Taxation in the Digital Economy: How Should Digital Service Taxes be Implemented?

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Abstract

The digitalization of the economy has presented profound challenges to the traditional international tax framework, which is predicated on the principle of physical presence through a "Permanent Establishment". This long-standing concept has proven inadequate for capturing the economic activities of multinational enterprises operating within the digital sphere, leading to significant tax base erosion in market jurisdictions and raising fundamental questions of fairness in the allocation of taxing rights. This article aims to synthesize and analyze the multifaceted legal issues arising from this paradigm shift. Through a documentary research methodology, it conducts a comparative legal study of the approaches adopted by various jurisdictions, namely, unilateral Digital Services Taxes and adaptations of indirect tax systems. The study further dissects the principal legal challenges, including compatibility with double

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taxation conventions and World Trade Organization law. Ultimately, this article proposes a desirable hybrid policy approach for Thailand, advocating for long-term alignment with emerging global standards while implementing prudent and contextually appropriate transitional measures.

Keywords: digital service tax, permanent establishment, pillar one

1. Introduction

The international tax law system, which has long been in force, is founded on the principle that a state may only tax the profits of a foreign enterprise if that enterprise has a significant physical ‘nexus’ within that state, typically in the form of a ‘Permanent Establishment’ (PE). This principle was developed in an era dominated by a brick-and-mortar economy. However, the dynamics of the global economy have been fundamentally altered by the advent of the digital economy, which has now become an inseparable part of the real economy, encompassing various business models such as app-stores, online advertising, cloud services, and digital platforms. This transformation has dismantled physical barriers, allowing multinational enterprises to conduct business, interact with consumers, and generate substantial revenue in states worldwide without needing a single permanent establishment. In many cases, even when substantial economic activities occur in a market jurisdiction, that state lacks the authority to tax such transactions due to the absence of a PE, resulting in the taxing rights on that income falling solely to the residence state[1]. Furthermore, there is a discernible trend of digital firms deliberately establishing their income-generating entities in low-tax jurisdictions to minimize their tax liabilities. This situation has created a severe mismatch between modern business models and traditional tax rules, leading to the erosion of the tax base in market jurisdictions and reflecting an inequity in the international allocation of taxing rights.

However, the dynamics of the global economy have been fundamentally altered by the advent of the digital economy, which has now become an inseparable part of the real economy, encompassing various business models such as app-stores, online advertising, cloud services, and digital platforms. This transformation has dismantled physical barriers, allowing multinational enterprises to conduct business, interact with consumers, and generate substantial revenue in states worldwide

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[1]Daniel Bunn, Elke Asen and Cristina Enache, **Digital Taxation around the World)** [Online], available URL: https://files.taxfoundation.org/20200527192056/Digital-Taxation-Around-the-World.pdf, 2024 (July, 19).

without needing a single permanent establishment. In many cases, even when substantial economic activities occur in a market jurisdiction, that state lacks the authority to tax such transactions due to the absence of a PE, resulting in the taxing rights on that income falling solely to the residence state[2]. Furthermore, there is a discernible trend of digital firms deliberately establishing their income-generating entities in low-tax jurisdictions to minimize their tax liabilities. This situation has created a severe mismatch between modern business models and traditional tax rules, leading to the erosion of the tax base in market jurisdictions and reflecting an inequity in the international allocation of taxing rights.

This article, therefore, aims to synthesize and analyze the relevant legal issues and, through a comparative study of foreign jurisdictions, to propose a suitable approach for the implementation of tax laws in Thailand. This study is documentary research, relying on the analysis of statutes, conventions, reports from international organizations, and related academic literature.

2. Content

2.1 Limitations of the Traditional International Tax Framework and Developments Towards a Global Standard

First and foremost, an inquiry into the problem must commence with establishing a conceptual framework for what constitutes a sound tax system. Adam Smith's Four Canons of Taxation[3], despite their age, remain an influential theory and serve as a robust benchmark for evaluating tax policy. These four principles consist of: (1) Equality, which posits that the tax burden should be in proportion to the taxpayer's ability to pay, and those with equal ability should bear an equal tax burden; (2) Certainty, which requires that tax rules be clear and predictable; (3) Convenience, meaning that the method and timing of tax payment should be as convenient as

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[2]Ibid.

[3]Adam Smith, **Wealth of Nations** (UK: Bantam Classics, 2003), pp. 1043-1045. Peter Harris and David Oliver, **International Commercial Tax** (UK: Cambridge University Press, 2010), pp. 43-44.

possible for the taxpayer; and finally, (4) Economy, which signifies that the state's cost of tax collection should be minimized, ensuring that the cost incurred by the state does not exceed the tax revenue it collects.

In designing tax policies, especially tax object, tax base and tax rate, regard shall be had to these foundational principles in order to deliver a fair and effective tax imposition.

The canon of equality must especially be addressed in relation to the challenges of digital economy: taxpayers with the same ability to pay tax should be taxed equally. A sound and reasonable tax system should not leave a room for distortion of tax imposition merely by the reason of differences in physical locations where the business premises are situated while the economic value is created and rendered in the same manner.

The main concern would be about allocation of taxing rights between jurisdictions. It is crucial that a jurisdiction to which a taxpayer owes an appropriate economic allegiance, which is normally presented in the forms of source of income and residence, shall have the right to tax[4]. In an international context, a taxpayer may owe economic allegiance to more than one jurisdiction. A taxpayer may be a resident of a jurisdiction and have a source of income in another jurisdiction. This is the case where the economic allegiance is divided, and it would come with a question of which jurisdiction shall have the right to tax. Therefore, many countries entered into double tax agreements, which determine the taxing rights of the contracting states on a particular item of income.

Based on double tax agreements adopted by most countries, which are OECD Model[5] and UN Model[6], a certain level of physical presence is required in order to impose income tax on business profit. A source of income state cannot impose tax on business profit unless there is a permanent establishment in the source of income state, and such income is derived through the permanent establishment, pursuant to article 7 and article 5 of the treaty model. In the absence of a permanent

[4]Peter Harris and David Oliver, **International Commercial Tax** (UK: Cambridge University Press, 2010), pp. 43-44.

establishment, only the state in which an enterprise is a resident can impose tax on that amount of business profit. Permanent Establishment is generally defined as "a fixed place of business through which the business of an enterprise is wholly or partly carried on". In most cases, Permanent Establishment would be considered to exist by a presence of (1) a place of management; (2) a branch; (3) an office; (4) a factory; (5) a workshop; and (6) a mine, oil or gas well a quarry or any other place of extraction of natural resources. In addition, Permanent Establishment may be deemed to exist by other activities, such as having an agent or dependent status in a source of income state or furnishing of services in a source of income state for a certain specified period in DTAs entered into by contracting states.

However, in the era of digitalization, it becomes evident that the "Permanent Establishment" (PE) principle, as stipulated in the model conventions of the Organization for Economic Co-operation and Development (OECD) and the United Nations (UN) and widely adopted globally, is no longer adequate to address the borderless nature of digital business models. This limitation has spurred efforts to seek a new global standard. A significant development in this regard is the concept of a "Digital Permanent Establishment," introduced by the EU Commission in 2018[7], which represents a theoretical attempt to reform the criteria for establishing a tax nexus. This concept shifts the focus from a reliance on physical presence to a consideration of significant economic presence. It redefines economic connection through new, non-physical quantitative criteria, such as revenue thresholds, the number of users,

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[5]OECD, **Model Tax Convention on Income and on Capital: Condensed Version 2017** [Online], available URL: https://www.oecd.org/ctp/treaties/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm, 2024 (June, 16).

[6]United Nations, **United Nations Model double Taxation Convention between developed and developing countries 2021** [Online], available URL: https://financing.desa.un.org/sites/default/files/2023-05/UN%20Model_2021.pdf, 2024 (June, 16).

[7]European Commission, **Fair taxation of the digital economy** [Online], available URL: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/1163-Fair-taxation-of-the-digital-economy_en, 2024 (July, 1).

or the number of business contracts for digital services within a state. This theoretical shift aims to address the shortcomings of the traditional PE model in capturing the economic activities of digital firms and to ensure that profits are taxed in the jurisdiction where substantial economic activities take place.

Even more significant is the OECD/G20's Two-Pillar Solution[8], particularly Pillar One, which represents a veritable paradigm shift in international tax law. Its core lies in the "Amount A" principle, a mechanism that establishes new taxing rights for market jurisdictions, obviating the need for a physical nexus[9]. This mechanism applies to large multinational enterprises with global revenues exceeding €20 billion and profitability over 10%. It mandates that 25% of the residual profits, defined as profits exceeding a 10% margin on revenue, be reallocated to market jurisdictions in proportion to the revenue generated in each state. This principle would enhance fairness in tax collection between the market jurisdiction and the residence jurisdiction. Therefore, Pillar One is not merely an amendment to existing principles but the creation of a new profit allocation system that operates alongside the traditional one, representing a historic attempt to reform international tax law[10].

[8]KPMG, **BEPS 2.0: Pillar One and Pillar Two** [Online], available URL: https://kpmg.com/xx/en/home/insights/2020/10/beps-2-0-pillar-one-and-pillar-two.html, 2024 (July, 29).

[9]OECD, **Fact Sheet Amount a Progress Report on Amount of Pillar One** [Online], available URL: https://www.oecd.org/content/dam/oecd/en/topics/policy-issues/cross-border and-international-tax/pillar-one-amount-a-fact-sheet.pdf, 2024 (July, 29).

[10]OECD, **Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint: Inclusive Framework on BEPS** [Online], available URL: https://www.oecd.org/en/publications/tax-challenges-arising-from-digitalisation-report-on-pillar-one-blueprint_beba0634-en.html,2024 (July, 11).

2.2 Lessons from International Jurisdictions: A Comparative Legal Study

In response to the aforementioned challenges, various jurisdictions have adopted different approaches, which can be classified into two main groups:

2.2.1 Group One: States Adopting Unilateral Digital Services Tax (DST) Measures

This approach is prominent among European countries such as the United Kingdom[11], France, and Italy.

Concurrent with the consideration of unilateral Digital Services Tax (DST) measures by several European nations, significant developments were also taking place at the European Union level. In March 2018[12], the European Commission put forward a set of proposals aimed at ensuring fair taxation in the digital economy. These proposals consisted of two main components:

1) A long-term, comprehensive solution: This proposal aimed to reform corporate tax rules so that profits are registered and taxed where businesses have a significant digital interaction with users. It introduced the concept of a 'Digital Permanent Establishment'.

2) A short-term, interim measure: This was a proposal for a temporary tax on revenues from certain digital activities. The proposed DST would apply at a rate of 3% on gross revenues derived from specific digital services, intended as a provisional measure until a comprehensive global solution was implemented.

However, the EU-wide DST proposal failed to achieve the required unanimous agreement among all member states, bringing the initiative to a halt. This lack of consensus at the EU level was a key factor that prompted individual member states, such as France and Italy, to proceed with their own national DST legislation. These countries viewed their unilateral measures as a necessary interim step while awaiting a clear global framework from the OECD.

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[11] HM Treasury, UK Agrees Transition Toward New Global Tax System [Online], available URL: https://www.gov.uk/government/news/uk-agrees-transition-toward-new-global-tax-system#:~:text=the%20UK%20introduced%20a%20temporary,global%20agreement%20is%20in%20place, 2024 (July, 19).

[12] European Commission, **Press release - Fair taxation of the digital economy: Commission proposes new measures to ensure that all companies pay fair tax in the EU** [Online], available URL: https://ec.europa.eu/commission/presscorner/detail/en/ip_18_2041, 2025 (September, 15).

The scope of these measures focuses on specific types of digital services believed to generate value from the user base, including online advertising, digital intermediary services and the sale of user-collected data. A key feature of DST is the taxation of gross revenue at a relatively low rate (approximately 2-5%), often with both global and domestic revenue thresholds to target large multinational enterprises. However, the primary intention of these states is to implement such measures on a temporary basis, with the goal of repealing them once a global agreement comes into force.

The advantage of this approach is that it allows a state to assert its tax sovereignty and collect revenue immediately, without waiting for an international consensus, which is often a lengthy and complex process. However, this approach carries several risks. These include the risk of trade disputes and retaliatory measures, as seen in the tensions between the United States and European nations[13]. Secondly, it leads to unavoidable double taxation, as gross revenue is taxed as DST in the market jurisdiction while net profit is subject to corporate income tax in the residence jurisdiction, a point which will be elaborated upon later. Lastly, it risks being viewed as a measure that contravenes the non-discrimination principle under World Trade Organization (WTO) law, which will also be discussed in a subsequent section.

2.2.2 Group Two: States Adapting Their Indirect Tax Systems

This approach is popular in many countries, including Thailand (VAT for e-Services)[14] and most nations in Southeast Asia. Its scope involves amending existing Value-Added Tax (VAT) or Goods and Services Tax systems to cover the provision of electronic services from abroad to consumers. This includes services such as video and music streaming, software and game downloads, and cloud services. The mechanism requires foreign service providers to register and remit VAT to the state where the consumer resides.

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[13]Deloitte, US extends ‘truce’ with countries imposing digital services taxes [Online], available URL: https://dhub.deloitte.com/Newsletters/Tax/2024/TNV/240216_3.pdf, 2024 (July, 22).

[14]EY, Thailand’s application of VAT on digital services (e-services) provided by foreign operators will apply as of 1 September 2021 [Online], available URL: https://www.ey.com/en_gl/tax-alerts/thailand-s-application-of-vat-on-digital-services-e-services-provided-by-foreign-operators-will-apply-as-of-1-september-2021, 2024 (July, 29).

The most significant strength of this approach is its consistency with international tax principles and WTO rules, as it treats domestic and foreign service providers equally. It also builds upon an existing tax framework, which is easier to understand and administer than creating a new tax type. However, this approach is limited to the collection of a consumption tax and does not resolve the issue of income tax. That is, while the state can collect VAT revenue, it does not address the profit allocation of multinational enterprises, which continue to be taxed (or not taxed) in other jurisdictions. Furthermore, under tax mechanics, the economic burden is often passed on to the end consumer, making it an unavoidable burden for them.

2.3 Legal Challenges Arising from the Implementation of Digital Service Tax Measures

The unilateral implementation of DST measures gives rise to complex and significant challenges in international law, which can be analyzed as follows:

Compatibility with Double Taxation Conventions: This issue stems from the interpretation of Article 2 (Taxes Covered) of the conventions, which typically applies only to “taxes on income and on capital.” By the literal meaning, DST would not be covered by the Article 2; however, the fact that DST is levied on gross revenue without any deduction for expenses creates a classification problem as to whether DST can be considered a disguised “income tax” within the meaning of the convention. This leads to the risk of domestic law conflicting with or overriding treaty obligations (Treaty Override), an act that undermines the stability of the international legal system. Although, in theory, a state implementing a DST might invoke the principle of a Fundamental Change of Circumstances (Rebus Sic Stantibus) under Article 62 of the Vienna Convention on the Law of Treaties,[15] arguing that the rise of the digital economy was an unforeseeable event at the time the treaty was concluded. However, proving the conditions for this principle is exceedingly difficult in practice.

Rebus sic stantibus is a principle of international law that allows a state to withdraw from or modify a treaty when there has been a fundamental and unforeseen change of circumstances that formed the basis of the parties’ original consent to be bound by the treaty. Codified in Article 62 of the Vienna Convention on the

[15]Vienna Convention on the Law of Treaties 1969, Article 62.

Law of Treaties, it operates as a narrow exception to the general rule of pacta sunt servanda (agreements must be kept). For the doctrine to apply, the change must be (1) fundamental, (2) unforeseeable at the time of treaty conclusion, (3) essential to the treaty's foundation, and (4) radically transform the nature or scope of obligations remaining to be performed. Because these conditions are interpreted very strictly by international courts and tribunals, successful invocation of rebus sic stantibus is extremely rare in practice.

Theoretically, a state implementing a DST could attempt to invoke the doctrine of rebus sic stantibus under Article 62 of the Vienna Convention on the Law of Treaties as a legal justification for deviating from existing treaty obligations.

The argument would rest on the claim that the rapid and unprecedented rise of the digital economy constitutes a "fundamental change of circumstances" that was neither foreseen nor foreseeable at the time most bilateral tax treaties were concluded.

In this line of reasoning, the traditional nexus rule based on physical presence, central to most double taxation conventions, no longer reflects the economic reality of value creation in the digital era. Consequently, a state may contend that the basis upon which it consented to limit its taxing rights has fundamentally changed, thus entitling it to modify or withdraw from its treaty obligations regarding income taxation.

Issues under World Trade Organization (WTO) Law: DST measures may be challenged as being inconsistent with the non-discrimination obligations under the General Agreement on Trade in Services (GATS), particularly Article II:1, which establishes the Most-Favoured-Nation (MFN) treatment principle, requiring member states to treat services and service providers of any other member state equally and without discrimination. Although DST legislation is neutral in its wording and does not specify any country, the high global revenue thresholds mean that only a few enterprises are subject to the tax, which could be interpreted as de facto discrimination.[16]

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[16]Chris Forsgren, Sixian Song and Dora Horváth, Digital Services Taxes: Do They Comply with International Tax, Trade, and EU Law? [Online], available URL: https://taxfoundation.org/research/all/federal/france-digital-tax-international-tax-law-trade-law-eu-law/#:~:text=The%20French%20DST%20Could%20Be,DST%20under%20international%20trade%20law, 2024 (July, 29).

Double Taxation and Relief: This problem is a direct consequence of the treaty compatibility issue because reliefs under tax treaties would apply only to the taxes covered by such tax treaties. For example, in most tax treaties entered into by Thailand, the taxes covered, in respect of Thai taxes, encompasses only income tax and petroleum tax. This means that the reliefs under tax treaties would apply to only income tax and petroleum tax.

Generally, there are two mechanisms for the relief of double taxation under tax treaties: the Exemption Method under Article 23A and the Credit Method under Article 23B of the model convention.

Under Exemption Method, the residence state agrees to exempt foreign-sourced income from domestic taxation once it has been taxed in the source state. In practical terms, this means that if a company earns income abroad and that income is subject to tax in the source jurisdiction, the residence jurisdiction will exclude that income from its own tax base, thereby avoiding any further taxation on the same amount.

Under Credit Method, the residence state continues to tax the income but grants a credit for taxes already paid in the source state. This allows the taxpayer to deduct the amount of foreign tax from the domestic tax liability, ensuring that the total tax burden is capped at the higher of the two rates rather than being cumulative.

Therefore, if a DST is not considered a tax covered by the convention, neither the mechanisms for eliminating double taxation under Article 23A (Exemption Method) nor Article 23B (Credit Method) could be applied. Consequently, the same income base is taxed twice: first as DST on gross revenue in the market jurisdiction, and second as corporate income tax on net profit in the residence jurisdiction. The residence state is not obliged to provide a tax credit for the DST paid by its enterprises. Such a state of complete double taxation poses a significant obstacle to international trade and investment.

2.4 The Current Thai Legal Framework: VAT on Electronic Services

In response to the challenges of the digital economy, Thailand has already taken a significant legislative step by adapting its indirect tax system. The primary legal instrument governing this area is the **Amendment to the Revenue Code Act (No. 53)**

B.E. 2564 (2021)[17], which came into force on September 1, 2021. This legislation effectively extends the Value-Added Tax (VAT) regime to cover electronic services provided by non-resident businesses to non-VAT registered customers in Thailand.

The key mechanics of this framework are as follows:

1) Definition of Electronic Services: The law provides a broad definition of "electronic service" (e-Service) to encompass a wide range of digital products and services that are intangible and delivered over the internet or other electronic networks. This includes, but is not limited to, online advertising, digital content streaming (music and videos), software downloads, and platform intermediary services.

2) VAT Liability for Foreign Providers: The core provision imposes a duty on foreign e-Service providers and foreign electronic platforms to register for VAT in Thailand if their annual revenue derived from providing such services to non-VAT registrants in Thailand exceeds THB 1.8 million. Once this threshold is met, the foreign entity is obligated to file VAT returns and remit the 7% VAT to the Thai Revenue Department without being able to claim input tax.

3) Simplified Administrative System: To facilitate compliance, the Revenue Department has established a simplified, online registration and remittance system known as the **VAT for Electronic Service (VES) system**. This "One-Stop Service" platform allows foreign operators to manage all their VAT obligations, from registration to filing and payment, remotely, thereby minimizing the administrative burden that would typically be associated with cross-border tax compliance. This framework represents Thailand's pragmatic initial step, aligning with the 'Group Two' approach of adapting existing indirect tax systems to the realities of the digital age.

2.5 An Analysis of the Thai Fiscal Landscape in the Digital Era

Before formulating a bespoke policy for Thailand, it is imperative to analyze the domestic fiscal landscape to contextualize the legal challenges and opportunities presented by the digital economy. Three core dimensions warrant examination: the

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[17] Revenue Code Amendment Act (No. 53) B.E. 2564 (A.D. 2021), published in the Royal Thai Government Gazette, Vol. 138, Part 10A (10 February 2021).

scale of the digital market, the performance of existing tax measures, and the potential impact of future tax instruments.

First, the sheer scale and growth trajectory of Thailand's digital economy establish a compelling case for policy reform. The market's Gross Merchandise Value (GMV) reached an estimated $36 billion in 2023 and is projected to expand to approximately $50 billion by 2025, driven primarily by e-commerce and online media consumption.[18] This burgeoning economic activity represents a substantial and dynamic tax base that, under the constraints of the traditional physical-nexus principle, remains largely outside the jurisdictional reach of Thailand's corporate income tax system. The continued erosion of this potential tax base necessitates an urgent reconsideration of how taxing rights are allocated in the modern economy.

Second, the successful implementation of Thailand's Value-Added Tax (VAT) on electronic services supplied by foreign providers, effective since September 1, 2021, offers critical empirical insights. The measure has proven to be a robust source of revenue, yielding THB 10.67 billion in its first full fiscal year (FY2022) and maintaining a strong performance with THB 10.03 billion in FY2023 and over THB 11.1 billion collected in the first eleven months of FY2024.[19] This outcome not only validates the administrative capacity of the Thai Revenue Department to manage and enforce tax collection from non-resident digital enterprises but also confirms that an indirect tax framework—as discussed in the comparative analysis of 'Group Two' states—is a viable and effective policy tool for the Thai context.

Lastly, while a unilateral Digital Services Tax (DST) presents a direct mechanism for taxing income, its potential fiscal benefits must be carefully weighed against its inherent legal risks. Several European nations have adopted this model; for instance, France, Italy, and Spain have set their DST rates at 3% of gross revenues, while the United Kingdom's rate is 2%. Based on international benchmarks and

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[18]Temasek and Bain & Company, **e-Conomy SEA 2023: Reaching new heights of digital growth** [Online], available URL: https://www.bain.com/insights/e-conomy-sea-2023/, 2025 (September, 17).

[19]Bangkok Post, **E-service tax revenue exceeds target in first 10 months, 16 August 2024** [Online], available URL: https://www.bangkokpost.com/business/general/2975471/revenue-collection-for-first-5-months-surpasses-target, 2025 (September, 17).

OECD modeling, a narrowly tailored DST levied at a rate of 3% could, hypothetically, generate an additional THB 3 to 5 billion in annual income tax revenue for Thailand. However, as this article has already established, such a measure carries significant risks of provoking trade disputes, contravening international treaty obligations, and creating conditions of economic double taxation. Therefore, this potential revenue gain cannot be the sole determinant of policy, but rather must be assessed within the broader legal and strategic framework. This fiscal analysis provides the essential, evidence-based foundation upon which a prudent and context-specific policy for Thailand can be constructed.

It is crucial, however, to distinguish the nature of a 2-3% DST from Thailand's 7% VAT on e-Services, as they are fundamentally different taxes in both principle and application. A DST is a tax on the gross *revenue* of a company, designed as a proxy for an income tax on profits generated from a user base in a market jurisdiction. In contrast, Thailand's 7% VAT is a tax on *consumption*, levied on the transaction value paid by the end consumer. Although remitted by the foreign provider, the economic burden is designed to fall on the customer. Therefore, the lower rate of a DST reflects its application to a broad revenue base without deductions for expenses, whereas the 7% rate is consistent with standard consumption tax principles. In essence, they serve distinct policy goals: a DST addresses the challenge of corporate profit allocation, while the VAT on e-services ensures that consumption within Thailand is taxed uniformly, regardless of the provider's location.

2.6 Foreign Policy Risks and Potential Trade Retaliation from the United States

Beyond the multilateral framework of the WTO, a unilateral implementation of a DST by Thailand would introduce significant foreign policy risks, particularly concerning its trade relationship with the United States. The U.S. government has consistently and unequivocally opposed unilateral DSTs, viewing them as discriminatory measures that unfairly target American technology companies.[20]

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[20]United States Trade Representative, **Section 301 – Digital Services Taxes** [Online], available URL: https://ustr.gov/issue-areas/enforcement/section-301-investigations/section-301-digital-services-taxes, 2025 (September, 17).

The primary instrument for U.S. response is Section 301 of the Trade Act of 1974, which authorizes the United States Trade Representative (USTR) to investigate and retaliate against foreign trade practices deemed unfair or burdensome to U.S. commerce. This is not a theoretical threat; the USTR has initiated Section 301 investigations into the DSTs of numerous countries, including France, India, Italy, Spain, and the United Kingdom, and has prepared retaliatory tariffs on their goods.[21] While these tariffs were ultimately suspended to allow for negotiations at the OECD, the actions signal a clear willingness by the U.S. to leverage trade sanctions to protect its interests.

For Thailand, this risk is particularly acute. The United States is not merely a significant trading partner; it is Thailand's largest export market, with bilateral trade in goods valued at over $72 billion annually.[22] Key Thai export sectors, such as computer equipment, automotive parts, and agricultural products, are vital to the national economy and could become targets for retaliatory tariffs.

Therefore, any policy consideration of a unilateral DST must carefully weigh the potential, and relatively modest, revenue gains against the profound and potentially disruptive risk of damaging a vital trading partnership. This geoeconomic reality serves as a powerful deterrent and reinforces the argument for pursuing a consensus-based, multilateral solution in alignment with the OECD framework.

2.7 Policy Recommendations and a Proposed Approach for Thailand

After considering the developments and legal issues, the author believes that the most desirable approach for Thailand should be a **Hybrid Approach**, which can be broken down into concrete policy recommendations as follows:

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[21]Sandler, Travis & Rosenberg, P.A., **Section 301 Investigation of Digital Services Taxes** [Online], available URL: https://www.strtrade.com/trade-news-resources/tariff-actions-resources/section-301-investigation-digital-services-taxes, 2025 (September, 17).

[22]United States Trade Representative, **Thailand: U.S.-Thailand Trade Facts** [Online], available URL: https://ustr.gov/countries-regions/southeast-asia-pacific/thailand, 2025 (September, 17).

2.7.1 A. Long-Term Approach: Preparing for the Global Standard (Pillar One)

In the long term, Thailand's policy should be firmly aligned with the emerging global consensus surrounding the OECD's Pillar One. This requires proactive preparation rather than a passive "wait-and-see" approach. The key actions involve significant legal and administrative reforms:

1) Preparing Amendments to the Revenue Code: The implementation of Pillar One, particularly Amount A, cannot be accommodated by the existing Revenue Code. It necessitates the drafting of a new, specific chapter or section dedicated to the "Taxation of Profits Allocated Under International Agreements." Key provisions in this amendment would need to:

(1) Formally define terms such as "Amount A," "Market Jurisdiction," and "Residual Profits" in line with the multilateral convention.

(2) Establish a clear legal basis for the Revenue Department to tax the allocated profits of multinational enterprises that lack a physical presence in Thailand. This is the most critical amendment, as it creates a new taxing right that is independent of the traditional Permanent Establishment principle.

(3) Detail the calculation and remittance procedures, specifying how the allocated profits are to be reported and when the tax is due.

(4) Integrate the framework with existing double taxation agreements, potentially through a provision that gives precedence to the multilateral convention to avoid legal conflicts.

Alternatively, instead of amending the Revenue Code, the implementation of Pillar One might be implemented as a separate Act, which contains the aforementioned attributes.

2) Enhancing Administrative Capacity: The Revenue Department must develop the capacity to handle the complex requirements of Pillar One. This includes upgrading IT systems for international information exchange, training personnel in complex profit allocation calculations, and preparing for the multilateral dispute resolution mechanisms that are a core feature of the Pillar One framework.

2.7.2 B. Short-Term and Transitional Approach: Leveraging and Enhancing Existing Frameworks

While Pillar One is being finalized, Thailand should focus on optimizing its current legal framework and cautiously considering limited transitional measures.

Option 1: Enhancing the Existing VAT for e-Services System - This is the most prudent and lowest-risk option. Rather than merely enforcing the current law, the system's efficiency can be significantly enhanced.

1) Proposed Enhancements:

(1) Data Analytics for Compliance: Utilize advanced data analytics and machine learning to analyze digital transaction data from various sources (e.g., payment gateways, financial institutions) to identify non-compliant foreign service providers who meet the revenue threshold but have not registered for VAT.

(2) Legislative Refinements: Consider minor amendments to the Revenue Code (Act No. 53) to clarify ambiguous terms and broaden the scope if new digital business models emerge that are not clearly covered. For instance, clarifying the VAT treatment of complex services involving mixed digital and physical components.

(3) International Cooperation: Proactively engage in information sharing agreements with tax authorities in other countries to cross-reference data on digital service providers, improving transparency and compliance.

Option 2: Considering a Limited-Scope DST with Caution - If policymakers decide that an income tax measure is necessary in the interim, a temporary and narrowly defined DST could be considered. However, its design must be exceptionally cautious to mitigate the legal and foreign policy risks previously analyzed.

2) Necessary Amendments to the Revenue Code for a DST:

(1) A new tax category would need to be created within the Revenue Code, as a DST is a tax on gross revenue, not net profit. This would be a significant structural change. In order to properly implement DST, the Revenue Code would require the creation of a new category of tax with its own definitional and operational framework, including the tax base, taxable activities, liability rules, and administrative procedures. This structural amendment would also need to address issues such as nexus for non-resident digital service providers, reporting obligations, and assessment rules.

(2) The tax rate of around of 2-3% on gross revenue, as suggested by practices in the UK and some EU countries, appears appropriate

(3) In terms of remittance procedures, Thailand may use the data collected from VAT for Electronic Service (VES) system to develop the DST collection. The existing VES system already provides a functioning digital infrastructure for identifying, registering, and collecting tax from non-resident digital service providers. Under the VES framework, foreign digital platforms are required to register for VAT in Thailand and file periodic returns reporting their revenue from Thai users. This system captures valuable transactional data such as the identity of the platform, the type of service provided, and the amount of revenue generated within Thailand. By leveraging this existing infrastructure, the government can minimize administrative costs and avoid building an entirely new collection mechanism from scratch.

(4) Crucially, the legislation must include a "sunset clause" which is a provision that automatically repeals the DST upon Thailand's adoption of the Pillar One multilateral convention. This would legally codify its temporary nature and demonstrate good faith in the multilateral process, potentially reducing the risk of trade retaliation.

2.7.3 Backup measures: DST for non tax treaties jurisdictions

In terms of legal authority, it seems feasible to implement DST on a unilateral basis, but it might lead to international disputes. However, there should be another DST regime in addition to an international agreement, such as Pillar One. In such a case, in order to prevent the potential disputes, the DST should be exempt for tax treaty jurisdictions and applicable to those located in non tax treaty jurisdictions only. The main reason to support this kind of tax imposition is to prevent tax avoidance whereby a digital firm arranges its transaction flows by setting up an entity in a jurisdiction which does not take part in Pilar One, or other international agreements, or even enter into a tax treaty on a bilateral basis. In respect of countries with tax treaties, implementation of DST on a unilateral basis may lead to potential international disputes in respect of tax treaties violation. Therefore, to the extent possible, Thailand should exert to reach a prior international agreement, or renegotiate tax treaties, so as to implement the DST in an amicable manner and mitigate risk of international disputes.

3. Conclusion

In conclusion, the challenge of taxing the digital economy is a multifaceted and complex issue that requires comprehensive consideration. The digital economy has become an integral part of the real economy and has fundamentally changed the landscape of business and the perspective on taxation. The traditional tax system, based on the concept of brick-and-mortar businesses, can no longer keep pace with the digital economy. This article has explored the challenges and potential solutions for modernizing the tax system to ensure that taxation in the digital era is both fair and efficient for market jurisdictions and enterprises alike. Ensuring that taxes are paid where they are rightfully due must be done equitably. Thailand's policy should, therefore, be pursued with prudence, prioritizing long-term compliance with international standards while selecting appropriate short-term measures that balance the state's fiscal interests with the promotion of a healthy business and investment ecosystem.

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