



## Computer & Communications Industry Association (CCIA) Comments to Department of Finance Canada on “Digital Services Tax Consultation”

June 2021

### Summary

CCIA is an international, not-for-profit trade association representing a broad cross section of communications and technology firms. For nearly fifty years, CCIA has promoted open markets, open systems, and open networks.<sup>1</sup> CCIA appreciates the opportunity to provide its views on Canada’s proposal to introduce a digital services tax (DST).<sup>2</sup>

The U.S. and Canada have a vibrant digital trading relationship, representing two strong digital economies.<sup>3</sup> According to Statistics Canada, “up to \$11.2 billion of the maximum \$16.4 billion of digitally delivered services exports were generated from demand in the United States” and “in-scope exports to the United States, a maximum share of 82% of these services were digitally delivered”.<sup>4</sup> According to the U.S. Department of Commerce, in 2019, the United States exported \$38.4 billion (USD) in digitally-enabled services to Canada.<sup>5</sup> This trade relationship is threatened by discriminatory measures such as a DST that targets a handful of U.S. companies.

CCIA strongly opposes the imposition of DSTs and similarly discriminatory digital taxation measures that depart from long standing taxation norms and target a specific set of U.S. firms. DSTs and other unilateral measures threaten to undermine the progress made at the global level on international tax reform. A long-term, multilateral solution that does not discriminate against U.S. services remains the only path forward to provide certainty, and reduce trade tensions caused by countries’ decisions to enact unilateral measures.

In the increasingly globalized economy, changes to international taxation may be warranted to reflect business practices of the digital age. To this end, CCIA supports the efforts of the Organization for Economic Cooperation and Development (OECD) and the Group of 20 (G20) to negotiate a consensus-based solution to the tax challenges arising from the digitalization of the

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<sup>1</sup> For more, visit [www.ccianet.org](http://www.ccianet.org).

<sup>2</sup> Budget 2021 Annex 7 entitled Consultations on Other Tax Measures: Supplementary Information, *available at* <https://www.budget.gc.ca/2021/report-rapport/anx7-en.html>.

<sup>3</sup> See generally *The Coming North American Digital Trade Zone*, COUNCIL ON FOREIGN RELATIONS (Oct. 9, 2018), <https://www.cfr.org/blog/coming-north-american-digital-trade-zone>.

<sup>4</sup> STATISTICS CANADA, *Canada’s Services Exports Through the Lens of Digital Trade* (Dec. 7, 2020), <https://www150.statcan.gc.ca/n1/pub/13-605-x/2020001/article/00005-eng.htm>.

<sup>5</sup> U.S. DEP’T OF COMMERCE, Bureau of Economic Analysis, *International Trade Data* <https://apps.bea.gov/iTable/iTable.cfm?ReqID=62&step=1#reqid=62&step=9&isuri=1&6210=4>.

economy. CCIA supports an ambitious, comprehensive, and long-term solution by 2021 that does not ring-fence the digital economy, and is encouraged by agreement reached in recent weeks among key leaders contributing to the work.<sup>6</sup> Industry is committed to this important process and remains optimistic that the result will provide certainty needed to enhance investments, trade and growth globally.

## **1. Flawed Justifications for Unilateral Digital Services Taxes**

The consultation states, “The government is committed to ensuring that corporations in all sectors, including digital corporations, pay their fair share of taxes on the money they earn by doing business in Canada.” However, studies demonstrate that the firms that would fall into the scope of the DST “pay taxes at rates equal or higher than the average large Canadian company.”<sup>7</sup> The notion that digital firms are undertaxed compared to physical counterparts has also been challenged in the European context.<sup>8</sup> Additionally, the costs of the DST are likely to be passed onto Canadian consumers and businesses.<sup>9</sup> The DST would result in higher costs to users of these services, including SMEs who rely on these services for business operations.

If changes are warranted to corporate tax rules to reflect the nature of global business, these changes should be pursued at the multilateral level and on a non-discriminatory basis relative to specific business models. CCIA supports the efforts of governments under the OECD process to reach a consensus based solution on global taxation norms. This holistic approach will provide a future-proof framework and speed economic recovery around the world.

## **2. Digital Services Taxes as Unreasonable Tax Policy**

DSTs are unreasonable tax policy for a number of reasons.

First, thresholds that were created were set at arbitrary levels, with the apparent goal of ensuring that foreign companies shouldered the vast majority of the tax burden. The global thresholds closely follow the once-abandoned EU proposal, while in-country thresholds are crafted in a manner to exclude leading domestic companies that would be within scope. Domestic companies that provide identical intermediary and ad-supported services will likely not be taxed.

Second, the taxation of revenue rather than profits departs from international norms. Historically, corporate taxes have been levied where value is created, not where it is consumed. If this were to change, governments should seek consensus on the methodology and degree to which taxation rights should shift. With narrow definitions and targeted policy instruments, the risk is that every country could seek to impose new taxes on whatever products and services they import, while

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<sup>6</sup> CCIA Welcomes G7 Finance Ministers’ Support for Global Tax Deal (June 5, 2021), *available at* <https://www.cciainet.org/2021/06/ccia-welcomes-g7-finance-ministers-support-for-global-tax-deal/>.

<sup>7</sup> Montreal Economic Institute (MEI), *Taxing the Tech Giants – Why Canada Should Not Follow the French Example* (2020), *available at* [https://www.iedm.org/wp-content/uploads/2020/01/cahier012020\\_en.pdf](https://www.iedm.org/wp-content/uploads/2020/01/cahier012020_en.pdf).

<sup>8</sup> PwC, *Understanding the ZEW-PwC Report, “Digital Tax Index, 2017”*, *available at* <https://web.archive.org/web/20210124130524/https://www.pwc.com/us/en/press-releases/2018/understanding-the-zew-pwc-report.html>.

<sup>9</sup> MEI, *Taxing the Tech Giants– Why Canada Should Not Follow the French Example*, *supra* note 5.

maintaining direct taxes on those that they export.

Third, the administrative burdens associated with compliance and auditing will likely offset any relative gains to be made by foreign tax collection authorities. Firms are required to make complex determinations on whether covered digital activities were supplied in country, a determination that varies across different DST legislation around the world and corresponding implementing guidelines. The lack of clarity could lead to different interpretations of the law between firms in the scope of the tax and foreign tax authorities.

### **3. Potential Conflicts with International Commitments**

DSTs may conflict with international commitments, and international agreements these countries are party to. The consistency of DSTs with commitments under tax treaties and World Trade Organization (WTO) obligations has been questioned by the OECD and other stakeholders.

#### *(a) Tax Treaties*

The Canada-U.S. Tax Treaty contains provisions that may conflict with the imposition of a DST.<sup>10</sup> Article VII details parties' rights to tax corporate entities operating in the country that extend to entities with a physical presence. Further, the Treaty contains a non-discrimination commitment in Art. XXV. As it is likely that only a handful of predominantly U.S. companies will be in scope of the DST, the DST may be considered to discriminate based on nationality.<sup>11</sup>

#### *(b) Potential Conflicts with WTO and USMCA Commitments*

The DSTs predominately apply to U.S. firms. The covered activities (online marketplace, digital advertising, social media), combined with the revenue thresholds make clear that the target of the DST is a handful of U.S. companies. Their local competitors are likely out of scope. To this end, the United States has found on multiple occasions that DSTs similar to what Canada is proposing are clearly discriminatory against U.S. firms,<sup>12</sup> and has made clear that any unilateral digital services tax measures will be met with scrutiny by the Office of the U.S. Trade Representative.<sup>13</sup>

Policymakers make clear their target of these new taxes, singling out other American “tech

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<sup>10</sup> United States – Canada Income Tax Convention, <https://freemanlaw.com/wp-content/uploads/2020/07/canada.pdf>.

<sup>11</sup> BENNETT JONES, *The Digital Services Tax: Canada Takes Aim at Tech Giants* (May 14, 2021), <https://www.jdsupra.com/legalnews/the-digital-services-tax-canada-takes-2504482/>.

<sup>12</sup> See OFFICE OF THE U.S. TRADE REP., Section 301 Report France Digital Services Tax (Dec. 2019), *available at* [https://ustr.gov/sites/default/files/Report\\_On\\_France%27s\\_Digital\\_Services\\_Tax.pdf](https://ustr.gov/sites/default/files/Report_On_France%27s_Digital_Services_Tax.pdf); Section 301 Report Various Digital Services Taxes, *available at* <https://ustr.gov/issue-areas/enforcement/section-301-investigations/section-301-digital-services-taxes>.

<sup>13</sup> See Readout of Ambassador Katherine Tai's Virtual Meeting with Canada's Minister of Small Business, Export Promotion, and International Trade Mary Ng (May 17, 2021), <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2021/may/readout-ambassador-katherine-tais-virtual-meeting-canadas-minister-small-business-export-promotion>; *Canada Could Face U.S. Tariff Retaliation Over Proposed Tax on Digital Services*, NATIONAL POST (Apr. 5, 2021), <https://nationalpost.com/news/politics/canada-could-face-u-s-tariff-retaliation-over-proposed-tax-on-digital-services>.

giants”. Some follow French policymakers and refer to the tax as a ‘GAFA’ tax (a moniker to describe Google, Amazon, Facebook, and Apple), or cite only U.S. companies as the basis for introducing the tax. As noted above, the discriminatory nature of DSTs is motivated at least in part by inaccurate characterizations of current tax payments of digital firms.

The discriminatory nature of the DST conflicts with commitments under the WTO’s General Agreement on Trade in Services (GATS), notably the non-discrimination principles under Article II and Article XVII. Article II mandates that members offer “treatment no less favorable than it accords to like services and suppliers of any other country.” Domestic firms that offer the same targeted services in DSTs – such as intermediary and ad-supported services – as their U.S. competitors are unlikely to be taxed.

Further, these commitments are outlined in the recently negotiated U.S.-Mexico-Canada Agreement (USMCA). The USMCA represents the gold standard for a 21st century trade agreement that sets strong rules across digital services trade, reflecting shared priorities among North American trading partners. Discriminatory taxes, especially ones that the United States have made clear will be met with trade scrutiny, conflict with the spirit of this renewed partnership.

## **Conclusion**

CCIA strongly encourages the Government of Canada to reconsider the creation of a DST. Instead, Canada should continue its efforts under the multilateral process to address broader corporate taxation issues. A long-term, multilateral solution that does not discriminate against U.S. services remains the only path forward to provide certainty, and reduce the threat of heightened trade tensions.