Intelligence MEMOS

From: Daniel Schwanen

To: The Honourable Chrystia Freeland and Canada's NAFTA negotiators

Date: March 14, 2018

Re: **Maximizing de Minimis in NAFTA**

If NAFTA negotiations succeed for Canada, it will be because Canada will have fended off threats by the US administration to raise barriers to trade between the three NAFTA economies, barriers that would raise costs for industry and raise prices for consumers.

Yet, Canada maintains its own barriers that hurt Canadian consumers and impose unnecessary costs on the broader economy. Logic, as well as concern for the economic well-being of the middle class, suggests that Canada should accept a reduction in these barriers as part of the negotiations.

One such costly barrier is the low de minimis threshold (DMT), currently at $20, below which goods coming into Canada are not subject to customs duties or taxes applied at the border. Canada's threshold is much lower than that of most other advanced economies.

The result of the low DMT is that a wider array of goods purchased by Canadian consumers are delayed at the border, and subject to additional fees and paperwork, than goods available to consumers elsewhere, notably in the United States. At the same time, Canadian authorities spend more valuable resources processing these small packages than they collect in additional revenues from them, as this C.D. Howe Institute study has shown. Canadian consumers already pay higher retail prices than their US counterparts, with a significant part of this gap due to government policies themselves and notably trade barriers, as shown in this report. The low de minimis threshold only adds to these higher costs faced by Canadians.

Canada's retail industry has objected to Canada raising its de minimis threshold, because their customers would have access to more lower-priced goods purchased from elsewhere.

Beyond this general worry about more competition, a major fear of the retail industry is that a higher de minimis would tilt the tax playing field between what they sell and what is imported, because GST on these small shipments might not be collected at the border.

To be clear, while facilitating e-commerce would greatly benefit consumers, I do not suggest that tax authorities should countenance buyers and sellers circumventing sales taxes such as the GST. There should be a level playing field between goods purchased via electronic means originating from abroad, and those originating from Canada.

Indeed, the benefits for Canadians of raising the DMT, documented in the first study mentioned above, arise entirely from lower customs duties – already at zero for a myriad of goods – and in general less paperwork and processing costs at the border. The study does not assume that Canadians will avoid paying the GST on their imported goods.

Canada's retail industry has predicted job losses of some 50,000 for the sector if the DMT rises to $200, even in a scenario where Canadians pay GST on imported goods below the new threshold.

But these estimates assume that individual Canadians can only benefit at the expense of business and retailers will not take steps to become even more competitive – including by stepping up their own booming e-commerce efforts, or by demanding that governments reduce the many regulatory and other barriers that unnecessarily raise costs. They assume, in short, that the interests of Canadian consumers and retailers are less congruent than they really are – both can benefit from much needed competition and lower barriers to doing business.

As Canada berates the United States for potentially imposing border taxes that will add hundreds of dollars per year to families' cost of living, it would do well to look at what it can do to reduce the unnecessary costs Canadian families bear at the border.

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