Bridging the Digital Tax Divide to Ensure a Fair and Equitable Fiscal Environment for All Businesses*

DESCRIPTION

More and more consumers and businesses are turning to e-business. More than just a trend, it presents many opportunities and has shown its transformative potential by dramatically changing the way we buy and sell goods and services.

The time has come for countries to adjust their taxation for the digital world to ensure the competitiveness of Canadian businesses and the principle of fairness in our tax system.

BACKGROUND

In our digitized world there is no existing strategy in Canada that would ensure not only continued business competitiveness but tax fairness to those companies who have bricks and mortar locations employing Canadians selling advertising, generating content, abiding by current regulations, and engaging in the public discourse.

Foreign companies that have no assets or employees in Canada and are selling intangible products to Canadian consumers are not required by current tax regulations to collect sales taxes nor to remit them to federal and provincial governments.

The Organisation for Economic Co-operation and Development (OECD) in its 2018 interim report on the Tax Challenges Arising from Digitalisation states that "digitalisation also allows some highly digitalised enterprises to be heavily involved in the economic life of a jurisdiction without any, or any significant, physical presence, thus achieving operational local scale without local mass. Currently, Canadian companies are required to charge HST/GST or the appropriate provincial value added tax (VAT) on their products. This tax does not apply to ads placed with foreign suppliers, yet companies can claim tax deductions for these advertising spends .

Not enrolling these foreign companies in the Canadian tax system has significant consequences.

Firstly, the federal and provincial governments are depriving themselves of important tax revenues, and this forces them to get more from other sources (i.e. income tax on individuals and corporations). Continued debt and deficit budgets by the federal government into the next four or five years are exacerbated by significant year over year dollars are being left off the table – in this case through lost sales tax revenue. In the 2018 federal budget, the federal government announced a deficit of $17.8 billion dollars.

Secondly, this situation represents an inconvenience for Canadian companies. Canadian businesses are at a disadvantage compared with foreign companies because the price of goods and services they sell is, due to consumption taxes, higher than those of non Canadian companies.

Australia recently announced that after a review of tax strategies by multi-nationals they asked select foreign digital firms to pay millions in back taxes.

Several other countries, including the European Union and Japan have joined Australia, in adapting their taxation to the digital world, having overcome the administrative challenges associated with tax collection. Despite the broad consensus on the pertinence of taxing foreign products and services equally, Canada's government has not yet taken action.

- The European Commission is calling for “large technology companies to pay a 3% tax if they make money from user data or digital advertising in a country, regardless of their bricks-and-mortar presence. The commission estimates that digital businesses pay an effective average tax rate of 9.5%, compared with 23.2% for bricks-and-mortar firms.”
- In Canada, the Quebec government announced in its March 27th, 2018 budget “a new QST registration system to collect QST from suppliers that are non-residents of Québec and thereby ensure tax fairness. Foreign suppliers (suppliers outside Canada) will have until January 1, 2019, to register for the QST using this new system, while Canadian suppliers (suppliers outside Québec) will have until September 1, 2019. Note that registration will also be mandatory for certain digital platforms acting as an intermediary between suppliers and consumers.”

Recently the federal government set a questionable precedent in this space by agreeing to allow Netflix to contribute to Canada’s cultural industry instead of subjecting the company to collect the same sales tax as Canadian broadcasters.

There is the potential that this exception will encourage other large companies, foreign and national, to try to create tax avoidance strategies of general application through special agreements with the government. These special agreements weaken the tax regime and impact taxpayer confidence in its fairness.

The 10 Ways to Build a Canada That Wins document published by the Canadian Chamber of Commerce encourages the federal government to make Canada a magnet for business investment. This includes responsive and competitive tax regimes for all who do business in Canada.

The recommendations are designed to move toward a level playing field in the digital economy and to ensure continued competitiveness of Canadian companies.

RECOMMENDATIONS

That the federal government:

1. Examine how to apply VAT evenly and predictably across provinces and sectors in a digital world, including an assessment of potential revenue from foreign digital companies.
2. Require foreign digital companies to charge an appropriate provincial VAT (e.g. GST/HST) on sales related to the purchase of their services in Canada and remit the revenues from these taxes to the proper tax authorities.
3. Require foreign digital companies to register with the Canada Revenue Agency.