out by comparing national measures between Indonesia and the EU. The data obtained will then be analyzed by qualitative methods to determine whether the implementation of PTE in Indonesia and DST in the EU violate the non-discrimination obligations of WTO member states.

The next two sections of this paper will focus respectively on the implementation of Indonesian and European Digital Services Tax. It will then be followed by an explanation of the Non-Discriminative Principles of WTO, which serves as a basis for the following analysis of the compliance of Indonesia's and EU's digital services tax to the Non-Discrimination Principles of WTO. Lastly, the findings of this work will be presented in Conclusion.

## II. DIGITAL SERVICES TAX REGULATION OF INDONESIA AND THE EU

### A. INDONESIAN DIGITAL SERVICES TAX

Digital services tax by Indonesia or *PTE* is imposed based on Perppu No. 1 of 2020. The imposition of digital services tax in Indonesia does not use the ring-fencing method but applies to all digital services activities that meet the threshold for significant economic attendance instead. Apart from domestic and foreign digital services providers, Perppu No. 1 of 2020 also imposes taxes on foreign traders and foreign service providers, as regulated in Article 6 paragraph (5).

The approach of Perppu No. 1 of 2020 to tax the digital economy is to impose direct tax (income tax) and indirect tax (VAT) obligations on foreign sellers, service providers, and foreign e-commerce platforms that earn income through digital transactions from the Indonesian consumer market:

#### 1. Income Tax

Based on Article 6 paragraph (6) of Perppu No. 1 of 2020, the income tax obligation will apply to foreign digital service providers with a significant economic presence in Indonesia, because they will be considered as a permanent form of business that has permanent establishment. The rate, the imposition of and the procedure for calculating the said Income Tax will be regulated by a Government Regulation. Meanwhile, the provisions regarding thresholds constituting significant economic presence, procedures for payment and reporting of income tax or PTE, and procedures for appointing

<sup>21</sup> Suharsimi Arikunto, *Prosedur Penelitian: Suatu Pendekatan Praktik, Edisi Revisi Keempat* [Research Procedure: Practical Approach, Fourth Edition] (Jakarta: PT Rineka Cipta, 2006), 236.

representatives are all regulated in the Minister of Finance Regulation.<sup>22</sup>

## 2. Value Added Tax

The legal basis for implementing Value Added Tax (VAT) collection for types of digital products is regulated in Minister of Finance Regulation (MoFR) No. 48 of 2020 concerning Procedures for Appointment of Collectors, Collection and Deposit, as well as Value Added Tax Reporting on the Use of Intangible Taxable Goods and / or Services Taxes from Outside the Customs Area within the Customs Area through Trade through Electronic Systems (Digital Taxes), which is a special implementing regulation for Article 6 paragraph 13 (a) of Perppu No. 1 of 2020 which regulates the procedures for collecting, paying and reporting VAT for transactions digital cross-border will be further regulated. Based on MoFR No. 48 of 2020, 10% VAT needs to be applied to the provision of intangible foreign goods or services through electronic devices or systems in the Indonesian market.<sup>23</sup>

## B. EUROPEAN DIGITAL SERVICES TAX

Meanwhile, the EU DST is regulated in the Council Directive 2018/0072 and the Council Directive 2018/0073. The Council Directives divides the EU DST into two forms as follows:

### 1. Tax on Digital Revenues

Taxation on digital income uses the ring-fencing method, meaning that the tax is only imposed on certain digital service sectors. Article 3 paragraph (1) of the Council Directive 2018/0073 further specifically regulates the services referred to, namely as follows: services comprising within the setting on a computerized interface of advertising targeted at users of that interface; as well as multi-sided digital interface provider services which can be referred to as “intermediary services” that allow a user to find other users and interact with them.

In accordance with Article 4 paragraph (1) of the Council Directive 2018/0073, an entity that qualifies as a taxable business actor is an entity that

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<sup>22</sup> Ichsan Sukardi and Sophia She Jiaqian, “Taxing the digital economy in Indonesia,” *International Tax Review*, 22 September 2020, accessed 23 September 2020, <https://www.internationaltaxreview.com/article/bIngz37n2ts6ct/taxing-the-digital-economy-in-indonesia>.

<sup>23</sup> Indonesia. *Peraturan Menteri Keuangan tentang Tata Cara Penunjukan Pemungut, Pemungutan, dan Penyetoran serta Pelaporan Pajak Pertambahan Nilai Atas Pemanfaatan Barang Kena Pajak Tidak Berwujud dan/atau Jasa Kena Pajak dari Luar Daerah Pabean di Dalam Daerah Pabean melalui Perdagangan melalui Sistem Elektronik*, PMK No. 48 tahun 2020. (Minister of Finance Regulation concerning Procedures for Appointing Collectors, Collections, and Deposits, as well as Reporting Value Added Tax on the Utilization of Intangible Taxable Goods and/or Taxable Services from Outside the Customs Area Inside the Customs Area through Trading Through the Electronic System. MoFR Regulation No. 48 of 2020). Art. 3.

fulfills the following two thresholds:<sup>24</sup>

- 1) Total global revenues reported for the most recent financial year exceed € 750 million; and
- 2) The total taxable income in the most recent financial year exceeds € 50,000,000.

## 2. Tax on Digital Profits

The proposed tax on corporate digital profits will apply to companies that have a significant digital presence or SEPs in member states. A significant digital presence exists when at least one of three such thresholds are met.<sup>25</sup>

- 1) company revenues from digital services provided in member states exceeding € 7 million in the tax period (usually one year);
- 2) the number of users in the member states exceeding 100,000 in the tax period; or
- 3) the number of business contracts for digital services exceeds 3,000. The threshold is intended to exclude incidental small companies and digital service providers.

### **III. COMPLIANCE OF INDONESIA'S AND THE EU'S DIGITAL SERVICES TAX TO THE NON-DISCRIMINATION PRINCIPLES OF WTO**

#### **A. THE NON-DISCRIMINATION PRINCIPLES OF WTO**

As mentioned above, the implementation of digital services tax draws allegation of violation towards the non-discrimination principles of WTO, namely the Most-Favoured Nation and National Treatment principles regulated each in Article II and Article XVII of the GATS. According to this Most-Favoured Nation principle, all member states are bound to give other member states the same treatment in the implementation of import and export policies and regarding other costs.<sup>26</sup> The same treatment must be carried out immediately and unconditionally for products originating from or submitted to all the GATS member states.<sup>27</sup> Meanwhile, the National Treatment principle

<sup>24</sup> European Commission, *Council Directive 2018/0072/EC on the common system of a digital services tax on revenues resulting from the provision of certain digital services*, Art. 4.

<sup>25</sup> European Commission, *Council Directive 2018/0072/EC on laying down rules relating to the corporate taxation of a significant digital presence*, Art. 5.

<sup>26</sup> Huala Adolf, *Hukum Perdagangan Internasional [International Trade Law]* (Jakarta: Raja Grafindo, 2006), 108.

<sup>27</sup> *Ibid.*



regulates that products from one country which are imported into another country must be treated the same as domestic products.<sup>28</sup>

Determining whether the forms of the EU and Indonesian digital services tax are based on the WTO non-discrimination principle in the GATS requires testing the following criteria:

a. Actions Covered by the GATS

Article I: 1 of the GATS stipulates the following provision: “*This agreement applies to the actions of Members that affect trade in services.*”<sup>29</sup> Therefore, for an action to be covered by the GATS, it must be an:

- a) Action by Members,<sup>30</sup> and
- b) Action affecting trade in services.

An action affects trade in services when it has an effect on competitive conditions for supply.<sup>31</sup> Determination of whether an action is covered by the GATS can be proven by the inclusion of the related services in the commitment schedule in the GATS by member states.

b. Like Service and Service Providers

The GATS do not set any criterion to determine the likeness of services and service providers, and there are almost no relevant cases to date regarding likeness in the GATS.<sup>32</sup> Therefore, to prove likeness, this study uses the criteria in the case-law of the General Agreement on Tariffs and Trade (GATT) which are relevant to be applied in service trade regulated by GATS.

The basic criteria for determining likeness in the GATT are stipulated in the Report of the Working Party on Border Tax Adjustments, namely (i) the product’s end uses in a given market or product objectives in a particular market, (ii) consumers’ tastes and habits or tastes and habits consumers, (iii) the product’s properties, and (iv) the nature and quality of the product.<sup>33</sup>

<sup>28</sup> Adolf, *Hukum Perdagangan Internasional*, 111.

<sup>29</sup> General Agreement on Trade in Services, opened for signature 15 April 1994, 1869 UNTS 183 (entered into force 1 January 1995), Art. 1(1).

<sup>30</sup> Article I (1) of the GATS provides that the actions of individuals, companies or organizations, which are not carrying out delegated government duties, will not be considered as ‘actions by the Member’. In accordance with Article I (3)(a) of the GATS, Members are obligated to take all reasonable steps to ensure that governments and non-governmental bodies with governmental powers comply with obligations under GATS.

<sup>31</sup> European Communities — Regime for the Importation, Sale and Distribution of Bananas, WTO Dispute Settlement, Appellate Body Report, para. 7.281.

<sup>32</sup> “Determining ‘likeness’ under the GATS: squaring the circle?” World Trade Organization, accessed 6 December 2020, [https://www.wto.org/english/res\\_e/reser\\_e/ersd200608\\_e.pdf](https://www.wto.org/english/res_e/reser_e/ersd200608_e.pdf).

<sup>33</sup> World Trade Organization, *Report of the Working Party (97-109) Border Tax Adjustments*, adopted on 2 December 1970.

These criteria and parameters have been used consistently by the Panel and the WTO Appeal Board in the case of the GATT. Apart from these instruments, there are also two known approaches to determining likeness, namely the aim-and-effect test and like circumstances. The determination based on the instruments and approaches mentioned above are as follows:

i) Classification of Services and Service Providers

Two main instruments have been used by member states to describe the sectors / subsectors covered by their commitments, namely the Services Sectoral Classification List (SSCL) and 1991 UN Provisional Central Product (CPC).<sup>34</sup> SSCL categorizes services into twelve sectors and about 160 subsectors. Both instruments are complemented by an *ad hoc* sectoral classification, as listed in the Annex on Financial Services. Member states are encouraged, but not obliged to, use this instrument. Most of the GATS schedules are based on SSCL.<sup>35</sup> The CPC defines only the activity of the service provider and not the service provider. Therefore, it can be concluded that the classification approach is irrelevant in comparing service providers.

ii) Physical Characteristics

Criteria that focus on the physical characteristics of a product, such as those used in the context of the GATT, are not relevant in the context of intangible services. Putting physical characteristics aside, it can be explored whether there are intrinsic characteristics that can differentiate one service from another.

In the *US - Gambling* dispute, the parties developed detailed arguments around the characteristics of the type of game in the gambling industry. For example, the nature and various types of games are discussed in detail, including comparisons between gambling with software algorithms, such as the case of internet gambling, versus physical gambling fixtures in casinos.<sup>36</sup>

Furthermore, regarding the likeness of service providers, some commentators suggest that criteria such as skills, company size, number of employees, type of assets, technology equipment, business fields, experience and knowledge could be relevant.<sup>37</sup> So far, the Panel

<sup>34</sup> WTO, "Determining 'likeness' under the GATS: squaring the circle?"

<sup>35</sup> World Trade Organization, Guidelines for The Scheduling of Specific Commitments under The General Agreement on Trade in Services (GATS), adopted on 23 March 2001, Part II, Section A.

<sup>36</sup> United States - Measures Affecting the Cross-Border Supply of Gambling and Betting Services, WTO Dispute Settlement, Appellate Body, Panel Report, section III.B.5(a).

<sup>37</sup> Werner Zdouc, "WTO Dispute Settlement Practice Relating to the GATS," *Journal of International*

has not relied on this type of criterion to assess the likeness of service providers, although many have asked for this criterion to support claims of likeness or unlikeness.

iii) Consumers' tastes and end uses

The Appellate Body analysis in the EC - Asbestos dispute is considered applicable in the context of services. The end-use concept will require determining the extent to which the product is capable of performing similar functions. Meanwhile, the criteria for consumer taste will refer to the extent to which consumers are willing to choose a product compared to others to get that end use, or in other words, whether consumers perceive two service products as substitutes for each other in a particular market.<sup>38</sup> The application of these criteria becomes an indicator of the competitive relationship between two services or service providers.

iv) Aim-and Effect Approach

Based on the "aim-and-effect" approach, the Panel considers differences in regulations between products that have bona fide objectives and whether this creates a protective effect in favor of domestic products.<sup>39</sup> Regulators are allowed to treat two products differently if regulations that differentiate the two have no purpose or effect of protecting domestic products. In other words, there will be a determination of likeness if and when the regulation in question has the objective and effect of providing protection. Not long after, the aim-and-effect approach was rejected in the context of the GATS. In the *EC - Bananas III* dispute.<sup>40</sup>

c. Like Circumstances

In this criterion, service providers and / or services will be considered

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*Economic Law 2*, (1999): 333.

<sup>38</sup> European Communities - Measures Affecting Asbestos and Products Containing Asbestos, WTO Dispute Settlement, Appellate Body Report, para. 117.

<sup>39</sup> US – Taxes on Automobiles, WTO Dispute Settlement, Panel Report, para. 5.10. "A measure could be said to have the aim of affording protection if an analysis of the circumstances in which it was adopted, in particular an analysis of the instruments available to the contracting party to achieve the declared domestic policy goal, demonstrated that a change in competitive opportunities in favor of domestic products was a desired outcome and not merely an incidental consequence of the pursuit of a legitimate policy goal". As to 'effect', the panel stated that "a measure could be said to have the effect of affording protection to domestic production if it accorded greater competitive opportunities to domestic products than to imported products."

<sup>40</sup> WTO Dispute Settlement, EC – Bananas III, para. 241.

similar only if they are subject to the same regulatory framework.<sup>41</sup> This approach conforms to the principle of equality where equal treatment must be given to parties in similar conditions. In other words, this criterion would ensure that comparisons between foreign and national services and providers would be limited to services as well as service providers operating in the same mode of service provision.

In addition, another case-law from the WTO regarding likeness in services is Argentina - Financial Services. In that case, the WTO Appeal Board determined that the main criterion for similarity in the context of the GATS was whether and to what extent the service and service providers in question were in a competitive relationship. However, these similarities must be assessed on a case-to-case basis.

d. There is less favorable treatment

The GATS principle of non-discrimination stipulates that member states must agree to the provision of ‘no less favorable treatment’ or no less favorable treatment for similar services or service providers from other member states. The WTO Panel on the EC - Bananas III and China - Publications and Audiovisual Products disputes determined that this treatment includes both *de jure* and *de facto* discrimination.<sup>42,43</sup>

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<sup>41</sup> Agreement on Trade in Services, Communication from the United States, MTN.GNS/W/75, 17 October 1989.

See also: Concepts for a Framework Agreement in Services, Communication from the United States, MTN.GNS/W/24, 27 October 1987: “National treatment should generally require that foreign service providers receive treatment no less favorable in such circumstances than given to domestic service providers in connection with government actions affecting the service sector in question.... In most cases, the national treatment for foreign service providers will be identical to the treatment accorded to domestic service providers in the service sector concerned. regulations may require a modified approach to national treatment, which should be permitted under such frameworks in terms of national security considerations and fiduciary responsibilities. However, such treatment should at least be equal. non-identical treatment and ensure that there are no veiled violations of the principle of national treatment.”

<sup>42</sup> WTO Dispute Settlement, EC – Bananas III, paras. 231-234.

<sup>43</sup> China - Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products, WTO Dispute Settlement, Panel Report, paras. 7.978-7.979. “Formally identical or formally different treatment shall be considered to be less favourable if it modified the conditions of competition in favour of services or service suppliers of the Member compared to like services or service suppliers of any other Member. In our view, a measure that prohibits foreign service suppliers from supplying a range of services that may subject to satisfying certain conditions, be supplied by the like domestic supplier cannot constitute treatment ‘no less favourable’, since it deprives the foreign service supplier of any opportunity to compete with like domestic suppliers. In terms of paragraph 3 of Article XVII, such treatment modifies conditions of competition in the most radical way, by eliminating all competition by the foreign service supplier with respect to the service at issue.”

## **IV. INDONESIA'S AND THE EU'S DIGITAL SERVICES TAX COMPLY TO THE NON-DISCRIMINATION PRINCIPLES OF WTO**

Based on the test criteria described above, Indonesia's *PTE* and the EU's DST do not violate the GATS non-discrimination principle, because they only meet two of the three existing criteria. The test analysis criteria are as follows:

### **A. ACTIONS COVERED BY THE GATS**

As stated earlier, the GATS defines services as any service in any sector except those provided by a governmental authority. Based on this definition, digital services referred to in Council Directives are included in the service category covered by the GATS. In addition, the principle of Most-Favored Nation and National Treatment only applies to services performed in member states' Schedule of Commitment. Digital services in the *PMSE* that are subject to *PTE* in Government Regulation No. 1 of 2020 is also a service that does not exercise governmental authority. *PMSE* is defined in Article 1 paragraph (2) PP No. 80 of 2019 concerning Trading through Electronic Systems as follows: "*PMSE* is a trade whose transactions are carried out through electronic devices and procedures." Such services are included in Indonesia's Schedule of Commitment.

Similarly, the EU has liberalized the services covered by DST, such as advertising services as well as computer-based services and related services. This means that the European Union cannot enforce DST which discriminates against like services and service providers from other member states.<sup>44</sup> Therefore, it is clear that the service is provided for commercial purposes, therefore covered by the GATS.

### **B. LIKE SERVICES AND SERVICE PROVIDERS**

Several digital services imposed by Indonesia's *PTE* are considered similar. The first examples of such services or providers are Zoom and Skype. Zoom is an American communications technology company that provides video telephone and online chat services via a peer-to-peer software platform. Likewise, Skype which originates from Luxembourg and specializes in video chat and voice call services. The final functions used by users of the two services are also similar, that is, the two services are generally used for teleconferencing purposes. In addition, there is likeness between Amazon service providers from the United States and Shopee from Singapore. Both

<sup>44</sup> The EU cannot claim that to the extent the digital services covered by DST were not available or planned at the time its commitment schedule was agreed. See WTO Dispute Settlement, Appellate Body Report, China — Publications and Audiovisual Products.

are intermediary services in the form of an online shopping platform.

In the case of the imposition of the EU's DST, it can be seen that some EU digital services are similar to foreign digital services. One example of such service is Zalando, which is an online intermediary mode service based in Germany. Zalando has a similar service with Amazon which is also an online intermediary service originating from the United States. In fact, Zalando is often referred to as the European version of Amazon.<sup>45</sup> Both service providers use the platform method to connect service users, in this case sellers and buyers of products. The difference between the two services is in the products offered, namely the products offered by sellers on the Zalando platform only focus on the fashion and lifestyle categories.

Apart from these two service providers, there are other service providers that are considered similar, namely Trivago from Germany, Booking.com from the Netherlands and Airbnb from the United States. The three service providers provide an online hotel and lodging rental platform.<sup>46</sup> As in the case with Zalando and Amazon, these three service providers are also included in intermediary service providers.

## C. THERE IS NO LESS FAVORABLE TREATMENT

### 1. *De jure* discrimination is not proven

*De jure* discrimination, which is referred to as formal discrimination, is defined as the use of citizenship as an express regulatory criterion or the use of nationality as a certain regulatory criterion.<sup>47</sup> This means that actions can be categorized as *de jure* discrimination if they explicitly set different criteria, namely those that are less favorable, for like services and service providers from certain member states.

To determine whether there is national discrimination in Indonesia's PTE and the EU's DST, it is necessary to look at Perppu No. 1 of 2020 and Council Directives, especially regarding the service criteria imposed by digital services tax. In both of these regulations, there are no existing rules that

<sup>45</sup> Richard Weiss, "Zalando Gets Chance to Prove Itself Against Amazon," Bloomberg, 15 July 2020, accessed 11 December 2020, <https://www.bloomberg.com/news/articles/2020-07-16/zalando-gets-chance-to-prove-itself-against-amazon-during-covid>.

<sup>46</sup> Robert Carey, Del Ross, and Nathan Seitzman, "The (ongoing) trouble with travel distribution: Customer experience," McKinsey & Company, 27 February 2017, accessed 11 December 2020, <https://www.mckinsey.com/industries/travel-logistics-and-infrastructure/our-insights/the-ongoing-trouble-with-travel-distribution-customer-experience>.

<sup>47</sup> Federico Ortino, "WTO Jurisprudence on De Jure and De Facto Discrimination," in *The WTO Dispute Settlement System 1995-2003*, Federico Ortino and Ernst-Ulrich Petersmann, eds. (The Hague: Kluwer, 2004), 217.

explicitly give unfavorable treatment to like services and service providers from certain member states based on the origin of the services, therefore *de jure* discrimination is not proven to exist.

## 2. *De facto* discrimination is not proven

In Indonesia, the Directorate General of Taxes (*Direktorat Jenderal Pajak* or *DJP*) through its press release has confirmed 28 entities appointed as VAT collectors as part of PTE Indonesia. The 28 entities come from different countries, including Tiktok and Jingdong from China, Spotify and Mojang from Sweden, Novi from India, Zoom and Netflix from the United States, Skype from Luxembourg and Shopee and PCCW Vuclip from Singapore.

The 28 entities appointed by *DJP* are subject to *PTE* with the same nominal value, and based on the same criteria, namely these entities meet the standards of significant economic presence as stipulated in the Directorate General of Taxes Regulation Number PER-12 / PJ / 2020. Therefore, it can be concluded that there is no *de facto* discrimination in the imposition of *PTE* by Indonesia.

Meanwhile, there are opinions that the EU' DST is a form of *de facto* discrimination, as it is aimed at several US digital companies. Among these opinions were that the threshold for implementing DST was very high and would mostly include US companies. This is considered as evidence that DST is aimed at only a few US companies, because the largest digital service provider in the EU, Spotify, which is one of the few EU companies that meets the opinion threshold is exempted from the definition of digital services imposed by the EU's DST.<sup>48</sup>

In reality, the EU's DST applies to many companies from the United States and China. However, this is due to the fact that most of the digital service providers with the largest revenue in the world come from these two countries. The top five digital service providers with the largest revenue are Amazon, Google, JD.com, Facebook, and Alibaba, Amazon, Google, and Facebook from the United States, while JD.com and Alibaba are from China. However, this does not mean that all service providers outside the two countries are excluded. There are several EU service providers that meet the DST imposition criteria, including Zalando and Booking.com.<sup>49</sup> In addition, the regulations in DST that exclude Spotify, namely in Article 3 paragraph (4) of the Council Directive 2018/0072 / EC, also exclude other services such as Apple Music and Google Playstore. Therefore, it cannot be concluded that

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<sup>48</sup> Hosuk Lee-Makiyama, "The cost of fiscal unilateralism: Potential retaliation against the EU Digital Services Tax (DST)," *ECIPE Occasional Paper* 5 (2018): 6.

<sup>49</sup> Zalando's global revenue reaches € 6,483 billion and Booking.com's global revenue reaches € 12,363 billion. See Weiss, "Zalando Gets Chance."



there is de facto discrimination as alleged.

## V. CONCLUSION

This paper concludes that there are two types of digital service tax regulated in Indonesia and in the EU, namely Income Tax and VAT in Indonesia's *PTE* and tax on digital company profits and income tax on digital flows in the EU's DST. The Income Tax imposition regulation for electronic trade providers (*Penyelenggara Perdagangan Melalui Sistem Elektronik* or *PMSE*) does not use the ring-fencing method but instead applies to all *PMSE* that meet a threshold of significant economic presence similar to that of the EU. In contrast to Income Tax, VAT only applies to foreign digital service providers who are appointed as VAT collectors by *DJP*. Meanwhile, the regulation on the imposition of income tax on digital streams uses the ring-fencing method, so that taxes are only imposed on two service categories, namely the provision of an electronic interface that connects one user to another and targeted advertising services.

The imposition of *PTE* by Indonesia and the DST by EU does not violate the WTO's non-discriminatory principles, namely the National Treatment and Most-Favored Nation principles in Article II and Article XVII of the GATS. The reason is that the imposition of digital services tax in Indonesia and the EU does not meet the overall criteria used to determine discrimination. To be declared discriminatory, an action of member state must meet the following three criteria: (i) whether the act is covered by the GATS; (ii) whether the service or service provider between member states is similar; (iii) whether they are given unfavorable treatment, either de jure or de facto discrimination. The implementation of *PTE* by Indonesia and DST by the EU only fulfills two criteria, namely that these measures are covered by the GATS, and that services and service providers from Europe and outside of Europe subject to DST are also assessed similarly. However, the last criterion was not met.

In order to respond to the allegations of discriminatory practices made towards the implementation of digital services tax, this work recommends that (i) should there are WTO member states that file a claim for discrimination against Indonesia's *PTE* or the EU's DST, Indonesia and the EU must prepare evidence to thwart the allegation of discrimination. Evidence prepared by Indonesia and the EU must show that in practice, Indonesia's *PTE* and the EU's DST not only impose taxes on the service providers of certain member states, but all digital service providers of all member states, as long as they meet the requirements for the imposition of electronic transaction taxes in



regulatory instruments related; and (ii) should a member state takes retaliatory action against Indonesia or the EU because of the imposition of a digital service tax, then Indonesia and the EU can file a discrimination suit against the WTO for such action. This is because unilateral sanctions from these member states cannot be justified, so that claims of discrimination in international trade between WTO members must be resolved through the WTO dispute resolution mechanism. Therefore, the action of retaliation can be categorized as unfavorable treatment and therefore can be sued to the WTO.

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