February 22, 2022

DST Act Consultation
Tax Policy Branch
Department of Finance Canada
90 Elgin Street
Ottawa, Ontario
K1A 0G5

Re: Canadian government consultation requesting comments on its proposed Digital Services Tax Act to DST-TSN@fin.gc.ca by February 22, 2022.

To Whom it May Concern:

The U.S. Chamber of Commerce ("U.S. Chamber") appreciates the opportunity to present the following comments to the Government of Canada on its proposed Digital Services Tax Act.

The U.S. Chamber is a strong proponent of close trade and investment ties between Canada and the United States. The Government of Canada notes that approximately 1.9 million Canadian jobs depend on trade with the United States. In the same vein, one recent study found that approximately 7.8 million American jobs depend on trade with Canada.

Recognizing the unique power of these ties, the U.S. Chamber has long been an outspoken proponent of maintaining and strengthening free trade within North America. The U.S. Chamber championed negotiation, approval, and implementation of the Canada-United States-Mexico Agreement (CUSMA); elimination of the U.S. Section 232 tariffs on imports of steel and aluminum from Canada (achieved in May 2019); and the need for a balanced approach to U.S. domestic procurement preferences that reflects the benefits of North American supply chains. In short, Canada-United States commercial relations should reflect the benefits of these remarkably extensive trade and investment ties.

In this context, the U.S. Chamber welcomes the opportunity to submit these comments to express several concerns about Canada's proposed Digital Services Tax Act and the application of a Digital Services Tax (DST) by Canada:

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1) **DSTs pose a substantial risk to the economic recovery in Canada and globally given the outsized importance of digitization and the potential growth in global services trade.**

In the U.S. Chamber's view, the negative consequences of a DST for economic recovery in Canada are likely to be considerably larger than widely appreciated. This stems in large part from the growth in the very large North American professional and business services sector, its importance to middle class jobs, and its potential for trade-driven growth.

In Canada, as in the United States, the professional and business services supersector employs more workers at higher average wages than manufacturing. Professional and business services include such sectors as audiovisual, software and ICT services, architecture, accounting, engineering and project management, advertising, banking, and insurance.

Further, professional and business services are increasingly tradeable thanks to digital technologies. Worldwide, half of all services exports can now be delivered to customers abroad digitally, according to a report by UNCTAD. Partly as a result, global trade in services is expanding 60% more rapidly than trade in goods, according to a report by the McKinsey Global Institute.

In particular, the U.S. Chamber recently issued an extensive report on these issues—*The Digital Trade Revolution*—that we commend for your close examination. It shows that the potential for services to be traded digitally is almost untapped. To illustrate, U.S. exports represented 7.1% of services sector value-added output in 2020; for manufacturing the share was three times higher. There is every reason to believe that a similar dynamic holds in Canada.

In this context, Canada's proposed DST risks undermining potential growth. The knock-on effects for digital trade generally could sap expansion and job creation not just among firms considered "digital companies" but among firms that simply use digital tools. Large numbers of small and medium-size businesses could be affected by the potential slowdown in the growth of digital trade.

Further, the proposal targets U.S. companies that have invested billions of dollars in Canada and engage in mutually beneficial commercial relationships with Canadian citizens. The chilling effect on investment could be significant.

2) Canada's DST proposal is discriminatory and violates obligations Canada has undertaken as a party to the WTO Agreement, CUSMA, and the U.S.-Canada tax treaty

Canada's proposed DST appears to violate obligations Canada has undertaken as a party to the WTO's General Agreement on Trade in Services (GATS). Specifically, it violates the national treatment principle, which enjoins WTO Members to "accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favorable than that it accords to its own like services and service suppliers" (GATS Article XVII). The GATS explicitly prohibits Members from implementing measures that afford de facto discrimination even when the measure provides "formally identical" treatment. The Canada-United States-Mexico Agreement (CUSMA) includes similar, enforceable trade obligations.

The DST proposal violates these obligations and discriminates against U.S. companies in several ways. First, thresholds in the DST proposal are set at a level that captures large U.S. technology companies while sparing Canadian industry almost entirely. The proposed DST will apply only to companies with "global revenue from all sources of €750 million or more (the threshold for country-by-country reporting under an OECD standard) in the previous calendar year; and in-scope revenue associated with Canadian users of more than $20 million in the particular calendar year." While a number of U.S. firms would be impacted, it is unclear if any Canadian companies would be.

Further, the proposed DST targets a selection of digital services in which U.S. firms are market leaders but excludes digital services where Canadian firms are significant actors. The subsectors targeted include online marketplaces for goods and services, social media, and online advertising. The DST does not apply to other digital services where Canadian firms are significant actors (e.g., financial services, payment services, communications services, or other types of intermediation services). In this regard and in its proposed thresholds, the Canadian proposal closely resembles the French model, which has been widely described as violating WTO national treatment obligations.

In addition, the DST proposal conflicts with principles developed as part of the OECD's Inclusive Framework on Base Erosion and Profit Shifting process. Through this process, more than 130 governments are developing a global approach to the challenges posed by digitization of the economy. Specifically, the proposed Canadian DST conflicts with the following principles:

- No ring fencing of the digital economy;
- The principles of international taxation, including taxation of net income;
- Avoidance of multiple taxation of the same income;

- Providing certainty for taxpayers and minimizing tax disputes;
- Minimizing the compliance burden on tax administrations and taxpayers;
- New taxing regimes should be implemented on a prospective basis;
- Consistency with the principles of proportionality and sustainability; and
- Deviation from the arms-length standard.

The Canadian DST proposal also appears to violate the U.S.-Canada Convention with Respect to Taxes on Income and on Capital, which upholds many of these same principles.

The proposed DST will also impose significant compliance costs and administrative burdens on Canadian and U.S. firms. For example, some companies will need to engage in significant re-engineering of accounting systems to ensure that they can accurately assess DST liability for Canadian advertising transactions. Estimated costs are in the millions.

3) Canada should comply with the commitment it made under the OECD/G20 Inclusive Framework to forgo any DST until the end of 2023 or the implementation of the Pillar One framework.

The Digital Services Tax Act proposes that Canada's DST would not come into force (and thus would not be collected until 2024), but it intends to apply this novel tax retroactively to the beginning of 2022. The enactment of such a retroactive, unilateral measure is directly contrary to both the spirit and the explicit terms of the OECD/G20 Inclusive Framework on BEPS agreed to by 137 countries, including Canada, and signed on October 8, 2021. The following provision on Unilateral Measures in the OECD/G20 agreement provides that *any* newly enacted DSTs will not be imposed before the earlier of December 31, 2023, or the implementation of the Pillar One framework:

> *No newly enacted Digital Services Taxes or other relevant similar measures will be imposed on any company from 8 October 2021 and until the earlier of 31 December 2023 or the coming into force of the MLC.*

Despite this explicit commitment, the Government of Canada is advancing the Digital Services Tax Act with the goal that "the DST would be payable as of the year that it comes into force in respect of revenues earned as of January 1, 2022." This means that, while the DST will not come into effect until 2024, it will be retroactive to 2022 should the OECD Pillar 1 framework not be implemented. There are a number of problems with this approach. First, there appears to be no earlier example of a two-year retroactive Canadian tax, raising questions about the legality of the approach. Furthermore, the OECD is still negotiating the terms of Pillar One, and the process is likely to continue through 2022. Overall, this aggressive approach violates the OECD/G20 agreement to which the Canadian government has recently committed.

In sum, this proposed DST is a serious concern for North American business and our economic recovery. In addition to violating commitments Canada has made under CUSMA, the WTO, and the OECD/G20 agreement, the real-world costs would be substantial. A Canadian DST would heighten the risk of double taxation for U.S. companies large and small, undermine regulatory predictability, present enormous administrative complexity due to its retroactive application, complicate tax planning, and raise new hurdles to recovery for workers and companies across North America.

The U.S. Chamber appreciates the opportunity to offer these comments and looks forward to engaging with the Government of Canada on these important issues.

Sincerely,

John Murphy
Senior Vice President for International Policy

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