

Alas! In E-Commerce Taxland

By J. Stephen Pope

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In trying to comply with tax laws for your e-business, you may find yourself falling down the rabbit-hole, going through the looking glass, and attending a Mad Tea-Party.

Common sense, logic, and fairness never did apply fully to the field of taxation but this is especially true of e-commerce transactions.

1. Canada Customs Welcomes You to Canada!

Since I`m located in Canada, let`s start here.

Canada has what you might call a national sales tax or a value added tax (VAT). This Goods and Services Tax (G.S.T.) of seven percent is applicable to many Canadian transactions.

Not only is it critical to determine whether a taxable sale was made in Canada or not, but also where in Canada. If it was made (or deemed to be made) in any of the Harmonized Sales Tax (H.S.T.) provinces (Nova Scotia, New Brunswick, and Newfoundland and Labrador), a higher, fifteen percent H.S.T. rate applies. This is because those provinces have allowed Canada to collect their provincial sales taxes for them.

As well, each province and territory has its own rules. Ontario charges eight percent retail sales tax on many typical Internet transactions whereas Alberta

has no provincial sales tax.

Of course, this is only scratching the surface. This entire article is an over-simplification of a very complex subject. You will definitely need professional advice to help you through E-Commerce Taxland.

2. When Exports Aren't Exports

In Canada, exports are "zero-rated" sales for G.S.T. purposes. This means that when you ship a product to someone outside Canada, you don't charge G.S.T. Yet, you get to claim (or deduct from the G.S.T. collected by you) all the "input tax credits" (G.S.T. that you paid for business purposes) to make that export. The idea, I suppose, is to encourage exporting.

However, if you export products other than tangible, physical goods, beware! There are many pitfalls to watch out for.

As one example, consider digitized products that you might sell from your Canadian website, such as e-books, downloadable software, or subscriptions to content. You would be considered to be selling "intangible personal property". Unless your product is also considered "intellectual property" (such as software or e-books that you produced or have obtained the rights for), you will have to charge G.S.T. The reason why, according to the Canada Customs and Revenue Agency, is that it COULD be used inside Canada, even if it isn't.

Say you sold a membership for accessing digitized content (from various sources) on your Canadian website to a customer in the United States. Since there are no restrictions as to where the intangible personal property may be used, and the property is not considered intellectual property (nor the provision of a service), the American customer is subject to G.S.T., even if he never comes to Canada.

Strangely, the same logic doesn't apply when an American buys a regular book (or a car) which he COULD bring into Canada with him and use here. It is true that it is easier for Canada to assess such items at the border than in cyberspace, but I know of no cases of Americans being taxed on the books or cars they bring with them when they

come to live in Canada for about half the year.

As a Canadian registrant, one way you might legally avoid this silly March Hare is to explicitly state on your website and invoice that use of such intangible personal property in Canada is prohibited (or requires an additional fee and the payment of G.S.T.).

3. When Imports Aren't Imports

Goods shipped to Canada are subject to G.S.T. on importation. Such tax is often assessed at the border. But what if you are a Canadian registered for G.S.T., selling to a Canadian customer but your supplier is in a foreign country?

Pretend that your Canadian customer has bought a book from you from your Canadian website. Your drop ship supplier is located in the United States and is registered for G.S.T. You fax your order to the American company, and they, in turn, ship the book for you (complete with Customs Declaration and their G.S.T. Business Number).

Since they paid the G.S.T., you wouldn't think you would have to charge it again, would you? "Wrong!", smiles the Cheshire cat. Since you are a registrant located in Canada, you are required to charge and remit the G.S.T.

But you are entitled to input tax credits, aren't you? In many cases, the answer is "No".

It may be very difficult for you to satisfy the documentary and other technical requirements. As an example, it is not uncommon for American suppliers to absolutely refuse to give an invoice breaking down the G.S.T. or to allow you to be the Importer of Record. This complicates their life unnecessarily and they just don't need the aggravation.

There are relieving tax provisions covering drop shipping, sales agencies, and other situations. In many cases, unfortunately, the most practical solution is to allow the tax to be paid twice.

4. When You're Subject to Tax Where You're Not Subject to Tax

It makes sense that countries impose a tax on sales and income made in their own jurisdiction. But does it make sense for Germany to tax sales made in the United States?

In effect, starting July 1, 2003, the European Union has done just that by imposing an online sales tax.

This means that if someone from England buys an e-book from someone in the United States, the American should submit this tax. Of course, If the sale was to someone in Germany, the tax rate would be different.

The rationale behind this follows: Since countries can't collect sales tax on Internet transactions at their borders, the only way they can collect it (other than a self-assessment system) is with an online sales tax. Further, it is claimed that businesses in the European Union suffer a major competitive disadvantage because they have to collect Value Added Tax (VAT) but others don't.

I know what they mean. Welcome to the club!

RESOURCE BOX:

J. Stephen Pope, President of Pope Consulting Inc., <http://www.popeconsultinginc.com/> has been helping clients to earn maximum business profits for over twenty years.

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