

Cost Estimate of Election Campaign Proposal

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Short title: New digital services tax

Description: This proposal will introduce a new 3% tax on corporate revenues in certain digital sectors. This policy will replicate the proposed digital services tax announced by the Government of the United Kingdom. It is expected to be introduced in 2020-21.

The tax will strictly target the following services: social media platforms, search engines and online marketplaces. The companies' worldwide revenues will have to be more than \$1000M, and the tax will apply to revenue earned in Canada in excess of \$50M.

The new tax will act as a tax credit on corporate income tax. The exemption mechanism for low-profit companies proposed by the Government of the United Kingdom will not be applied.

Operating line(s): Corporate income tax

Data sources:	<u>Variable</u>	<u>Source</u>
	Public companies' revenues by geographic segment	Capital IQ
	T2 income tax returns	Statistics Canada
	Nominal GDP	World Bank database
	Adjustment factor for behavioural response	Office for Budget Responsibility – Economic and fiscal outlook – October 2018

Estimation and projection method: The tax base was constructed using data taken from the financial statements of public companies meeting the above criteria. When the data breakdown did not specify revenues earned in Canada, an estimate was made based on the regional segments available and the relative size of Canada's economy in this segment. The tax base was then projected from the average historical growth rate observed in the T2 income tax return data of companies in the targeted technology sectors. The tax base was also adjusted to factor in behavioural response impacts set at 30%. This assumption is based on the work of the United Kingdom's Office for Budget Responsibility in their October 2018 Economic and Fiscal Outlook.

The tax rate on the average revenues of companies in the targeted technology sectors was calculated from T2 income tax returns. The proposed measure acts as a tax credit on corporate income tax. Consequently, the effective tax rate was estimated by subtracting from the 3% tax rate the corporate income tax ratio of the targeted technology sectors. The estimated revenues were

calculated by multiplying the tax base constructed above by the resulting effective tax rate (2.1%).

Uncertainty
assessment:

The estimate has high uncertainty. The uncertainty comes mainly from the difficulty in accurately estimating the tax base. As well, data volatility means that there is a great deal of uncertainty underlying the tax base projection. Implementation of the proposal then depends on the companies' worldwide revenues, information not collected by Statistics Canada. Furthermore, companies in the targeted sectors are expected to adjust their services and rates in accordance with the new legislation. These behavioural changes are difficult to estimate and are based on strong assumptions, adding uncertainty to the estimate.

Cost of proposed measure

\$ millions	2019- 2020	2020- 2021	2021- 2022	2022- 2023	2023- 2024	2024- 2025	2025- 2026	2026- 2027	2027- 2028	2028- 2029
Total cost		-410	-450	-500	-560	-610	-680	-750	-830	-920

Notes:

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Estimates are presented on an accruals basis as would appear in the budget and public accounts.

Positive numbers subtract from the budgetary balance, negative numbers contribute to the budget balance.

"-" = PBO does not expect a financial cost