Tax Insights from Tax Services

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Digital Services Tax (DST): Will the DST's potential implementation affect your business?

July 13, 2023

In brief

July 13, 2023 update: *On July 12, 2023, the Organisation for Economic Co-operation and Development (OECD) announced that 138 countries and jurisdictions have agreed to extend for another year the standstill from imposing newly enacted digital services taxes (DSTs), or relevant similar measures, while work on a multilateral convention (MLC) to implement Pillar One continues. More specifically, they have generally agreed to refrain from imposing newly enacted DSTs until December 31, 2024 (extended by one year from December 31, 2023), provided the signature of the MLC has sufficiently progressed by the end of 2023 (i.e. at least 30 jurisdictions accounting for at least 60% of the Ultimate Parent Entities of in-scope multinational enterprises signing the MLC before the end of 2023).*

On the same day, Canada's Deputy Prime Minister and Minister of Finance, Chrystia Freeland, issued a press release stating that although Canada fully supports the MLC, it does not support the one year extension. Accordingly, it appears that Canada remains committed to moving forward with a DST as of January 1, 2024 if the MLC has not come into force. Canada's March 28, 2023 budget announced that revised draft legislative proposals to implement a Canadian DST would be released for public comment, but these legislative proposals have not yet been released.

The remainder of this Tax Insights *was published on February 23, 2023. It has not been altered to reflect the July 12, 2023 OECD news release, the Deputy Prime Minister and Minister of Finance press release or the March 28, 2023 federal budget comments.*

As recently as the November 3, 2022 Fall Economic Statement, Canada's federal government confirmed its intention to proceed with draft legislative proposals to introduce the *Digital Services Tax Act.* If the government proceeds with its implementation, the Digital Services Tax (DST) would be imposed on certain domestic and foreign corporations retroactive to January 1, 2022, but would not be payable before June 2025.

The government has also communicated that it has a strong preference for a multilateral approach and that the proposed DST is an interim measure that would only be imposed if a multilateral convention implementing the Organisation for Economic Co-operation and Development's (OECD's) Pillar One[1] solution has not come into force by December 31, 2023; in that event, Canada would start imposing the DST on January 1, 2024, in respect of

[1] The OECD supports a two-pillar solution to address the tax challenges arising from the digitalization of the global economy. The main element of Pillar One is to allocate a formulaic share of the consolidated profit of certain multinational enterprises to the market jurisdictions where revenue is earned. For more information, see our *Tax Insights* "The new international tax framework and Canada's digital services tax" at www.pwc.com/ca/taxinsights.

in-scope revenues earned since January 1, 2022. Pillar One and the DST share a common goal of ensuring companies pay tax where they are earning revenues. However, the two measures apply to very different groups of taxpayers, because of their applicable revenue thresholds.

The Canadian government has indicated that it intends to complete the multilateral negotiations so that the treaty to implement Pillar One can be signed in the first half of 2023, with a view to it entering into force in 2024. Although significant progress continues to be made in establishing the new technical rules for the multilateral approach and public consultations on these new rules are ongoing, the timeline to implement the multilateral convention by January 1, 2024, is tight. Considering this ambitious timeline, along with the fact that Canada's proposed DST would apply to in-scope revenues earned in 2022, affected businesses should begin to prepare for the DST's potential implementation.

In detail

The DST is proposed to be a 3% non-income tax on certain in-scope revenue earned by large domestic and foreign businesses.

In-scope revenue would comprise of digital services revenue arising from:

- online marketplace services
- online advertising services
- social media services
- the sale or licensing of user data

The DST would apply for a particular calendar year to businesses that meet both of the following revenue thresholds (to be calculated on a consolidated group basis):

- Total revenue threshold – global revenue from all sources of €750 million or more in a fiscal year of the taxpayer or group that ends in the previous calendar year
- Canadian in-scope revenue threshold – in-scope revenue associated with Canadian users of more than CAD$20 million in the particular calendar year

The tax would be calculated on Canadian in-scope revenues for the particular calendar year that exceed CAD$20 million (the CAD$20 million is shared among group members).

The takeaway

Should the DST be enacted, it will require a business to look back at its revenues and activities for 2022 and 2023, to determine whether a DST obligation exists for those years.

To ease the process of considering historical data to evaluate a potential DST obligation, and budgeting for any DST payments that may become due in 2025, we recommend that businesses begin to take the following steps now:

- learn about the four categories of in-scope revenues and the sourcing rules, and consider whether revenues earned in 2022 and 2023 fall into these categories
- calculate global consolidated revenues for 2021 and 2022 to determine whether the business meets the DST total revenue threshold for 2022 and 2023, respectively
- calculate the 2022 (and, if available, 2023) consolidated revenues derived from any of the four in-scope revenue activities associated with users in Canada
- for budgeting purposes, calculate estimated DST payable in 2025 for 2022, 2023 and 2024

Let's talk

For a deeper discussion of how the DST might affect your business, please contact:

Eric Paton, *National Indirect Tax Leader*
eric.paton@pwc.com

Jeff Frobel
jeffrey.a.frobel@pwc.com

Marcos Tabatschnic
marcos.x.tabatschnic@pwc.com