International Online Sales: An Important Shortfall for Governments

Background

Online sales through companies outside Canada are a growing phenomenon due to the rapid development of the digital economy.

Foreign companies that have no assets or employees in Canada and are selling digital products to Canadian consumers are not forced by current tax regulations to collect the Goods and Services Tax/Harmonized Sales Tax (GST/HST) nor to remit the tax to federal and provincial governments.

Digital products are products entirely downloaded by Internet clients, for example, electronic books, movies, television programs and video games.

Consequently, tax revenues are lost (i.e. Goods and Services Tax/Harmonized Sales Tax (GST/HST)) because of the loopholes in Canada's current tax system.

It seems essential to fix the problem so federal and provincial governments can collect the Goods and Services Tax/Harmonized Sales Tax (GST/HST) on all online sales in Canada by foreign suppliers.

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

Losses of tax revenues: The federal and provincial governments are depriving themselves of these tax revenues, and this forces them to get more from other sources (i.e. income tax on individuals and companies) or to reduce spending and the level of service to citizens. With the continued growth of online business, the phenomenon will grow.

An inconvenience for Canadian companies: Canadian companies are at a disadvantage compared with foreign companies because the price of goods and services they sell is, due to consumption taxes, about 13% higher than those of non-Canadian companies.

A constraint to investment in Canada: Foreign companies are not encouraged to invest here, because in so doing they would add 13% to the price charged to Canadian clients, which would reduce demand for their digital products and services.

The Commission d'examen sur la fiscalité québécoise (Commission Godbout) analyzed this phenomenon and recognized that collecting taxes and duties for these activities is a major challenge.

For Quebec only, Revenu Québec estimated in 2012 that the Quebec state lost $165 million in tax revenues due to online purchases by Quebeckers from suppliers located outside Canada. Even if it seems difficult to estimate losses tied to online purchases by Quebeckers from suppliers in another province or country, is it probably a significant amount. An amount of $300 million was once been mentioned by Revenu Québec.

In its Budget 2015-2016 presentation, the Quebec Government adopted the recommendations of the Commission sur la fiscalité québécoise and intends initiating discussions with the Federal Government on the matter.

Furthermore, the Business and Industry Advisory Committee to OECD (BIAC) agrees that the most efficient way to collect the Value Added Tax (VAT) on cross-border B2C services is to force foreign suppliers (non-resident) to register and record these services in the customer's jurisdiction. Countries should examine a simplified registration system to reduce the compliance burden.

Recommendations

That the federal government:

1. Impose the consumption tax system to foreign companies selling digital products and services to Canadian consumers, specifically that companies:

    a. Register with the Canada Revenue Agency (CTA);

b. Collect the Goods and Services Tax/Harmonized Sales Tax (GST/HST/QST) from Canadian clients;

c. Remit the revenues from these taxes to the proper tax authorities.

2. Intensify its efforts as part of ongoing OECD work on the collection of the following tax and duties:

a. Sales taxes on Internet transactions by suppliers in foreign countries;

b. Income taxes on companies tied to electronic commerce.