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Department of Finance Canada
Tax Policy Branch
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The Electronic Transactions Association (“ETA”) provides these comments in response to the Department of Finance’s request for feedback with respect to the proposal to implement a new Digital Services Tax (“DST”) by January 1, 2022. It is our hope that these comments will assist government in understanding the significant concerns of ETA members, including Canada’s leading financial institutions, global payment networks, and the broader FinTech industry, associated with the proposed DST.

[The Electronic Transactions Association](#) (ETA) is the leading trade association for the payments industry, representing over 500 companies that offer electronic transaction processing products and services. Its membership spans the breadth of the payments industry to include independent sales organizations, payments networks, financial institutions, transaction processors, mobile payments products and services, payments technologies, equipment suppliers, and online small business lenders. ETA member companies are creating innovative offerings in financial services, revolutionizing the way commerce is conducted with safe, convenient and rewarding payment solutions and lending alternatives. ETA advocates for the payments industry in Canada to help drive innovation in the global market for payments technology services.

Multilateral Approach

ETA and its members favour a multilateral solution to the tax challenges arising from the digitalization of the economy, and we are encouraged by the recent discussions towards ensuring fair international taxation of multinational corporations that resulted in an historic G7 agreement on the parameters of a broader international framework that includes a commitment to “appropriate coordination between the application of the new international tax rules and the removal of all Digital Services Taxes, and other relevant similar measures, on all companies”.¹ ETA hopes this momentum can continue into the global discussions at the July G20 Finance Ministers and Central Bank Governors Meeting in Venice, which is seeking agreement among the members of the G20 and the OECD-led Inclusive Framework on Base Erosion and Profit Shifting.

Notwithstanding this progress, the Government of Canada has signalled its intention to proceed unilaterally with the proposed DST as an interim measure. ETA encourages the Government of Canada to defer any consideration of a unilateral measure so as to clearly demonstrate its commitment to the OECD negotiations.

ETA also believes that unilateral responses to complex tax issues like the implementation of the DST could stifle innovation and make it more challenging for new products and services to

¹ G7 Finance Ministers & Central Bank Governors Communiqué. June 5, 2021.

launch and operate in Canada. We therefore caution that a unilateral approach should only be considered as a last resort.

International Best Practices

The creation of the DST has been under discussion internationally for several years and has been proposed as a way of ensuring digitally-intensive or consumer-facing companies pay taxes in jurisdictions where they conduct business – even if they do not have a physical presence in that jurisdiction. Based on our preliminary review, however, the proposal put forward appears to go much wider than that and will see the DST imposed on a significant number of Canadian-based digitally intensive companies – like FinTechs – that already pay taxes in this country.

ETA members do not believe that the Canadian DST proposal is intended to apply to the business model of its members, but in the interest of removing any ambiguities, proposes an explicit exclusion from the DST on revenue connected to supplying financial and other payment services as well as activities already captured by banking regulation or technology provided to the financial sector to facilitate activities that would otherwise be performed by individuals. Such exclusions would be consistent with the OECD Pillar One Blueprint and jurisdictions that have implemented or proposed a DST, such as the United Kingdom, Italy, France, Spain, Turkey, Belgium, Kenya, New Zealand, and the Czech Republic.

The broadly defined in-scope business models listed in the proposed measures target highly digitalized businesses. However, the definitions are imprecise and risk to capture existing financial services given digital activities in the sector develop all the time. Unlike targeted businesses, for our members, user participation does not play a significant role in the value creation process. Instead, members generate revenues by investing in their network activities and infrastructure.

Since 2018, countries with DST legislation and Member States of the European Parliament and Council of the European Union have excluded financial service providers from a DST given the business model's similarity and inter-dependence to telecommunications and the banking sectors. We would recommend a similar exclusion in this case.

As an example, we draw your specific attention to the case of payment service providers. The DST introduced by the United Kingdom ("UK DST") defines in-scope revenue by referencing revenue to a particular business model like the proposed Canadian DST. The UK DST includes an express exemption from the online marketplace definition for financial and payment service providers. France includes a similar exclusion "when the person providing [payment services] uses [digital interface services] primarily to provide users" with such service.

Other examples include the Italian DST which exclude the provision of "interbank settlement systems..." through the use of a "digital interface" and the Spanish DST exempting "the rendering of online intermediation services, when the unique or main reason of those services supply by the entity that makes the digital interface available, is to supply users with ...payment services." Finally, the European Commission justified the exclusion of payment service providers to DSTs in its detailed explanatory memorandum to Member States:

"the value creation for such other services, which can be generally defined as communication or payment services, lies with the development and sale of support software which enables that interaction to take place, and it is less attached to the users'

involvement. Therefore, communication or payment services remain outside the scope of the tax...”.

Given the examples provided, ETA submits that the Canadian DST should include a definitive exemption excluding payment service providers from all in-scope or taxable services subject to the DST.

User-Data Provisions

The proposed provision covering revenues from data gathered from users, also present a significant concern for many ETA members – and for the emerging FinTech industry in Canada.

ETA recommends that Canada introduce a purpose test to any proposed Canadian DST to limit its application to those business models where the “main purpose or one of the main purposes” of the business and use of data is to provide in-scope services. The introduction of a purpose test is consistent with the DST legislation of other jurisdictions, including the United Kingdom and France. In that case, the introduction of a purpose test was intended to clarify significant uncertainty regarding the inadvertent application of the UK DST to certain businesses from the definition of “online marketplaces.” ETA would welcome similar legislative drafting for each of the in-scope activities. The clarifying language ensures that where businesses have integrated in-scope and out-of-scope business activities, they will be required to take an integrative and holistic approach to assess the potential application of the Canadian DST.

Given these concerns, it will be very important that Finance Canada understands and considers the broad use cases that will be captured, perhaps unintentionally. A few examples include: (a) the use of data generally by entities that is necessary to the function of a revenue generating service and/or to improve services and offerings that are not distinctly commercialized or tracked but made available as improved services for which income tax is already paid; (b) data services for which income tax is already paid; (c) data from loyalty programs; (d) data from payment and payment system services; (e) customized insights about a merchant’s business through their payment services; and (f) detecting risk patterns to better assess exposure and loss probabilities.

In the case of data from payment and payment system systems, consumer data collected from financial transactions by members is used for value-added services such as consultancy services for products and services to protect Canada’s banking system. They include products to detect and deter anti-money laundering activity and financial crimes. Collected data is aggregated and de-identified. Under the current definition of “users,” such activities risk to be within the definition of the scope of the DST. If a Canadian DST were to apply, payment service providers could be inadvertently penalized for supplying and developing digital tools and information intended to protect and improve upon the financial integrity of Canada’s economy. To avoid the inadvertent application of the DST, the definition of “user” in the consultation document should be refined to mean individual users to ensure that the Canadian DST excludes business-to-business transactions. As an additional measure to ensure only highly digitalized businesses are captured, the ETA recommends the introduction of a predominant character test whereby the predominant character of a bundled supply is considered to determine whether the revenue is in scope of the DST.

ETA also believes that an unnecessarily broad approach to the DST could undermine several aspect of the Government of Canada’s innovation agenda, namely the goals defined in Canada’s Digital Charter and the legislation to modernize Canada’s National Privacy

Legislation, *The Personal Information Protection and Electronic Documents Act* (PIPEDA), as well as Government's efforts to create a Consumer Directed Finance (CDF) framework in Canada. ETA supports both the Digital Charter and the proposed changes to the PIPEDA that would provide citizens with clear privacy rights that would offer enhanced protection and the opportunity to access new products and services that can be enabled through corresponding frameworks like CDF. ETA warns that placing all business revenues from user-generated data within the scope of the DST would challenge the ability of businesses to introduce new digital products and services that Government is looking to prioritize and support through its innovation agenda.

To address these and any other unintended consequences, should Canada move forward unilaterally, **ETA recommends that the DST's scope be limited to only capture highly digitalized business models that involve the active participation of users on an internet platform (such as online marketplaces, social media, and online advertising).**

To be more specific, we urge Finance Canada to exclude the sale of user data gathered from users of an online interface or to limit its application, in order to ensure that data gathered by traditional businesses like manufacturers, payment processors and card networks, and financial institutions are not in scope. If a DST were to apply, the addition of a purpose test and a refined definition regarding "user" would introduce greater certainty to key elements that are currently vague and imprecise.

Double Taxation

ETA members also submit the proposed DST also creates broader concerns with respect to double taxation. Currently, any taxes imposed on gross revenue will result in a far greater burden than a net income tax. The current proposal does not permit the deduction of costs from gross revenues. The result is that a 3% DST results in a higher income tax rate than the indicated rate. The OECD has acknowledged this problem and has warned that "economic double taxation could also arise through cascading effects where a certain supply of e-services is made to a person that incorporates those services into an onward supply that is itself subject to the tax". Therefore, ETA believes the DST should be creditable against any tax a group might already pay in Canada on the same revenues, including corporate income tax and value added taxes such as the GST/HST.

To address concerns with respect to double taxation of specific business activities, ETA also submits that a proposed DST should treat all companies equally and avoid double taxation: meaning that all business activities subject to the DST should be fully creditable against any tax, excluding customs and excise duties, paid in Canada.

Revenue Thresholds

If Canada were to impose a temporary Canadian DST, the tax would result in significant compliance burdens to businesses in this sector, given the low local revenue threshold of \$20 million CAD for the DST to apply. This amount is lower than both the United Kingdom (£25 million) and France (€25 million), and ETA believes consideration should be given to setting the revenue threshold at a commensurate amount.

Businesses must also be presented with the opportunity to complete an impact analysis of the scope of the proposed legislation and identify approaches to analyzing information required to calculate the amount of a Canadian DST based on the proposed global and local thresholds.

ETA members will also require more time to source data, validate information, appropriately apportion revenues, and generate consistent reports and data that support the payment of a Canadian DST. There is no assurance or certainty that similar information required for country-by-country reporting will align with what is anticipated for a Canadian DST.

Implementation Date

Given the complexity of implementation, ETA would also suggest that the January 1, 2022 timeline to create a new tax regime this multifaceted, that for instance requires detailed sourcing and tracing of yet defined revenue streams, is overly ambitious and will be challenging for obligated parties to manage from an administrative perspective. ETA therefore recommends that should Canada proceed unilaterally with a DST, that it should delay the enforcement date until at least July 1, 2022 and publish detailed guidance to allow companies to achieve compliance with the requirements of the new regime.

Conclusion

ETA thanks you for the opportunity to submit these comments and looks forward to providing whatever additional information we can provide to inform the Government of Canada's deliberations to implement the proposed DST.

Respectfully submitted,



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