

# A new tempest this way comes

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Earlier we wrote about a communication by President Trump about the unfairness of the Value Added Tax. Now the U.S. Commerce Secretary has added his [official perspective](#) on the matter. Mr. Lutnick “has warned that Canada’s national sales tax will be subject to retaliation.”

Retaliation is, of course, a curious term. It is not clear how Canada’s non-discriminatory national sales tax is harming the United States, U.S. exports to Canada, or - to pick up on a favourite theme - border security. What is the issue? These are the reported words of the Commerce Secretary of the United States:

“We’re supposed to have a free trade agreement with Canada, but they have a 5 per cent national tax,” Lutnick told Fox News, in an interview following the first cabinet meeting of the Trump administration. “They tax so many different things. It’s outrageous. They basically cheat around the sides, and then when we don’t act, they stop cheating around the sides. They cheat right down the middle. And the President is sick and tired of it.”

It’s difficult to wrap one’s mind around this.

Every client or potential client, every colleague, every student, every family member, has been asking the same question since November 25, when President Trump threatened to impose a 25 per cent tariff on all goods from Canada. And then, on February 1, when the Executive Order was signed. And then, ten days later, when a proclamation was issued re-imposing 25 per cent tariffs on steel and aluminum from Canada. And when new tariffs were threatened on automotive goods and pharmaceuticals. And then again when a new study was commissioned to impose tariffs on copper. The question is a valid one: “We’re supposed to have a free trade agreement.”

“They have a 5 per cent national tax. They tax so many different things. It’s outrageous.”

[All but four U.S. states](#) have local and state sales taxes. So, the idea of a sales tax is not alien to US consumers or policymakers. There is nothing in a national sales tax that would make it outrageous. Sales taxes cover goods and services, which is also normal

at the state and local levels in the U.S. and should not be seen as “outrageous” at the national level.

Variations in tax rates result in consumer and business arbitrage. This could be a good thing, or not such a good thing. The fact that there is a national sales tax limits that sort of arbitrage between Canadian provinces, but of course it has no impact on trade with the United States. At any rate, as indeed we can see in the U.S., different levels of government need to find sources of revenue, and there is nothing in the structure or scope of a sales tax that suggests it should be limited to local or sub-federal authorities. One could even say that the fact that municipalities can have sales taxes in the U.S. is the “outrageous” thing.

“They basically cheat around the sides, and then when we don't act, they stop cheating around the sides.”

Mr. Lutnick is trying to imitate President Trump in this sort of diction; that, as they say, is a choice.

Since 1947, three basic and unchanging principles have applied to fiscal measures of states affecting trade in goods. They are at the very heart of how governments, including, until recently, the United States, design those measures - but also, if there are trade concerns, how we attack them.

- **Article II of the GATT** requires that each Member of the WTO establish a higher limit on its tariffs - and not impose border fiscal measures higher than those negotiated and agreed limits.
- **Article III of the GATT** requires that each Member apply its domestic taxes in a non-discriminatory manner to both domestic goods and imported goods that compete with those domestic goods.
- An interpretive note to Article II further provides that a WTO-consistent - that is, non-discriminatory - domestic tax may be applied at the border, and this would not constitute a border measure.

Each of these is uncontroversial.

Canada’s “national sales tax” is a domestic tax that applies, in Canada, to the sale of goods regardless of origin. It covers most goods and services - and there is nothing “outrageous” about it, either in fiscal policy terms, or indeed in trade terms. There has not been - as there could not have been - a single argument in the long history of the GST, by any of our trading partners, that the GST is in any way discriminatory, because of course it is not.

For imported products, the GST is collected at the border. This is what the GATT has permitted since 1947. There is nothing unfair about it: products sold into Canada pay the same tax as products sold in Canada, regardless of origin. Again, the practice is uncontroversial to the point of banality.

Against this background, it is not entirely clear who is cheating, who is acting, what Canada is supposed to be doing that is against internationally agreed rules, or what the point of the latest outburst is.

Which brings me back to Mr. Lutnick's observation that "we're supposed to have a free trade agreement." That free trade agreement sets out specific obligations in respect of tariffs and taxes. It also has a dispute settlement mechanism to address concerns about measures of trading partners. If Mr. Lutnick is serious about the agreement, surely the only avenue to express those concerns is through the dispute settlement mechanism of the trade agreement that Mr. Trump negotiated, signed, and implemented.

By

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