SUBMISSION TO THE ADVISORY PANEL

ON CANADA'S SYSTEM OF INTERNATIONAL TAXATION

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By: H. ARNOLD SHERMAN, C.A.

I am a Chartered Accountant, a life member of both the Alberta and Ontario Institutes of Chartered Accountants. I am also a Fellow of the Institute of Chartered Accountants in England & Wales and a Chartered Tax Adviser (UK). I am a member of the International Tax Sub-Committee of the Chartered Institute of Taxation.

I have been involved in international tax planning since 1961. I was actively involved in making representations on behalf of my then employer, Massey-Ferguson Limited, Toronto, following the publication of the Carter Commission Report in 1967, the Benson White Paper and Bill C259, implementing the first stage of Canadian tax reform.

In my capacity as Director, Taxation of Massey-Ferguson Limited, I was extensively involved in discussions and meetings with the Department of Finance, which led to the 1974 relieving changes to the FAPI legislation.

This is not intended to be a technical submission. Rather, it is a request that the Panel consider some of the adverse non-tax consequences of Canada's current tax legislation in respect of outbound foreign investment.

In my experience, the present Canadian tax system has the unfortunate effect of encouraging both Canadian business and resident individuals to leave Canada.

I incorporated my professional practice in Calgary in 1982. During the period ending with the 1994 Federal Budget, I was frequently consulted by Canadian individuals and businesses seeking to minimise their Canadian tax liability. Under the Canadian tax legislation then in force, it was almost always possible to assist clients in such a way that they were comfortable with the results. Consequently, the question of leaving Canada did not arise.

The problem followed the changes to the foreign affiliate rules, which were propounded in the 1994 Federal Budget and in subsequent legislation. These changes successfully closed practically all of the loopholes previously available.

Thereafter, when I told clients that there was little or no possibility of reducing their current Canadian tax burden, the discussion inevitably turned, in the case of individuals, to leaving Canada and in the case of business, to considering whether proposed new ventures should be set up elsewhere. In some cases, even existing Canadian businesses were moved abroad. The (capital gains tax) cost of the move to my client was more than offset by future tax savings.

I am a sole practitioner based in Calgary. My personal experience may not be representative. However, in the last 14 years I have advised countless clients seeking to reduce their Canadian tax burden. Many clients reviewed the possibilities and made the (unfortunate) decision that their future lay elsewhere. Individuals paid, or gave security for, the one-time departure tax and left for more favourable jurisdictions (many for the UK – mentioned below). Some businesses closed and re-incorporated in a different jurisdiction. Others, which were considering either expanding their existing Canadian business or a new venture, decided that these activities would be best carried on outside Canada, in a more favourable environment.

Tax considerations related to the relocation of business to another country are important, but are not the only factor. However, in many cases within my experience, tax was the factor on which the decision turned.

As a tax professional acting in the best interest of my clients, I am satisfied with what I achieved. As a proud Canadian, I am sad to have contributed to such a significant loss to Canada of income-earning assets, business activities and employment.

In the past, there was a well-known theory that national tax systems should provide for a certain amount of tax "leakage". Several reasons were suggested. It tended to limit what today is called aggressive tax planning and to reduce tax evasion. The availability of this "leakage' was often a significant factor in major business and personal decisions.

This theory has long gone. Loophole-closing has been an annual (or even more frequent) world-wide ritual for tax administrations. Canada has been a leader in these activities.

I submit to the Panel that the additional tax revenue collected as a result of loophole-closing is insignificant when compared with the horrendous loss to Canada of talent, assets and business activities since 1994.

Internationally, these are two quite different solutions dealing with this problem.

The first is to maintain appropriate loopholes. A good example was the United Kingdom. The limited taxation of individuals resident in the UK who were not domiciled there resulted in the growth of major industries, such as shipping, insurance and specialised financial activities in the City of London. Many commentators credit the UK personal tax system as a major reason for the growth in importance of the City of London as the primary business centre of Europe. This seems borne out by the effect of the recent adverse changes in UK personal tax legislation, which have resulted in many individuals and businesses relocating to other countries.

To take two more examples, Singapore and Hong Kong have developed as leading international financial centres by taxing their residents only on domestic source income. Foreign source income is generally not subject to tax.

The second solution, being increasingly adopted in the European Union, is to reduce the level of taxation. The best example is the Republic of Ireland, where the corporate tax rate of 12.5% attracted an enormous amount of foreign-owned business to the Republic. The 10% tax rate in Cyprus seems to be having a similar effect.

In the last while, two major UK companies have announced plans to move their operations to the Republic of Ireland. One (United Business Media) indicated that the 12.5% Irish tax rate and Ireland's "less complex tax system" were the reasons for the move. The current UK corporation tax rate is 28%.

The US current 15% tax rate on certain capital gains and dividends is another example.

However, loopholes need to be thought through carefully.

An interesting example of a Canadian loophole, intended to encourage immigration by wealthy individuals, is the five year tax exemption of investment income for new arrivals. While it may have achieved its intent, the law of unintended consequences also applied. Wealthy individuals moved here solely to obtain Canadian citizenship and left permanently before the end of the five year period. The rules should have made it clear that the exemption was intended only for permanent residents. For example, anyone leaving Canada within the ensuing five years could have been subject to a special tax, intended to claw back the earlier tax benefits.

In my view, those responsible for Canada's tax policy have failed to appreciate the harm that has been caused by high tax rates, combined with the closing of loopholes. They consider actual tax revenue, but have no idea of the amount of revenue lost to Canada because individuals have left Canada and businesses are earning their income elsewhere.

I urge the Panel to consider this aspect when making their recommendations.