Échec aux paradis fiscaux is a collective of organizations engaged in public awareness and political action campaigns against tax havens, which erode funding for public institutions and public services.

The collective is made up of the following organizations:

- APTS (Alliance du personnel professionnel et technique de la santé et des services sociaux)
- ATTAC-Québec (Association québécoise pour la Taxation des Transactions financières et pour l’Action Citoyenne)
- CSD (Centrale des syndicats démocratiques)
- CSQ (Centrale des syndicats du Québec)
- FTQ (Fédération des travailleurs et travailleuses du Québec)
- FECQ (Fédération étudiante collégiale du Québec)
- FEUQ (Fédération étudiante universitaire du Québec)
- FIQ (Fédération interprofessionnelle de la santé du Québec)
- SISP (Secrétariat intersyndical des services publics)
- SFPQ (Syndicat de la fonction publique et parapublique du Québec)
- UC (Union des consommateurs)
- Les Amis de la Terre de Québec
- RJFQC (Réseau pour la justice fiscale).

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The Réseau pour la justice fiscale Québec (RJFQC) is a non-profit, independent, non-partisan research organization associated with the international Tax Justice Network. The RJFQC’s aim is to generate discussion on taxation as an essential collective instrument for financing public services and maintaining rigorous social, environmental and economic policies.

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May 2014, Montreal
SUMMARY

Background

There is no justification for framing the debate on taxation and public finances as a false dichotomy between either raising personal income tax and other taxes on individuals, or cutting public services. If governments are doing a poor job of fulfilling their social mission, that’s primarily due to the paltry revenue they’re levying from the most affluent social and economic elites. Generalized use of both legal and illegal tax avoidance schemes by the most powerful forces of capital (major corporations, banks and the ultra wealthy) is now reaching new historic heights. Statistics Canada estimated somewhat conservatively that in 2013, about 170 billion dollars in cash reserves were held in tax havens by multinational corporations. This explains the current context of budget restraint, austerity measures and perpetual cuts in public services.

Another false assertion is that in the international arena, Canada is in an isolated position and would suffer the consequences if it took unilateral action against tax havens. The opposite is true, however. Through a number of its policies, Canada is currently encouraging the use of legal tax havens, and finds itself on the sidelines as its peers in the OECD push for concerted multilateral programs to tackle tax havens. Clearly, Canada can participate in this global movement to stop the erosion of our tax base, and it can do so right now by implementing tangible solutions.

This report proposes a preliminary series of basic recommendations for the federal government, to tackle the problem of generalized tax avoidance. These recommendations should be seen as a first step, to be followed by additional measures to effectively combat the scourge of international tax avoidance.

Recommendation 1

Modify the present voluntary disclosure programs to include strict penalties (which are currently non-existent), based on the US Offshore Voluntary Disclosure Initiative (OVDI) and the Streamlined OVDI Program

Under Canada’s voluntary disclosure programs, taxpayers who’ve failed to declare all the information required by tax laws can disclose that information on a voluntary basis if they meet the required conditions. If Canada Revenue Agency accepts their voluntary disclosure, they only have to pay their previously unpaid taxes plus interest. No penalty is imposed and no criminal procedures are launched. Our procedures should be more like the US programs (OVDI and Streamlined OVDI), with penalties ranging from 0% to 30% of the previously unpaid amount, depending on the circumstances.

Recommendation 2

Take part in multilateral agreements to automatically exchange tax information

Although tax information exchange agreements (TIEA) allow Canadian tax authorities to obtain information on the foreign bank holdings of Canadian citizens when the banks are located in a country that has signed such an agreement with Canada, these agreements prove to be of little use in practice. The foreign banks require such a vast quantity of information on the taxpayer that it undermines the effectiveness of these procedures. Given this situation, we recommend that Canada participate actively in international efforts to develop automatic procedures for exchanging tax information.

Recommendation 3

Eliminate tax benefit provisions in tax information exchange agreements

We recommend that Canada eliminate tax benefits for Canadian corporations operating in countries that have a tax information exchange agreement with it. At present, Canadian companies can use current tax advantages to distribute profits from their active businesses as tax-free dividends, to the benefit of their Canadian parent company. These tax giveaways result in harmful erosion of the Canadian tax base while creating unfair competition for other Canadian companies that are left out.

To rectify the situation, we recommend that the definition of a “designated treaty country” in subsection 5907 (11) of the federal Income Tax Regulations be modified to include only countries and jurisdictions that have entered into a comprehensive agreement or convention with Canada for the elimination of double taxation on income, and exclude those that have entered into a comprehensive tax information exchange agreement with Canada. This change would considerably limit the tax optimization options that the Canadian government now offers when signing the current tax information exchange agreements.
Recommendation 4
Revise some of our tax treaties

We recommend that Canada revise its comprehensive double taxation treaties that are signed with countries where very low rates of personal and corporate income tax are levied on certain types of income and certain types of companies.

Recommendation 5
Modify the definition of a “designated treaty country” in subsection 5907 (11) of the federal Income Tax Regulations

We recommend that certain types of corporations prescribed by regulation, such as Barbados’ International Business Companies, be deemed not to be resident in a designated treaty country. This would allow the Canadian finance minister to selectively remove the tax advantage given to residents in designated treaty countries, when the countries in question fail to ensure adequate tax treatment.

Recommendation 6
Eliminate non-taxable income trusts

Cross-Border Income Trusts (CBIT), also known as Foreign Asset Income Trusts (FAIT), enable companies operating in the oil, gas and mining industry to avoid paying any income tax on their corporate revenue. These tax vehicles have turned Canada into a de facto tax haven for the mining industry. Canada must immediately eliminate these tax benefits for mining companies masquerading as income trusts.

Recommendation 7
Join the Base Erosion and Profit Shifting (BEPS) project of the Organisation for Economic Co-operation and Development (OECD)

The OECD’s BEPS project aims to stop tax base erosion by limiting the transfer of assets and capital to low or no-tax locations. At the time this report was written, the Canadian government had yet to show any sign of wanting to participate in this multilateral initiative or to implement its recommendations, and instead seemed to want to go it alone. This is clearly not the best approach. Canada has to play an active role in the BEPS project, engage in concerted action with other member countries, and swiftly implement the OECD’s recommendations in order to stop the erosion of our tax base.
# TABLE OF CONTENTS

## SUMMARY

1. A PRELIMINARY ASSESSMENT
   - Evaluating the public funds lost to tax havens

2. OVERCOMING A SENSE OF POWERLESSNESS: IMMEDIATE SOLUTIONS
   1. Penalize capital flight to tax havens within a strict regulatory framework
   2. Revise double taxation agreements and tax information exchange agreements
   3. Eliminate non-taxable income trusts
   4. Stop the erosion of Canada’s tax base
Every year, Canadian corporations put billions of dollars in tax havens to circumvent their tax obligations. Unfortunately, it’s difficult to rigorously quantify the losses that these movements of capital by financial institutions and large corporations represent. This is due to the fact that governments haven’t devised proper tools to analyze the problem in either qualitative or quantitative terms.

Statistics Canada continues to be the source of the most widely available public data used to gauge the scale of offshore tax avoidance: i.e., data on the volume of foreign direct investment (FDI), which it compiles every year. This type of investment involves financial capital that a business circulates from one corporate entity to another among operations it controls around the world. In principle, capital invested in foreign direct investment finances fixed assets that help develop economic activities outside the country in which the group has registered its head office.

Evaluating the assets in tax havens using statistics on direct foreign investment is problematic for ascertaining the actual status of offshore investments. One problem with tax havens is that we continue to talk about them in terms that correspond to the real economy. Very often, the official terms for depicting tax haven transactions mask financial transfers or accounting operations that are made out to be something they’re not. For example, charitable foundations incorporated in the Cayman Islands own fleets of aircraft belonging to major commercial airlines. One individual can be both the beneficiary and the fund manager (a contradiction in terms) of an income trust in certain tax havens. Special Purpose Vehicles make it possible for off-balance-sheet instruments to mask accounting reports. The same goes for foreign direct investment. Although defined as capital invested abroad in fixed assets expected to yield returns, in reality, FDI is capital disguised as investments, sent offshore solely for the sake of tax optimization.

This phenomenon is steadily growing. The portion of assets that Canadian multinational corporations report as being invested in tax havens has increased by 1500% since 1990, from $11 billion in 1990 to $170 billion today. In 2012, according to Statistics Canada, Canadians had $155 billion invested at that time in the seven largest tax havens involving Canadian investments. In Barbados alone, Canadians invested close to $60 billion in 2012, making it Canada’s third preferred country for investment. Barbados is also the top third country where multinational corporations “invest” the most, precisely because these corporations are not investing in anything, save billions of dollars of volatile funds in tax avoidance vehicles. As these pseudo-investments are not connected to any tangible asset and can be channelled back to Canada tax-free (due to double taxation agreements), we have to conclude that the funds, rather than accumulating from year to year, are rechannelled into tax havens for the sole purpose of dodging taxes in Canada.

Tax havens have thus entered into competition with traditional states. To stem the massive outflow of capital to tax havens, governments have been prompted to lower their corporate tax rates and eliminate other key levies on capital. The list of some of the tax measures that cater to the major forces of capital in Canada is impressive:

1. the federal corporate tax rate was lowered from 37.8% in 1981 to 15% in 2012;
2. the federal capital tax was eliminated in 2006;
3. the percentage of taxable capital gains was lowered from 75% in 1998 to 50% in 2000;
4. export companies were exempted from sales tax and customs tariffs (Canada’s Gateways program);
5. the number and magnitude of dubious tax deferrals granted to major corporations have steadily increased: between 1992 and 2005, the total sum of “the twenty largest tax deferrals in Canada rose by $29.4 billion (or 199%), from $14.8 billion in 1992 to $44.2 billion in 2005”; 5
6. the flow-through shares program for the Canadian extractive industries (mining and oil and gas), has been made even more accommodating;
7. certain oil, gas and mining companies now have the possibility of incorporating as non-taxable income trusts;
8. Section 116 of the Canadian Income Tax Act has been modified to allow for a reduction of the tax rate (from 25% to 0%) on the sale of taxable Canadian property owned by non-residents, if the investor resides in a country with which Canada has signed a tax treaty.

Tax havens consequently engender a considerable flight of capital and substantially lower corporate tax rates. The fact that many of these tax avoidance operations are legal is all the more problematic, as their legality attests to a degree of government complicity.

The rationale that’s often given for such measures is that they allow corporations to free up funds that, logically, will be reinvested in the real economy and result in job creation. In reality, however, corporate cash reserves have been steadily growing ($544 billion in 2012) and are not being spontaneously reinjected into the real economy. Corporations are not reinvesting their profits, and the jobs they’re actually creating tend to be in “free zones” where labour standards are lax and social safety nets are non-existent. This in no way does justice to the social programs developed by the populace in rich countries, thanks to labour action and other campaigns waged over the decades.

OVERCOMING A SENSE OF POWERLESSNESS: IMMEDIATE SOLUTIONS

There's nothing inevitable about the situation we just described. Canada's hands are in no way tied by the international context. On the contrary, Canada is the one that's straggling far behind the others in the fight against tax havens. There's no reason why Canada isn't actively participating in the international movement to stop the erosion of the tax base. Nor is there anything to prevent the Canadian government from taking immediate action, on its own, to implement tangible solutions through legislative changes that don't require international co-operation. All it needs is political will. A few of these solutions are outlined here.

1. Penalize capital flight to tax havens, within a strict regulatory framework

BACKGROUND: The Canada Revenue Agency (CRA) allows taxpayers to voluntarily disclose tax information that they failed to fully or accurately report as required under the federal Income Tax Act, providing that they meet the necessary conditions. If this voluntary disclosure is accepted by the CRA, the taxpayer only has to defray the unpaid taxes plus interest. No further penalty is imposed and no criminal procedures ensue as a result of the person's transgression. Except in certain circumstances, those who have been dodging the taxman for years – even illegally - run absolutely no risk of having to pay a penalty or face imprisonment, as long as they voluntarily disclose their actions before being audited by the tax authorities.

Today, the Canadian government is in a good position to alter these provisions in order to curb the practice of shifting assets offshore into tax havens.

It would be in Canada's interest to draw on the US voluntary disclosure mechanisms for inspiration. In 2009 and 2011, our neighbours to the south implemented three different programs directed specifically at funds held in hidden offshore accounts. All three programs are part of the Offshore Voluntary Disclosure Initiative (OVDI). The first two were short-term programs lasting six or seven months, and were designed to produce a rapid inflow of capital into government coffers. Under pressure to meet the deadline, 15,000 taxpayers came forward with voluntary tax disclosures on these two occasions. They were required to pay their outstanding taxes plus interest, as well as a penalty of between 20% and 25% of the amount they owed in unpaid taxes. The understanding was that the penalties would be much higher for taxpayers who failed to disclose key tax information to the Internal Revenue Service (IRS) by the end of these six- to seven-month periods and were later found out. In 2012, the United States ended up establishing a permanent voluntary disclosure program. A penalty of 27.5% of the previously unpaid taxes is the new standard for voluntary disclosures in the US. A separate program called the Streamlined Voluntary Disclosure Program was also created. This program allows for non-resident taxpayers who have a good tax record and relatively modest assets to voluntarily disclose their revenue without any penalty.

These policies proved to be particularly useful when dealing with the Swiss bank UBS, which was the target of an investigation for having actively encouraged US and Canadian taxpayers to evade taxes. More than 10,000 taxpayers in the US filed voluntary disclosures concerning UBS on that occasion, while only a handful did so in Canada.

Given that the Canadian voluntary disclosure program doesn't impose any penalties and the CRA doesn't conduct particularly thorough investigations into its citizens' offshore accounts, there's little incentive for Canadian taxpayers to come forward and disclose their undeclared revenue.

Recommendation 1:

We recommend that the Canadian voluntary disclosure programs be formulated more like those in the US (OVDI and the Streamlined Program). Accordingly, voluntary disclosures would go hand-in-hand with penalties of between 0% and 30%, depending on the specific details of the case, the source of revenue, the conduct of the taxpayer and the circumstances that led to the disclosure. The point would be to encourage the practice of voluntarily disclosing previously undeclared revenue, which is already on the rise in any event.

In order to facilitate a harmonious transition with the new program, a six-month transition period should be envisaged.

In essence, these are promising mechanisms for getting individual tax-dodgers to come forward after fraudulently concealing their assets, but they aren't geared to stop businesses engaged in legally sanctioned corporate tax avoidance.

6 CANADA REVENUE AGENCY [http://www.cra-arc.gc.ca/gncy/nvstgtns/vdp-eng.html]
2. Revise double taxation agreements and tax information exchange agreements

BACKGROUND: In many ways, Canada is the author of its own misfortune. By ratifying multiple tax treaties and tax information exchange agreements with well-known tax havens, we have actually facilitated the flight of capital to offshore accounts that are beyond the reach of the taxman. Nearly 35 years ago, Canada signed a treaty with Barbados to avoid double taxation, thereby legalizing tax avoidance schemes in this offshore financial centre. In 1979, Barbados enacted the Offshore Banking Act and the International Business Companies (Amendment) Act. These two laws allowed foreign corporations to create shell companies in Barbados that would be taxed at a rate of no more than 2.5%. It was in 1980 (the following year) that the Canadian government, under the brief reign of Joe Clark’s Conservatives, signed the controversial double taxation treaty with Barbados. No government since then has challenged this treaty, which enables Canadian corporations to transfer their assets to Barbados practically tax free, and channel them back into Canada as non-taxable funds. This treaty also allows for a tax avoidance scheme called transfer pricing, which has proven to be notoriously effective in shielding trademark rights from the rules governing market prices.

Our successive governments have continued to revise the terms of this treaty to further increase corporations’ transfers from Canada. In 2010, the entire insurance industry was given the right to transfer its assets to accounts in Barbados, to circumvent its tax obligations. On December 19, 2013, Canada eliminated the only remaining obstacle preventing Canadian corporations from taking advantage of these tax benefits, by guaranteeing that decisions made by their subsidiary would be made Barbados-style. Until then, Canadian corporations used Barbados to their advantage under subsection 5907 (11) of the federal Income Tax Regulations, which had a grandfather clause enabling International Business Companies whose decisions were actually made in Barbados to be considered residents in that country. They could then benefit from the rules on exempt surplus, and repatriate their profits to the Canadian parent company. Since then, it seems that the amendment to the treaty will no longer require decisions to be made in that location.

A reality that’s blatantly obvious is that the amount of Canadian money pouring into Barbados is completely out of sync with this tiny country’s real economy. Tax accountant Jean-Pierre Vidal from HEC Montréal reports that “in 2006, Barbados received $89 million per square kilometre in Canadian foreign direct investment in 2006, which amounts to $136,653 per resident.” This just doesn’t add up. “Clearly, some investments are not being used to buy factories.”

The Canadian government is still increasing these types of benefits for the corporate world to this day, but is doing so more discreetly. Under our fiscal policies, when a tax haven signs a tax information exchange agreement with Canada, our government allows Canadian corporations to set up schemes similar to the ones it allows in Barbados (i.e., reporting assets there and subsequently transferring them to Canada as dividends, without paying taxes). Canada has ratified 19 tax information exchange agreements. Three more have recently been signed but have yet to be implemented, and eight more are presently being negotiated. The signatory countries include such tax havens as Anguilla, Bahamas, Bermuda, the Cayman Islands, Dominica, St. Lucia, the Dutch West Indies, St. Vincent and the Grenadines, San Marino, St. Kitts and Nevis, and the Turks and Caicos Islands.

To boost the incentive for these countries to sign tax information exchange agreements with Canada, our government has in fact offered them an appreciable advantage. In terms of calculating exempt surplus under Canadian tax legislation, corporations residing in their territorial jurisdiction will be treated in the same way as if a tax treaty had been signed with them.

In legal terms, countries that have signed a tax information exchange agreement with Canada will from now on be considered “designated treaty countries” within the meaning of subsection 5907(11) of the Income Tax Regulations. This will allow subsidiaries residing in such jurisdictions to channel their profits back to their Canadian parent company as tax-exempt dividends.

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8 For a Canadian company, such a scheme would first involve creating a subsidiary, notably in Barbados, where it would officially transfer key assets for its operations: trademark rights, real estate ownership rights, company cars, etc. The Canadian parent company would then regularly start paying rent or rights of usage to its Barbados subsidiary for theoretically using such property. The objective: to funnel as much capital as possible into the subsidiary, where it can take advantage of the extremely low tax rate in that tax haven. The funds can then be channelled back into the Canadian parent company, tax-free, under the tax treaty between the two countries. This scheme enables the Canadian company to reduce its revenue in Canada considerably and as a result, pay as little taxes as possible.


10 “Nouvelle position de l’Agence du revenu du Canada concernant les compagnies d’assurance exemptées de la Barbade” [on-line], 2010 [Osler.com].


Before 2008, this tax benefit was reserved for corporations residing in countries that had signed tax treaties with Canada. Generally speaking, there was nothing amiss about this, given the applicable tax rate for corporations in countries that had signed these treaties. But under Canadian tax regulations, this privilege was also extended to International Business Companies formed under the laws of Barbados (which had signed a tax treaty with Canada), despite the fact that such companies are taxed at a rate of no more than 2.5%. This low corporate tax rate is not in line with Canadian tax policy or with the fiscal policies of most of the countries that have signed tax treaties with Canada to eliminate double taxation, and preferential treatment should not be extended under such circumstances.

Under Canada’s tax legislation, the leniency shown to corporations residing in territorial jurisdictions that have concluded tax information exchange agreements with Canada results in a harmful degree of erosion of our national tax base. It also leads to unfair competition for Canadian corporations that aren’t privy to these tax avoidance mechanisms.

Many western countries have enacted legislation based on US measures aimed at controlling the flight of capital into offshore accounts. Unfortunately, Canada is not among them. The US government under President Barack Obama enacted the Foreign Account Tax Compliance Act (FATCA) in March 2010. This act is intended to fight tax evasion and tax avoidance through information exchange. The FATCA obliges foreign financial institutions that operate on US soil to disclose to the IRS any information on US citizens who have used their financial services to channel money offshore: account holders’ names, taxpayer ID numbers, addresses, etc. The FATCA applies to all US citizens, whether they live on American or foreign soil. This crucial information in the fight against tax evasion is often hard to obtain for revenue agencies, due to bank secrecy laws that exist in most low-tax jurisdictions. To ensure access to this information, the FATCA stipulates very stiff sanctions for financial institutions and countries that fail to co-operate: i.e., a penalty equivalent to 30% of all their assets on US soil. The FATCA is decidedly innovative in that it ties tax obligations to US citizenship rather than residency.

The point here is not for Canada to replicate the US model as it stands today. The FATCA has major problems. Few countries have Washington’s political leverage when it comes to forcing financial institutions to pay penalties of that magnitude. In terms of privacy safeguards, the FATCA is highly controversial, as it requires financial institutions to disclose private information to the government about non-US citizens who are found to be linked to a US account holder. Also, the administrative costs of such a program are staggering.14 The FATCA adds another element to a whole set of initiatives being promoted in a variety of ways around the world by the OECD. In February 2014, the OECD released a key report on exchanging tax information, which has become the standard reference for tax information exchange agreements. Contrary to the FATCA, the OECD’s initiative encourages multilateral co-operation between countries. The US model (FATCA) doesn’t make any clear reference to reciprocity (i.e., reciprocal disclosure of information by US financial institutions), and the OECD is trying to rectify this.15 The European Union, for its part, is currently considering a directive aimed at increasing co-operation among EU members.16 Unfortunately, the proposals discussed there fail to include sanctions or tackle the issue of “free zones” linked to offshore factories or “export-processing zones”. For the time being, they only involve individuals, not corporations.17 Ultimately, however, they may inspire broader public policies that also target flag of convenience states, corporations and financial institutions.

In this vein, many countries around the world are negotiating mutually binding agreements requiring them to transfer financial information on the assets of their respective nationals. These agreements are inspired by US measures stemming from the FATCA, as well as a whole array of European laws on multilateral information exchange, and OECD directives on tax information exchange between countries. The driving force behind these separate but interrelated initiatives is finding concrete expression in the Global Account Tax Compliance Act or GATCA, which is still in the developmental stage. While not yet a formal pact, GATCA reflects a general trend in countries around the world to mutually provide access to bank information that is circulating from country to country in various financial institutions. The governments of Australia, Belgium, Great Britain, Spain, France, Italy, Mexico, the Netherlands, Norway, Poland, Romania and the Czech Republic have all voiced their desire to participate in this global regulatory movement.18 Great Britain is even talking about including its overseas territories (which often happen to be tax havens) in such initiatives. On the diplomatic front, Canada would definitely stand to gain from actively participating in this international movement instead of officially tying its international policy outlook to that of countries known to be tax havens (as it does at the International Monetary Fund and the World Bank).19

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Recommendation 2:
Given the questionable efficacy of the current information exchange mechanisms set out in tax treaties and tax information exchange agreements signed by our country, we recommend that Canada actively participate in the international movement to develop multilateral automatic information exchange agreements. These would add to the current arsenal of provisions in automatic exchange agreements concluded by a number of EU member countries, and to the new American FATCA program that will enable the US Treasury Department to gather information on investments held abroad by US residents. At present, a number of countries have enacted multilateral treaties to mutually share the tax information that they transmit to the US tax authorities. The Canadian government has already undertaken to provide the US government with the information required under FATCA. Now all it has to do is join the networks that have been created to conclude multilateral information-sharing agreements.

Recommendation 3:
We recommend cancelling the tax benefit for companies residing in countries that have signed a tax information exchange agreement with Canada, which enables them to channel profits from active businesses back into Canada as tax-exempt dividends.20 To this end, we recommend that the definition of “designated treaty country” included in subsection 5907(11) of the Income Tax Regulations be modified to include only countries and jurisdictions that have signed a comprehensive agreement to eliminate double taxation with Canada – not those that have signed a tax information exchange agreement. This amendment would substantially reduce the tax optimization options that the Canadian government allows through tax information exchange agreements in their present form.

Recommendation 4:
We recommend that Canada revise its comprehensive double taxation treaties that are signed with countries where very low rates of personal and corporate income tax are levied on certain types of income and certain types of companies.

Recommendation 5:
We recommend that certain types of corporations prescribed by regulation, such as Barbados’ International Business Companies, be deemed not to be residents in a designated treaty country. This would allow the Canadian finance minister to selectively remove the tax advantage given to residents in designated treaty countries when the countries in question fail to ensure adequate tax treatment.

3. Eliminate non-taxable income trusts

BACKGROUND: In its own legislation, Canada has created legal entities that bear all the hallmarks of offshore tax havens: i.e., Cross-Border Income Trusts (CBIT) and Foreign Asset Income Trusts (FAIT). These trusts enable asset-holders in the mining, oil and gas sector to avoid paying any income tax in Canada, and have turned Canada into a de facto tax haven for the mining industry.

These income trusts differ substantially from the classic ones. Traditional income trusts are set up to shelter a family inheritance from taxation until the heirs take possession of it. The income trust itself, as a financial entity, is generally not taxed. Only payments from the trust to its beneficiaries are taxable. 21 In time, corporations were granted the right to legally convert to income trusts, allowing them to reduce their corporate taxes to zero. In the first few years of the 21st century, as the dot com bubble was bursting,22 a staggering number of Canadian corpo-

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20 Technically, only “exempt surplus” can be channeled back to the Canadian parent corporations as tax-exempt dividends. For the sake of plain language, we’ve opted here to use the terms “profits” or “corporate profits” instead of “exempt surplus.”

21 As with shareholders in a publicly traded company.

22 During the 1990s, enthusiasm for new internet companies like Yahoo and Altavista led to a new “gold rush” involving the stock market. These dot com companies were flooded with speculative financial investments, and their stock prices sky-rocketed. The return on investments was impressive, but when the ensuing speculative bubble finally burst, investors began searching for new high-yield investment opportunities. Canadian income trusts seemed like the answer to their prayers.
rations converted to income trusts. In 2004, there were over 150 income trusts listed on the TSX, with a combined value of $91 billion. That same year, $3.8 billion of the $4.6 billion invested in Initial Public Offerings (IPOs) went into income trusts.\textsuperscript{23} The legal transformation from a corporation to an income trust had little impact on daily operations, but made it possible to achieve exceptional profitability through tax avoidance.

In 2006, finance minister Jim Flaherty announced that starting in 2011, all Canadian income trusts would be taxed at the same rate as other private corporations. Whether deliberately or not, Flaherty’s reform nonetheless left a few loopholes for investors still intent on reaping the tax benefits of income trusts. To this day, companies listed on the stock exchange still can convert to income trusts and avoid paying any corporate income tax, on condition that they have no assets in Canada. Foreign companies, particularly those in the mining industry, can thus incorporate as cross-border trusts and use Canada as a tax haven while they conduct their operations abroad.\textsuperscript{24}

This makes Canada the ideal tax haven for mining companies all over the world. Any mining company can set up a trust structure that will officially own all the company’s operations in any part of the world as long as those operations take place outside Canada. By the same token, the company can reduce its tax rate to 0% and rechannel the profits it generates (in whatever location) to Canada and elsewhere in the form of dividends. And if there’s a tax treaty between Canada and the country where these dividends are channelled, the dividends will not even be taxed in Canada.

**Recommendation 6:**
We recommend that the system of cross-border income trusts and any structure offering similar advantages be abolished.

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\textsuperscript{23} BECK, Peter and Simon ROMANO (2004). Canadian Income Funds: your complete guide to income trusts, royalty trusts and real estate investment trusts.

\textsuperscript{24} FYFE, Stephen and Stephanie WONG (2012). Canadian Cross-Border Trust Structures. Tax Notes International [on line], [www.blg.com/en/newsandpublications/documents/Canadian_Cross-Border_Trust_Structures_-_OCT2012.pdf]. Since the implementation of the Flaherty reform in 2011, four new income trusts have appeared on the TSX: Eagle Energy Trust, Parallel Energy Trust, Argent Energy Trust and Crius Energy Trust. All have a number of things in common: (i) they own assets in the energy sector, (ii) they were all listed on the TSX by the same Alberta law firm, Bennett Jones, (iii) they hold only foreign assets (in the US, specifically), (iv) they pay no taxes in Canada, (v) they pay minimum taxes in the United States, and (vi) they set no investment limits on non-residents of Canada.
4. Stop the erosion of Canada’s tax base

BACKGROUND: The OECD is presently working on implementing the Base Erosion and Profit Shifting (BEPS) project, which is designed to eradicate the various mechanisms leading to tax base erosion through the transfer of corporate activities to low or no-tax locations. The project’s preliminary expected results (“deliverables”) were published in the fall of 2014, and the plan is to complete the BEPS project in 2015. 25

On the heels of the 2014 federal budget, the Canadian government also stated its intention to combat tax base erosion and profit shifting. The finance minister then announced extensive consultations on various aspects of international tax policy. He plans to do this behind closed doors, in isolation, without participating in the international movement that’s been building momentum. In addition, he has already made it clear that he doesn’t want to modify any tax treaties or agreements signed with countries that serve as tax havens.26 The fact that Canada isn’t making it a priority to work with the countries that are tackling these practices and reining in their nationals who are involved in tax havens doesn’t lend much credibility to the government’s stated intentions.

Recommendation 7:

We recommend that Canada participate actively in the Base Erosion and Profit Shifting project, play a leadership role with OECD countries, and together with other member countries, promptly implement the OECD recommendations to curb tax base erosion.


26 DENEAULT, Alain, Pascale CORNUT ST-PIERRE et Clément CAMION (2013), « Chalandage fiscal »: Pour une approche politique, Réseau Justice Fiscale, Montréal.