



CANADIANS FOR TAX FAIRNESS
CANADIENS POUR UNE FISCALITÉ ÉQUITABLE



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Comments from *Canadians for Tax Fairness*
Toby Sanger, Executive Director
to OECD Public Consultation on
**Addressing the Tax Challenges of the
Digitalisation of the Economy**

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General Comments

Canadians for Tax Fairness, our thousands of supporters and tax justice allies in Canada and around the world have been very supportive of many of the measures and actions included in the OECD's Base Erosion and Profit Shifting (BEPS) initiative. While they were limited and consisted more of patching the existing complex and flawed system, they've been the first serious substantial attempt to address international corporate tax avoidance and evasion.

However, the limitations of our current system and of the original BEPS reforms have become abundantly clear, as major nations have already taken steps or are proposing tax measures that move well-beyond the existing system and original BEPS Action Plan, with measures aimed particularly at larger corporations active in the digital economy.

The tax challenges associated with the digitalisation of the economy are highlighting problems that are increasingly pervasive throughout the economy, as more industries become digitalized, as intellectual property becomes more important, and as multinational corporations restructure to exploit tax loopholes and preferences.

The ability of the largest corporations in the world to exploit the international tax system to minimize their taxes is not only unfair to smaller and medium-sized businesses but also contributes to disturbingly high and harmful degrees of concentration within many industries.

National governments have lost hundreds of billions in revenues and lower income countries — in even more need of revenues for public services—lose much more as a share of their revenues. Ordinary taxpayers and workers in all countries have had to shoulder more of the tax share and suffer cuts to public services as governments have engaged in race to the bottom corporate tax cuts. Our existing international tax system also provides incentives for multinational corporations to engage in more precarious and non-standard employment relations to reduce taxes and avoid permanent establishment status, resulting in lower quality and often lower wage jobs.

For these numerous reasons we welcome proposals to address the tax challenges of the digital economy, the recognition there are much deeper challenges that need to be addressed, and that a broader group of countries and stakeholders should be involved.

While we support the direction of these specific proposals, we also emphasize that reforms should ultimately be guided by fundamental principles of equity and fairness, simplicity, ease of administration, transparency, and ensuring that all countries preserve the ability to generate revenues required to fund sustainable development goals and quality public services in a progressive manner.

We support the growing global consensus that the international corporate tax system must be reformed to a system with unitary taxation of multinational enterprises and formulary apportionment of profits according to real economic factors. Systems of formulary apportionment of corporate profits between provinces and states have been used with much success and little controversy in Canada and in other federal jurisdictions for many years. Furthermore, we agree that nations should also negotiate a minimum global effective tax rate at a sufficient level to prevent a race to the bottom through harmful downward tax competition.

We in Canada are particularly keen to achieve progress through these discussions because our Finance Minister has said Canada is delaying action on related BEPS measures because they are awaiting progress on these OECD discussions.

2. Revised profit allocation and nexus rules

1. What is your general view on those proposals?

We welcome that all three proposals involve a shift away from the arm's length principle and towards approaches that would shift taxing rights towards market jurisdictions.

The UK's "user participation" model breaks new ground by recognizing the value users contribute to firms by providing detailed information about themselves to advertisers even when they aren't paying customers. However, it would only apply to a narrow group of firms and also to non-routine profits. The U.S. "marketing intangibles" proposal would apply to a

broader range of activities, but would also be limited to residual/non-routine profits from “marketing intangibles.

Both these approaches are too narrow in the scope of activities they would apply to and limited to non-routine residual profits. By introducing additional concepts that could be interpreted in different ways and applying yet another partial patch, they would further complicate the international tax system.

The “significant economic presence” proposal would involve more fundamental changes to a more extensive range of activities and allocate profits between countries using formulas reflecting sales, employment assets and potentially users. While many details need to be worked out, this is by far the most attractive and promising proposal.

2. To what extent do you think that businesses are able, as a result of the digitalisation of the economy, to have an active presence or participation in that jurisdiction that is not recognised by the current profit allocation and nexus rules?

The degree to which businesses are able to avoid taxes in countries where they have an active presence is becoming ever more apparent, is more pronounced among more digitized businesses, and has accelerated as more types of businesses become increasingly digitized. The extent of this is not yet known because public country-by-country reporting is not yet in place. While digitized businesses are more able to avoid taxes, digitization is becoming more pervasive. It will ultimately be impossible to ring-fence these types of businesses, would not be helpful to do so, and therefore taxation rules should be designed to apply broadly.

3. What would be the most important design considerations in developing new profit allocation and nexus rules consistent with the proposals described above, including with respect to scope, thresholds, the treatment of losses, and the factors to be used in connection with profit allocation methods?

The rules should be designed to make the tax base as broad as possible, with low thresholds, and consistent rules applying to losses. We agree that profits should be allocated between jurisdictions based on a formula apportionment system reflecting sales, employment, assets, users where applicable; and that multinationals and their related entities should be taxed on a unitary basis.

4. What could be the best approaches to reduce complexity, ensure early tax certainty and to avoid or resolve multi-jurisdictional disputes?

The best approach to reduce complexity and disputes is to develop and apply broad-based, uniform and simple rules, as we have proposed. Canada has used a straightforward method to allocate corporate profits between provinces for many years, with very little disagreement or dispute. Public reporting of country-by-country financial information, consistency with

accounting rules and transparent dispute resolution mechanisms will help to avoid and resolve disputes. These will also ensure much more effective engagement by all jurisdictions.

3. Global anti-base erosion proposal

- 1. What is your general view on this proposal? In answering this question please consider the objectives, policy rationales, and economic and behavioural implications of the proposal.*

The global anti-base erosion proposal would enable countries to “tax back” profits in instances where other countries are undertaxing foreign entities. It would provide a complementary tool to preserve the tax base and help prevent a race to the bottom, but it shouldn’t be considered a substitute for a more robust and reformed international tax system.

- 2. What would be the most important design considerations in developing an inclusion rule and a tax on base eroding payments?*

In our view the most important design consideration related to this is the scope of entities and payments covered by the rules and how a minimum tax rate would be determined. In our view these should be broad and the minimum tax should be established at a sufficient rate to reduce incentives for this behavior. While the US GILTI reforms involve a step forward, the rate applied is far below the U.S. and international average tax rates. The right to tax back should be applied at the full domestic rate, otherwise there will be no incentives to maintain a minimum effective tax rate.

- 3. What, if any, scope limitations should be considered in connection with the proposal set out above?*
- 4. How would you suggest that the rules should best be co-ordinated?*
- 5. What could be the best approaches to reduce complexity, ensure early tax certainty and to avoid or resolve multi-jurisdictional disputes?*

The scope of these rules should be broad with few exemptions and thresholds limited or avoided. The best approach to reduce complexity and avoid disputes, including rule coordination through these measures would be to ensure that they are complementary to much more fundamental reforms of the international corporate tax system as discussed above. Otherwise we will have an increasingly complex system of patchworks upon patchworks. These rules can also be supported by having wide adoption by jurisdictions of these rules, more consistent and more rigorously applied accounting standards, and transparent dispute resolution mechanisms.