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by Keith R. Evans†

In February 2001, the OECD issued a draft report on "Consumption Tax Aspects of Electronic Commerce".[1] The purpose of this report was to seek comments on Working Party No. 9's conclusions and recommendations in respect of the approach to be taken on the application of consumption taxes to e-commerce in light of the Ottawa Taxation Framework Conditions.[2] The 1998 Conditions called for the taxation principles that applied to traditional commerce to be the guide for the taxation of e-commerce, to ensure non-discriminatory tax treatment of electronic commerce transactions. In November 2001, the Canada Customs and Revenue Agency ("CCRA") issued its own discussion paper in respect of the application of GST/HST to electronic commerce.[3] By July 2002, the CCRA was able to issue its formal views on this issue, with the publication of its GST/HST Technical Information Bulletin.[4] The purpose of this article is to review the position taken by the CCRA in the GST Bulletin insofar as it relates to the application of the GST/HST to cross-border electronic commerce transactions, and to assess how the position taken by Canada stacks up to the principles set out in the OECD Draft and the position being formulated by certain other major OECD members.

Where's the Beef? E-commerce Defined for Consumption Tax Purposes

In order to assess the principles recently adopted by Canada (and to compare that approach to that developing elsewhere) in respect of the application of consumption taxes to e-commerce transactions, it is important to clearly outline the kind of transaction that qualifies as an e-commerce transaction. The term "e-commerce" can be defined broadly as "the use of computer networks to facilitate transactions involving the production, distribution, sale and delivery of goods and services in the marketplace". As such, an e-commerce transaction can fall into one of three broad subcategories: the use of electronic means to sell tangible goods; the sale of digitized content (in the sense that the good/service itself is delivered/downloaded over the Internet); and the provision of Internet access and telecommunications services.[5] In terms of what is meant by an "e-commerce" transaction, the CCRA in the GST Bulletin simply states this as being "a supply made over the Internet",[6] and as such the GST Bulletin deals with only the final two categories. Given the specialist nature of telecommunications services, and to keep the length of this article to manageable proportions, I am further restricting its scope to only one of the three categories — the sale of digitized content.

However, even within this narrow category of transaction, there is a further subcategorization necessary in the consumption tax field, based on the nature of the buyer. When the buyer of digitized content is itself a business (including for this purpose an individual who is acquiring the content for use within that individual's business operations), this form of e-commerce is a business to business (B2B) transaction. When the buyer is a true consumer (i.e., a non-business purchaser) acquiring for a non-commercial use, the transaction is a business to consumer (B2C) transaction. As shall be seen below, the rules being developed to tax consumption of digitized content may be different, depending on whether the transaction in question is a B2B or a B2C transaction.

Having set the stage by defining "e-commerce" in this context, it is important to stress that even a business engaged exclusively in "e-commerce" is not a "virtual" business. Such a business must still maintain many of the trappings of a traditional "brick and mortar" operation, as so eloquently stated as follows:

> Nevertheless, all e-commerce business, like any other business, requires traditional inputs of buildings, equipment and human participation. Even where customer transactions are ultimately carried out electronically, businesses still require a capital and labor infrastructure in order to develop, produce, and promote their products and services and in order to operate their affairs. The relative mix of inputs may be somewhat different, as in the e-commerce economy intellectual capital may be relatively more important than tangible capital. The e-commerce economy also includes a greater proportion of products that are non-phys-

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ical, such as electronically distributed music, software and video. None of these differences, however, means that an e-commerce company has no physical presence anywhere.

It is true that e-commerce provides an additional avenue of communication with customers that expands opportunities for businesses to penetrate foreign markets without establishing physical connection in those markets.[7]

Tax administrators need to bear this in mind when evaluating the application of traditional tax concepts to the world of digital content, as there may be more similarities between the two than are at first glance apparent.

GST/HST Rules For Tangible Cross-Border Trade

Before highlighting the special problems e-commerce (as narrowly defined above) presents for consumption taxes in general, and the CCRA approach thereto in the GST/HST context in particular, it is useful to briefly review the application of the GST/HST regime to a sale of a tangible good by a foreign seller to a Canadian buyer. ("Canadian" in this context simply refers to the fact that the purchaser is located in Canada and will "use" the good within the boundaries of Canada.) Such a sale could be made in various ways, but two contrasting examples will suffice to outline the basic application of the GST/HST system to sales of tangible products. In one option, the foreign seller has no local (i.e., Canadian-based) business establishment or agent acting in respect of the sale, the sale contract is concluded by telephone or facsimile exchanges between the offices of the buyer and the seller located in different countries, and the good is delivered from a foreign location by a carrier or through the mail system, with the good in either case having to cross the border to reach the buyer. Alternatively, a non-Canadian entity may maintain a local (Canadian-based) office or agent for the purpose of making such sales, with the goods coming either from a stock of goods maintained in Canada, or again from a foreign location once the sale is arranged.

The GST/HST in Canada is basically a tax on goods (both tangible and intangible) and services that are "consumed" in Canada — it is a destination-based tax which is payable by the recipient of a taxable supply made in Canada, [8] or by an importer upon import of tangible goods into Canada. The buyer, under either of the scenarios above, will consume the good within Canada, and GST/HST should be paid on the transaction. However, the tax will be collected in different ways under our two scenarios above. In the first of the two alternatives, the buyer will in most circumstances be the importer of record, and will pay the GST upon clearance of the good through the usual customs clearance procedures.[9] The need for the good to clear through the customs process provides a natural point of collection for the consumption tax. However, as the GST/HST is a value-added type of consumption tax, to the extent that the buyer uses/consumes the good in the course of its own commercial activity of making taxable supplies in Canada, the buyer will be able to credit the tax paid on the imported good against the tax it charges to its own customer under the system, remitting the net to the government or claiming a refund as the case may be.

Under the second alternative, the foreign vendor may be required to register as a taxable supplier under the system, in which case it will need to invoice the buyer for the GST/HST charge, collect the tax due and remit it to the government. Registration is required where a person (1) makes a taxable supply (2) in Canada (3) in the course of a commercial activity engaged in by that person in Canada, except where that person is:

(i) a small supplier;[10] or

(ii) a non-resident person who does not carry on any business in Canada.[11]

In general, if the level of activity of the foreign supplier in the second alternative is sufficient to constitute a "carrying on of business" by that person in Canada (aspects of which will be examined in more detail below in the context of the e-commerce issues), the foreign vendor must register, collect and remit GST/HST in respect of qualifying taxable supply in Canada. A non-resident will not qualify for the exclusion under item (ii) above in respect of activities which the non-resident conducts through a permanent establishment in Canada[12] (the definition of which will be addressed below in the context of the e-commerce issues).

A foreign vendor that does not meet the requirements for mandatory registration may elect to register for collection of tax on taxable supplies in Canada where that person is:

(i) engaged in commercial activity in Canada (where the activity falls short of carrying on business in Canada — when registration becomes mandatory as discussed above); or

(ii) a non-resident person who, in the ordinary course of carrying on business *outside of (emphasis added) Canada, either*

(a) regularly solicits orders for the supply of tangible personal property for export to or delivery in Canada, or

(b) enters into an agreement for supply of services to be performed in Canada, or enters into an agreement for the supply of intangible personal property to be used in Canada that relates to real property situate in Canada, tangible personal property ordinarily situate in Canada or services to be performed in Canada.[13]

Such voluntary registration would be considered where the non-resident person is charged GST/HST on supplies made to them in Canada and wants to be able to credit those input charges against the tax levied on its supplies to customers.

To the extent that e-commerce business channels result in an order for a tangible good which is to be delivered across an international border, no special rules are required for the application of consumption tax to that transaction. The usual mechanisms above will fully accommodate that form of business, with tax being paid by the Canadian purchaser either on import, or through the vendor registration regime.

Consumption Tax Challenges of E-commerce

The taxation challenge presented by e-commerce differs depending on whether one looks at the matter from the point of view of a tax administrator or a business engaged in commercial e-commerce activity. The former view is well stated in the GST Discussion Paper:

> The technology underlying electronic commerce facilities the delivery of products and services by suppliers to customers located throughout the world. A business will often have no physical presence in the jurisdiction of its customers. In other cases, the only physical presence it may have in that jurisdiction is a server. As well, products that could previously be supplied in a tangible format can now also be supplied electronically in a digitized format, and services that once required the physical presence of personnel at the location of the customer may now be performed from a remote location by electronic means. This fundamentally alters the way business is conducted and presents challenges to consumption tax administrators throughout the world.[14]

From the business perspective, the challenge is to ensure that consumption taxation of e-commerce does not impede or restrict the development of this commercial segment of the economy, as best outlined by the concepts of neutrality, efficiency and simplicity set out in the Taxation Framework Conditions.[15] Neutrality requires that taxation should be neutral and equitable between e-commerce and conventional forms of commerce, so that taxpayers in similar situations and carrying out similar transactions are subject to similar levels of taxation. The objective is to create a level playing field, allowing business decisions to be motivated by economic and not tax considerations. In this vein, digital supplies of music or computer software should be subject to the same consumption tax burden as a supply of hard copies of records and disks crossing borders. Efficiency and simplicity require that compliance costs for taxpayers, and for businesses which have to collect tax for governments, are minimized as much as possible, and for the tax rules to be clear and simple to understand.

While the challenges can be stated differently, depending on your perspective, they both throw up three significant issues for resolution in the consumption tax field:

(1) Identification of the jurisdiction in which tax should be applied. This is the issue of where consumption of a digitized product or service is viewed as taking place.

(2) How is the tax to be collected? In the case of tangible goods, territorial borders and customs clearance procedures create an easy means for collection of consumption taxes. Given current technology, product and services supplied in digitized format over the Internet have no comparable natural barrier or process.

(3) The categorization of intangible products and services supplied digitally. Categorization will have an impact in some cases on both the place of supply and the manner of tax collection, and hence overlaps both of the prior issues. It also affects the timing of the liability for the tax and, in some cases, the rate of tax applicable.

Place of Consumption

For sales of tangible goods across international borders, the delivery address of the buyer or recipient of the goods can easily be used to identify the most likely place of consumption of the good in question.[16] If the good is not ultimately to be consumed in that location, the customs clearance procedures can again trigger appropriate adjustments to the consumption taxes charged. The same cannot be said for an item of intangible property which is capable of digital delivery to a customer online, where there is often no clear indication of the physical location in which the digital good is destined to be used (although it is entirely possible that future technological developments will permit a clearer ability to determine the location of a customer at the time of an online purchase).[17] To suggest that vendors should be required currently to verify the jurisdiction of intended use of such products would impose a considerable and likely unacceptable administrative burden on e-commerce businesses.

Delivery of a service gives rise to additional location problems. In fact, the OECD Draft usefully breaks services into two types, tangible and intangible. A tangible service is one which is performed or takes place in an identifiable location and may be considered to be consumed in that location. Examples of such services include services performed in respect of specific real property, transportation services and physical performance services such as concert performances, hairdressing and restaurant services. Intangible services such as consultancy, professional services, advertising, information access, and data processing, etc., by contrast, can be physically performed in one location, but could typically be viewed as consumed by the intended recipient in another location.[18] It is the supply of intangible property and intangible services which creates the greatest place of consumption challenge.

In the GST/HST context, place of consumption is not directly addressed by the legislative regime. Instead, the issue of place of consumption is tied to whether or not the supply is made in Canada. If it is, then it is subject to GST/HST (and hence treated as being consumed here) unless the supply is an exempt supply or is zero-rated. It might be zero-rated, for example, if a Canadian-based service provider makes the supply to a non-resident and therefore effectively "exports" the intangible good or service.

A supply of intangible personal property is deemed to be made in Canada[19] if:

(1) The property *may be used in whole or in part in Canada. The CCRA has stated that the key here is the ability (emphasis added in both cases) to use the intangible property in Canada, and not its actual use, and goes so far as to indicate that a supply could still be viewed as having been made in Canada even if the recipient is outside Canada at the time of supply.* [20] Hence, the express and implied contractual restrictions (from a geographic perspective) will be a key issue in the determination of whether the sale of an intangible/digital product is made in Canada.

(2) The property relates to any of the following: real property situate in Canada; tangible personal property ordinarily situate in Canada; or a service to be performed in Canada.

By contrast, a supply of intangible personal property is deemed to be made outside of Canada if the property may not be used in Canada, or the property relates to real property situate outside of Canada, to tangible personal property ordinarily situate outside of Canada, or to a service to be performed wholly outside of Canada.[21]

In terms of services, the GST/HST focus of attention in determining whether the supply is made in Canada is on the place of "performance" of the service — a supply of a service is deemed to be made in Canada if the service is or is to be performed, in whole or in part, in Canada.[22] The GST Bulletin elaborates on this in a number of respects:[23]

- The place where a service is performed is usually the place where the person physically doing the work is situated.
- As only part of the service need be performed here for the supply to be made in Canada, it is enough if only part of the service activity is carried out by the supplier in Canada.
- A foreign supplier can provide a service to a customer in Canada without ever being physically present in Canada. This would occur, in the CCRA view, if the supplier's employees perform technical work outside of Canada by electronically accessing a customer's computer physically located in Canada (except where the service is performed wholly outside of Canada and the results are simply delivered electronically to the local equipment). In this case, in the CCRA's view, the services are performed partly in Canada and partly elsewhere, and deemed to be supplied in Canada.
- Likewise, if the supplier's equipment is located in Canada and the supplier's service is performed by that equipment, the CCRA's view is that the supply is made in Canada.

The consumption nature of the GST/HST system is perfected by linking the place of supply rules with the *zero-rating of supplies made to non-residents — or exported — from Canada. If the supply of an intangible product or service is a taxable supply in Canada under the rules above, GST/HST will be payable unless the zero-rating provisions apply. In the event that the supply in question is a supply of intangible personal property, the supply is zero-rated only if the supply is made to a* non-registered non-resident customer and is a supply of either intellectual property (an invention, patent, trade secret, trademark, trade name, copyright or industrial design) or the right, licence or privilege of using such property.[24] Hence, the sale to a non-resident non-registered customer of software downloaded from the Canadian supplier's Web site is zero-rated, but the sale of a subscription service to digitized music, videos or games used but not downloaded online is not and is therefore subject to GST/HST.[25]

A supply of a service to a non-resident is generally zero-rated,[26] but this zero-rating is not available for a range of specified services, including:[27]

- a service made to an individual who is in Canada at any time when in contact with the supplier in relation to the supply;
- a service rendered to an individual while the individual is in Canada;
- certain advisory, consulting and professional services;[28]
- a service in respect of tangible personal property situated in Canada at the time the service is performed.

In the e-commerce context, the GST Bulletin confirms that the provision by a GST/HST registered business of Web site hosting services to a non-resident non-registered customer, and the sale of banner advertising on a Web site to such a customer, are both zero-rated.[29]

The zero-rating provisions above are tied to the supply being made to a non-resident. It would seem that the general body of common law applies to the issue of whether one is resident or not,[30] although the Act contains certain provisions which would deem residence,[31] including a provision which states that where a non-resident person has a permanent establishment in Canada, that person is deemed to be resident in Canada in respect of the activities conducted through that permanent establishment.[32] The corollary — a resident of Canada with a permanent establishment outside of

Canada — is also deemed to be a non-resident in respect of activities of that person carried on through that establishment.[33]

It is clear from the discussion above that the CCRA has cast a wide net when considering the range of services and intangible goods which it views as being consumed in Canada. As such, it appears to go beyond the proposed guidelines issued with the OECD Draft.[34] That Draft suggests that in respect of cross-border supplies of intangible goods and services capable of digital delivery into member countries by a non-registered vendor not required to register for VAT/GST that:

- In B2B transactions, the place of consumption for cross-border supplies should be the jurisdiction in which the recipient has located its business presence.[35]
- In B2C transactions, the place of consumption should be the jurisdiction in which the recipient has its usual residence.

In fact, there is no apparent distinction made by the CCRA in respect of the place of consumption based on the status of the recipient as either a consumer or a business. And, while the OECD Draft provisions are only directed to in-bound supplies, the commercial need for fair treatment on a level playing field suggests that Canadian suppliers should not be required to charge GST/HST under the OECD proposals in certain circumstances where the GST Bulletin would require this to be done:

(1) In respect of the supply of intangible personal property, such property is deemed to be supplied in Canada if it *may be used in Canada*, and is only zero-rated on export if it is a supply of intellectual property or the right to use such property. As the GST Bulletin itself notes, this means that a Canadian supplier must charge a non-resident customer GST/HST on a gaming subscription fee — putting Canadian businesses which supply such subscription services to foreign users at a distinct competitive disadvantage to a foreign supplier who can supply the same service without foreign-use tax thereon. The OECD proposals would suggest that such a supply is consumed outside of Canada, and should not be subject to Canadian GST/HST.

(2) Likewise, a Canadian-based supplier of an intangible service to a non-resident customer will have to charge GST/HST if the service is not within the list of permitted zero-rated service exports under the system — again placing the Canadian provider at a competitive disadvantage to a foreign supplier of the same service.

The European Union, by contrast, appears to have agreed largely to follow the OECD proposal. At an Ecofin Council meeting on February 12, 2002, political agreement was reached on a Directive amendment in respect of the application of VAT to digital products.[36] Once the rules are implemented by EU member states (which is required by July 1, 2003),[37] B2B Internet supplies, whether between EU members, or supplied from outside the EU, will be treated as consumed in the location where the business recipient has its business presence for the purpose of the supply and will be subject, in the case of all supplies into an EU member state, to a reverse charge mechanism (see the collection discussion below). Supplies made to a business outside of the EU (and which were previously treated as having been consumed in the jurisdiction from which the supply was made and hence subject to VAT) will be treated as exported and subject to a zero-rating.[38] B2C transactions will be treated differently depending on whether the supplier is supplying from an EU location or from outside the EU. In respect of the former, the supplier will charge the EU-based consumer the VAT applicable in the jurisdiction from which the supply is made (in which case the supply is treated as "consumed" in the state of the supplier). However, supplies made from a business supplier located outside the EU now will be treated as consumed in the location where the consumer is established, has his/her permanent residence or usually resides,[39] and will be subject to the VAT rate applicable in the destination location. Tax will need to be collected and paid by the non-EU supplier under a simplified registration process (addressed below).

In the United States, sales and consumption taxes are state and local matters, and there is no federal consumption or value-added tax system. At the state level, most states that levy such taxes apply a more traditional retail sales tax where the focus is on the need for vendor registration (as to which, see below). In this context, the place of sale or source of the transaction, and not the place of consumption, tends to be paramount. Therefore, the place of consumption issue has not been canvassed to any great extent in the United States, although in terms of sales by U.S. vendors to international customers, there is a relatively high level of support for the OECD framework discussions.[40]

Australia, to the extent it has formulated a position, conforms with the OECD approach. Australia uses three categories for its GST legislation — tangible goods, real property, and things other than goods and real property. As such, the Canadian dichotomy of intangible personal property and services is not relevant in that jurisdiction, and digital supplies would appear to fall into the last category. Such supplies are connected with Australia if either the thing is done in Australia or if the supplier makes the supply through an enterprise that the supplier carries on in Australia. If supplies are not so connected, they are GST taxable only if: (1) the recipient acquires the thing solely or partly for the purpose of an enterprise of the recipient carried on in Australia, but not solely for a creditable purpose; (2) the supply is for consideration; and (3) the recipient is registered or required to be registered.[41] This conforms with the OECD Draft approach on B2B transactions. While Australia supports the concept of taxation of digital supplies in the location of consumption, it has not issued a clear policy view on where such supplies are "consumed" in the consumer context, as it does not currently seek to collect GST on supplies to private Australian customers in a cross border context, stating instead that it will monitor international developments before acting.[42] In the reverse scenario, digital supplies made by Australian registrants to non-residents are zero-rated on a broad basis, dependent on the location of the recipient or where the recipient carries on its enterprise.[43] It remains to be seen whether Australia will follow the OECD approach when and if it decides to tax cross border B2C transactions.

How To Collect GST on E-commerce Transactions

Due to the fact that digital products delivered over the Internet do not need to pass a natural customs barrier at which the consumption tax can be collected, the tax collection mechanism is in fact the most significant issue affecting consumption taxes in an e-commerce environment — both from the point of view of tax administrators who are concerned about maintenance of their tax base, and for e-commerce businesses which are concerned about requirements to register, collect and remit the tax (a process which can be administratively time consuming and costly). In the digital environment, the two most obvious tax collection requirements are a mechanism which requires the supplier/vendor to register and collect the tax, and a system which requires the recipient of a supply to "self-assess" the tax due (i.e., determine that the transaction is subject to consumption tax and calculate the amount of tax payable) and remit it voluntarily to the tax collector. The unlikelihood of large groups of individual consumers sending cheques to the government after having downloaded digital property or services over the Internet in the privacy of their own home indicates the potential for tax leakage under the second alternative. (It is truly utopian for consumption tax administrators to expect that any "consumption tax can be enforced and collected 100%, or anything like it".[44])

In respect of collection matters, the OECD Draft makes the following proposals:

> The most viable collection mechanisms ... lie:
>
> (i) In a reverse charge or self-assessment mechanism for B2B transactions; and
>
> (ii) In the near term (pending adoption of technology-facilitated options), in some form of registration-based mechanism for B2C transactions. The latter has its shortcomings ... and there is a recognized need to promote simplified approaches to registration of non-resident suppliers.[45]

Even in respect of a registration model, the OECD Draft goes on to suggest that thresholds for registration of suppliers are advisable. Thresholds would help to minimize the compliance burden for small- and medium-sized enterprises, or even for large enterprises making a limited number of sales to a particular location.[46] The Draft also notes that to ensure compliance, a simplified (and electronic) process for registration and filing of returns would be useful.[47]

In the GST Bulletin, the CCRA does not initially adopt any distinction in the way in which tax is collected on B2B versus B2C transactions, electing instead to apply the normal registration and filing procedures, and the need for registered businesses to collect and remit GST/HST, for all cross-border Internet supplies of digital content in Canada, irrespective of the character of the recipient. As noted above, the general rule here is that a supplier is required to register, and to collect and remit GST/HST on supplies, if that person makes a taxable supply in Canada in the course of a commercial activity engaged in by that person in Canada, other than as a small supplier or a non-resident who does not carry on any business in Canada.

In analyzing whether a non-resident is required to register, one must first consider whether the non-resident maintains a permanent establishment in Canada or not. If the non-resident has a permanent establishment in Canada, that person is deemed to be a resident of Canada in respect of the activities of that person carried on through that permanent establishment.[48] "Permanent establishment" is a defined term, meaning:

> "in respect of a particular person"
>
> (a) a fixed place of business of that particular person, including:
>
> (i) a place of management, a branch, a factory or a workshop, and
>
> (ii) a mine, an oil or gas well, a quarry, timberland or any other place of extraction of natural resources,
>
> through which the particular person makes supplies, or
>
> (b) a fixed place of business of another person (other than a broker, general commission agent or other independent agent acting in the ordinary course of business) who is acting in Canada on behalf of a particular person and through whom the particular person makes supplies in the ordinary course of business.[49]

This definition is similar to but not as detailed as definitions of "permanent establishment" found in the context of international income taxation,[50] where there has been significant work done on the issue of how to apply the well-known concept of permanent establishment to e-commerce business.[51] The CCRA appears to support the application of these international tax developments in the GST/HST context, by concluding that:

- A Web site alone, consisting merely of software and electronic data, and not being tangible property, cannot be a place of business and hence cannot be a permanent establishment.

- A server on which a Web site is stored/hosted is tangible property having a physical location and can, therefore, if that server is in Canada, constitute a permanent establishment of a non-resident person if the server is at that person's disposal (i.e., being operated, owned or leased by that person). By contrast, if an independent ISP provides the server on which the Web site is hosted, this would not generally create a permanent establishment for that non-resident whose Web site is so "hosted".
- Presence of personnel in Canada is not required to create a permanent establishment.
- An ISP that hosts a Web site of a non-resident person on the ISP's servers in Canada will not generally be an agent (and hence not constitute a permanent establishment) of the non-resident either because it does not usually have the authority to conclude contracts on behalf of the non-resident, or because it hosts a number of Web sites for different businesses and is therefore an independent agent.[52]

The CCRA appears to give the impression, on a quick reading of the GST Bulletin, that as soon as a permanent establishment in Canada exists, the non-resident must register for GST/HST purposes. This is an unfortunate and perhaps erroneous position. Under the provisions of the legislation which require registration, even resident persons are required to register only if they make taxable supplies in Canada above the threshold levels "in the course of commercial activity" engaged in by that person in Canada,[53] and "commercial activity" is defined by reference to a "business carried on by" that person.[54]

Internationally, in the income tax context, likewise, having a permanent establishment in a location does not carry with it a consequence of incurring liability to income tax unless the non-resident carries on business through that permanent establishment.[55] A more careful reading of the Bulletin reveals the need for the non-resident to carry on business through the permanent establishment before registration is required. The CCRA notes that the functions carried on by the non-resident through a permanent establishment such as a server must "on their own be an essential and significant part of the business activity of the enterprise as a whole, or constitute other core functions" of the non-resident[56] before registration is needed. Hence, the operation of a server in Canada by a non-resident ISP in the business of hosting Web sites will be a permanent establishment, and trigger the need for the ISP to register (as here Web site hosting is a core business activity of the non-resident ISP), but another non-resident with its own Canadian server, the use of which is restricted to preparatory or auxiliary activities for that business, will not be viewed as having a permanent establishment for GST/HST purposes. Therefore, it would appear that if a facility in Canada falls within the basic definition of a permanent establishment, the non-resident need only register if there is sufficient activity in Canada conducted through that permanent establishment to constitute a carrying on of business here.[57]

Simply avoiding a permanent establishment in Canada will not, however, circumvent the need to register for HST/GST purposes — as it is possible for a non-resident to carry on business in Canada, and hence be engaged in commercial activity here, without having a permanent establishment.[58] This would again trigger the need for that non-resident to register for GST/HST in respect of taxable supplies in Canada above the small supplier threshold, although the issue of whether the registration requirement can be enforced effectively where the non-resident has a limited presence in Canada is an open issue.[59] Case law in Canada suggests that the determination of whether a business enterprise is "carrying on a business" requires a functional analysis of the activities that must be conducted in order to generate the income for that business, in order to determine whether in fact the operations which are key to the production of the income take place here.[60] Cases also indicate a need for the recurrence of the activity.[61]

The CCRA appears to adopt a similar position in the e-commerce field, noting that for both e-commerce and traditional business it is necessary to look at a whole range of business factors in order to determine whether the activities of the non-resident in Canada are significant. A significant enough presence (which might fall short of creating a permanent establishment) will result in a determination that the non-resident is carrying on business in Canada,[62] and trigger a relevant registration requirement where taxable supplies are made in Canada above the small supplier threshold. The factors noted specifically by the CCRA (at least those of direct relevance in the specific e-commerce context) include: the place where agents or employees of the non-resident are located; the place of delivery, payment, and where purchases are made; the place from which the transaction is solicited; the place of contract; the location of bank accounts; the place where the non-resident's name and businesses are listed in a directory; the location of branches and offices; and the place where the service is performed (which has been analyzed above). The CCRA adds that some of these factors have to be considered differently in e-commerce, as opposed to traditional commerce — noting that in determining the place of payment made electronically, it may be necessary to consider the place where approval of the electronic funds takes place, whereas in traditional commerce, this factor would consider the place of posting or place of receipt of cheques, etc.

The discussion above deals only with the "vendor registration" option for consumption tax collection. The fact that a non-resident supplier does not have to register and collect GST/HST does not mean that a cross-border supply of an intangible good or service is tax exempt — the recipient may still be required to reverse charge or self-assess for consumption taxes on the supply. Canada has not adopted a general need for registrants to reverse charge for GST/HST for any imports of intangible property and services[63] — but maintains a self-assessment requirement for non-registered recipients.[64] In general, GST/HST is not imposed on services and intangible personal property imported by registrants for use exclusively (which the CCRA views as being 90 per cent or more) in a commercial activity and no input credits arise in respect of such imports. However, non-registered recipients, and registered recipients using the import other than exclusively for commercial activity, are required to self-assess and pay the GST/HST (with the registered recipient being able to claim input credits for that part of the supply used in commercial activity).[65]

Canada's approach to collection can therefore be summarized as follows. The normal supplier/vendor registration rules (adapted as necessary in terms of application given the contextual realities of e-commerce) apply. In general this appears to fit with the tenor of the OECD Draft. In respect of imports of taxable supplies from a vendor who is not required (and who chooses not voluntarily) to register, no self-assessment or reverse charge is required if the buyer is a registrant who will use the product or service exclusively in a commercial activity, a position which is again consistent with the OECD Draft.[66] However, where the purchaser is a consumer acquiring for personal use, technically a self-assessment mechanism applies, a position which runs counter to the OECD Draft and which appears to ignore reality. As the OECD Draft notes:

> Where currently in use for B2B transactions (in most OECD Member countries), the [reverse charge] system has proven feasible, effective and carries a low compliance and administrative burden. Self-assessment/reverse charge, however, has not been effective in ensuring the collection of tax on transactions involving private recipients (B2C).
>
> . . . For B2C transactions, however, the Technology TAG concluded that self-assessment was the least practical option from a technology perspective.[67]

Canadian insistence on a personal consumer self-assessment regime which will more likely be honoured in the breach than in compliance is curious, particularly in light of a general view, often expressed, that the level of B2C e-commerce is relatively small and insignificant,[68] and the OECD Draft position favouring registration regimes for B2C transactions.

As noted in the previous section, Australia's position on inbound B2B sales by a supplier which is not required to register is similar to that taken by Canada — the registered recipient should reverse charge, but only if the recipient is not entitled to a full input tax credit on the supply. However, no self-assessment is currently required on comparable inbound B2C supplies — Australia for the moment choosing not to tax such supplies pending international developments.[69] In both respects, Australia does not depart from the position taken in the OECD Draft.

The European Union takes a slightly different approach to B2B sales made by non-registered non-resident suppliers, although again its position is in accord with the OECD Draft. A non-EU supplier selling to business customers does not need to register for VAT — VAT is to be paid by the customer under the self-assessment system.[70] Verification of the registered status of the customer can be obtained by the vendor through a check of the customer's VAT registration number.[71] However, a non-EU supplier (i.e., one not otherwise required to be registered (due to having its seat of business or a fixed establishment in the EU) or which has not voluntarily registered for VAT) making an e-commerce supply to a private customer (a B2C transaction) must register in any member EU state of the supplier's choice (using a simplified, online registration process), but must charge the customer the VAT rate levied in the state where the customer resides. The VAT collected is paid to the state where the supplier has registered, and then there is to be a government-to-government settlement of the sums collected,[72] with the relevant sum transferred to the state of residence of the customer. This position is again consistent with the OECD Draft, save for the fact that the EU has set no minimum threshold of B2C sales in the EU before registration is required.[73] The original proposal did indicate that an 100,000EU threshold would apply,[74] but this was abandoned in the search for political agreement on the new rules. Therefore, a single sale to a consumer in the EU by a non-EU supplier, where that supplier has no other EU nexus, geographic or otherwise, appears to trigger a registration requirement under the new regime.

From a theoretical perspective, as the consumer purchaser will likely consume the product in his or her residential location, it is appropriate for the EU to require vendor registration for a consumption tax regime based on a sale to a local consumer as the only nexus between the vendor and the tax jurisdiction in question. It is curious to note that Canada, by contrast, has opted for a greater degree of nexus requiring that a non-resident have either a permanent establishment in this country through which certain core business functions are conducted, or to otherwise carry on business here before registration is required. This appears to make Canada's requirement much more similar to state requirements for sales tax regimes for traditional commerce in the United States. In the United States, states can impose sales taxes only on transactions completed within their borders, and can require that vendors collect use taxes for the state (at least as far as tangible products are concerned) only from vendors with a "physical presence" in the state.[75] This restriction applies to all vendors, whether based in another U.S. state or in a foreign country. While the U.S. "geographic nexus" position is largely based on constitutional provisions for which comparable problems might not exist in Canada, given the fact that U.S.–Canada trade continues to represent the lion's share of Canada's international two-way trade, having use tax registration requirements that are similar in structure to those with which U.S. suppliers might be familiar has some merit.

The vendor registration issue has been the focus of attention in U.S. consumption tax policy development over the past five years.[76] The tax challenge of e-commerce in that jurisdiction is more significant than that internationally. Given that sales and use taxes are matters for state and local governments, there are some 30,000 potential taxing jurisdictions, of which over 7,500 actually levy some sort of tax.[77] In November 2002, and as a result of the Streamlined Sales Tax Program, some 30 states have endorsed a multi-state platform for simplification of sales tax regimes in the United States. This regime will come into effect at a date after July 1, 2003[78] when at least 10 states representing at least 20% of the U.S. population have actually amended state law to conform to the agreed regime.[79] This initiative includes:

- application of common definitions of products in all participating states and their sub-jurisdictions;
- implementation of common sourcing rules in respect of place of sale;
- a simplified online registration system under which registrants need register in only one member state, but then must collect tax on all taxable sales in all member states;
- state level administration for all sub-state jurisdictions levying retail taxes.

While the streamlined system will still require registration only if the previously required physical nexus (discussed above) is present, voluntary registration by vendors is permitted and will be encouraged through the ability to keep administration costs low through adoption of one of three permitted automated tax collections systems, a limited duration tax amnesty for prior but uncollected taxes, and monetary allowances granted to vendors to help cover their administration costs. More significantly, it is hoped that the simplified system will give impetus to action by the U.S. Congress to enhance state powers to force remote sellers to collect tax.[80] The adoption of a simplified online registration system for tax collection is consistent with the OECD Draft. However, as most states still tax products but few tax services (see below), it may well be that e-commerce suppliers will largely escape such taxes in the United States in the near term. Congressional action, if it happens, may change this by clarifying the factors needed to establish a state nexus in the e-commerce world, so as to take registration requirements out of the voluntary category and make registration mandatory.[81] This ability to require registration might then prompt states to extend their range of taxable sales to include the sale of digital content to in-state buyers.

Categorization of Intangible Services and Property

The GST Bulletin spends a lot of time categorizing particular aspects of e-commerce as being either the supply of an intangible product or service, and in respect of the latter, distinguishing an ordinary and a telecommunications service (the latter not being reviewed in this article for the purposes of keeping it to manageable length). Treatment of a digital supply as being a supply of a good (or property), even an intangible one, appears another departure in the Canadian context from the OECD Draft position.[82] In the domestic context, proper categorization will have a major impact on a number of issues, the most significant of which, for the purposes of this article, are the place of supply rules that apply to the item and whether or not a registration requirement might be triggered as a result of the nature of the supply and what is being done in the context of that supply in Canada. These issues have already been discussed in detail above. While they are not relevant from the point of view of this article, proper categorization can also impact, in appropriate cases, the rate of tax applicable and the timing of the liability to pay it.

The GST Bulletin notes that as supplies made in digitized format do not constitute tangible property, they must either be a supply of intangible personal property or of a service.[83] In distinguishing the two, the CCRA adopts a factoral approach, considering relevant factors present in each case to decide whether the nature of the agreement between the supplier and the customer is in substance for work (or work and materials) and hence the supply of a service, or for the provision of (intangible) property (including a right or interest of any kind). By way of general guidance, the CCRA states:

> Factors that generally indicate that a supply made by electronic means is one of intangible personal property are:
>
> - a right in a product or a right to use a product for personal or commercial purposes is provided, such as:
>   — intellectual property or a right to use intellectual property (e.g., a copyright); or
>   — rights of a temporary nature (e.g., a right to view, access or use a product while on line);
> - a product is provided that has already been created or developed, or is already in existence;
> - a product is created or developed for a specific customer, but the supplier retains ownership of the product; and
> - a right to make a copy of a digitized product is provided.
>
> Factors that generally indicate that a supply made by electronic means is a service are:

- the supply does not include the provision of rights (e.g., technical know-how), or if there is a provision of rights, the rights are incidental to the supply;
- the supply involves specific work that is performed by a person for a specific customer; and
- there is human involvement in making the supply.[84]

The GST Bulletin then goes through a list of some 28 indicative examples with a categorization outcome as follows:

Supply of intangible property

(1) Electronic Ordering and downloading of digitized products, and add-ons and up-dates.

(2) Supply of limited duration software and other digitized information licenses.

(3) Subscription to a Web site that allows the downloading of digitized products.

(4) Software maintenance (through downloading updates).

(5) Customer support over a computer network (where actual access to technical personnel is incidental to on-line documentation and information data bases).

(6) Application Hosting — bundled contract.

(7) Data Retrieval service.

(8) Subscriptions to interactive Web sites.

(9) Providing a right to use undisclosed technical information.

(10) Subscription for delivery of information (such as a news clippings or a stock market quotation service) tailored to personal preference of customers.

(11) Acquisition of right to use copyrighted content.

Supply of Service

(1) Customer support over a computer network by access to technical personnel where access to online documentation and databases is incidental.

(2) Application Hosting (separate license).

(3) Application Service Provider situations.

(4) Web site hosting.

(5) Data warehousing.

(6) Provision of Web site advertising space.

(7) Provision of Online Shopping Portals.

(8) Provision of Online Auction services.

(9) Providing access to tailored professional advice online/development of technical information for a client.

(10) Development of copyrighted content for the customer.

(11) Preparation and Electronic Data Interchange (EDI) transmission of income tax returns.

Supply of Telecommunications Service

(1) Internet access services.

(2) Provision of Email services.

(3) Provision of bundled Internet access, email and Web Site location services.

(4) Voice telephony services over the Internet.

(5) EDI transmission of income tax returns.

(6) Web based broadcasting.

While categorization issues in the e-commerce field have been discussed by the OECD in the income tax field,[85] in the consumption tax area, as noted, the OECD view is that supplies of digitized products should not be treated as being a supply of goods. As shown above, Canada has not adopted this approach. The EU by contrast appears to have adopted the OECD Draft position by treating most digital supplies as supplies of services and applying the new EU regime outlined above. Electronically supplied services for the EU regime are defined as:

(1) Website supply, web-hosting, distance maintenance of programmes and equipment.

(2) Supply of software and updating thereof.

(3) Supply of images, text and information, and making databases available.

(4) Supply of music, games, films and games of chance and gambling games, and of political, cultural, artistic, sporting, scientific and entertainment broadcasts and events.

(5) Supply of distance teaching.[86]

Likewise, as noted above, Australia appears to treat digital supplies as a single category, namely, as "things other than goods or real property".[87] In the United States, most states and their sub-jurisdictions apply their retail sales taxes to sales of goods only, with only a few states actually taxing services.[88] While the Streamlined Sales and Use Tax Agreement will contain a definition of computer software which will apply to software delivered on media as well as digitally[89] (and hence treating the supply as a supply of goods contrary to the OECD Draft), Congressional action to extend the states' ability to require registration of remote vendors who have more limited physical nexus to the states in question will be required before a more serious extension of use taxes to the full range of digital content becomes likely. It is only at that stage that most issues of categorization will come to the fore in the United States.

Conclusion

In its Taxation Framework Conditions, the OECD lists as its first objective, in the field of consumption taxes, that the "rules for the consumption taxation of cross-border trade should result in taxation in the jurisdiction where consumption takes place and an international consensus should be sought on the circumstances under which supplies are held to be consumed in a jurisdiction".[90] It is apparent from the comparisons above that rather than obtaining consensus, there is a divergence amongst various members of the OECD on proper categorization of e-commerce supplies, and consequentially on the issue of the place of consumption for the purpose of imposition of use taxes. The European Union appears to be leading the charge in adopting rules close to those proposed in the OECD Draft, but the Canadian position contains a number of points of divergence. The United States, one of the world's most significant economies, both in respect of traditional and e-commerce, currently appears to be focusing on place of sale requirements, and is therefore out of step with most other OECD countries.

These divergences continue when one examines the approaches of these jurisdictions in respect of the need for non-resident suppliers to register for consumption tax collection purposes for B2C transactions, and in their approach to self-assessment or reverse charging for cross-border supplies to business customers. While Canada and Australia appear to apply their normal rules for registration, Canada adopts a self-assessment requirement for sales by non-registered suppliers to individual consumers, with Australia doing the opposite and choosing not to tax currently such supplies. The EU has adopted a special and very broad registration regime for sales by non-resident suppliers of digital content to non-registered EU customers, while the United States currently maintains a very restrictive physical nexus state registration requirement which makes it very difficult to apply use taxes to cross-border supplies of digital content to individual consumers.

In the international context, as the OECD Draft suggests, a consensus on the categorization of supply and the rules for determining the place of consumption for that supply is essential to ensure fair and adequate, and non-duplicative, taxation. Given the ease with which suppliers can use the Internet to make a product or service available to a customer in another location, some consistency of approach to registration, self-assessment and reverse charging might also have been useful. Given the work of the OECD in this field to date, it is perhaps unfortunate that the tax administrations in the various member states are developing divergent rules that will increase the administrative burdens and costs of a industry that has the potential to work beyond international borders and which has a potential for significant expansion. This divergence may be a reason why the OECD Draft has not been able to progress beyond the draft format. Canada and the CCRA should be encouraged to take a "work in progress" view of their current position, in light of the EU adherence to the OECD Draft, although it might be less inclined to do so until the position of its most significant trading partner, the United States, becomes clearer. Whether this approach is justified when the nature of the consumption taxes in the two countries is so different, is open to question. Whether the lack of comprehensive consensus within OECD member states will have a negative impact on international e-commerce trade remains to be seen.

Notes:

1 OECD, *Consumption Tax Aspects of Electronic Commerce: A Report from Working Party No. 9 on Consumption Taxes to the Committee on Fiscal Affairs (February 2001), online: OECD http://www.oecd.org/pdf/M00022000/M00022378.pdf [OECD Draft].*

2 OECD, Committee on Fiscal Affairs, *Electronic Commerce: Taxation Framework Conditions (1998), online: OECD http://www.oecd.org/pdf/M000015000/M00015517.pdf [Taxation Framework Conditions].*

3 CCRA, *GST/HST and Electronic Commerce, A discussion paper for public comment on the administration of the Goods and Services Tax/Harmonized Sales Tax in an electronic commerce environment (Excise and GST/HST Rulings, Policy and Legislation) (2001) [GST Discussion Paper].*

4 CCRA, Technical Information Bulletin B-090, "GST/HST and Electronic *Commerce" (July 2002), online: CCRA http://www.ccra-adrc.gc.ca/E/pub/gm/b-090/b-090-e.pdf [GST Bulletin].*

5 Charles E. McClure, Jr., outlines these three categories of e-commerce in "Taxation of Electronic Commerce: Economic Objectives, Technological *Constraints, and Tax Laws" (1997) 52 Tax Law Rev. 269 at 298, after adopting the more general definition as set out by Professor Abrams and Doernberg in "How Electronic Commerce Works" (1997), 13 St. Tax Notes 123 at 136.*

6 GST Bulletin, *supra note 4 at 2.*

7 Michael P. Boyle, John M. Peterson, Jr., *et al., "The Emerging International Tax Environment for Electronic Commerce" (1999) 28 Tax Mgt. Int'l. J. 357 at 365-66.*

8 *Excise Tax Act, R.S.C. 1985, c. E-13, s. 165(1) (Division II of Part IX) (Justice Canada).*

9 *Ibid., s. 212 (Division III of Part IX).*

10 Under s. 148(1), *supra note 8, a small supplier is generally one with annual taxable supplies of less than CDN$30,000.*

11 *Supra note 8, s. 240(1). There is an additional exclusion in respect of certain sales of real estate which is not relevant to the example given in respect of a cross-border sale of goods.*

12 Under s. 132(2), *supra note 8, the non-resident is then deemed to be resident in respect of the activities of that person carried on through the permanent establishment.*

13 *Supra note 8, s. 240(3).*

14 GST Discussion Paper, *supra note 3 at 3.*

15 Taxation Framework Conditions, *supra note 2 at 4.*

16 In fact, s. 142(1)(*a) of the Excise Tax Act, supra note 8, deems a supply to be made in Canada in the case of a sale of a tangible good delivered or made available in Canada to a recipient.*

17 OECD Draft, *supra note 1 at 12, para. 30.*

18 *Supra note 1 at paras. 25-26.*

19 The general deeming rules are set out in s. 142(1)(*c) of the Excise Tax Act, supra note 8.*

20 GST Bulletin, *supra note 4 at 16-17.*

[21] *Supra* note 8, s. 142(2)(c).

[22] *Supra* note 8, s. 142(1)(g). Again, the corollary is true — a service performed wholly outside Canada is deemed by s. 142(2)(g) to be a supply made outside of Canada.

[23] GST Bulletin, *supra* note 4 at 17-18. It should be noted that in Canada, a federal state, one need also consider the application of provincial sales tax regimes in the context of the issues addressed herein. Three provinces, Nova Scotia, New Brunswick and Newfoundland, operate the Harmonized Sales Tax under the federal GST legislation, and so the rules discussed here will apply to those provinces. The GST Bulletin also outlines the CCRA's approach to the determination of which province to assign HST revenue, but this part of the Bulletin goes beyond the scope of this article. In other provinces, the relevant local regime would need to be considered by non-resident suppliers in order to determine whether provincial registrations are required, whether the sales into those provinces are taxable, and when tax becomes payable.

[24] *Supra* note 8, s. 10 (Part V of Schedule VI).

[25] GST Bulletin, *supra* note 4 at 25.

[26] *Supra* note 8, s. 7 (Part V of Schedule VI).

[27] These exclusions are listed in s. 7, *supra* note 8.

[28] While listed as excluded from zero-rating under s. 7 *supra* note 8, s. 23 of Part V of Schedule VI restores the ability to zero-rate in respect of certain such services.

[29] GST Bulletin, *supra* note 4 at 26-27.

[30] See Alan Wilson, "The Application of the Goods and Services Tax to International Transactions" (1991), *Canadian Tax Foundation Conference Report* at 43:2.

[31] *Supra* note 8, s. 132.

[32] *Supra* note 8, s. 132(2).

[33] *Supra* note 8, s. 132(3).

[34] The guidelines are set forth in Annex I to the OECD Draft, *supra* note 1.

[35] OECD Draft, *supra* note 1. This guideline is qualified by a suggestion that where its application would lead to a distortion of competition or avoidance of tax, such as in the context of a reverse charge or self-assessment mechanism, different criterion could be used to determine the place of consumption.

[36] See the report of this agreement in (2002) 36 Tax News Service 153 (IBFD).

[37] The amendment to the Directive is found in EC, Council Directive 2002/38/EC of May 7, 2002 amending and amending temporarily Directive 77/388/EEC as regards the value-added tax arrangements applicable to radio and television broadcasting services and certain electronically supplied services, [2002] O.J.L. 128/41, online: European Union Online http://europa.eu.int/eur-lex/en/dat/2002/l_128/l_12820020515en00410044.pdf [EC Council Directive 2002/38/EC of 7 May 2002].

[38] For a review of the EU position and a discussion of a prior version of the proposed amendment to the Directive, see Peter Jenkins, "The Application of VAT to E-commerce in the EU" (2001), 22 Tax Notes Int'l 427.

[39] EC Council Directive 2002/38/EC of May 7, 2002, *supra* note 37, Art. 1(b).

[40] A majority of members on the Advisory Commission on Electronic Commerce, in U.S., *Report to Congress* (Washington, D.C.: The Advisory Commission, 2000), online: ECommerce Commission http://www.ecommercecommission.org/acec_report.pdf [Report to Congress], recognized the OECD's leadership role in co-ordinating international dialogue concerning the taxation of e-commerce, affirmed support for the OECD framework conditions for the taxation of e-commerce, and supported the OECD's continued role for furthering effective international discussion on the issues. As noted by David Hardesty, "Streamlined Sales and Use Tax Agreement — Part 3", *infra* note 79, the new Streamlined Agreement contains some rules to assign use to a state in which the sale is not sourced, but they largely deal with purchases by centralized buying offices for businesses which ship goods elsewhere for use by the business, and not with consumer situations. He also notes, *infra* note 79 at 4, that the source rule in the Agreement to the effect that "services are sourced where they are provided" begs the key questions when it comes to place of consumption or source of a sale of digital services.

[41] *A New Tax System (Goods and Services Tax) Act, 1999*, (Cth), ss. 9–25(5), 84-5, online: Australian Taxation Office http://www.ato.gov.au. While Australia has yet to issue a comprehensive statement of policy comparable to the GST Bulletin, it has issued a number of specific rulings to confirm the discussion above, including ATO ID 2001/578, dated 4 May 2001 (GST and the subscription for Internet information services acquired from abroad); ATO ID 2001/413, dated August 25, 2001 (GST and software downloaded from the Internet (recipient not registered nor required to be registered for GST); and ATO ID 2001/574, dated October 12, 2001 (GST and the acquisition of an IT industry domain name from a non-resident overseas supplier by a resident GST registered Australian entity), all of which are available through the ATO site noted.

[42] Austl., Commonwealth, Australian Taxation Office, Tax and the Internet Second Report — December 1999, paras. 7.3.12, 7.3.13 and 7.4.17, online: Australian Taxation Office http://www.ato.gov.au/content.asp?doc=/content/businesses/ecommerce_tati2.htm; ATO ID 2001/463, *ibid.*

[43] See ATO ID 2001/573 (GST and supply of software products to a non-resident recipients [*sic*] outside Australia), dated October 12, 2000 and available through the Australian Taxation Office site, *supra* note 41.

[44] Peter Jenkins, "The Application of VAT to E-commerce in the EU", *supra* note 38 at 427.

[45] OECD Draft, *supra* note 1 at para. 11.

[46] *Supra* note 1 at para. 47.

[47] *Supra* note 1 at paras. 57, 60.

[48] *Excise Tax Act*, *supra* note 8, s. 132(2).

[49] *Supra* note 8, s. 123(1).

[50] See, for example, the definition of "permanent establishment"contained in Article 5(1) of the OECD, *Model Tax Convention on Income and Capital* (Paris OECD) (looseleaf) [OECD Model Treaty].

[51] See OECD, *Clarification on the Application of the Permanent Establishment Definition in E-Commerce: Changes to the Commentary on the Model Tax Convention on Article 5* (Paris: OECD, 2000), the recommendations of which were then incorporated into OECD, *Draft Contents of the 2002 Update to the Model Tax Convention* issued by the OECD (2001).

[52] GST Bulletin, *supra* note 4 at 28.

[53] *Excise Tax Act*, *supra* note 8, s. 240(1).

[54] *Supra* note 8, s. 123(1) definition of "commercial activity". It is true that commercial activity is also defined to include an adventure or concern in the nature of trade, which could result in any single activity of a commercial or business enterprise being viewed as sufficient to trigger registration, but this is clearly inconsistent with the CCRA statements in the GST Bulletin below which suggests that activity through the permanent establishment must be an essential and significant part of the activity of the enterprise as a whole before the CCRA views registration as being required.

[55] Under Article 5(1) of the OECD Model Treaty, *supra* note 50, in order to constitute a permanent establishment for income tax purposes, a non-resident must maintain: (1) a place of business; (2) that place must be fixed; and (3) the business of the enterprise must be carried on through that fixed place of business. The author explored these issues in the leased equipment context in "Leased Equipment: When Does a Permanent Establishment Exist?" (2002) 50 C.T.J. 489.

[56] GST Bulletin, *supra* note 4 at 28.

[57] It should be noted that under s. 143(1) of the *Excise Tax Act*, *supra* note 8, the non-resident with a permanent establishment in Canada loses the ability to argue that a supply of personal property or a service is made outside of Canada under that section, as the s. 143(1) deeming provision, which would deem a supply made by a non-resident to be one made outside of Canada, is only applicable to non-residents, and under s. 132(2), that non-resident is deemed to be resident simply by having a permanent establishment here, at least in respect of the "activities" of the non-resident carried on through that establishment.

[58] A non-resident carrying on a business in Canada and which is required to register is required, in the absence of a permanent establishment in Canada, to post security for the payment of tax due. See *Excise Tax Act*, *supra* note 8, s. 240(6).

[59] This issue was raised by Jim Vincze and Randy Schwartz in "Canada Keeps Apace with E-Commerce Taxation" (2000), 21 Tax Notes Int'l 767 at 769, where they note that the Department of Finance had indicated that it would look to new consumer self-assessment procedures and incentives to non-residents to register as potential solutions to the problem.

[60] *Cutlers Guild Ltd. v. The Queen*, [1981] DTC 5093 (F.C.T.D.); *GLS Leasco Inc. et al. v. M.N.R.*, [1986] DTC 1484 (T.C.C.); *J. Rutenberg v. M.N.R.*, [1979] C.T.C. 459 (F.C.A.).

[61] See the Exchequer Court decision in *Tara Exploration and Development Co. Ltd. v. M.N.R., [1961] DTC 6370.*

[62] GST Bulletin, *supra note 4 at 30.*

[63] Canada's position in this regard is consistent with the OECD Draft, *supra note 1. In para. 6 of Part B of Annex 1 to the Draft, the Working Party* notes that "Member countries may also wish to consider dispensing with the requirement to self-assess or reverse charge the tax in circumstances where the customer would be entitled to fully recover it through deduc*tion or input tax credit". It should be noted that other than in Quebec, Nova Scotia, New Brunswick and Newfoundland, registered businesses may need to self-assess for such inputs under the provincial consumption tax regimes. See Jim Vincze and Randy Schwartz in "Canada Keeps Apace with E-Commerce Taxation", supra note 59 at 771.*

[64] GST Bulletin, *supra note 4 at 29.*

[65] This system is imposed under Division IV of the *Excise Tax Act, supra note 8, and is outlined by the CCRA in their publication CCRA, "G300-9 Imported Services and Intangible Property (GST300-9)", online: CCRA http://www.ccra-adrc.gc.ca/E/pub/gm/g300-9/g300-9-e.htm.*

[66] *Supra note 63.*

[67] OECD Draft, *supra note 1 at paras. 43-44.*

[68] The OECD Draft, *supra note 1 at 55, notes that B2C online trade is very much in its infancy, with the Technology TAG suggesting compliance* costs needs to be critically assessed in relation to expected revenue yield. Many commentators have noted that the real, substantive traffic is in B2B transactions. See, for example, Michael P. Boyle, John M. Peterson, Jr., *et al. "The Emerging International Tax Environment for Electronic Commerce", supra note 7 at 358, where the authors note: "The online delivery of digital products to consumers, which is expected to present the most difficult compliance challenges for tax authorities, fortunately represents* only a tiny fraction of expected e-commerce revenue and is expected to grow at a slower pace than business-to-business transactions". Later (at *367), they add "… although e-commerce is clearly of growing significance, it will still represent only a small fraction of U.S. and global gross domestic product, and only a small fraction of that represents cross border transactions".*

[69] Australian Taxation Office, *Tax and the Internet Second Report — December 1999, supra note 42; ATO ID 2001/463, supra note 42.*

[70] *Supra note 36. The same rules apply to a B2B supply from an EU supplier to a customer in a different EU state.*

[71] This verification regime is the subject of a second EU Council initiative, *EC Council Regulation No. 792/2002 of May 7, 2002 amending temporarily Regulation (EEC) No. 218/92 on administrative cooperation in the field of indirect taxation (VAT) as regards additional measures regarding electronic commerce, O.L.J. 128/1, online: European Union Online http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/l_128/l_12820020515en* 00010003.pdf.

[72] EC Council Directive 2002/38/EC of May 7, 2002, *supra note 37. By contrast, a digital supply by a supplier registered for VAT in one EU-member state to a non-registered customer in another EU-registered state is treated as supplied in the state of the supplier and is subject to the VAT rates applied in the supplying state (see Jenkins, supra note 38.)*

[73] The OECD Draft, *supra note 1, discusses the threshold issue in paras. 45–49, and references the concept in its recommended approaches to collection issues in para. 9 of Part B of Annex 1. However, it also notes in para. 82 that this is an area where further work is appropriate.*

[74] See the report of the original proposals in (2000) 34 Tax News Service *279 (IBFD). However, under the final regime, the non-EU supplier need only register with one EU member state, even if it makes sales to customers in a number of EU states, and there is a simplified and electronic registration and filing system required. On the negative side, the non-EU supplier must charge varying rates of VAT, depending on the rate of VAT applied in the state of the customer, a somewhat burdensome administrative requirement.*

[75] McClure, *supra note 5 at 369.*

[76] In the United States, as value-added systems are not the norm, the issue of reverse charging does not surface and no serious attempt has been made to apply a self-assessment requirement in any context.

[77] See the Advisory Commission on Electronic Commerce, *Report to Congress, supra note 40, section II A.*

[78] In 1998, the United States Congress adopted *The Internet Tax Freedom Act, Title XI of Pub.L. No. 105-277, imposing an initial three year moratorium (and now extended to November 1, 2003) on any new state and sub-state taxes on Internet access, or any new multiple or discriminatory taxes on electronic commerce. The moratorium did not apply to state or local taxes previously valid under the U.S. Constitution or federal law. The authors of the original Act are attempting to make the moratorium permanent (see online: U.S. Rep. Cox http://cox.house.gov/html/release.cfm?id=597). If the Streamlined Sales Tax initiative becomes operative prior to November 1, 2003 or during any further extension of the moratorium period, a court challenge might be made based on whether the Streamlined proposals exceed the carve-out in respect of previously permitted state or local taxes.*

[79] The common platform is found in the Streamlined Sales & Use Tax Agreement, November 12, 2002, online: Streamlined Sales Tax Project http://www.geocities.com/streamlined2000 and is discussed in a number *of articles by David Hardesty, "Streamlined Sales and Use Tax Agreement", online: E-Commerce Tax News http://www.ecommercetax.com/index.htm.*

[80] David Hardesty, "Streamlined Sales and Use Tax Agreement — Part 2", online: http://www.ecommercetax.com/doc/122202.htm.

[81] The Advisory Commission on Electronic Commerce, in its *Report to Congress, supra note 40, made a majority proposal in section II, suggesting a Congressional need to clarify that certain factors (such as the use of an ISP, the placing of digital data on a server, etc.) would not establish sufficient nexus for this purpose.*

[82] The second core element of the Taxation Framework Conditions, as set *out in the OECD Draft, supra note 1, states that "For the purpose of consumption taxes, the supply of digitized products should not be treated as a supply of goods".*

[83] GST Bulletin, *supra note 4 at 4.*

[84] *Supra note 4 at 4. It should be noted that for supplies made into a non-harmonized (HST) province, the relevant provincial sales tax regimes may categorize the same transaction in a different way.*

[85] The OECD has addressed the issue in the context of categorization of e-commerce activity as either business profits, royalties or technical fees from the point of view of income tax treatment under international tax *treaties. See OECD, Tax Treaty Characterisation Issues Arising from E-Commerce: Report to Working Party No. 1 of the OECD Committee on Fiscal Affairs (February 1, 2001), online: OECD http://www.oecd.org/pdf/M000015000/M00015536.pdf. This does not have a direct overlap in the consumption tax field and therefore is not addressed here.*

[86] Annex to EC Council Directive 2002/38/EC, *supra note 37.*

[87] See ATO ID 2001/578, *supra note 41 and ATO ID 2001/573, supra note 43.*

[88] *Report to Congress, supra note 40, section II. Many tax telecommunications services but that discussion is outside the scope of this article.*

[89] *Supra note 79, Appendix C.*

[90] *Supra note 2, as reported in the OECD Draft, supra note 1 at para. 5.*