

## US issues findings of Section 301 investigation regarding France's Digital Services Tax; proposes imposition of tariffs

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### Executive summary

On 2 December 2019, the United States (US) Trade Representative (USTR) announced the findings of an investigation under Section 301 of the *Trade Act of 1974* (Section 301) into France's Digital Services Tax (DST).<sup>1</sup> The USTR determined that the French DST creates an unreasonable or discriminatory burden to US Commerce and in response proposed that the US impose tariffs of up to 100% on approximately US\$2.4<sup>2</sup> billion of French-origin goods.

### Detailed discussion

On 6 March 2019, the Government of France published a proposal for a DST. The tax, signed into law on 24 July 2019 by France's President Emmanuel Macron, consists of a 3% levy on global revenues generated by "digital interface" services provided to French users. The tax is retroactive to 1 January 2019 and applies to companies that have global, annual revenues in excess of €750 million, or \$845 million at the current exchange rate, and that have €25 million, or \$28.15 million, of digital sales that are generated in France. The tax is estimated to impact 30 companies, which includes one French company, and is expected to raise approximately €500 million (See EY Global Tax Alert, [US initiates action against France's Digital Services Tax, issues additional exclusions on China-origin goods and supplements list of products under EU subsidies dispute](#), dated 12 July 2019).

As the DST bill moved through the French legislative process, the USTR announced on 10 July the initiation of a Section 301 investigation into the French DST. The investigation had three objectives: to determine if the French tax was discriminatory against US companies; to assess the fairness of the retroactivity of the tax; and to determine if it was an unreasonable tax policy based on US and international tax norms.<sup>3</sup> Additionally, the USTR sought public comment regarding concerns about the tax and what action the US should take should the DST be found to be harmful to the US economy.

On 2 December 2019, the USTR released a report of the investigation findings along with the issuance of a USTR notice summarizing the findings, proposed actions, and next steps. The USTR's notice states that the DST creates a burden on US commerce due to five primary findings: (i) the tax is discriminatory against US digital companies; (ii) the retroactive application is inconsistent with prevailing tax principles; (iii) the tax's application to revenue rather than income is inconsistent with existing tax principles; (iv) the tax's application to revenues unconnected to a physical presence in France contravenes prevailing international tax principles; and (v) the tax's application to a small group of digital companies violates international tax principles against targeting the digital economy. Based on these findings, the US is entitled to take appropriate, responsive action under Section 301. On this basis, the USTR proposed tariffs of up to 100% on French-origin goods, preliminarily covering 63 tariff subheadings, with an estimated value of approximately \$2.4 billion of import value.

Products on the preliminary list include:

- ▶ Various cheese imported under harmonized tariff of the US (HTSUS) 0406
- ▶ Sparkling wine imported under HTSUS 2204.10
- ▶ Make-up, such as lip make-up preparations and eye make-up preparations imported under HTSUS 3304.10 and HTSUS 3304.20, respectively
- ▶ Soaps imported under HTSUS 3401.11
- ▶ Various handbags imported under HTSUS 4202.21 and HTSUS 4202.22
- ▶ Porcelain and china imported under HTSUS 6911

The USTR is seeking public comments regarding the specific products to be subject to tariffs and the level of duty rate increase, if any. A public hearing has been scheduled following the comment period.

In addition to the proposed duties, the USTR is considering the imposition of fees or restrictions on services from France and seeks public comments with respect to which services, if any, should be covered by a fee or restriction. Specifically, if a fee is imposed, the USTR requests comments on the rate (flat or percentage) of the fee and the basis upon which any fee should be applied, and if a restriction is imposed, the USTR requests comments on the form of such restriction and whether the imposition of fees or restrictions on services from France would be practicable or effective in obtaining the elimination of France's acts, policies, and practices.

The timeline for public comments and hearings is as follows:

- ▶ 30 December 2019: Due date for submission of a request to appear at the public hearing and a summary of testimony
- ▶ 6 January 2020: Due date for written comments
- ▶ 7 January 2020: The Section 301 Committee will convene a public hearing in the main hearing room of the US International Trade Commission, 500 E Street SW, Washington DC 20436 beginning at 9:30 am ET
- ▶ 14 January 2020: Due date for submission of post-hearing rebuttal comments

It should be noted that no tariff increases under this action will take place until after the 14 January post-hearing rebuttal comments, allowing for the US and France to negotiate a deal prior to any tariff or fee implementations. President Trump stated before a recent bilateral meeting with President Macron at the North Atlantic Treaty Organization (NATO) summit in London on 3 December that the US conducts significant trade with France and he believes that a resolution may be attainable with respect to the USTR proposed tariffs.

Additionally, in a press release from the USTR regarding the Section 301 report and findings, USTR Robert Lighthizer stated that the USTR is, "exploring whether to open Section 301 investigations into the digital services taxes of Austria, Italy, and Turkey" as the USTR is "focused on countering the growing protectionism of EU member states, which unfairly targets U.S. companies, whether through digital services taxes or other efforts that target leading U.S. digital services companies,"<sup>4</sup> suggesting this may be the start of further investigations that highlight how trade in goods and trade in services are beginning to intermingle.

## Actions for businesses

Companies that import French-origin goods on the preliminary list should closely monitor the progression of the proposed USTR actions and negotiations between the two nations. Immediate actions companies can consider are:

- ▶ Fully understand the extent of products impacted on the proposed list of 8-digit Harmonized Tariff codes
- ▶ Consider filing comments in response to the announced list and, based on the degree of impact, consider requesting to appear at the public hearing on 7 January 2020
- ▶ Explore strategies to defer, eliminate, or recover the additional duties such as use of bonded warehouses, Foreign Trade Zones, substitution drawback, and Chapter 98
- ▶ Explore strategies to minimize the customs value of imported products subject to the additional duties and for US imports, considering US customs strategies, such as First Sale for Export
- ▶ Consider current transfer pricing of imported products, keeping in mind the importance of alignment of the income tax transfer price with the customs value to avoid inventory basis limitations under Internal Revenue Code Section 1059A

US distributors who purchase from related parties will almost certainly have transfer prices impacted by the imposition of 301 duties. Along with the strategic importance of mitigating duty impact while aligning the income tax and customs approaches, mechanics for reporting any transfer pricing adjustments to US Customs should also be reviewed. This process may be particularly complex when duties are present for only a portion of the year, and in many cases, actions need to be taken in advance of importations.

US Customs has very specific rules for reporting adjustments to prices made after importation, such as transfer pricing adjustments. These rules require that the importer take specific actions before importation of goods for which prices may be adjusted, including adding customs specific language to transfer pricing policies. As these new 301 duties, if implemented, will likely take effect early next year, importers are well advised to address these requirements now in order that they be in place when 301 duties are imposed.

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## Endnotes

1. [https://ustr.gov/sites/default/files/Notice\\_of\\_Determination\\_and\\_Request\\_for\\_Comments\\_Concerning\\_Action\\_Pursuant\\_to\\_Section\\_301\\_France%E2%80%99s\\_Digital\\_Services\\_Tax.pdf](https://ustr.gov/sites/default/files/Notice_of_Determination_and_Request_for_Comments_Concerning_Action_Pursuant_to_Section_301_France%E2%80%99s_Digital_Services_Tax.pdf)
2. Unless otherwise designated, all currency references in the Alert are in US\$.
3. 84 FR 34042.
4. See USTR press release, [Conclusion of USTR's Investigation Under Section 301 into France's Digital Services Tax](#).

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