Tax fairness: An opportunity to lead

A progressive government's guide to the OECD Action Plan on BEPS

Association of Canadian Financial Officers

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Joe Boughner
Director of Communications
Association of Canadian Financial Officers
613-728-0695 ext. 241
jboughner@acfo-acaf.com

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Contributors

- Scott Chamberlain, Association of Canadian Financial Officers
- Arthur Cockfield, Queen's University
- Dennis Howlett, Canadians for Tax Fairness
- Brittany Lambert, OXFAM Canada
- Wilson Prichard, Munk School of Global Affairs, University of Toronto
- Toby Sanger, Canadian Union of Public Employees (CUPE)
- Armine Yalnizyan, Canadian Centre for Policy Alternatives

Executive Summary

This paper will act as a progressive government's guide to enhancing tax fairness both domestically and globally. It includes six recommendations for combatting tax exploitation using the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan as a jumping-off point. In some cases our recommendations focus on implementing the OECD's actions in the most effective and progressive ways possible; in others, where Canada is already complying with an OECD recommended action, we take the spirit of the recommendation and go one step further, showing how Canada can act as a leader for tax fairness on the world stage.

- First we call on the government to implement the OECD's first action item and address the challenges of the digital economy by requiring over-the-top service (OTTS) providers not based in Canada to collect value-added tax (HST, PST, or GST) and pay corporate taxes.
- We recommend that the government take the OECD's most-discussed recommendation, country-by-country reporting, one step further by requiring it at a lower threshold than the one cited by the OECD and by making most of the information contained in these reports available to the public.
- In this same spirit of transparency and accountability, we also call on the federal and provincial governments to work together to require all entities incorporated in Canada to reveal beneficial ownership, and we ask that this information be made available on a central public database.
- Canada is already leading on the OECD's Action 12, requiring taxpayers to disclose aggressive tax planning, so we recommend that government take one step further and require all tax products be vetted and registered before facilitators make them available to consumers.
- We also call on Canada to take a leadership role on the international stage by supporting developing nations' calls to support parallel discussions and work on international tax reform at the United Nations, where all nations voices can be equally heard.
- Finally, we recommend that the government commit itself more fully to not just investigating potential tax evasion but enforcing existing penalties against tax evasion to the fullest extent of the law.

This paper views implementation of the OECD's BEPS Action Plan through the principles of transparency, accountability and inclusiveness, which we see as essential to combatting tax abuses broadly and improving tax fairness worldwide.

Introduction

Like many countries, Canada has weathered years of punishing austerity measures, low employment rates and public service cuts, at the same time as the federal government seemed to turn a blind eye to corporate tax abuses. Tax burdens have shifted, weighing more heavily on Canadian families and less on large corporations; one calculation put the percentage of government revenue from personal income at 49%, while the percentage of income from corporate taxes at only 13%.[1] Meanwhile at the same time, estimates put the amount of Canadian money stored offshore at $187 billion.[2] This legacy of frustration with government cuts and austerity, combined with two recent tax avoidance scandals involving accounting firm KPMG and, separately, Panama legal firm Mossack Fonseca, has brought tax justice issues into the global and Canadian spotlight.

Curbing tax exploitation is essential to improving tax fairness and protecting the best interests of middle-class Canadians. The average middle-class Canadians are not using complex tax-avoidance schemes on the financial advice and encouragement of facilitators and gatekeepers. They are paying their taxes as required and trying to use the public services these taxes are supposed to fund. It is large multi-national corporations that are taking advantage of public services like transit, highways, schools, and healthcare for their employees while refusing to contribute their fair share. Collecting owed tax revenue would allow the government to invest in infrastructure and revitalize public services, creating good, stable jobs for middle class Canadians.

With the government's commitment to a gender-equal cabinet and support of the recent pay equity committee, the government has helped spark a national conversation on gender equity, so it is worth noting that tax exploitation is a gendered issue as well. This is especially true when an eroded tax base is followed by public service cuts. Research demonstrates that while men are more likely to benefit from BEPS and tax avoidance schemes, women are more likely to both use public services and be employed as public servants.[3] Furthermore, it is worth noting that tax avoidance is also sometimes done as a method of avoiding family or spousal obligations. Allowing aggressive tax avoidance to continue unchecked means lining men's pockets at the expense of Canadian women.

As issues of tax fairness have come increasingly into the public eye and onto governments' radar, the Organisation for Economic Cooperation and Development (OECD) has been studying a series of related forms of tax avoidance called base erosion and profit shifting (BEPS). The OECD was first urged to look into the root causes of BEPS at the Los Cabos 2012 G20 summit, and was asked to

[1] John Chipman, "Corporate Canada pays low taxes but contributes in 'lots of other ways'," *CBC News*, April 26, 2014 http://www.cbc.ca/news/business/corporate-canada-pays-low-taxes-but-contributes-in-lots-of-other-ways-1.2621944
[2] "Canadian $$ in Tax Havens Reach $199 Billion," Canadians for Tax Fairness, accessed July 22, 2016 http://www.taxfairness.ca/en/news/canadian-tax-havens-reach-199-billion
[3] https://taxlinked.net/blog/march-2016/on-feminism-taxes-gender-inequality http://www.taxjustice.net/wp-content/uploads/2013/04/TJF_2015_Women.pdf

report back with their findings the following year.[4] After the release of their report in February, the OECD was tasked with creating a comprehensive action plan for addressing and combatting BEPS. After study and consultation with representatives from sixty nations, the OECD released their final reports in October of 2015.[5]

The OECD BEPS Action Plan contains fifteen recommendations for actions to curb BEPS-related tax abuses and improve global tax fairness. Its recommendations range from proposed minimum standards to common approaches. None are legally binding, but governments around the world are being encouraged to adopt some or all of the OECD's recommendations. The OECD BEPS Action Plan represents a coordinated, international move against tax abuse. Many tax justice advocates and experts see it as a significant first step toward improving global tax fairness.

At the same time, the OECD's BEPS Action Plan is not without its limitations. Many of its recommendations have been softened between the draft and final stages, and the results are largely perceived by critics to be too conservative to be truly effective. The OECD has also faced some criticism for the limited opportunities developing nations were given to participate in the process of creating the action plan. While the OECD's BEPS project itself began in 2012 with G20, it wasn't until 2014, after pressure from developing nations and civil society, that the OECD admitted non-G20 nations into the consultation process.[6] At this point, the project's agenda had already been set and the first round of outcomes already decided.[7] The number of developing nations admitted to the consultation process continued to increase, but the opportunity for active participation of these developing nations was limited. Accordingly, the OECD's recommendations have been criticized for not reflecting the concerns and priorities of developing nations, who are often the hardest hit by base erosion, profit-shifting, and other forms of aggressive tax avoidance.

We see three major themes as essential to implementing the OECD's BEPS recommendations and taking new, progressive strides in combatting tax abuse in Canada and around the world: transparency, inclusiveness and accountability.

It is a new age of transparency and openness in the Canadian federal government; we believe large multinational corporations operating in Canada must be held to the same standard. Multinational entities (MNEs) cannot be allowed to hide tax abuses behind a veil of secrecy, and any demands for special privacy protections must be weighed against the public interest.

Canada has also recently declared its intention to return to a leadership role on the world stage. To truly deliver on this promise, Canada must act as a model to other developed nations and adopt

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[4] Pascal Saint-Amans, "What the BEPS are we talking about?," Organisation for Economic Co-operation and Development, accessed July 22, 2016 http://www.oecd.org/forum/what-the-beps-are-we-talking-about.htm
[5] Ibid.
[6] ICRICT Declaration," *Independent Commission for the Reform of International Corporate Taxation*, June 2015 http://www.icrict.org/wp-content/uploads/2015/06/ICRICT_Com-Rec-Report_ENG_v1.4.pdf
[7] Ibid.

progressive, inclusive international policies. Canada must use its influence and clout to support developing nations and to advocate for their needs and priorities where appropriate.

Finally, Canada must take a firm stance on holding tax abusers responsible for their actions. The Canadian government and government bodies such as Canada Revenue Agency must hold corporations accountable for contributing back their fair share to the Canadian economy. In some cases, this means enacting new legislation criminalizing aggressive tax avoidance, but it also means improving enforcement of existing anti-tax-evasion legislation.

In this paper, we will examine how Canada can implement some of the OECD's BEPS action items in a practical, progressive way. In some cases, Canada already has the OECD's anti-BEPS measures in place, and so our recommendations will focus on further steps Canada can take that are in the same sprit as the OECD's proposed actions. Our recommendations will touch on issues including:

- Taxing the digital economy and over-the-top services
- Country-by-country reporting
- Beneficial ownership
- Registering and vetting tax products
- Supporting the call for complementary discussions on international tax practices at the UN
- Stepping up existing enforcement

We believe the OECD's BEPS recommendations can be the key to significant improvements to tax fairness both in Canada and globally; however, for this to be true Canada will require the strong leadership of a government committed to progressive, fair solutions to tax abuse and injustice.

Recommendation:

Address the tax challenges of the digital economy

Context

The rapid growth of the digital world is making it increasingly difficult for global governments to regulate and collect taxes. The complexities of tackling the digital international tax system are reflected in the OECD's Action Plan: the OECD devotes its first action item solely to tax challenges of the digital economy, and these challenges are also relevant to Actions 3-7, 8-10 and 13.

Over the past decade there has been an increase in what are called "over-the-top services" (OTTS). "Over-the-top" refers to video coverage or digital products or services provided for consumption by way of the internet. The entities providing these services may or may not have a physical presence in the country where the product is consumed. For instance, over-the-top services such as Netflix provide video service for consumption by people outside of where that company has a physical presence. The lack of physical presence by these digital companies makes it difficult for governments to tax and regulate. In conjunction with double tax agreement treaties, it also creates opportunities for companies that provide over-the-top services to achieve double non-taxation, which occurs when income earned by a corporation or individual is not taxed in any jurisdiction.

To address this issue, the OECD recommends that governments compel non-resident companies to register and collect value added taxes (VAT) on cross-border transactions at the point of consumption.[8]

Canadian-based digital services and producers are required to collect and pay taxes, while corporations that do not have a physical presence in Canada are currently exempt from paying value-added taxes, harmonized sales tax (HST), goods and services tax (GST) or provincial sales tax (PST). According to the Canadian Centre for Policy Alternatives, this exemption is costing Canada between $62.4 to $90.48 million a year in lost tax revenue from Netflix alone.[9]

Neither the Canadian *Income Tax Act* nor the international tax system has worked seriously on tackling the changing culture of the digital world. The current international tax system dates back to

[8] "OECD/G20 Base Erosion and Profit Shifting Project: 2015 Executive Summaries Final Reports," *Organisation for Economic Co-Operation and Development*, 2015 https://www.oecd.org/ctp/beps-reports-2015-executive-summaries.pdf
[9] John Anderson, "An Over-the-Top Exemption: It's Time to Fairly Tax and Regulate the New Internet Media Service," *Canadian Centre for Policy Alternatives*, June 21, 2016 https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2016/06/Over_the_Top_Exemption.pdf

the 1920s and is based on bilateral tax treaties that are increasingly out of date.[10] There are now over 3,000 of these tax treaties.

The international tax system is simply not keeping pace with the increasingly globalized digital economy. As the digital economy continues to grow, it is becoming more and more important for governments to address the tax challenges it poses.

Recommendation

We are calling on the federal government to address the challenges of taxing the digital economy and over-the-top services.

We recommend that the Finance Minister amend the *Income Tax Act* to collect value added taxes on over-the-top services that do not have a physical presence in Canada and to require OTTS to pay corporate income tax.[11] Digital corporations should not be treated differently than corporations that have a physical presence.

In 2014 the Canadian government proposed to amend the *Income Tax Conventions Interpretation Act (ITCIA)* with a domestic anti-treaty-shopping rule, but put this decision on hold until the OECD BEPS process was complete.[12] We now urge the government to renew its focus on the anti-treaty shopping initiative and ensure their treaties with countries in which many OTTS are located correspond are modified to prevent treaty abuse and double non-taxation.

We also recommend that the federal government work with the provinces to determine the amount of value added taxes they will collect for digital online services delivered from foreign e-commerce services and suppliers.

Finally, we hope that the federal government will reconsider its stance on ratifying the Trans-Pacific Partnership (TPP), as its terms would strip Canada of its power to tax OTTS within its own borders.[13]

Rationale

Addressing the challenges of the digital economy is essential to ensuring tax fairness for all Canadians and Canadian corporations.

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[10] "OECD/G20 Base Erosion and Profit Shifting Project: 2015 Executive Summaries Final Reports," *Organisation for Economic Co-Operation and Development*, 2015 https://www.oecd.org/ctp/beps-reports-2015-executive-summaries.pdf
[11] Ibid.
[12] Steve Suarez, "Canada to Unilaterally Override Tax Treaties With Proposed New Anti-Treaty-Shopping Rule," Tax Notes International, March 3 2014 https://www.blg.com/en/NewsAndPublications/Documents/Canada_to_Unilaterally_Override_Tax_Treaties_-_March_2014.pdf
[13] "OECD/G20 Base Erosion and Profit Shifting Project: 2015 Executive Summaries Final Reports," *Organisation for Economic Co-Operation and Development*, 2015 https://www.oecd.org/ctp/beps-reports-2015-executive-summaries.pdf

If Canada wants to protect its Canadian based e-commerce cultural services and products, it must address the unregulated digital sector. Non-established status gives these OTTS providers a special advantage over Canadian providers. Entitles offering over-the-top digital media services operate within Canadian borders and profit off of Canadian consumers, but are not required to collect VAT or pay corporate tax. They are in direct competition with Canadian e-commerce firms such as Rogers, Bell, and Quebecor/Vidéotron that offer nearly identical services (for example, Crave or Shomi) and that collect and are subject to tax.

The same is true of non-media services such as Airbnb and Uber. These services are unregulated, do not pay or collect taxes and because they are not established in Canada, the revenue they make flows out of the country. They compete with Canadian hotel and taxi industries that are regulated and do pay and charge tax.

Canada will need to remain competitive on the international stage or risk losing revenue and, eventually, jobs to OTTS providers. Canadian based services in the film and television sector generated 260,000 jobs in 2011.[14] If Canada doesn't address the digital economy issues threatening Canadian jobs, it could see a decline of 15,000 jobs by 2020, with an annual drop of $1.4 billion from the Canadian economy.[15]

A report prepared for the European Parliament concluded that cracking down on the digital economy and OTTS would significantly reduce competition between states, "as taxing at consumption stage would prevent businesses from picking and choosing their place of establishment according to tax rates. It would also improve distributional equity as Member States could collect VAT on the supplies consumed on their territory and share the cost of taxation amongst individuals."[16]

In addition to the report made to the European Parliament, our recommendations to require OTTS to collect VAT and pay corporate taxes have precedents in countries such as Australia, New Zealand and Japan, which have already begun to take action by taxing OTTS.[17] Australia has set out to apply their country's 10% GST on Netflix services by 2017, which will bring in AUD$350 million into their country within the next 4 years.[18]

Taxing OTTS that do not have a physical presence in Canada will help crack down on tax avoidance, strengthen and boost Canada's cultural and creative industries, protect jobs in Canadian-based

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[14] Nordicity, Peter Miller, "Canadian Television 2020: Technological and Regulatory Impacts," *ACTRA*, December 2015 http://www.actra.ca/wp-content/uploads/Nordicity-Miller-Lets-Talk-TV-economic-impact-forecast.pdf p.21
[15] Ibid.
[16] "Tax Challenges in the Digital Economy," *European Parliament*, June 2016 http://www.europarl.europa.eu/RegData/etudes/STUD/2016/579002/IPOL_STU(2016)579002_EN.pdf
[1717] John Anderson, "An Over-the-Top Exemption: It's Time to Fairly Tax and Regulate the New Internet Media Service," *Canadian Centre for Policy Alternatives*, June 21, 2016 https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2016/06/Over_the_Top_Exemption.pdf
[18] Ibid.

digital services and restore government revenue. This is why it is essential that Canada take the OECD BEPS recommendations one step further and be a leader on the world stage with tackling the digital economy.

Recommendation: Country-by-country reporting

Context

Country-by-country (CbC) reporting is generally perceived to be one of the most important and potentially effective recommendations made in the OECD's BEPS Action Plan. Action 13 addresses both transfer pricing and CbC reporting through a three-tiered approach. The portion of this action involving CbC reporting calls for the development of regulations that would require large multinational entities (MNEs) to file a country-by-country report that will "provide annually and for each tax jurisdiction in which they do business the amount of revenue, profit before income tax and income tax paid and accrued. It also requires MNEs to report their number of employees, stated capital, retained earnings and tangible assets in each tax jurisdiction."

Canada has already made significant progress toward complying with this recommendation. This spring the Canadian government acted on the commitment made in Budget 2016 to combat tax abuse by signing the Multilateral Competent Authority Agreement (MCAA) on country-by-country reporting.

As recommended in the OECD's BEPS Action Plan and specified in the MCAA, country-by-country reporting is required of companies with an annual turnover of €750 million (the equivalent of over $1.1 billion CDN). These reports are filed only in the country where the company is headquartered. They are not available to the public and are only shared among governments according to reciprocal bilateral agreements.

These details are concerning to many tax justice advocates. According to the OECD's own calculations, the €750 million threshold would exclude 85 to 90 percent of all multinational entities. Under OECD's proposed threshold, only 160 corporations in Canada would be required to provide country-by-country reporting. This high threshold is especially concerning for developing nations, which often host MNEs that may be comparatively small (grossing less than one hundred million) but still have a significant effect on the national economy.

Most of its original advocates championed country-by-country reporting specifically as a tool of transparency, so denying public access to the reports is also a significant concern. If the basic contents of CbC reports are not made public, developing nations are again at a disadvantage. Many developing nations do not have the resources or capacity to participate in a tax exchange or to comply with the confidentiality standards required to access this information, but could benefit greatly from the information contained in these reports.

Recommendation

Commitment to CbC reporting itself is a step in the right direction, but the details of CbC reporting as delineated in the OECD BEPS Action Plan and codified in the MCAA limit its effectiveness as a tool for tax fairness and transparency.

We recommend that the Canadian government lower the threshold for country-by-country reporting in Canada so that it is required of any company with an annual turnover of $60 million or more. This threshold is in line with the figure recommended by some European NGO groups even a major EU parliamentary party.

We also recommend that Canada require all MNEs meeting these requirements to disclose to Canada Revenue Agency at a gross level: revenues, taxable profits, taxes paid, employee numbers, total salaries, and details of gross and the net assets for every country in which they operate. CRA should then make information about revenues, profits, and taxes paid available on a publicly accessible registry.

Rationale

A lower threshold and public registry for country-by-country reporting are essential to making it an effective tool for tax justice and to increasing transparency in Canadian society.

A lower threshold would require more companies to participate in country-by-country reporting, giving the Canadian tax administration a fuller, global picture of where MNEs are profiting and where tax and economic activities are reported. This in turn would allow the government to use this information to assess BEPS risk and target audit resources where they will be most effective.

One of the major aims of CbC reporting is to shine a light on corporate behavior. There is a significant public interest in providing access to information about which corporations are paying their fair share of taxes. Access to this information would allow citizens to make an informed decision about the products and services they consume. Public attention and the risk of reputational damage could act as a deterrent to corporations who might otherwise use aggressive tax avoidance tactics. A publicly-accessible registry of country-by-country reports would also be a tool for journalists and parliamentarians to hold both companies and the government accountable.

Making information from country-by-country reports publicly available would also ensure developing nations have access to this information even if they do not have existing exchange of information agreements in place, or the capacity to meet privacy requirements. CbC is perceived as one of the most important recommendations to come out of the OECD BEPS project but it must be implemented in a way that does not exclude the countries that could be its greatest beneficiaries.

There is already a precedent for this level of reporting. In 2013, the EU passed a law that required banks in 15 EU member states to submit fully public country-by-country tax reports by 2015. It has already been demonstrated that the available data allows for risk analysis of potential profit shifting and base erosion by banks . Furthermore, a study conducted by the EU Commission in 2014 "found that public country by country reporting would have "no significant negative effects" on the economy, noting instead the possibility of "some limited positive impact." And as the European Commission notes, increased transparency would help lighten the burden on tax authorities by making it easier to identify tax avoidance risks and crack down on treaty abuse and double non-taxation. Simply put, there is no legitimate economic reason not to make these reports public.

One of the primary arguments against a public registry of CbC reports is that it would violate corporations' privacy but it is important to look carefully and consider what that claim of "privacy" is intended to shield and to weigh this argument against the public interest. Tax avoidance schemes cannot fairly be considered a trade secret or competition parameter. Transparency International argues that this kind of advantage “distorts the functioning of the market and breeds complex and opaque business structure,” while the Tax Justice Network notes that “a company that uses a tax loophole may be able to use that to bring down its prices and steal a march on its competitors – but in the process it has done absolutely nothing to improve its efficiency or the quality of what it provides.” The case for privacy is especially insignificant when weighed against the overwhelming public interest as described above.

The Canadian government has made a strong, public commitment to transparency and openness in government and has announced its intention to return to a leadership position on the world stage. Public country-by-country reporting with a lower threshold would be an important way to demonstrate Canada's leadership and ensure full transparency.

Recommendation: Disclose beneficial ownership

Context

Anonymous shell companies are a tremendous drain on national economies around the world. Practices involving shell corporations, such as transfer pricing and tax shifting, have an enormous cost to global governments. The UN office on Drugs and Crime estimates that between US$ 800 billion and US$2 trillion is laundered each year.[19] Shell companies also cost governments in other ways too: they facilitate corruption, resulting in eroded public trust and the potential for misuse of public resources. A recent World Bank study of over 200 cases of grand corruption found that 70 percent of them involved the use of anonymous shell companies.[20]

This is an especially important issue in Canada. A recent study by Oxfam found that of the G20 nations, Canada is the third largest loser of untaxed corporate revenue.[21] Canada is also known as one the countries in which it is easiest to set up a shell company. In fact, the Panama Papers leak revealed that tax firm Mossack Fonseca marketed Canada to their clients in precisely this way.[22] This is hardly a reputation Canada wants to cultivate.

In our interviews with several tax experts, one of the most commonly-cited recommendations for combatting base erosion and tax avoidance that is not directly addressed by the OECD's BEPS action plan was to require all corporations to register beneficial ownership, and to make this information publicly accessible.

The current incorporation and registration system sees the federal and provincial governments maintaining separate corporate registries; not all provinces require the same information. The information released by these bodies results in a picture of the corporate landscape that is complicated and opaque.

Recommendation

We recommend that the federal government, under the Ministry of Innovation, Science and Development Canada, work with their provincial counterparts to ensure that all companies

[19] "Money-Laundering and Globalization," *United Nations Office on Drugs and Crime*, accessed July 22, 2016 https://www.unodc.org/unodc/en/money-laundering/globalization.html
[20] "The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do About It," *The International Bank for Reconstruction and Development / The World Bank,* 2011 http://star.worldbank.org/star/sites/star/files/puppetmastersv1.pdf
[21] "Still Broken: Governments must do more to fix the international corporate tax system," *Oxfam*, November 10, 2015 https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/bn-still-broken-corporate-tax-101115-embargo-en.pdf
[22] "How offshore banking is costing Canada billions of dollars a year," *The Toronto Star*, April 4, 2016 https://www.thestar.com/news/world/2016/04/04/how-offshore-tax-havens-are-costing-canada-billions-of-dollars-a-year.html

incorporated on the federal or provincial level are required to publicly reveal beneficial ownership, and should eventually work toward making this information available in a single, unified registry.

For guidance on how to implement this recommendation, Canadian governments should look to the significant control registry implemented by the United Kingdom in June 2016. Companies in the United Kingdom are now required to disclose beneficial ownership or significant control with the Companies House executive government agency. The onus is on companies to register and maintain their information.

In the United Kingdom's system, "significant control" refers to those that hold more than 25% of shares or voting rights. Under this model, these individuals are required to register their full names, dates of birth, nationalities, the country or state of usual residence, their residential addresses and service addresses, and the details of the beneficial interest. This information, with the exception of date of birth and residential address, is made available to the public on a central database.

Rationale

In his letter to his Cabinet, Prime Minister Trudeau reiterated his commitment to openness and transparency in government and said that "government and its information should be open by default." Requiring corporations to register beneficial ownership and making that registry available to the public would be strong demonstration of that commitment to transparency and the public accessibility of government information.

Registering beneficial ownership would be much more than just a symbolic commitment. It would also go a long way in stemming the loss of revenue from federal and provincial government coffers as a result of shell corporations. The federal and provincial government lose a combined $8 billion in revenue to tax havens each year, so both levels of government have an incentive to work together to establish a registry.[23]

Once the public registry is well-established and global compliance is assured, the private sector also stands to gain from a public, centralized beneficial ownership registry. Under FINTRAC guidelines, banks and financial institutions are required to investigate beneficial ownership of potential clients. Some criticism of a public database beneficial ownership is grounded in the fear of damaging consequences if companies did not immediately comply and provide all required information and financial institutions relied solely on the database for information. This, however, is not a convincing reason not to create a database at all; financial institutions would simply be instructed not to rely solely on the database until all information was made available. In the long term, having a central registry with relevant, secure, and up-to-date information would make it easier for these groups to do

[23] "Canadian $$ in Tax Havens Reach $199 Billion," *Canadians for Tax Fairness*, accessed July 22, 2016 http://www.taxfairness.ca/en/news/canadian-tax-havens-reach-199-billion

their due diligence and to provide greater investor protection. A registry of beneficial ownership would also allow law enforcement to track and prosecute corruption cases more effectively.

The OECD's BEPS Action Plan recommends actions such as:

- requiring clear country-by-country reporting shared via automatic reporting;
- more effectively countering harmful tax practices by taking into consideration transparency and substance;
- adopting rules designed to prevent treaty shopping through the establishment of shell companies; and
- requiring tax payers to disclose aggressive tax planning. The overall move is one toward accountability and transparency.

Registering beneficial ownership is not specifically included in the OECD recommendations, but it is a natural continuation of this ethos and a recommendation that is increasingly gaining traction around the world. In its report on anti money laundering and countering the financing of terrorism measures released this September, the intergovernmental body Financial Action Task Force recommended that Canada ensure its financial institutions are complying with the requirement to determine beneficial ownership and to extend that requirement of compliance to designated non-financial businesses and professions.[24] It also suggests the government consider additional measures to support the current beneficial ownership framework.[25]

As previously mentioned, the United Kingdom is registering beneficial ownership in a publicly-accessible forum, joining nations like France and Nigeria. Other EU countries are set to introduce central registers of corporate beneficial owners by 2017 as part of their implementation of the EU's Anti-Money Laundering Directive.[26] In creating a public central registry of corporate beneficial owners, Canada will be taking a strong stance on transparency and aggressive tax avoidance and joining in good global company.

[24] "Anti-money laundering and counter-terrorist financing measures: Canada," *Financial Action Task Force*, September 2016 http://www.fatf
-gafi.org/media/fatf/documents/reports/mer4/MER-Canada-2016.pdf
[25] Ibid.
[26] "Panama papers: neither major Australian party will outlaw shell companies," *The Guardian*, April 7, 2016
https://www.theguardian.com/news/2016/apr/08/panama-papers-neither-major-party-plans-to-outlaw-shell-companies

Recommendation:

Require the vetting and registration of tax products

Context

Action 12 of the OECD's BEPS Action Plan recommends the disclosure of aggressive tax planning arrangements to national tax administrations. The Action Plan calls for either "promoters" or taxpayers *and* promoters to be required to disclose aggressive tax planning. This requirement would apply to those whose tax schemes "present certain hallmarks or features" as specified in the Plan.[27]

Canada already has in place legislation requiring both the taxpayer and promoter to disclose the use of tax planning strategies after the fact. Canada does not currently require any formal registration or vetting of tax products by lawyers or accountants. These firms can, however, contact Canada Revenue Agency and to get an opinion on the applicability of tax laws to a specific plan or product. This is a freely-available feature of the CRA, but it is not often used by the wealth management industry. As disclosed in a House Finance Committee meeting on June 7, facilitators are able to conceive of, develop, sell, market, promote and profit from tax products that have not been vetted by the Canada Revenue Agency.[28]

Recommendation

We urge the government to take a proactive approach to promoting tax fairness by requiring all tax products be registered and vetted before accountants, lawyers, wealth managers and other facilitators are authorized to offer them to clients.

We believe this vetting and registration could be performed by the CRA, which has recently been granted additional resources for the express purpose of cracking down on tax evasion and aggressive avoidance, or by an independent body of the Tax Court.

Rationale

We strongly agree with the spirit of accountability in the OECD's Action 12 and believe that because Canada is already fulfilling this recommendation, we are well-placed to act as a model of accountability and take one step further in curbing unethical tax avoidance.

Requiring facilitators to register tax products is an effective, proactive strategy for preventing tax abuse. The current model encourages risk-taking and fails to protect consumer taxpayers who may

[27] "OECD/G20 Base Erosion and Profit Shifting Project: Mandatory Disclosure Rules, Action 12 - 2015 Final Report," *Organisation for Economic Co-Operation and Development,* 2015 http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/mandatory-disclosure-rules-action-12-2015-final-report_9789264241442-en#.V5JhkPkrLIU#page1

[28] House Standing Committee on Finance, June 7, 2016 https://openparliament.ca/committees/finance/42-1/27/

be drawn in by facilitators offering aggressive tax planning products. Under the current regulations, taxpayers could end up unknowingly using illegal tax products offered to them by facilitators. Canada Revenue Agency would then be required to investigate the usage of these tax products on a case-by-case basis. The vetting we propose would occur before the tax products are made available to the consumers, meaning that our proposed model is a preventative measure and puts the onus more squarely on facilitators.

Upfront compliance measures are also advisable because of the cost savings attached. It is much more time consuming and resource intensive to investigate and prosecute those who do not comply with tax law than it is to prevent non-compliance in the first place.

The most common counter-argument to these kinds of measures is that they would violate accountant-client privilege. This is a misdirection on two fronts. First of all, since the vetting would occur before the tax product is made available to the public, no clients would yet be using said product. Second, simply put, "accountant-client confidentiality" does not exist. Canadian law does not recognize any such confidentiality.

Requiring the registration and vetting of all tax products is a reasonable, uncontroversial recommendation with a significant precedent: in the United States, vetting and registration of tax products with the IRS has been required by law for years.[29]

This recommendation is also directly in line with the mandate given the CRA in Budget 2016. Chapter 8 of Budget 2016 states that "the Government is committed to preventing underground economic activity, tax evasion and aggressive tax planning," and goes on to say that this effort "requires legislative and other actions to improve the integrity of Canada's tax system—on both the international and domestic fronts—to ensure that the system is functioning as intended." The registration and vetting of tax products is precisely the type of legislation described. It would improve the integrity of the Canadian tax system by ensuring all tax products offered in Canada have first been vetted by the government. It would also eliminate tax schemes designed to contravene or side-step tax regulations before they hit the market, thus helping to ensure the tax system is functioning appropriately.

[29] "U.S. Tax Shelter Industry: The role of accountants, lawyers, and financial professionals," *Minority Staff of the Permanent Subcommittee on Investigations of the Committee on Governmental Affairs, United States Senate*, 2003.

Recommendation:

Support developing nations' call for an UN international tax body

Context

The OECD's BEPS Action Plan is intended to be a global tool for addressing tax abuse in both developing and developed nations. However, when considering the universal applicability of the Action Plan's recommendations, it is important to note the limited opportunities given developing nations when it came to formulating the OECD's recommendations.

The BEPS project has been underway at the OECD since 2012 but it was only in 2014, after significant pressure from developing nations and civil society, that the OECD admitted 14 non-G20 nations into the BEPS consultation process.[30] By the time this select group of nations had been admitted, the BEPS agenda had already been set, the first round of outcomes had already been decided, and the second round of outcomes were well underway.[31] The opportunity for active participation was limited.

It is perhaps unsurprising, then, that the OECD's BEPS Action Plan has been criticized for not reflecting the realities and priorities of developing nations. One of the primary criticisms levelled at the plan is that the recommendations are so complex that implementing them would be untenable for developing nations with less robust tax authorities. Another concern is that much of the information provided between governments of developed nations will be inaccessible to developing nation governments because of a lack of pre-existing bilateral agreements. Instead, developing nations would have to file requests for information that are inefficient and slow.

In July 2015 at the United Nations Financing for Development conference, several developing countries called for the ability to take a more active role in the discussions and decision making on international tax standards and for the establishment of an inclusive, global tax body under the UN.[32] The group as a whole agreed to improve cooperation and to support capacity-building for tax authorities in developing nations, but they did not come to an agreement on a global tax body. This issue is integral to developing nations and is unlikely to disappear. Further calls for a move away from the G20-dominated OECD and toward an intergovernmental body under the UN will likely continue.

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[30] "ICRICT Declaration," *Independent Commission for the Reform of International Corporate Taxation*, June 2015 http://www.icrict.org/wp-content/uploads/2015/06/ICRICT_Com-Rec-Report_ENG_v1.4.pdf

[31] Ibid.

[32] Ibid.

Action

Over the past year the Canadian government has renewed its commitment to taking a leadership role on the world stage. One way for Canada to restore its international reputation for fairness and leadership is supporting developing nations when they call for an inclusive intergovernmental body under the auspices of the UN devoted to establishing international tax standards and curbing tax abuse.

We recognize that OECD members have specialized knowledge and training that make them uniquely qualified to address some of the more technical issues presented by international tax regulations, so we suggest the OECD could continue to serve as a complementary technical body parallel to the UN.

This issue is likely to come up again at the upcoming UN General Assembly, which will be held in September, and the UN Economic and Social Council meeting in spring of 2017. We call on the Canadian federal government to take a firm stance in support of developing nations on this issue, and to urge its fellow G20 countries to do the same.

Rationale

Base erosion and profit shifting, along with other forms of tax abuse, have a debilitating effect on governments across the world. Tax abuses increase the tax burden on average citizens, erode resources needed to fund essential public services and fight poverty, and exacerbate income inequality. But this impact is felt especially strongly in developing nations, though, where taxes abuses also contribute to an increased reliance on foreign aid.

Recent studies by the International Monetary Fund show that revenue loss for developing nations as a result of base erosion and profit shifting is thirty percent higher than for OECD countries.[33] According to the UN Conference on Trade and Development this revenue lost due to profit shifting amounts one-third of the total corporate income taxes due.[34] In a dollar amount, that's $100 billion per year.[35]

This loss of revenue is taking a tremendous toll on the governments of developing nations, specifically on the services these governments are able to provide their citizens. Between 2008 and 2012, over half of developing nations reduced public spending on education and two-thirds decreased spending on health.[36]

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[33] Ernesto Crivelli, Ruud De Mooij and Michael Keen, "IMF Working Paper: Base Erosion, Profit Shifting and Developing Countries," *International Monetary Fund*, May 2015 https://www.imf.org/external/pubs/ft/wp/2015/wp15118.pdf
[34] "ICRICT Declaration," *Independent Commission for the Reform of International Corporate Taxation*, June 2015 http://www.icrict.org/wp-content/uploads/2015/06/ICRICT_Com-Rec-Report_ENG_v1.4.pdf
[35] Ibid.
[36] "Still Broken: Governments must do more to fix the international corporate tax system," *Oxfam*, November 10, 2015 https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/bn-still-broken-corporate-tax-101115-embargo-en.pdf

Developing nations disproportionately feel the impacts of tax abuses like base erosion and profit shifting. They cannot be excluded from discussions and decision-making on international tax standards if these standards are to be considered fair, progressive or truly global.

Excluding developing nations from conversations surrounding treaty and legislative reform creates the potential for confusion, uncertainty and competing international standards that could be exploited by multi-national entities to create double-non-taxation, and other avoidance measures.[37] It is in everyone's best interests for the international community to move forward with an inclusive framework and focus of discussion.

Our recommendation to establish an intergovernmental body under the UN has its roots in the OECD's own BEPS recommendations. Recommendation 15 calls for the creation of a "multilateral instrument" to implement the Action Plan and oversee the amending of tax treaties. A truly inclusive solution would be an international intergovernmental body under the auspices of the United Nations that is properly-resourced, has authority to implement its decisions, and most importantly, gives developing nations an equal voice.

[37] "Fixing the cracks in tax: a plan of action," *Oxfam*, Sep 3, 2013 https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/fix-the-cracks-in-tax_0.pdf

Recommendation:

Strengthen enforcement of existing penalties

Context

The focus of much of this paper has been on recommending measures to implement that would reduce aggressive tax avoidance and tax abuse, especially those involving offshore tax havens and corporate subsidiaries. It is also important, however, to take a closer look at how strongly Canada enforces the legislation against tax evasion already in place and any strides that could be made in the area of enforcement.

An essential aspect of enforcement is examining how often charges are actually brought against those who practice tax evasion and how many convictions are made. In the fiscal year of 2013, for example, the CRA convicted 128 people of tax evasion or tax fraud.[38] By contrast, in the same year, the United States saw 3,311 tax-related criminal convictions.[39] That is approximately twenty-five times the number of convictions in a country with only nine times the population.

Enforcement of rules against tax abuse have been the subject of much discussion in Canada over the past year, after it was discovered that firm KPMG used a sophisticated tax avoidance scheme in the Isle of Mann. In March of this year, an investigation by journalists from CBC revealed that CRA reached a settlement allowing KPMG clients to avoid penalties, fines and criminal sanctions if they paid their owed taxes and some moderate interest.[40]

In cases of both aggressive tax avoidance and outright tax evasion, individuals and corporations depend on the assistance and advise of facilitators or gatekeepers. These facilitators design complex tax schemes and offer them to their clients. In the Isle of Mann instance, KPMG was acting as a facilitator for their clients. KPMG's clients are not the only parties who have avoided penalties: as of yet, no charges have been filed against KPMG.

At a Parliamentary Finance Committee meeting on May 19th, Ted Gallivan, an Assistant Commissioner at CRA, admitted that "the CRA has an obligation to maximize value for the taxpayers … Sometimes we stand on principle and we risk coming away with nothing."[41] What Gallivan

[38] Sean Davidson, "Tax time 2015: Why tax cheats in Canada are rarely jailed," *CBC News*, March 2, 2015 http://www.cbc.ca/news/business/taxes/tax-time-2015-why-tax-cheats-in-canada-are-rarely-jailed-1.2960595
[39] Ibid.
[40] Harvey Cashore, Dave Seglins, Frederic Zalac, Kimberly Ivany, "Canada Revenue offered amnesty to wealthy KPMG clients in offshore tax 'sham'," *CBC News*, March 8, 2016 http://www.cbc.ca/news/business/canada-revenue-kpmg-secret-amnesty-1.3479594
[41] Ted Gallivan (testimony, House Committee on Finance, Ottawa, Ontario, May 19, 2016) https://openparliament.ca/committees/finance/42-1/23/

suggests is that the priority of the CRA is collecting tax revenues, not on defending the rule of law or providing a specific or general deterrent to future tax avoiders.

Recommendation

We call on the federal government to make the prosecution and punishment of high-risk, high-value tax evaders a priority. In addition to recouping lost revenue, the government should also create a significant deterrent to help prevent future tax avoidance and further crack down on tax evaders. Settlements can fail to provide a deterrent effect; investigations must be conducted and penalties must be imposed.

We call on the Minister of National Revenue and her department to prosecute, convict, and punish high-risk, high-value tax avoiders –both individuals and corporations – and to enforce the existing penalties. Where circumstances merit, non-compliant corporations and their high-level executives should be prosecuted to the fullest extent to the law, as in the case in the United States, in which some KPMG partners and executives actually served prison time for their crimes. We urge the government to commit not just to investigations, but to enforcing already-existing laws and penalties under the *Income Tax Act*.

We also ask that the Minister of National Revenue crack down on gatekeepers, accountants and lawyers who engage in reckless or negligent tax advice to their clients. In addition to enforcing the already-existing laws, we ask that the Minister of National Revenue and Minister of Justice work together to propose an amendment to the *Income Tax Act* to require lawyers and accountants to report suspected evidence of avoidance and evasion to the CRA or another tax enforcement body.

Finally, we call on the government to be transparent about settlements reached between non-compliant taxpayers and the Canada Revenue Agency. This information should be made available by CRA for the public on an open database. The names of individuals and corporations can be kept anonymous, but details on the number of investigations, the number of successful prosecutions, the number of settlements reached, the amount of money owed and repaid, and the penalties imposed, should be made public.

Rationale

Strong enforcement of existing legislation against tax evasion is important for creating a deterrent to prevent future abuses. Deterrents can also have the long-term effect of helping to create a "social norm of compliance" – a situation in which there is not just a legal but social expectation to pay taxes. Taxpayer studies have found that if tax compliance is considered a social norm, there is an

increase in voluntary compliance.[42] Stronger enforcement can contribute to improving both short- and long-term tax compliance.

Other research has compared the direct and indirect effects of tax investigations, where "direct effects" refers to revenues in the form of unpaid taxes and fines collected by the tax authority, and "indirect effects" refers to a measurement of the increase in tax compliance induced in the whole community of taxpayers, not only within those taxpayers being investigated.[43] Indirect effects can be hard to measure, but the results suggest that the indirect effect tended to be higher than the direct effect.[44] As previously discussed, CRA has acknowledged that its priority has been on value for taxpayers – the direct effect. We hope that when conducting their investigations and considering repercussions, CRA will consider the long-term indirect effect as well.

Cultivating a reputation of non-enforcement encourages risk-taking that can be extremely damaging to the economy. It also encourages the kind of behaviours exemplified by KPMG in the United States, when in 2003 it was found that the accounting firm declined to register their tax products are required by law because they did a cost-benefit analysis and decided the legal risk of non-compliance was outweighed by the financial benefits of not registering. Left to their own devices, MNEs will perform similar cost-benefit analyses and not comply with legal requirements, to the detriment of the government and the wider Canadian public.

Enforcement is not just important for tax abuses by consumer taxpayers or corporations. Individuals and corporations depend on the assistance and advise of facilitators to use tax havens. A stronger focus on gatekeepers and facilitators would help eliminate tax schemes at the source. There are already some penalties within the *Income Tax Act* for advisors who engage in reckless, negligent and willfully blind behaviour. Enforcing these would be an effective way to curb tax avoidance and outright evasion. The risk to facilitators of offering these services should be too high, even if the financial "reward" from client fees is significant.

Similarly, legislating a duty on lawyers and accountants under the *Income Tax Act* to report suspected evidence of avoidance and evasion and enforcing that duty, would go a long way to preventing tax abuse. This kind of legislation has a precedent in the United Kingdom, where the duty to report tax evasion and aggressive tax avoidance has been in place since 2002 under the *Proceeds of Crime Act*. Under the Act, all lawyers and accountants that suspect aggressive tax avoidance have a duty to report it to the revenue agency and a duty not to advise their client that they have done so. Neglecting this duty carries penalties up to a 14-year jail term. Faciliators cannot

[42] Marisa Ratto, Richard Thomas and David Ulph, "Tax Compliance as a Social Norm and the Deterrent Effect of Investigations," *University of Bristol*, July 2005 http://www.bristol.ac.uk/media-library/sites/cmpo/migrated/documents/wp127.pdf
[43] Ibid.
[44] Ibid.

be relied upon to regulate themselves, regardless of what some in the accounting and legal professional claim; government should and must take the lead on regulation.

While some professions in the industry may object on the grounds of confidentiality, in Canada the law does not recognize accountant-client privilege. The *Income Tax Act* covers privilege between lawyers and notaries, but not accountants.

Passing laws against current tax avoidance is important, but so too is upholding penalties already in place to punish and deter tax evasion. Canada must pair policy changes recommended by the OECD with the will to enforce the laws already in place. There is little point improving legislation if we do not enforce already-existing laws and regulations.

In the spring of this year, the government made the welcome announcement that it would crack down on tax evasion by committing $444.4 million over five years to the CRA to improve its investigatory capacity. The press release accompanying this announcement read, "The Prime Minister, Justin Trudeau, made a commitment during the campaign to strengthen the CRA and its ability to crack down on tax evaders. Today's announcement delivers on that promise."[45] It is our hope that delivering on this promise does not end just with strengthening the *ability* of the CRA to crack down on tax evaders, but extends to actually ensuring that CRA follows through and enforces penalties.

[45] "Government of Canada cracks down on tax evasion," Government of Canada, April 11, 2016 http://news.gc.ca/web/article-en.do?nid=1049689

Conclusion

We believe all approaches to tax fairness and combatting tax exploitation should be guided by the principles of transparency, accountability, and inclusiveness. In the context of our own recommendations, we would like to see transparency in the form of country-by-country reporting and beneficial ownership; accountability when it comes to taxing the digital economy, vetting tax products and enforcing existing penalties; and inclusiveness in terms of supporting developing nations call to bring conversation son international tax reform to the UN. We also hope that the Canadian government and all governments will continue to be guided by these principles going forward.

The OECD's BEPS Action Plan includes a number of important recommendations, but it is not the end of the line for tax fairness, or even for combatting base erosion and profit shifting. Instead, it is the beginning of a larger and longer conversation, one that we hope will equally value the perspectives of developed and developing nations, and that will privilege the voices of the people over those of corporations.

In order for the OECD's Action Plan or any anti-avoidance measures to be effective, they will need to be implemented by strong, progressive and forward-thinking nations. We believe that Canada, under this government, can be that nation. The conversation around tax justice is an opportunity for Canada, not only to drastically improve quality of life for its own citizens, working and middle class, men and women alike, but to lead by example on the world stage. We believe Canada is ready to be a model to other countries by putting its people first.

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