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Advisory Panel on Canada's System
of International Taxation Submission
333 Laurier Avenue West
15th Floor
Ottawa, Ontario
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Attn: David Messier

Dear Sir,

Advisory Panel on Canada's System of International Taxation

I realize I have missed the date for submissions. However, I was unaware of the request for submissions until recently and decided to make a brief submission in case it might be considered.

There are two issues I submit for consideration at this time.

Regulation 105

Regulation 105 of the Income Tax Act requires Canadian companies to withhold 15% of amounts paid to a non-resident in the form of "*…a fee, commission or other amount in respect of services rendered in Canada…*". The non-resident, if he is not taxable in Canada under a treaty, can reclaim this amount by filing a Canadian tax return.

It is assumed that the intention of this Regulation is to prevent tax leakage. However, the amount of such leakage is unclear and possibly minimal. In fact it also mirrors many provisions brought forward in the Canadian tax system over the years that could act as barriers to cross border commerce and competition, thus fostering inefficiency of Canadian enterprises and imposing costs on consumers over the long term. (The recently surrendered withholding tax regime on interest payments to foreign entities would have fallen into this category.)

There are number of detrimental effects to Regulation 105 that are likely to far outweigh any benefit, some of which are:

- Many service providers simply raise their prices by 15% rather than go through the expense and trouble of hiring a Canadian tax advisor and waiting a considerable time to get back the amount of the withholding. This essentially results in windfall tax revenue and an unintended effective tax burden on Canadian business and thus consumers.
- Reduces the available pool of international talent to Canada – many providers will not do business in Canada to avoid the troubles noted in the point above.
- It imposes an expensive administrative burden on both the payer and the recipient.
- Creates needless bureaucracy and work for the CRA to process tax returns and issue refunds.

Recommendation – for treaty country residents, at minimum institute a similar system to the U.S. where the foreign resident can supply Form W8-BEN to the payor who is entitled to rely on it and not withhold. Preferably eliminate the Regulation 105 withholding requirement entirely in line with the practice of many European countries

<u>CCPC, Foreign Income and low tax rate</u>

CCPC's benefit from a low tax rate on profits up to $400,000 arising from Canadian active business income. The question arises as to why foreign active business income earned by small Canadian businesses is penalized by not being eligible for the low rate. A further question arises as to why the low rate is not available to all small companies, regardless of whether or not they are CCPC''s. Both these situations could result in incorporation elsewhere in many cases and a total loss of potential tax revenue to Canada.

My business is a case in point. Without going into detail, I have formed an international consulting business with 2 Canadian resident partners delivering consulting services internationally. Although our preference would be to transact all business through a CCPC for simplicity and because about 50% of our business is in Canada, all our non-Canadian business is transacted through a UK company owned solely by myself. The United Kingdom also has a small company tax rate but it applies to all small companies regardless of ownership and regardless of the source of the income between domestic or foreign. This means a loss of tax to Canada to the advantage of the U.K for business that we transact in the U.S. and elsewhere. This is not in any way a tax avoidance arrangement as the UK small business rate is actually higher than in Canada. However, channeling this income through the Canadian CCPC would result in very penal effective tax rates for me.

Recommendation – apply the low tax rate currently available to CCPC's to all active business income, both Canadian and foreign and also make it available to all small companies regardless of ownership.

I note that Recommendation 9 in the submission dated July 11, 2008 by The Certified General Accountants Association of Canada covers this point.

I thank you for your possible consideration of these points and would be pleased to discuss them or provide further input at any time.

Yours truly,

Stephen McPhie