HOUSE OF COMMONS
CHAMBRE DES COMMUNES
CANADA

House of Commons Standing Committee on Finance – Pre-budget Consultations 2013

This brief is submitted by:

an organization **Organization name:** Tax Executives Institute, Inc.

or

an individual **Name:** ______

Topic:

*Recommendation 1: Replace Regulations 102 and 105 Withholding with Treaty Benefit Self-Certification

As the preeminent association of in-house tax executives worldwide, Tax Executives Institute (TEI) urges the Canadian government to enhance the international competitiveness of Canada's business tax system by abandoning the treaty exemption application and withholding tax waiver systems under Regulations 105 and 102 of the Income Tax Act. We urge replacing the current requirement to apply to Canada Revenue Agency (CRA) for a waiver from withholding tax 30 days in advance of the beginning of work with a treaty benefits self-certification system. The recommendation will substantially improve government efficiency, enhance competitiveness, and reduce red tape.

Expected cost or savings: From the pull-down menus, please indicate the expected cost or savings of your recommendation to the federal government and the period of time to which the expected cost or savings is related.

Pull down menu #1: ≤$499,999
Pull down menu #2: Immediately

Federal funding: Please provide a precise indication of how the federal government could fund your recommendation. For example, indicate what federal spending should be reallocated, what federal tax measure(s) should be introduced, eliminated or changed, etc.

Replacing Regulations 102 and 105 of the Income Tax Act, which govern withholding tax on cross-border services, with a treaty benefits self-certification system is likely to have a minimal tax cost for the federal government. Much of the withheld tax for treaty exempt service providers or employees will be refunded by CRA upon the filing of a return where the services performed by the employee or contractor did not benefit from an advance waiver. Where there is a residual income tax liability, the foregone withholding tax will be offset by a comparable amount of income tax paid by the non-resident taxpayer.

Intended beneficiaries: Please indicate the groups of individuals, the sector(s) and/or the regions that would benefit by implementation of your recommendation.

The recommendation will benefit all Canadian businesses by reducing the cost of obtaining services from treaty-exempt foreign suppliers, minimizing withholding and reporting of refundable taxes, and reducing fees paid to tax advisers for filing returns and claiming refunds of withheld taxes. Well-advised non-resident service providers request indemnification from Canadian service recipients to avoid the economic cost of withholding under Regulation 105. Hence, the withholding tax cost is often borne by a Canadian resident rather than the non-resident. Similarly, Canadian resident employers bear significant withholding and administrative costs for exempt employees under Regulation 102.

General impacts: Depending on the nature of your recommendation, please indicate how the standard of living of Canadians would be improved, jobs would be created, people would be trained, etc.

In its December 2008 report, the government's Advisory Panel on Canada's System of International Taxation found the costs associated with complying with Regulations 105 and 102 are significant; service providers commonly gross-up their fees to offset the withholding tax, resulting in additional costs to Canadian businesses and impairing their ability to engage skilled workers. Finally, the process for obtaining a waiver of withholding tax from CRA is cumbersome. The Panel recommended replacing the advance waiver system with a treaty-benefit self-certification system.

Recommendation 2: Adopt a Corporate Group Loss-Transfer System.

One area where Canada's current business tax system is out of alignment with other countries is the inability of corporate groups to freely transfer losses among group members. To be competitive with other countries' tax systems, Canada should create a tax-loss utilization system for corporate groups. Specifically, the government should adopt an annually elective tax loss- (or attribute-) transfer system similar to that used in the United Kingdom. TEI's recommendation will enhance the Canadian tax system's competitiveness, fostering greater economic growth and employment for Canadians.

Expected cost or savings: From the pull-down menus, please indicate the expected cost or savings of your recommendation to the federal government and the period of time to which the expected cost or savings is related.

Pulldown menu #1: ≤$499,999

Pulldown menu #2: Immediately

Federal funding: Please provide a precise indication of how the federal government could fund your recommendation. For example, indicate what federal spending should be reallocated, what federal tax measure(s) should be introduced, eliminated or changed, etc.

Canadian corporate groups can structure transactions today or make use of CRA's administrative concessions to transfer a tax loss to a profitable group member. Hence, we do not believe there is a current tax cost to the Federal government for implementing a loss transfer system. Although the tax cost at the provincial level is unknown, we do not believe it is as significant as the Provinces believe it to be. TEI's recommendation will also improve government efficiency by affording CRA the ability to re-direct its rulings resources to other tax matters.

Intended beneficiaries: Please indicate the groups of individuals, the sector(s) and/or the regions that would benefit by implementation of your recommendation.

The principal beneficiaries of the recommendation are businesses operating through multiple corporate entities, which tend to be larger. Tax planning techniques afforded by CRA's policy of administrative concessions for loss transfers require corporate groups to incur significant administrative costs and delay utilization of the loss. Moreover, regulatory or business constraints prevent some groups from structuring a tax loss transfer or making use of the administrative concessions thereby resulting in a permanent inability to utilize the loss.

General impacts: Depending on the nature of your recommendation, please indicate how the standard of living of Canadians would be improved, jobs would be created, people would be trained, etc.

Companies frequently establish multiple entities within a corporate group in order to manage their business more efficiently. A loss-transfer system helps to minimize the tax inefficiency of multi-entity corporate structures by permitting the expenses and net losses of one or more entities within the group to offset the taxable profits of other members of a group. Without a loss-transfer system, the group is subject to a higher overall tax burden. A tax-efficient corporate structure should not limit an efficient management structure. With improved cash flows, companies will be able to hire and train more Canadians and conduct more research.

Recommendation 3: Review and Revise the Excise Tax Act; Non-GST Portions

TEI recommends that the government engage in a public consultation process for revising the non-GST sections of the Excise Tax Act, which have become antiquated and no longer reflect their underlying policy goals. Businesses and the government must devote significant resources to comply with the application and administration of these outdated rules. TEI members have significant concerns with the Fuel Tax and the Insurance Premiums Tax where existing definitions, licensing requirements, and exemptions no longer reflect today's marketplace and result in wasteful administrative efforts for both government and industry or in unintended distortion of market or business practices.

Expected cost or savings: From the pull-down menus, please indicate the expected cost or savings of your recommendation to the federal government and the period of time to which the expected cost or savings is related.

Pulldown menu #1: ≤$499,999
Pulldown menu #2: Immediately

Federal funding: Please provide a precise indication of how the federal government could fund your recommendation. For example, indicate what federal spending should be reallocated, what federal tax measure(s) should be introduced, eliminated or changed, etc.

The government currently incurs significant costs administering and enforcing the Fuel Tax, Insurance Premiums Tax, and other non-GST portions of the Excise Tax Act. Modernizing and clarifying these areas would reduce the potential for differing interpretations, improve compliance, and minimize controversy and the time and expense associated with drawn-out appeals and litigation.

Intended beneficiaries: Please indicate the groups of individuals, the sector(s) and/or the regions that would benefit by implementation of your recommendation.

The number of groups, sectors, and regions that would benefit depends on the changes that are ultimately implemented. Some of the taxes, such as Fuel Taxes and Insurance Premiums Taxes, may seem limited and specific to certain sectors, such as refined petroleum products and the insurance industry. But the underlying effects of changes to the Excise Taxes will flow through and benefit customers and clients broadly across all industries and regions of the country and the economy. A streamlined Excise Tax will enhance economic growth and productivity, remove barriers to economic efficiency, and reduce government red tape.

General impacts: Depending on the nature of your recommendation, please indicate how the standard of living of Canadians would be improved, jobs would be created, people would be trained, etc.

Multinational companies often insure their risks globally with a single policy to reduce costs through economies of scale. Where Canadian insurance companies cannot provide adequate coverage, the Excise Tax Act provides an exception to the 10% Insurance Premiums Tax for premiums paid to non-Canadian insurers. The exception, however, is difficult to interpret and administer. Consequently, companies must pay the tax despite a tax policy choice to exempt the premiums. Similar situations arise frequently in the Fuel Tax area where the intent was to tax Motor Fuel used on roads and highways and not to tax fuel consumed in industrial applications.

Please use this page if you wish to provide more explanation about your recommendation(s).

Recommendation #1: Repeal Regulations 105 and 102 and Replace with a Treaty Benefit Self-Certification System

We have set out our concerns in respect of Regulation 105 above in our discussion of Recommendation #1. In respect of Regulation 102, the Advisory Panel on Canada's International Tax System determined that because it applies to such a broad range of situations, it places a significant administrative burden on non-residents as well as Canadian corporations that carry out administrative duties on behalf of related non-resident employers. Thus, the Panel recommended replacing the withholding tax system with a treaty benefit self-certification system similar to that in the United States.

A certification system based on retaining the current information reporting requirements for Regulations 102 and 105 will maintain CRA's enforcement capability, but shift compliance costs to the certifying party, minimize tax withholding refunded to exempt parties, reduce tax gross-up costs to Canadian payers, and minimize administrative burdens for CRA and business taxpayers alike. TEI urges adoption of the Advisory Panel's recommendation to replace the advance treaty benefit waiver system under Regulations 105 and 102 with a treaty benefit self-certification system.

Recommendation #2: Corporate Group Loss Transfer System

The 2013 Budget Message stated that "[t]he examination of the taxation of corporate groups is now complete. The Government has determined that moving to a formal system of corporate group taxation is not a priority at this time."

TEI regrets the government's decision not to move forward at this time. As explained in TEI's comments to the Department of Finance during the Department's consultation on corporate group taxation, implementing an efficient system of group taxation will provide a more competitive tax environment for businesses in Canada, thereby fostering economic growth and generating additional employment. Indeed, more than two thirds of OECD countries — including major Canadian trading partners such as the United States, the United Kingdom, Australia, and Germany — provide some form of group taxation or loss-transfer regime in their legislative or regulatory schemes for business taxation. Canada is the only G7 country that does not have such a feature. We urge the Standing Committee and Department of Finance to implement a corporate loss transfer system.

Recommendation #3: Review and Revise the Excise Tax Act; Non-GST Portions

Many of the non-GST provisions in the Excise Tax Act require updating to achieve the tax policy results they were intended to produce. The Fuel Tax and Insurance Premiums Tax have increasingly strayed from these policy goals, creating undue administrative burdens for both taxpayers and the government. Thoughtful changes to these and other non-GST provisions in the Excise Tax Act would foster a more competitive business environment in Canada. TEI recommends initiating a review and consultation process to revise the non-GST sections of the Excise Tax Act to modernize and clarify the underlying tax policies, provide a logical and consistent legal structure, and resolve ambiguities that result in inefficient and ineffective application and administration.