Pre-Budget Submission for Budget 2019

RCC appreciates the opportunity to provide comment to Canada's budgetary process for 2019. We are thankful for the forum that the Finance Committee allows for discussion of major public policy issues. Last year, RCC focused on the then-pending taxation of employee discounts. Observations made at and by the Committee were undoubtedly influential in the Government's decision to not tax those discounts. We are hopeful that our advocacy this year will be as successful.

Credit Card Interchange

This being the year of trade issues, most of our comments and recommendations fall within that sphere. The exception relates to costs faced by retailers for accepting credit card payments, specifically "interchange", the fee paid to a cardholder's bank whenever a credit card is used. Interchange costs $7 billion annually, borne first by retailers but ultimately, by all Canadian consumers. In effect, we have a reverse-Robin Hood situation, in which interchange charged for high-fee cards is then paid by all Canadian consumers, including grocery purchases by modest-income Canadians who do not themselves qualify for a credit card or a premium card because of income level.

At an *average* rate of 1.5%, interchange in Canada is among the highest in the world. By comparison, rates in Australia are capped at 0.88%, France at 0.28% and the rest of the European Union at 0.3%. Rates have also been capped in jurisdictions like Switzerland (0.5%), Israel (0.7%, headed for 0.5%) and China (0.45%). Globally, the same card networks operate at a fraction of the cost imposed on Canadians. Several commentators, including the Australian Productivity Commission and Mexican President-Elect Obrador recently proposed eliminating interchange altogether as an unnecessary and damaging part of the payments system.

The problem with interchange was highlighted by the Competition Bureau and Tribunal and by Private Members' Bills in the Senate and the House of Commons, most recently Mme. Lapointe's Bill C-236. In September 2016, the Finance Minister committed to reviewing the card payments market, including interchange fees. RCC is appreciative of the significant effort being put into this review but with interchange costing Canadian consumers $600 million each month, we hope for a speedy conclusion to the process.

Canada needs to echo the pro-consumer and pro-business approach taken by other countries and introduce a meaningfully lower interchange cap or average, whether through regulation or purposeful negotiations with the credit card networks.

TRADE ISSUES

De Minimis Rate

The U.S. has been pressing Canada to increase our de minimis threshold (DMT) to US$800, an outcome that would have catastrophic consequences for retailers in Canada and our over two million employees. DMT is the level below which goods shipped into Canada by post or courier are exempt from sales taxes and customs duties. PwC conducted the definitive study on this issue, concluding that even at US$200 DMT, Canada would lose 286,000 jobs and $11.5 billion in GDP. The reason is that merchants in Canada would pay the duties and collect the sales taxes from their customers, while foreign parcel shippers would be exempt from both. The resulting price differential would incentivize Canadians to shop from literally anywhere else but Canada.

There would additionally be obvious incentives to locate new investments *outside* Canada in order to gain a tax and/or duty advantage when servicing demand for online purchases.

Canada's retailers are frustrated by the unspoken U.S. rationale for increasing DMT. The U.S. already enjoys a preference for its own goods, which enter Canada duty-free. Instead, and though never articulated as such, the U.S. push could be characterized as "We will import goods from Asia via the Port of Long Beach, ship them with a tax and duty advantage into Canada and seize much of the retail market for goods currently subject to duty when landed in Vancouver and to sales tax in the final transaction".

Members may be familiar with recent moves elsewhere in the World to address these very inequities. Probably the best-known example is Australia which last monthreduced its DMT from AU$1000 to AUS$0.

Australia could have returned to its former DMT of AU$200 but in the face of rapid growth in tax-incentivized offshore online sales, chose to set up an equitable GST system from the first dollar. Australia understands that a greater or lesser DMT level on individual shipments is not the issue, it is the impact overall that matters. We agree. The problem facing Canada's retailers is not the DMT on $200 or $800 shipments, it is the impact on $50 and $100 sales, repeated over the hundreds of millions of transactions that make up the bulk of retail purchases. It is only when one understands the values of a typical retail basket size and the effect in aggregate that the risk of harm comes into focus.

Notwithstanding that the European Union has a €22 DMT on VAT, a level comparable to Canada's DMT, the European Commission decided in December 2017 to lower DMT for VAT to €0. The Commission found that even a DMT of €22 leads to unfair competition and distortion for EU companies and that "EU businesses are put at a clear disadvantage since unlike the non-

EU businesses they are liable to apply VAT from the first eurocent sold" (see: http://europa.eu/rapid/press-release_MEMO-16-3746_en.htm).

In June, the U.S. Supreme Court gave its decision in the *Wayfair* case. This ruling means that interstate online purchases will be subject to the same state and local taxes as are charged on sales made by retailers operating within a state. SCOTUS criticized the notion of discriminatory tax treatment depending on the location of the seller: "By giving some online retailers an arbitrary advantage over their competitors who collect state sales taxes, the [former] physical presence rule has limited States' ability to seek long-term prosperity and has prevented market participants from competing on an even playing field."

Here in Canada, we have recently seen a push to eliminate inequitable sales tax treatment of electronic goods like online movie services, music streaming and the like. Quebec in its 2018 budget has also moved to eliminate discrimination in the collection of QST as between goods sold *in* Quebec and those sold *into* Quebec.

As Government deliberates on the DMT, RCC suggests that viewing the current $20 DMT as being somehow too low a value is to look at the issue from the wrong end of the telescope. The real question is why there should be any inequity at all between Canada's merchants and foreign online vendors. Canadian retailers are not pressing to eliminate the $20 DMT. What we are saying is that the current $20 is a vestige of a pre-internet, catalogue-sales era and that the context has fundamentally shifted with online sales in much larger volumes. We have yet to hear a decent argument as to why the DMT should be increased upward, other than to feather the nest of U.S.-based online vendors at the cost of Canadian retailers, employees, lower investment and reduced revenues for federal and provincial governments.

Interrelationship between Retaliatory Tariffs and MFN Tariffs

RCC supports Canada's retaliation against U.S. tariffs on Canadian steel and aluminum, notwithstanding that these retaliatory tariffs fall on $10 billion worth of goods sold by retailers. One weakness in the Government's position, however, is that it continues to levy MFN tariffs on substitutable goods emanating from non-U.S. sources. Major appliances are a good example. None are manufactured in Canada, so customers turning away from U.S.-made goods have limited alternatives and it turns out that substitutes from China are subject to an MFN tariff of 8.0%. Bedding (14% MFN) and upholstered furniture (9.5% MFN) face similar problems. While some supply is available from Canada, the scale and price required by many retailers make China the most plausible alternative source of supply.

The Government's intention is not to have Canadian consumers pay higher prices for U.S. goods. If consumers end up doing so, then the retaliatory tariffs will fail in their purpose of bringing political pressure to bear in the U.S. But if the price delta between U.S. goods and their non-U.S. substitutes is kept narrow by the existence of MFN tariffs on the same items from other sources, there is less incentive for Canadians to switch.

RCC believes that the Government will better achieve its purpose by eliminating MFN tariffs on the goods subject to retaliatory tariffs for as long as those are in place. By so doing, the government will alleviate the cost impact on Canadian families and, by making them more likely to switch away from U.S. goods, will help bring political pressure to bear in the U.S.

Visitors Sales Tax Rebate

Until 2007, Canada offered visitors a GST/HST rebate on products bought in Canada. Since then, there has been only a limited rebate for certain types of tour packages. Canada is almost unique among countries with a value-added tax (VAT) in not providing a visitors' rebate. Australia, Japan, the UK and the entire European Union do so, as do countries like India and China. These rebates make sense. Notwithstanding that the goods are purchased in Canada, they are exported as soon as the visitor returns to their country of residence. All other Canadian exports are relieved of GST/HST, so not only is Canada anomalous among VAT countries by not offering a rebate, goods purchased by visitors are unique in being the only Canadian exports subject to the sales tax.

The reality for Canadian merchants is that their sales are lower than they would otherwise be, as tourists and business visitors face taxes that they would not face when purchasing the same items in other VAT countries. Especially for higher-priced goods, the existence of an unavoidable sales tax may serve to dissuade prospective visitors from coming to Canada at all, with inevitable consequences for the Canadian retail and tourism industries, for employment in those sectors, and for Canadian manufacturers whose goods might otherwise have been purchased.

RCC proposes that the Government's should reinstate a visitors' rebate program for GST/HST, subject to appropriate controls, on which the large number of other VAT countries can serve as models.

Regulatory Cooperation

Canada is dedicated to regulatory cooperation under initiatives such as the Regulatory Cooperation Council and the Regulatory Red Tape Reduction initiative, a commitment which was reiterated in Budget 2018 and reconfirmed by the President of the Treasury Board on June 5, 2018. RCC and its members are strongly supportive of this direction, both in terms of alignment and in establishing world-class requirements. Joint requirements allow for greater product availability and lower prices for Canadian consumers. Current Government of Canada commitments allow for a high degree of discretion within regulatory departments. While they have done little to lower existing regulatory misalignments (e.g., child car seats) entirely new ones continue to be created (e.g., corded window coverings).

RCC asks that Budget 2019 further Canada's commitment to regulatory reform and regulatory alignment by including a clear commitment for Canadian regulatory departments to work collaboratively with major trading partners including the United States to create joint regulatory *requirements as a matter of course, except in exceptional and clearly-defined circumstances (e.g. official language labelling or differences in climate).*

About Retail Council of Canada

Retail is Canada's largest employer with over 2.1 million Canadians working in our industry. The sector annually generates over $76 billion in wages and employee benefits. Core retail sales (excluding vehicles and gasoline) were $369 billion in 2017. RCC members represent more than two-thirds of core retail sales in the country. RCC is a not-for-profit industry-funded association that represents small, medium and large retail businesses in every community across the country. As the Voice of Retail™ in Canada, we proudly represent more than 45,000 storefronts in all retail formats, including department, grocery, specialty, discount, independent retailers and online merchants.

RCC grocery members represent over 95% of the market in Canada. They provide essential services and are an important source of employment in large and small communities across the country. They have strong private label programs and sell products in every food category.