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The Honourable Wayne Easter

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● (1105)

[*English*]

The Chair (Hon. Wayne Easter (Malpeque, Lib.)): We'll call the meeting to order as we look further at Bill C-82, An Act to implement a multilateral convention to implement tax treaty related measures to prevent base erosion and profit shifting.

We have two witnesses: Patrick Marley, partner and co-chair of taxation at Osler, Hoskin & Harcourt LLP; and Toby Sanger, executive director of Canadians for Tax Fairness.

I assume you probably have opening remarks, and then we'll go to questions.

Who wants to start?

Go ahead, Toby. You've been here before.

I don't know if you have ever been here, Patrick.

Mr. Patrick Marley (Co-Chair of Tax Group, Osler, Hoskin & Harcourt LLP, As an Individual): No, I haven't.

The Chair: All right, it's a new experience, a new day.

Go ahead, Toby.

Mr. Toby Sanger (Executive Director, Canadians for Tax Fairness): Thank you very much, Mr. Chair, and members of the committee.

First of all, I'd like to express my condolences at the loss of a colleague and friend of many of you, former Ottawa Centre MP Paul Dewar. Paul was the same age as me. He was a neighbour and a friend. He always built on the positive side of people and situations all through his life of public service. He was devoted to the less fortunate right through to his final days, and I hope he inspires many others to do the same.

This legislation, Bill C-82, which would enable Canada and other countries to effectively implement wholesale changes to their numerous bilateral tax treaties is, in general, very much a positive step forward to reduce the hundreds of billions in revenues that are lost annually around the world from aggressive international tax avoidance, primarily by larger corporations. This represents approximately $1 billion in Canada, if you include everything.

This multilateral instrument is the culmination of five years work through the OECD's base erosion and profit shifting initiative. It's an efficient way of consistently adjusting the thousands of bilateral tax treaties that have been signed between nations in order to implement a number of action measures of the whole BEPS process. By having a generally consistent set of measures, it will limit but not entirely eliminate the practice of treaty shopping that many large corporations have engaged in to avoid taxes and drive a race to the bottom.

The introduction of these changes will be especially beneficial for lower-income countries by strengthening the rules for taxation based on the source of the economic activity and not the putative residence, often in the tax haven of the corporation. It will limit tax avoidance through hybrid mismatch arrangements that exploit differences in tax treatments, treaty abuse through double non-taxation, and the avoidance of permanent establishment. These are all positive measures.

At the same time, there are some concerns about the part IV provisions for mandatory binding arbitration, as these opaque and secret panels rarely favour source countries, and they should consider not opting into them.

Article 17 also has some problematic measures, and countries should consider making a reservation under this section.

While this bill and the 2015 BEPS initiative that it stems from are positive, they are limited. They are all about patching a system that has a lot of problems, and they are now about to be eclipsed by much more important and fundamental changes that need to be made to the international corporate tax system.

Two weeks ago, following meetings with almost 100 countries in Paris, the OECD issued a policy note entitled “Addressing the Tax Challenges of the Digital Economy”. In the words of Alex Cobham, chief executive of the Tax Justice Network, “The three pages of text in this...policy note may be more significant than the thousands that made up the BEPS project.”

The archaic arm's-length transfer pricing system that underlies our international corporate tax system, which this bill is trying to patch up in different ways, is so broken and ineffective for our new economy that major countries around the world, including the United States, the U.K., France, Germany and others are already leapfrogging it with a range of different measures to tax large digital corporations using different approaches based on their actual economic activity in their country.

National revenue authorities have found that the transfer pricing approach also enables traditional and resource sector corporations such as Cameco to easily avoid billions in tax. There has been a case of CRA taking Cameco to court, but the courts have sometimes sided with the companies over transfer pricing.

What we ultimately need to do is to move to a unitary international corporate tax system with an apportionment of corporate profits to different countries based on their share of sales, payroll and/or other factors, preferably with a minimum corporate tax rate. This is a very straightforward system, and it's exactly what we have in place in Canada to apportion corporate profits for tax purposes between provinces. It's also the system used by American states and other federal countries to apportion corporate profit. We have this in place within Canada and other countries. We need to move to this globally as well.

In addition to its simplicity, the beauty of this approach is that a global agreement isn't necessary to proceed. It's preferable that Canada could move forward in this way, just as the United States, the U.K. and other European countries are doing.

The other beauty of this approach is that it would increase tax revenues from multinational corporations by about 33% to 50% according to the IMF, and by significant amounts for lower-income countries, which are the ones most harmed by the existing system.

In conclusion, this bill is a positive step, but we can and must take much bigger steps forward to develop a more equitable and functional international corporate tax system, and it doesn't need to be that complicated. It's the smaller and medium-sized businesses that lose out, mostly from the international corporate tax system that we have right now. They often pay a higher rate of tax than do the large corporations that are able to exploit the system that exists right now.

Thank you very much.

● (1110)

The Chair: Thank you, Mr. Sanger.

Mr. Marley, the floor is yours. I believe you've given out a paper. Thank you.

Mr. Patrick Marley: Thank you for having me here today. I just want to start by saying that I, too, generally support Bill C-82 and the ratification of the MLI in Canada. However, I do have some important concerns that I want to mention to you with respect to the process and manner in which it's ratified and adopted in Canada. I'm going to break that down into four points. I'll touch on each of them in more detail.

The first is on the principal purpose test, which I think is one of the most significant aspects of the multilateral instrument. We're in dire need of more guidance on how that's going to apply in Canada. Because it's the result of an OECD project, where they strived to get consensus among a broad group of nations, the text is very broad and ambiguous, and the examples that the OECD has provided give very little practical guidance as to how it's going to work in practice.

In contrast, when Canada introduced the general anti-avoidance rule domestically, the CRA, at the same time, came out with a detailed information circular, going through different examples in how they would apply in Canada. I think more guidance is needed on the principal purpose test, particularly with respect to private equity and other collective investments, which is an area that the OECD has struggled with in terms of how that test should apply to collective investors. Really, there's a huge amount of capital that gets invested into Canada that way.

The second point is that I think Canada should be opting into article 7(4). We've currently reserved on that. I'll touch on why it's inappropriate to not have article 7(4) applying, and, really, the double tax or the unfairness that could result without that.

My third point is that Canada should continue to reserve on all of the changes to the permanent establishment threshold. I think that's consistent with the approach Canada has taken to date, and it's really for two reasons. One is that what we have now, in terms of when you have a permanent establishment, is effectively a bright-line test. It's easy to understand. It's well recognized. What the changes bring in the permanent establishment test is a lot of uncertainty, ambiguity, and, really, the ability for countries to argue that there's a permanent establishment when otherwise there might not have been. That, again, can lead to a potential explosion in tax disputes among countries, and could have negative implications for Canadian revenue.

The last point I was going to make is with respect to binding arbitration. I think we should continue to push for binding arbitration in as many treaties as we can. Our firm is perhaps the largest tax litigation disputes firm in the country. I can say, from working at Osler for the past 20 years, the amount of tax disputes in the country have really continued to expand year after year. Binding arbitration is really an effective process for resolving disputes among countries on allocating taxing rights and who should have the right to tax different countries.

To turn back to my first point on the need for more guidance on the principal purpose test, again, the test applies if one of the principal purposes of an investment is to avoid tax. It's often difficult to determine what is a purpose versus a principal purpose, let alone what all of the principal purposes are and whether tax avoidance was a principal purpose. Particularly, as I said, with private equity or other investments, I'll just give a quick example, obviously oversimplified, to illustrate that, together with, in my view, the need for article 7(4) to be applicable.

If you have two investors, one in the U.S. and one in India, each wanting to invest collectively into different countries, including Canada, what will generally happen in this example is the U.S. investor would not want to invest through an Indian company, the Indian investor would not want to invest through a U.S. company. What they would often do is form a holding company, in a third country, to invest collectively. That serves a number of business purposes, including raising larger pools of capital to make larger investments in, say, mines or other development projects.

In my example, if the U.S. and the Indian companies invest, say, in a Luxembourg holding company, the Luxembourg holding company, in turn, could invest in Canada or other jurisdictions around the world. In that simple example, under our current system, if Canada pays a dividend to the Luxembourg company, we would have a 5% withholding tax, which is the same withholding tax that would apply if the Canadian company paid directly to the U.S. company. However, it's different from what would apply if it paid a dividend directly to the Indian company, because we have a 15% withholding tax rate under the Canada-India treaty.

● (1115)

What happens under the MLI is that if the principal purpose test applies—if you determine, in my example, that tax avoidance was the purpose of using this Luxembourg company—then treaty benefits are denied. There's a 25% withholding rate applicable on dividends out of Canada, which is more than what would have applied if either the Indian or U.S. companies had invested directly. Article 7(4) turns off that tap, or allows Canada, in this example, to apply a 5% or 15% withholding tax rate rather than revert to a 25% rate, particularly if it was as a result of commercial reasons that the Indian and U.S. companies invested together.

Admittedly, that's an overly simplified example. What typically would happen is that you'd have a larger number of jurisdictions of investors. Obviously, the U.S. is a major capital-exporting country, so it's not uncommon for large pools of U.S. investments to come into Canada. It's often commingled with investors in Europe or Asia or other jurisdictions. Because we have 93 tax treaties, in most cases the ultimate investors are in one of those 93 countries. That's where the largest capital pools are.

I'll turn now to the “permanent establishment” changes. As I mentioned, if we opt in to that change, it would have a permanent effect, because the election is irreversible, and it would apply to a vast number of treaties. As I believe Stephanie and Trevor mentioned two days ago, Canada might win or lose on that. To give a quick example, in the resource sector right now, resource companies in Canada can sell their resources around the world and pay taxes in Canada based on not having permanent establishments in those other countries. If we were to opt in to that test, it would allow foreign countries in Asia or Europe or other jurisdictions to potentially tax some of Canada's resource profits by arguing that those resource companies have permanent establishments around the world in their jurisdictions based on facilitating contracts or facilitating access to the local markets. It creates significant uncertainty. The taxpayer will always lose, because they'd have to file returns in more jurisdictions, and potentially pay taxes in more jurisdictions, but Canada could lose because it could be ceding taxing rights to other jurisdictions.

As well, because it's such a fundamental change and is irreversible, in my view it should have parliamentary approval; an order in council and subsequent governments should not be allowed to make those changes. As we stand now, any significant changes to tax treaties go through Parliament. In my view, removing that reservation on the permanent establishment changes is of such significance that it should be something for Parliament to decide, and not be done by order in council.

Thank you.

The Chair: Thank you very much, Patrick. If that was a simplified example, I don't know whether I would really want to see a complicated one. It's obviously a complicated system.

Thank you both for that.

We'll turn now to questions, beginning with Ms. Rudd.

Ms. Kim Rudd (Northumberland—Peterborough South, Lib.): Thank you for your presentation. For some of us it's fascinating stuff.

I'll start with you, Patrick, with regard to one of your comments. Canada has decided to adopt some of the articles and provisions and hold back on others, which I would frame as a prudent approach. As we adopt them, they become permanent; we have no choice. We're in the game, if you will, by taking them. In your comments about some of the guidance, that you feel more guidance is required in some of the areas of those provisions and articles, I think it's really important to hear from folks like you. I'm very familiar with Osler's work and with how they are one of the foremost firms dealing with these disputes.

Perhaps you could tell us a little bit about one of the mechanisms that you think might be helpful, as each of these articles or provisions is looked at, in terms of whether or not it is in Canada's best interest to adopt them, and about what process you think might be useful for you and Toby and others to provide advice and counsel on that.

● (1120)

Mr. Patrick Marley: Sure.

First, in terms of which provisions Canada should adopt, some of them are mandatory, so—

Ms. Kim Rudd: Yes.

Mr. Patrick Marley: —I think that's kind of been decided already. Others are optional. I think your question is focusing more on the optional ones.

Ms. Kim Rudd: Correct.

Mr. Patrick Marley: My point on the guidance was really about the mandatory ones. That's what I wanted to confirm, because a limitation-on-benefits rule is easier to apply objectively—you know when it applies—but it's much more complicated and, therefore, it's generally done on a bilateral basis. That's the approach the U.S. has taken, and that's in large part why the U.S. has not signed on to the multi-level instrument at all.

Canada and a number of other countries have gone with the much more subjective, ambiguous and difficult to understand, but much easier to draft, principal purpose test. That's why I'm saying we need more examples of when the principal purpose test would apply. I think the OECD's were limited, because they wanted consensus among members and all members to be able to read each example in whichever way they wanted, to determine whether they wanted it to apply or not.

In my view, Canada should use much more difficult, real-life examples, to be able to then ask if there is a certain amount of substance required for this rule not to apply. What can businesses look to in determining whether it will apply or not?

I think a quick example is with collective investors. If there were any sort of threshold, would it be enough if 99% of investors had identical treaty benefits? Is 50% enough? Is there anything below 100% that would be sufficient not to apply the rule? If it requires 100%, I think it would be helpful if Canada at least said that it's 100%. That way, taxpayers would know to invest in other countries and to avoid Canada. They'd at least get a sense of what their after-tax returns would be. After-tax returns are quite simple: they are just your revenues, costs and taxes. If you take one of those three factors, the tax part, and make it unclear what taxes are going to apply, either on distributions or on a sale, then investors won't know how to properly value that investment.

Ms. Kim Rudd: Okay, thank you.

You mentioned article 7, paragraph 4, as something that is of concern to you. The way I'm reading it, through all of this wonderful research we're able to get from the Library of Parliament and other places, is that the principal purpose test is really to prevent treaty shopping and abuse. That is the intent of it. Could you elaborate? I think you're suggesting that the principal purpose test doesn't do that.

Mr. Patrick Marley: To clarify, I'll go back to my example, and I'll try to make it—

Ms. Kim Rudd: The Luxembourg example?

Mr. Patrick Marley: Yes, the Luxembourg example.

You're absolutely right. If it's determined that one of the principal purposes, in that example, for using a Luxembourg holding company, is to invest into Canada, the principal purpose test turns off treaty benefits under the Canada-Luxembourg tax treaty. For dividends, Canada would impose a 25% withholding-tax rate on dividends to Luxembourg. Article 7(4) says that even if we're applying the principal purpose test, countries like Canada are nevertheless allowed to apply whatever withholding tax rate would be reasonable in the circumstances, rather than applying our full 25% withholding-tax rate.

If your ultimate investors in this example could have been entitled to either a 5% or 15% rate, it would be reasonable in the circumstances for the CRA to apply either a 5% or a 15% withholding rate, rather than the 25% withholding rate, which is what I think we have under Bill C-82.

● (1125)

Ms. Kim Rudd: The presentation we had on Tuesday really delineated between the TIEAs and the tax convention treaties. I guess the MLI does not apply to the TIEAs. I wonder if you could talk a little bit about those differences. When I was listening to your presentation, I felt that maybe it was a bit conflated, but I could be wrong.

Mr. Toby Sanger: Sure. I could speak a little bit to it, but my main point here is that this is patching up a system that has a lot of holes in it, and we need to move towards a new system in the broader sense of taxing international corporations in this way.

I'm sorry—

Ms. Kim Rudd: No, I'm sure someone else will answer the question.

Mr. Toby Sanger: —but I didn't follow the presentation on Tuesday.

Ms. Kim Rudd: No, I just didn't have much time to frame it, so I'll pass.

The Chair: Thank you.

Mr. Kmiec.

Mr. Tom Kmiec (Calgary Shepard, CPC): Mr. Marley, first, at the very end of your presentation, you talked about resource companies that sell their commodity product worldwide. Is there a possibility in the permanent establishment test provisions that if we opt in or stop withdrawing from those provisions, those companies could be taxed in the future on that?

Can you just elaborate a little bit more? Which articles are you speaking of specifically? There are the optional ones in articles 10, 12 and 13, but if there are others, can you just explain how that might work if we were ever to opt in?

That's the first part of my question. I want to talk to you more about what you said about how Parliament should be the final arbitrator on whether we should be participants in it rather than it going through the order in council process. I'd like to hear you talk more about how this could potentially affect resource companies.

Mr. Patrick Marley: Sure, and again, I'm just using resource companies as a simple example—

Mr. Tom Kmiec: I'm from Alberta.

Mr. Patrick Marley: —but it can apply across industries, just to be clear.

I'm going to simplify, as much as I can, international tax and try to translate from tax to English, but please excuse me if I don't get fully out of tax.

What tax treaties do is to really allocate taxing rights between a residence country and a source country. For a source country, generally, if you have a permanent establishment, then you're carrying on business in that country, and that country has a right to tax, really the primary right to tax. The residence country would then give a tax credit to avoid double taxation. That's the normal process.

So right now, if Canada is both a residence and a source country by virtue of Canadian resources being sold around the world, Canada is taxing 100% of the profits and the foreign countries where those resources might be consumed are not taxing the profits from that business. If in turn the Canadian company does have a permanent establishment in those foreign countries, then those foreign countries would have the primary right to tax those profits—any income attributable to that permanent establishment. Canada would then lose the tax revenues, because instead of taxing 100% of the profits, Canada would be giving a foreign tax credit and ceding some of that tax to the foreign country.

The articles you just referred to relate principally to what we call an “agency permanent establishment”. Under the current treaties, that occurs if contracts are concluded in a particular jurisdiction. In my resource example, if the contract to sell the resources is concluded out of Canada, then only Canada is taxing those profits. If the contracts are concluded in the foreign jurisdiction or if somebody in the foreign jurisdiction is concluding those contracts on behalf of the Canadian company, then the foreign country would have the ability to tax some of the profits.

These changes take away that bright-line test of whether that agent in the local country is concluding contracts, and it changes it to ask in general—there are a few options—whether the person in that foreign country is conducting activities that assist in or facilitate or generally result in the conclusion of contracts, and if so, that's enough to have a permanent establishment.

It's very ambiguous what level of activity is needed in that foreign jurisdiction in order to create a PE, so the concern again is that if you had somebody in a foreign jurisdiction helping to find a purchaser for your products, depending on their level of activity and their involvement and whether it leads to contracts, that could be enough for the foreign jurisdiction to say that that Canadian company has a permanent establishment in their country and so they're going to tax the profits. Then, if Canada also taxes the profits, we either have double taxation or we go potentially through binding arbitration or a mutual agreement process to determine how much profit should be allocated to the foreign country, and then those foreign taxes take away from the Canadian revenue because we provide a credit for those taxes.

● (1130)

Mr. Tom Kmiec: Those scenarios would only happen, though, if Canada were to participate in articles 10, 12 and 13?

Mr. Patrick Marley: That's correct.

Mr. Tom Kmiec: Then articles 12 and 13 are those we have reservations about from what the officials from the department said, in that there aren't many participating countries in them and therefore Canada won't participate. I would assume that if this were to change, there potentially would be a review of the situation in the future.

Does the fact there are not many participants in it give you any confidence that this probably won't be used in the future? There are not many participants today, and maybe many countries are having the same discussions with their tax experts and saying this is not worth going into because of this potential tax leak—I'm not sure if that's the appropriate term for it—or tax losses that would be incurred.

You talked about the change in process here, where Parliament would no longer be deciding whether we can participate in any of these particular clauses. There will be an order in council process, which is something that I dug into with the officials a bit more. Can you elaborate a little more about your concerns around that?

Mr. Patrick Marley: Sure. My concern is that those changes, the permanent establishment changes in particular, in my view, would be significant changes to our tax treaties. They're not just minor changes that would only affect a couple of companies and a couple of industries. It could affect virtually all cross-border businesses and could result in Canadian companies having to file tax returns, for example, in many countries around the world and having many countries around the world having a right to tax those Canadian profits.

Also, then, in many cases it could result initially in double or triple taxation or an infinite level of taxation. It would result in much more administrative compliance and much more difficulty in determining where your profits ought to be allocated, but also in many more disputes and, as I said, to the extent that profits are allocated to those foreign countries, it could result in a loss of revenue in Canada.

I think the reason that many countries have reserved on those rules is really for those exact reasons.

I think these are only the countries that would be confident that they would always win on expanding the PE threshold because, obviously, investment can be inbound and outbound. If a country is of the view that you're always going to win—perhaps if it's not resource-rich, for example, I guess, or if they think there are more capital inflows than outflows—then they might be inclined to make those changes.

Mr. Tom Kmiec: Just as an example, then, like Luxembourg...?

Mr. Patrick Marley: Yes, Luxembourg—

Mr. Tom Kmiec: I'm not sure if they're participating. It's just an example. It's not a resource-rich country but has large capital flows.

Mr. Patrick Marley: Right, but I believe they have a lot of capital inflows and outflows, so I'm just not sure what their position would be.

The Chair: We'll have to leave it there and go to Mr. Dusseault.

[*Translation*]

Mr. Pierre-Luc Dusseault (Sherbrooke, NDP): Thank you, Mr. Chair.

I'm pleased to be back at the Standing Committee on Finance and to discuss my favourite topic.

So far, the interesting thing about the debate on Bill C-82 is that the government is confirming, and admitting, that tax treaties are useful to people who want to abuse the Canadian tax system. It said openly, on Tuesday, and this is also found in its documents, that tax treaties can be abused. This is indeed the case, and I have two quotes in English to prove it.

The first quote is from a lawyer with the Rogerson Law Group, located on Bay Street, in Toronto. The lawyer explained how to take advantage of the tax treaty with Barbados. His article is entitled

● (1135)

[*English*]

“Taking Advantage of The Double Tax Treaty with Barbados”.

At the end of the article, in describing how to take advantage of this, he says:

> The net result of the above is as follows. A Canadian resident corporation establishes a foreign affiliate in Barbados in the form of an IBC. The IBC makes $100 profit. Barbadian tax on the profit is levied at 2.5% leaving $97.50 to be remitted by the Barbadian foreign affiliate to its parent company in Canada. The parent company receives the dividend completely free of Canadian taxation.

An IBC is an international business corporation.

It's clear. The fact is, it's so clear that you don't even have to read between the lines. It's legal to do that.

Another proof of this is from what's called “Barbados Offshore Advisor”. An adviser based in Barbados says:

> The foreign office must have “mind and management” on the island to qualify for attractive tax incentives. By providing an out-of-the-box solution with a full team at your disposal, service providers eliminate the human resource hassles and expensive start-up costs involved when opening an overseas office. Our team is responsive to your company's needs, providing rapid turnaround and dedicated management.

[*Translation*]

At this time, the most well-known and abused treaty is the treaty with Barbados. Do the witnesses also believe that tax treaties, such as the treaty with Barbados that has been in effect since 1980, are being abused, and that, as a result, Canadian taxpayers have lost billions of dollars in tax revenue?

[*English*]

The Chair: Who wants to take that on? My question in addition to Mr. Dusseault's is, can that really happen legally? Can it be done under this act?

Who wants to respond? Toby?

Mr. Toby Sanger: Sorry. Was that a question about whether this...?

Mr. Pierre-Luc Dusseault: The question is, do you characterize those conventions as potential places to abuse the tax system? Those examples are openly accessible on the Internet, how to abuse the Canadian tax system with the Barbados and Canada convention.

Mr. Patrick Marley: Our responses might be quite different.

Mr. Toby Sanger: Well, you go ahead.

Mr. Patrick Marley: Okay.

I'd start by saying that the Canadian tax system cannot be abused by just shifting profits, passive income, into Barbados or any country. That isn't affected at all by this multilateral instrument or Bill C-82. It's our detailed foreign accrual property income, or FAPI, rules.

We have a detailed anti-deferral system that has been developed and enhanced over several decades. It's aimed at taxing in Canada on a current basis any passive profits or income with sufficient connections to Canada, immediately in Canada, whether it's in a tax treaty country such as Barbados, a tax information exchange agreement country such as the Cayman Islands, or a country in which we have no treaty whatsoever. I don't find abusive in any way the fact that some countries impose low rates of tax.

A good example would be that if you want to open a hotel in Barbados, you might pay a low rate of tax in Barbados, but that allows you to compete with other hotels in Barbados, and that's a very appropriate result. Our FAPI regime is for stopping investment activities in foreign countries, and that's what our other anti-deferral rules are for. That has nothing to do with the tax treaty process.

Mr. Pierre-Luc Dusseault: Do you agree that some Canadian companies use Barbados as a place to do offshore business in other countries? Instead of doing their business from Canada, they use an offshore company in Barbados to do all the offshore business. Do you agree that it's how we characterize the use of Barbados?

● (1140)

Mr. Patrick Marley: Maybe it's the ambiguity in your question in the sense that I don't know what type of business you're talking about. If it's an active business, then Canada does not tax the profits. If it's passive income, Canada does tax the profits. That's the case whether it's in a treaty country or a non-treaty country. The system really just derives off whether it's an active business or not. Again, you can earn active business income in, say, the Cayman Islands, where we don't have a tax treaty, and Canada is not going to tax those profits. That's separate from the tax treaty process.

The Chair: Toby.

Mr. Toby Sanger: There is a ton of grey area in the application of legislation and our rules, but whether things constitute aggressive avoidance or evasion in different areas, 50% of Canada's foreign direct investment overseas is in the finance and insurance sector and 25% of our foreign direct investment is in countries that are considered to be tax havens in those ways. Certainly they're being used to avoid taxes in Canada in different ways, and there are complex arrangements around the world to do that.

[*Translation*]

Mr. Pierre-Luc Dusseault: It's certainly no coincidence that, according to the foreign direct investment statistics, Barbados ranks second or third each year, behind the United States or Great Britain. I've never received an explanation for why Barbados is the country where Canada makes the most foreign direct investments. Apparently, it's very profitable to build hotels in Barbados, which is why so much money is invested in the country.

However, the real reason is as follows, and it's even explained by the lawyers who work in the field and who help companies. Companies conduct foreign trade in countries with low tax rates rather than remaining strictly Canadian companies. The companies open subsidiaries in Barbados for all their foreign trade rather than remaining Canadian companies without subsidiaries anywhere in the world. Companies use the low tax rates in these countries, regardless of whether Canada has information exchange agreements or treaties with the countries.

[*English*]

The Chair: We'll have to see if we can get fairly short answers here because we're well over time.

Patrick.

Mr. Patrick Marley: I'll just be very quick. I think your question is largely addressing our broader domestic international tax system and not the tax treaty network, which is what this addresses. I think your question is more aimed at our FAPI regime and our domestic anti-deferral regime. I just don't think it touches on Bill C-82.

[*Translation*]

Mr. Pierre-Luc Dusseault: For the convention to be applied by both countries, such as Canada and Barbados, they must not only sign it, but also ratify and implement it. Is that correct?

I'm worried about the fact that Barbados signed the convention on January 24, 2018, but has never done anything more to date. The danger is that Barbados signed the convention only to please the rest of the world and that, unlike Canada, it won't pass legislation to implement the convention.

[*English*]

The Chair: We're going to have to end it there and go to Mr. Fragiskatos.

Mr. Pierre-Luc Dusseault: Can one of them answer whether it is true that both sides need to ratify?

The Chair: Can you give us a quick answer on that last question, either one of you?

Mr. Patrick Marley: The changes in the MLI don't take effect unless both countries to that ratify it—

Mr. Pierre-Luc Dusseault: And Barbados won't do it.

Mr. Patrick Marley: —but it's not relevant to....

The Chair: Mr. Fragiskatos.

Mr. Peter Fragiskatos (London North Centre, Lib.): I want a chance to set the stopwatch here to make sure that I stay on time, Mr. Chair.

The Chair: I'll make sure you get all of your time. Pierre got two minutes more.

Mr. Peter Fragiskatos: I appreciate the passion of my colleague opposite. I say that sincerely.

Thank you very much to both of you for being here this morning.

I have a few questions. They are general ones because I think we're still trying to get a very general sense of the issue. It's complex, but it's highly important. Both of you have worked on it, and it's appreciated.

First of all, Mr. Marley, is it possible for one agreement to address all the tax avoidance problems a federal government could face?

● (1145)

Mr. Patrick Marley: That's quite clearly “no”.

Mr. Peter Fragiskatos: Okay.

Mr. Patrick Marley: That's really by its nature. The multilateral instrument is really just meant to be an effective way of making uniform changes to all tax treaties around the world. That's the goal of it. As a result, it's limited in terms of what you can put into it with regard to things that Canada as a country would agree, in all of our treaties or most of our treaties, to give up.

It doesn't get into that bilateral negotiation of “I'll give you something if you give me something.” As a result, particularly on the anti-avoidance side, it has to be broad and ambiguous to give tax authorities around the world the ability to apply it in the way they would want to, even though that's going to create a lot of uncertainty for taxpayers.

Mr. Peter Fragiskatos: I appreciate that.

Basically, we have a step in the right direction. It's something that is addressing a number of issues, but it's not a panacea and, by definition, it can't be. It's not a magic wand.

Mr. Sanger, what do you think on that? Is it possible to have...? I know you have a number of issues with this particular agreement, but I think it's reasonable to say, as we just heard from Mr. Marley, that you can't capture tax avoidance problems—call it base erosion and profit shifting if you want to get technical—in one agreement. We can't deal with that challenge in one agreement.

Mr. Toby Sanger: No, you can't. As I said, this is an attempt at patching up a system that's, I would say, broken. Countries are moving beyond it. There's been a lot of discussion about what the definition of a permanent establishment would be in different areas. That's really problematic.

Mr. Peter Fragiskatos: So, we're patching—

Mr. Toby Sanger: Some of the exemptions or reservations that are being suggested, I think, would perpetuate some of those problems.

Mr. Peter Fragiskatos: We're patching things up.

Mr. Toby Sanger: I do think that we need to look at the system not just in terms of the self-interest of some sectors that might be represented in Canada. Canada is home to about 50% of the mining companies around the world.

Mr. Peter Fragiskatos: I appreciate that you're opposed to....

I'll have to interrupt you because I have limited time, Mr. Sanger.

Mr. Toby Sanger: Okay.

Mr. Peter Fragiskatos: I appreciate that you have issues with mining companies and I would suspect with many companies.

Mr. Toby Sanger: Yes.

Mr. Peter Fragiskatos: That's not the point here. The point is, as you put it—to be fair to you—that it's a patch.

Mr. Toby Sanger: Yes.

Mr. Peter Fragiskatos: With a complex matter like this, I think we have to proceed in a way where we are addressing things in an incremental approach because addressing the problem with one fell swoop is bound to create all sorts of uncertainties and questions. I don't think you can do it that way.

Can I go back to Mr. Marley?

Bill C-82 is a bill that all parties supported at second reading, which is very encouraging.

What's good about this? What's good about the MLI? I that know you pointed to some concerns that you have with it, but, if I remember from your earlier testimony, you said that you're generally supportive of this bill.

Why are you generally supportive? What's good here?

Mr. Patrick Marley: There are two main benefits, I think. The first is that this is a very efficient process for amending tax treaties. This is the first time that the OECD or other countries have done this. Traditionally, Canada does all our negotiations on a bilateral basis. To amend over 70 of our tax treaties would likely take a decade just as a practical matter because it's a very slow process to amend bilateral treaties.

Mr. Peter Fragiskatos: You say it would likely take a decade.

Mr. Patrick Marley: I don't want to speak for the Department of Finance on how fast they could get it done, but—

Mr. Peter Fragiskatos: It's just an estimate.

● (1150)

Mr. Patrick Marley: It would certainly take a lot longer than this process will take.

The first benefit is the efficiencies. The second benefit is the focus on the other mandatory aspect of this, which is dispute resolution. Even though the binding arbitration is optional, I think anything that we can do to not clog the courts up more than they are now is a good step in the right direction.

Mr. Peter Fragiskatos: Right. It's about efficiencies. I'm tempted to ask you about the arbitration element of this. I think it's a really important part, particularly from an efficiency perspective.

I know it's just an estimate, but you talk about it taking 10 years if we wanted to have a bilateral approach. The amount of money, the amount of tax, that could be sacrificed in that period of time is no doubt substantial.

Mr. Patrick Marley: It's hard for me to estimate what the amount would be.

Mr. Peter Fragiskatos: I have one more minute, if I'm not mistaken, Mr. Chair.

You've hinted at this, but I think it's proper to capture it as I'm summing up here. I always like to look at things from a counter-factual perspective. If we didn't have the bill in place, what would be the results?

I know you're going to talk about bilateral approaches, but we're really dealing with inefficiencies, right?

Mr. Patrick Marley: I think that's right. We could always renegotiate any of our tax treaties on a bilateral basis. As you said, if you wanted to negotiate bilateral treaties quickly, that could be done by just having more people within the Department of Finance involved in that function and meeting on an expedited basis with our counterparts.

Mr. Peter Fragiskatos: From your perspective, it's a step in the right direction, generally speaking? With the proviso that you do have some reservations, but generally speaking, we're going in the right direction.

What I take from your comments—and this is the last point, Mr. Chair—is that there's more to do. This is an important patch, as Mr. Sanger said, but we are moving in a positive direction.

Thank you very much for your testimony this morning.

The Chair: Mr. Kmiec for five minutes.

Mr. Tom Kmiec: I won't time you this time, Mr. Chair. Wait until in camera.

The Chair: Okay.

Mr. Tom Kmiec: On article 17, you mentioned in your opening remarks that you saw some problems with it. Article 17 is one of those reservation clauses, dealing with pricing and the corresponding adjustments that Canada is opting into.

Could you elaborate a little bit more about the problems you have with that particular provision?

Mr. Toby Sanger: Yes, I mentioned two. There's been discussion about mandatory binding arbitration. That's a concern because these panels meet in secret. There's not much transparency. It puts a lot of the source countries at a disadvantage on that.

In terms of the elements of article 17, it would require other countries to also adopt similar provisions on this, in terms of the relief from what they've called “economic double taxation” from transfer pricing. Some countries will want to opt out of that as well.

Mr. Tom Kmiec: Okay.

Mr. Patrick Marley: Could I make one quick comment?

Mr. Tom Kmiec: Sure.

Mr. Patrick Marley: I think article 17 is very important to have because it avoids the double taxation that could otherwise happen. If countries are in a dispute as to what the arm's-length price is and then finally agree on what it is, unless you have the corresponding adjustment, you're always going to have double taxation, which is what the treaties are trying to avoid.

Mr. Tom Kmiec: You mentioned that the problem with some of the arbitration is that it's done in secret. It's parallel to the problem of allowing us to opt into the different provisions the government has chosen not to opt into at this point. Equally, with orders in council or cabinet-level decision-making, there are no extensive minutes. The debates are not published. There's simply an order in council, an enumerated number that's published along with the year that says in one line what the decision is about. It doesn't provide a debate.

I'm asking, because it's something, Mr. Marley, that you brought up with some of the other provisions related to permanent establishments—articles 10, 12, and 13—that right now Canada is reserving its position on. In the future, though, by cabinet decision, we could be opted into it. We could withdraw our opposition to it. Then we could go into it without having a parliamentary debate and broader discussion on it.

Is that the right way to go? Should we, then, amend this bill and provide for that parliamentary review of certain optional sections of this international tax treaty—the “tax treaty of tax treaties”, as I called it in debate—or should we just leave it as it is at the cabinet level?

● (1155)

Mr. Toby Sanger: I agree with greater transparency. I think there should be greater transparency both in terms of the arbitration panels for.... Lower-income countries are at a disadvantage. They don't have expertise in that, and I'd absolutely agree about the need for transparency in making changes to the legislation.

This ends up being very complex legislation, and the application of it is complex. You have a number of law firms and highly paid accounting firms that employ their resources to deal with these issues. I think it's extremely important that we move to assist them in a way that is simpler and fairer for all companies. I want to underline the point that it is the larger corporations, in particular, that can most take advantage of these provisions and can afford to hire the higher-priced—

Mr. Tom Kmiec: Tax lawyers and tax accountants.

Mr. Toby Sanger: Yes, exactly.

Mr. Tom Kmiec: They're also the most exposed to it, on the other side, because they also do more business overseas—

Mr. Toby Sanger: That's right.

Mr. Tom Kmiec: —and so they have transactions they're doing everywhere.

Mr. Marley, can I ask you, then, with these arbitration panels, what would be a side effect of making the process more public? Have you participated in such arbitration panels in the past with different countries?

Mr. Patrick Marley: I have not, but I can say that, from the Canada-U.S. treaty perspective, they are not public. Neither Canada nor the U.S. publicizes the decisions. I believe, under U.S. law, once they've had a certain number of decisions, they're required under U. S. law to say what the statistics are.

I think the reason that countries have not made these public is to ensure that the process works effectively. In a sense, it's baseball-style arbitration, with each side coming in with one particular number and then the arbitrator chooses between one or the other. That's the process that Canada has followed.

I believe that style of arbitration works best if it's not public. What you want is for each side to come in with what they think is the realistic right answer and not, if it's for public consumption, be thinking about what impact that position might have on other taxpayers in other circumstances. Then they might be less willing to compromise and come to a result in that particular case.

Mr. Tom Kmiec: Thank you.

Mr. Patrick Marley: I think that's why it should not be public.

The Chair: Thank you, all.

Mr. Fergus.

[*Translation*]

Mr. Greg Fergus (Hull—Aylmer, Lib.): Thank you, Mr. Chair.

I have a question for you, Mr. Marley. Canada has already adopted general anti-avoidance rules. How is the situation different from the situation surrounding the multilateral convention?

Mr. Patrick Marley: Sorry, but I don't speak French.

[*English*]

What's different in this treaty? You're right, we do have a general anti-avoidance rule that does apply to tax fees. You mentioned tax evasion. Tax evasion is criminal activity, which isn't impacted at all —

[*Translation*]

Mr. Greg Fergus: You're absolutely right. Sorry, I didn't mean that, I meant that we must look for the best return. We've adopted rules to ensure that people pay their taxes, right?

The multilateral convention has created an international agreement. What's the difference between the two provisions?

[*English*]

Mr. Patrick Marley: I think the rule in the treaty is very broad and similar to our domestic GAAR. I think, as Stephanie and Trevor mentioned two days ago, in the government's view this is going to expand on our domestic anti-avoidance rule, and will therefore capture more circumstances like the one that Trevor mentioned in the MIL case.

This is new, in the sense that it expands on that domestic anti-avoidance rule.

[*Translation*]

Mr. Greg Fergus: If that's the case, then adopting these provisions is the same thing, in principle. Why do you have specific concerns regarding the multilateral convention?

[*English*]

Mr. Patrick Marley: There are two specific concerns. One is that because we're introducing this identical wording in so many treaties around the world, I think it subjects Canada to the uncertainty of following tax decisions of foreign countries around the world interpreting the identical provision in similar circumstances. It adds more uncertainty in international jurisprudence and how it might interpret it. Also, with our domestic general anti-avoidance rule, we have a few decades of jurisprudence. We know when it applies. We know who has the onus for proving different things. The onus is on the Crown to show the object and purpose of a particular rule under our domestic rules. That's appropriate because the Crown is drafting those rules. They're in the position to know the object and purpose.

In the multilateral instrument, it's unclear who has the onus of proving that. I think that's just one example of additional uncertainty that will arise, because if a taxpayer has to prove the object and purpose of a particular treaty provision, that will be very difficult because the taxpayer wasn't the one who negotiated the treaty to begin with. I think the onus should remain on the Crown, but it's unclear how that will be interpreted.

● (1200)

[*Translation*]

Mr. Greg Fergus: Mr. Sanger, do you have any comments or do you want to answer my questions?

[*English*]

Mr. Toby Sanger: Your question was partly, what is the point of this? I agree with Mr. Marley that it's important to have some consistency in international agreements on this.

I do have concerns about some of the suggestions he's had in some of the reservations in these areas. I recognize there may be some jurisprudence in that. It's also important that we have some international consistency in these rules as well, so that the whole multilateral instrument itself doesn't become a piece of Swiss cheese.

Mr. Patrick Marley: I left out one important part.

The CRA has said that they intend to apply the domestic GAAR and this principal purpose test simultaneously.

[*Translation*]

Mr. Greg Fergus: I gather that the CRA said that it would apply both simultaneously, until a list of decisions has been developed at the international level, which could be added to our Canadian rules.

[*English*]

Mr. Patrick Marley: Domestically, we have safeguards in place in the sense that we have a GAAR committee that is designed to ensure our domestic GAAR is applied consistently across the country. The hope is that same GAAR committee would also consistently review all applications of the principal purposes test to have those domestic safeguards in place.

As you said, I think CRA's published position to date is that they would apply both at the same time. This would cause a significant increase in tax dispute litigation time and expense, fighting two different rules as opposed to one in determining whether one or the other applies.

The Chair: I'm sorry, Greg.

● (1205)

Mr. Greg Fergus: Mr. Chair, just for the information of the colleagues, in case the translators didn't capture it, GAAR is the general anti-avoidance rules.

The Chair: All right.

Mr. Kmiec.

Mr. Tom Kmiec: I was going to ask what GAAR was, so thank you. That's very helpful.

I'm getting a little worried, because it's now all starting to make sense. I start to get worried when anything tax law-implicated starts making sense and I'm down in the weeds a little too much.

Can I ask you something I asked the officials? They said they had no real concerns about it, but my question is about the USMCA and how this convention would apply to agreement, because we are highly integrated in the North American market. The government has completed negotiations on it. It awaits ratification. However, the United States is not a party to this, and we do have a tax relationship with the United States. Mexico is a party to this.

Mr. Marley, I'm looking at you, because you come from the company side here. Will there be an impact? Is there an impact? What are some of the points at which this particular treaty's provisions will not fit well with either the new provisions in the USMCA or some of the old NAFTA provisions? Are there any touch points there that we should be looking at, as well?

Mr. Patrick Marley: In short, this should not impact the USMCA. I believe the Department of Finance officials mentioned it.

From a U.S. perspective, the U.S. has detailed an objective and "easy to understand whether they apply or not" limitation on benefits rules in their treaties both with Mexico and Canada. For cross-border investments with the U.S., then, it's just an exercise of going through those detailed rules and determining whether treaty benefits apply, and you will know whether they apply or not.

With respect to Canada and Mexico, we're going to have a principal purposes test once this is ratified in both Canada and Mexico. For investments between those countries, then, it's going to be the ambiguous principal purposes test to determine whether treaty benefits apply.

That's separate, as you said, from the USMCA, though, because I think the USMCA just does not impact on whether treaty benefits apply between Canada, the U.S. and Mexico.

Mr. Tom Kmiec: Our relationship then with the United States is clear just on the principal purposes test. It will be less clear with Mexico after this is ratified through our parliamentary process.

Mr. Patrick Marley: That's correct, because it will be less clear whether treaty benefits apply in any particular circumstances. In other words, there will be a risk that the tax authorities in either Canada or Mexico could seek to deny treaty benefits, and then you would have to go through the expensive and time-consuming process of going to court to prove them wrong.

Mr. Tom Kmiec: I want to pick up where Mr. Dusseault left off in his round, in talking about Barbados, because Barbados is one of the signatories to this convention. I went through the list of countries, looking at who was signing on and who wasn't. I see that the People's Republic of China has signed on. I see South Korea—and not Korea in general—the United Kingdom, and some really major countries.

However, just from my time on the foreign affairs committee, I know that places like Barbados—and there are other countries out there too—sign on to a lot of international agreements, but they never really go through the ratification process. What will be the impact of several countries in this not going through the ratification? They just sign on, and then they stop right there and don't continue with ratifying it.

Mr. Patrick Marley: I think the OECD has established a process to ensure that this doesn't happen, in the sense that, because there were certain minimum standards agreed to, the OECD also established a peer review process whereby they would review each country to determine whether it has complied with the minimum standards. Really, the stick, so to speak, is pressure from the OECD and other jurisdictions to ensure that the countries abide by the minimum standards in one of the different optional ways they can do so.

Mr. Tom Kmiec: Can you explain what the minimum optional ways are?

Mr. Patrick Marley: I'm sorry. With respect to this main treaty-shopping point, the optional ways are either a detailed limitation on benefits route, which is what the U.S. has done, or a principal purposes test-type rule, which is what Canada and Barbados have signed on to in the MLI.

Mr. Tom Kmiec: You've talked a lot about the principal purposes test and your worries around the extra ambiguity in the text that will be the result of it. I'm almost afraid to ask you, but can you give me a simple example?

Mr. Patrick Marley: I'll give you an overly simplified example, so we'll take it with that caveat.

When you invest in an RRSP in Canada, you might ask what your purpose is of investing in an RRSP. Is it to save for your retirement, or is it to avoid tax by getting a deduction on your RRSP contribution?

If you ask 10 different individuals, they might give 10 different answers. Some might say they did it just for retirement. Some might say they did it because they wanted the deduction. Many would say they did it for both reasons.

What this principal purposes test would do, if it applied to an RRSP deduction, is allow the government to step in and determine whether it thought the tax savings was one of your principal purposes, and if it were, then it would deny that deduction.

But I just use that as an example where it's difficult to determine at what point a purpose becomes a principal purpose, and whether it's one of your principal purposes. Quite frankly, in making any investment in any country around the world, if you don't take into account the tax result, you're negligent. It's part of computing your after-tax returns.

Because tax is always considered, it's very difficult to determine at what point you just considered the tax results and at what point it became your principal purpose.

And finally, on my RRSP example, I would say that it shouldn't matter in that example whether one person's purpose was retirement savings and another person's purpose was to get the current deduction. We should treat them equally, regardless of what their purposes were.

That's my other concern with the test is that it doesn't necessarily treat equal taxpayers equally because it bases the result on what their purpose was, as opposed to what they objectively did.

● (1210)

The Chair: All done?

Mr. Tom Kmiec: Quite.

The Chair: Mr. McLeod.

Mr. Michael McLeod (Northwest Territories, Lib.): Thank you to the witnesses here today.

Mr. Chairman, it's not very often that we have witnesses who come to present to us who are familiar with the Northwest Territories, and even less often do they know the community where I come from, called Fort Providence. It's a small aboriginal community along the Mackenzie River. But today we have a witness who has family who will be visiting my community. I was shocked to hear that, and I really hope she has a good visit.

There have been some comments in your presentation that point to the positive nature of this change. I think you said it was a positive step forward. I also heard that this was a positive measure.

I also heard Mr. Sanger mention $1 billion in Canada. I think that was the number you used.

Over the last while when we have talked to our witnesses, we have tried to see how big the problem actually is. Is there any way you can frame that for us, to the best of your knowledge? What impact would this piece of legislation have on that? I'm trying to get a handle on how well this would work? Do you expect it to cut it in half?

Mr. Toby Sanger: Well, it all depends on what provisions are included or not. Just following up on the discussion about the principal purposes test, it's an essential part of this and I hope that it isn't weakened going forward.

The estimates from some people in the industry are that it might increase payments from corporations by about 10% or 15%, so it's on a really significant bed. It's going to involve some patchwork in certain areas, but certainly it doesn't get at the magnitude of the problem.

It's hard to determine this, partly because a lot of this information is kept secret. We don't have information on where assets are kept and how corporations book their profits, as you probably know. A company like Apple, which I happen to have had the fortune to get some stock in, years ago, claimed it didn't have permanent residence in any particular country at that time. This is a significant thing.

The lower-end estimates from some international experts for how much Canada loses in this area are about $8 billion in revenue. Now that's not all related to corporations, but about two-thirds of that is corporations. It's a significant amount.

But it's an even higher share of the revenue from lower-income and developing countries. There is concern about the mining sector in Canada and preserving that, but it is the lower-income countries that lose out by taking advantage of these tax laws.

We can look at things in our own self-interest, but I do think we really do need to adopt some rules that are uniform, in the same way that we have in Canada, which we agree are fair for everybody involved around the world.

● (1215)

Mr. Michael McLeod: I'm not sure who mentioned it, but there was also a reference to the lack of binding arbitration, I think it was, in this provision.

Can you give us an example where its used in other agreements that maybe some other countries are using and where it works well?

Mr. Patrick Marley: Maybe I'll start with what it was modelled after, which was major league baseball. I think it's working extremely well there. When baseball players were up for free agency, there used to be a long and drawn-out process, and it was very difficult to get the players and the owners to agree.

What especially works well here is that, because we're following that baseball style, each country is required to come out with a final offer that's reasonable and likely to be accepted by the arbitrator.

The arbitrator can't saw it off in the middle; they pick one side or the other. Even without getting into the arbitration process, the two countries are forced to make compromises and settle cases before even reaching arbitration.

Without that process in place, countries could just continue to disagree, not compromise in any way, be completely deadlocked, and then the taxpayer would have to pay tax in both countries. It's an effective way of forcing Canada and the other country to compromise and agree on solutions.

Mr. Michael McLeod: Thank you.

The Chair: Mr. Dusseault, we have a three-minute round, if you want to use it.

[*Translation*]

Mr. Pierre-Luc Dusseault: Yes, thank you.

I want to continue the conversation on Barbados. I still have major doubts about whether the country is sincerely willing to implement the multilateral convention.

Mr. Marley, I want to ask you a question that has been on my mind for a long time and that has never been answered. Do you know why, for many years, Barbados has ranked third among all the countries in the world when it comes to Canadian direct investments abroad?

[*English*]

Mr. Patrick Marley: I don't know why Barbados is our third country. I don't know whether that's true, but I'll defer to you on the accuracy of it. In the case of investments from Canada in Barbados, I suspect that in many cases it's a case of using Barbados as a holding company for investments in other jurisdictions.

As I think I mentioned before that that doesn't result in any loss of Canadian tax. If Canada invested directly in any of 93 countries we have tax treaties with or any of the countries we have tax information exchange agreements with, which I think adds another 25-or-so countries, the profits would all come back to Canada tax-free. It thus doesn't impact the tax in Canada at all.

In many cases, investments might be made in Barbados because they're not adding an extra layer of tax; you're not being double-taxed or facing increased taxation compared with what you would have paid if Canada had invested directly in those countries.

[*Translation*]

Mr. Pierre-Luc Dusseault: Isn't the main reason the existence of the tax treaty between Canada and Barbados? As a result of the treaty, funds can be repatriated to Canada tax-free, as stated by the lawyer from Rogerson Law Group, located on Bay Street. The lawyers call this asset protection. There are a number of options.

[*English*]

They mention choosing an offshore tax haven, an offshore trust, segregated funds, IBCs and LLCs protecting your domestic assets, private foundations—always for asset protection.

[*Translation*]

I want to know whether your law firm also does this type of asset management or protection. Do you have any issue with the fact that Canadian companies or individuals use foreign countries to protect their assets? I'll quote the lawyer from the Rogerson firm:

[*English*]

"Asset Protection":

> Protection from what?
>
> Think of asset protection as a type of insurance policy covering a future risk of claims against you from financial predators.

[*Translation*]

He then made a list of financial predators.

[*English*]

He mentions:Others who could seek to stake a claim on your wealth include business creditors, the CRA, and dependents, in the case of your death.

How do you characterize lawyers who do that kind of stuff?

● (1220)

Mr. Patrick Marley: I'm not familiar with that lawyer, their firm or their marketing materials, but you asked a couple of questions there. I think you asked, first, if our firm provides similar services. No, we do not, in the sense that we practise exclusively Canadian law and U.S. law in our New York office. I'll just get back to the point that if somebody is using a Barbados company to evade tax, that's a criminal activity and we have laws in place now that aren't impacted by this treaty.

Mr. Pierre-Luc Dusseault: They don't evade; they avoid tax.

Mr. Patrick Marley: If it's tax avoidance, again, I think that's addressed in our domestic FAPI regime. Canada already taxes income through that regime, whether it's in a tax treaty country like Barbados or in a non-tax treaty country like the Cayman Islands.

Again, I'm failing to see the connection between Bill C-82 and.... I think what you're getting at is that you would like to see our foreign affiliate regime expanded, but that's separate from our treaty network. That's more a question for the Department of Finance and whether they ought to believe in their FAPI regime as is, or to expand it to other areas.

The Chair: We'll have to leave it there. We have to turn to committee business.

On behalf of the committee, I just want to thank both you, Mr. Marley and Mr. Sanger. I think that you've shed considerable light today on what is a complicated issue. I really appreciate your bringing your knowledge and experience before the committee on this issue, so thank you very much.

Mr. Patrick Marley: Thank you, Mr. Chair.

The Chair: With that, do you want to go to committee business right now, or do you want to suspend for a couple of minutes?

Mr. Pierre-Luc Dusseault: Right now.

The Chair: Right now? Okay.

An hon. member: One minute.

The Chair: Okay, we'll suspend for one minute.

● (1220)

(Pause)

● (1225)

The Chair: We'll reconvene to resume debate on the motion by Francesco Sorbara, which everyone has before them.

I believe, Mr. Fergus, you had an amendment you wanted to add to it based on the discussion the other day.

Mr. Greg Fergus: Mr. Chair, thank you very much.

As you know, it's really almost impossible for me to fill the shoes of Francesco, but in a very weak facsimile, I will try.

Ms. Kim Rudd: Is that on the record so you guys can read it?

Voices: Oh, oh!

Mr. Greg Fergus: I'd like to thank all members for seeking clarification and for their suggestions on how to improve this motion for the study.

There have been some changes to it, and I'll read it into the record:

> That, the Standing Committee on Finance undertake a study on open banking and report back the House on: a) whether open banking could provide benefits to Canadians; b) how potential risks related to consumer protection, privacy, cyber security and financial stability could be managed; c) what steps, if any, the Government should take to implement an open banking system;

—and here are the new parts, Mr. Chair—

> that the Committee dedicate up to four meetings to the hearing of witnesses in Ottawa; that the Committee examine opportunities to travel to jurisdictions that have implemented a framework for open banking, including the United Kingdom; and that the Committee report its findings to the House no later than Friday, June 7th, 2019.

Mr. Chair, one of the reasons.... As you know, open banking is a process that is currently under way, but the framework in which we should try to take a look at it, specifically on the questions of consumer protection, privacy, cybersecurity and the like, hasn't been fully developed.

We're sort of catching up, but it's important for us to have an opportunity for this committee, and hopefully for this Parliament, to set forth a proper framework to make sure that Canadians going forward, as this gains in currency, know that we've protected ourselves on this file very well and protected them very well by making sure that the system is sound.

To that end, not only should we take a look at what we're doing here within our own private financial sector, but we should also have the opportunity to take a look at what is going on in other jurisdictions that have had an opportunity to really set a better framework in place than what we currently have. We can learn from them and adapt that to our situation.

I'm hoping this motion will receive the approval of this committee. I think we can do some really good work, like we did on the Proceeds of Crime (Money Laundering) and Terrorist Financing Act, which, again, I think was a remarkable cross-party effort to really come to the aid of Canadians.

I lay this on the table, and I move it.

● (1230)

The Chair: You move this as an amendment, because it'll have to be an amendment.

Mr. Greg Fergus: I so move.

The Chair: Is there any discussion on the amendment?

Okay, then we have Mr. Richards and Mr. Kmiec.

Mr. Blake Richards (Banff—Airdrie, CPC): Thanks, Mr. Chair.

I appreciate the attempts here to add a little bit of substance and some kind of measure to make sure this leads somewhere. That's great.

I'll comment first on what in it concerns me, and then what's not in it. I have a greater concern about that part of it.

First, I'll just touch on the travel side of it. I think that's maybe unnecessary. Well, it's not maybe: It is unnecessary. I don't mean to say that we shouldn't look at the experience of other jurisdictions, but is there really a need to travel to do this? I don't believe there would be, Mr. Chair. I think it could certainly be done by video conference and teleconference, and through reports that have been put out that have looked at what's been done, without our having to travel. That seems to be a bit excessive. I would have a problem with that.

More important is what's not included. As I'm sure most members are aware, the Department of Finance currently has consultations under way on open banking. The advisory committee on open banking that was set up in September of last year has been tasked with consulting on this viewpoint. This isn't to say that the finance committee shouldn't look at it as well; that's not the point I'm making here.

Let me just read the mandate that committee was given to look at, including the following:

> [whether]open banking [would] provide meaningful benefits to and improve outcomes to Canadians...[and] in what ways....
>
> in order for Canadians to feel confident in an open banking system, how should risks related to consumer protection, privacy, cyber security and financial stability be managed?

and

> if you are of the view that Canada should move forward with implementing an open banking system, what role and steps are appropriate for the federal government to take in the implementation of open banking?

This is obviously something that at least the department and, one would think, the minister would have some thoughts on already. There's no indication in this as to what sort of direction, or whether there is a place, the government's looking to go to with this. It's fairly wide open, it seems. It's a consultation, but at least on the surface there doesn't appear to be any real direction, as there sometimes can be with these things, as to where the government is looking necessarily to go with it. My understanding from the people I've spoken to who have engaged with it is that it certainly seems as though that's the case. Those are the perceptions people have had of it as well.

I'm also of the understanding, from people whom I've spoken to, that there hasn't really been a lot occurring with this advisory committee. I don't know why that is or whether that means the government has no real intention of moving in that direction. If that's the case, is a study worth it? If it's not the case, then obviously this advisory committee on open banking—which, I will point out, is supposed to be wrapping up its consultations by February 11, which is just a few days away. What is supposed to occur after that is that—verbatim from the press release setting out the consultations—

> the Committee will deliver a report assessing the merits of open banking for Canada, with a strong focus on protecting consumer privacy, ensuring the security of financial transactions and maintaining the stability of the financial sector. The Committee will consider implementation opportunities and challenges later in the year.

That does give us some sense of the direction this is looking to go. Obviously, given the fact that this work has been done and that there is some kind of a direction there, hearing from this advisory committee would be very important, I would think, in this regard. I think that should be a part of the motion. We're obviously dealing with this amendment, so we can deal with that, and I think maybe that's another amendment we could look at here. But I think it should be specifically outlined in here that we should hear from members of this advisory committee and get a sense as to what they've heard and what sort of direction things might be moving in here. That would only seem to make sense to me.

I would think it would also make sense, of course, that we would hear from the finance minister on this and get a sense as to what direction the government is looking at, and what it would see as useful for the committee to look at and study. There's no point in the committee doing something in isolation.

● (1235)

If there are other things at work and at play here, why would we not all try to coordinate those things and do the best job we can to make sure that we're learning from the experiences of the other committee, the minister, and so on, especially given that it says here that this committee “will consider implementation opportunities and challenges”, and it says also, “later in the year”? Obviously, this indicates that there is an intention to take what comes out of this and move reasonably quickly with something. Therefore, why would we not be doing what we can to try to make sure that this work is informing what we would do, and that what we would do would inform what they do, so maybe we can get some sense as to the timelines?

When it talks about “later this year”, in government terms at least, that's fairly quickly, right? That would be good. Certainly that would be where the finance minister would be very helpful for us, to get some sense as to when the government is looking to move on this, and things such as that.

For example, we have an indication here of the committee reporting its findings to the House no later than June 7. Well, maybe that's too late. Maybe the government intends to move something forward before that. Therefore, we should probably be trying to make sure we're on the timeline that would allow this to be properly considered in what's going to take place, if something is going to take place.

Not only that, but it doesn't give an indication in here about reporting. It says “its findings”. It isn't indicating anything about recommendations. I would think if you're going to do a report, you want to ensure that recommendations are part of that, certainly. What's the point otherwise, right?

Those are some of my thoughts on it. The attempt of the amendment here is something that I appreciate, but there are some things in there that are of concern. More importantly, there are some things that are lacking there, so we need to firm those up a bit better.

The Chair: Mr. Kmiec, and then Mr. Fergus.

Mr. Tom Kmiec: I'm just picking up from where Mr. Richards left off. I know we had a conversation before, and I like the fact that some of those ideas are now in here. There are a set number of meetings, up to four meetings—so thank you for that—to hear from witnesses in Ottawa.

I have the same concerns Mr. Richards does about international travel. Mr. Saini will be very familiar with my opposition to travel by the foreign affairs committee more generally. I have generally been unhappy about travel internationally due to the costs for the taxpayer.

I did mention, and I think it would be a good idea, to not just have a report of our findings, but to have a report with recommendations, specifically, a recommendation to the government on whether or not to proceed with open banking. I'm going to read a part from the budget where Minister Morneau laid out his thoughts on open banking, because I have some other concerns about duplication of work between what the Government of Canada is doing and what this standing committee of the House of Commons would be doing.

I also think that we should be using Standing Order 109 more often and requiring the government to table a comprehensive report answering our own recommendations within 120 days. It's done almost routinely by certain committees of the House—not all—and I think it's a lost opportunity because it's a public document. Associations and groups who are interested in open banking can see it, as can the chartered banks and people who have concerns about open banking and how the government would proceed with it. They could then take a look at it.

I just think it's good, transparent, open government to require the government to produce a report in answer to the committee's work. I would also like to see the advisory committee on open banking be a witness, and that that would be embedded in the motion, because these are the people who are delegated by the minister of Finance with the authority to go out and consult on this. As Mr. Richards points out, they're supposed to have completed online consultation in four days, by February 11. I think that's an important component in all of this, so I ask myself the question, why are we at this time engaging in something that seems to have already been undertaken by the Government of Canada?

The open banking provision in budget 2018, on page 355, after talking about open banking as an opportunity for Canadian consumers, says:

> Recognizing these potential benefits, the Government proposes to undertake a review of the merits of open banking in order to assess whether open banking would deliver positive results for Canadians with the highest regard for consumer privacy, data security and financial stability.

Some of the language is very similar to the motion, but the committee would be undertaking something the government has already done. In fact, the minister has appointed several people to this advisory group. Now we would be duplicating its work. We'd be doing the same thing the government is doing.

I've a bit of a concern that their consultation would end on the 11th, and they would then produce an internal government report that I assume would be made public, but in reading the government website, it wasn't entirely clear to me whether that would be the case or whether it would be advice to the minister. If anybody has some clarity around that, I would appreciate hearing it.

We could potentially be duplicating the work of this advisory committee, which is why I think it would be important. Again, I'm fine with open banking as an idea to research and to look into. I just think that's a required component of this, and maybe a tighter timeline around exactly when we would report back with what I would to prefer be more than just findings, but recommendations, because right now it's Friday, June 7. That would probably be the time around we'd be considering the budget implementation act, part I. I don't want to stall on an open banking report. I'd like it to come back and have the time to do a good job on it with good recommendations that the government would then be able to reply to.

One thing I noticed when I was looking online for more information about open banking.... Among the members who are assigned to this, or at least the members I could find in the public sphere, are Colleen Johnston, who is TD channels head; fintech venture builder, François Lafortune; Kirsten Thompson from the law firm Dentons Canada; and—I'm not going to say this name correctly, so forgive me, Mr. Chair—

● (1240)

The Chair: I had that problem, too.

Mr. Tom Kmiec: —Ilse Treurnicht, former chief executive, Toronto's MaRS innovation hub. Again, I think these would be interesting individuals to meet with. The Canadian Banking Association, I note, is not enthusiastic because it says there's a risk of contagion to reputation or other types of risks with broad-ranging consequences from consumer data being shared. I know that the privacy component is in here.

The Competition Bureau also put out a fintech report back in 2017, supporting open banking, or generally being in support of it. It was entitled “Technology-led innovation in the Canadian financial services sector”, if any member wishes to take a look at it.

I think we could strengthen the motion some more. I think we could offer, maybe even a friendly subamendment if Mr. Fergus is willing to entertain it, to adjust the wording of the motion to get at what we would like.

There are a lot of jurisdictions doing this. I know it mentions the U.K. specifically, but Japan has done this too. Singapore has done this. Many other countries in the European Union have done this. A lot of this is already being done, from what I could gather, and 90% of it is already being undertaken by the private sector within the confines of the law, the way it is structured and the directives being issued by regulators. I really think that the real advantage we have here over, say, a government advisory committee, is to offer specific legislative changes to the Bank Act and other acts that would facilitate open banking, if that is our recommendation from this. If it's not, then fine, I'd be totally fine with that.

It's why I think it's critical to have recommendations. They should be very specific legislative recommendations, dealing with the Income Tax Act, for example, section so-and-so, that these are the changes that should be made, or to the Bank Act., etc. If it got to down to the specifics, it would be a great advantage to the government. A lot of the government's findings...and the Bank of Canada does a financial systems survey as well, where it asks how many people are interested in open banking, whether they see it as an issue. It's at 13% now amongst banking executives and senior executives in the financial services sector, so I think it's worth it.

One other thing I do think we could add to the motion, because I don't think it's covered, after the words, “how potential risks related to consumer protection, privacy, cyber security and financial stability”, is “and the automation of trading”. I think that would be a good addition to make. With automation of trading, the automatic traders, every second a trade is done by AI software, by artificial intelligence. We've seen other committees take on this subject, on whether there are issues with how fast trades can be made, automated trading creates systemic risks in the financial system, whether there are additional risks when people surrender their active participation and they just allow software to decide for them what their trades will be during a day and how that information is shared, perhaps, with different banking institutions. I think automation of trading could be added on here.

One other thing I don't see here is the potential job losses from open banking, given the brick-and-mortar style of banking that we mostly have in Canada right now. I know all of us have apps on our phones. For the major banks, at least, we have these apps, but perhaps a review and a specific mention of the impact on jobs in Canada would be a good addition.

I want to draw the attention of the committee members—I don't know if you've seen this—to an article in the Financial Post, “'Resistance is futile' in slow march to open banking in Canada”. Part of the committee's work, I assume, would be to make the march not as slow and speed it up a little bit.

I want to quote Matt Flynn:

> “Canada needs to speed things up, frankly,” Matt Flynn, a Toronto-based partner at Bennett Jones, a law firm, told me in an interview on Jan. 23, adding that “90 per cent” of the legal structure that would be needed to support open banking already exists. “It’s better to get ahead and export our prowess (in financial technology) to the rest of the world, rather than have others come, partner with our banks, and eat our lunch,” he said.

It has a header, “Some fintech companies think the legacy banks might be the problem”. I mentioned the Canadian Banking Association being unhappy about it. I'm just wondering whether automation of trading couldn't be added here. If there's a good reason for not putting it in, I'd love to hear from government caucus members on why. If there's an opportunity, perhaps, to amend the (b) section, just to include job losses.... That wasn't something I'd mentioned before. I think job losses in the banking sector would be of concern to people in the greater Toronto area, because there are a lot of financial institutions there.

● (1245)

I know for the credit unions back home, and for the Alberta Treasury Branches Financial, a quasi bank owned by the Alberta government, it would be of concern to them as well if we're moving away from bricks and mortar. It is also a concern how fast the shift will be, and how fast those jobs are substituted with more IT design, app design and API software companies. That might be fine, but perhaps we should do a deeper dive into that type of information, to specifically bind ourselves to looking at it. I think that would be a good signal to members of the public, organizations and companies that we are going to look at the job losses.

Often we look at innovation, and this is a lot about innovation and the changes to legislation and regulatory directives by our regulators. However, we don't often look at the impact on Canadian jobs and what could potentially happen. I don't mean outsourcing; I mean a move away from the jobs of old. I'm not one of those people, but perhaps you remember when milk used to be brought to the door. That's not the case anymore. We have to go to the grocery store. Those jobs don't exist anymore. I think this would be important to look at as well.

I will mention that there is a bank, a junior member of the big six, the National Bank of Canada, that is already participating in data sharing. It has started sharing its customers' data if asked to do so. Lionel Pimpin, senior vice-president of digital channels, made the point that open banking is a two-way street and that National Bank created a digital hub where its clients can display both in-house and external accounts, which they say is very convenient for its users. It's an opportunity for National Bank to take some business away from some competitors and people from downstream on the business side. We see a lot of consolidation going on in the United Kingdom as well, and it's driven by clients granting permission to view the data they have imported from rival institutions. They see this as a major opportunity, which is different from what their banking association is saying.

Pimpin said all of this in a January 28th interview.

That's going back to my point that 90% are already doing it, according to Flynn, and at least one of the major banks in Canada is already engaging in open banking.

Obviously, there is already a legal structure, a regulatory structure, that allows for it. That's why the motion should be further amended to provide for specific legislative amendments.

I'll take you back for a moment to the tax treaty witnesses we had today. This is going to be complex. I don't think it's just a policy discussion; I think it's a legal discussion around the rules and how comfortable the banks feel about sharing customer data, as well as what the customers have a right to and the legal protections they enjoy.

If there is more open banking, more data could be shared out there. How closely will customers in Canada look at the data they're sharing? How long do those permission sets last? When you give permission to a financial institution, is it permanent? Can you revoke it? What are the measures to revoke it? Those are legal questions. They're ethical and moral questions as well. I think those are also legal rules that we should be recommending to the government on what to do.

That's maybe the difference between we and the advisory committee can do. They will perhaps look at the broader policy environment that exists right now. That is why I think our motion should make recommendations on legal changes to those acts that Minister Morneau is responsible for.

Moody's Investors Service has done quite a bit of review of open banking, making suggestions on some areas. Some of them match closely with consumer protection and the privacy and financial stability components that are in the motion. However, as I mentioned, automation isn't included in the motion, and neither are jobs.

I want to quote this one section from the Moody's report on the government's initiative:

> The government initiative is credit negative for the largest Canadian banks' retail operations because it has the potential to incrementally weaken the industry's favourable industry structure of a few concentrated players, and therefore the banks' retail franchise strength and associated high profitability....

I get a lot of complaints from Albertans in my riding about bank profits. That's perhaps a a generalized feeling among the populace in western Canada, which I understand. At the same time, we should be looking at the impact this will have on how they operate. With regard especially to the back office that a lot of these banks have, will those be broken down into smaller financial institutions? What are the risks involved in doing that? What are the legal requirements for these almost subcontractors who will be doing business, and how much of your personal information will be changed?

● (1250)

Those are some of the concerns that I have with the way this motion is structured.

I'm also concerned that we won't be able to take on any other study if we approve this motion. I know it says we should hold only up to four meetings, but we only have one week sitting in March, if I remember correctly, which means that in April we'll be back, but it will be for the budget or BIA. I assume that will take us until May.

There will be no opportunity to look at my favourite subject, which, as many members know, is the stress test. I would love to take a look at that. I would be willing to stop talking, if I get some type of indication from the other side that you would be willing to set aside one or two meetings to hear the concerns of witnesses and members of the public about the stress test. We just need to do a simple review, and not make any recommendations. I have a motion ready before the committee on the subject, but I will not read it because it's not entirely germane to the discussion. I want to stay on subject, Mr. Chair. I think that is a worthy one, so if I can get indication from the other side that you'd be willing to consider passing it—as in actually doing it—then we can structure it within the calendar in a timeline that makes sense for the government caucus side.

I'll remind you that last year, Governor Poloz mentioned that he would need a year's worth of data from the Bank of Canada before being able to report back on the impacts of the stress test. There have been plenty of articles written on the subject already. I think it would be good for us to schedule it, which is why I'm concerned that if we pass this motion, this will be the last subject that we cover before we move on to the BIA and the estimates.

I will also mention that RBC, BMO and the Canadian Home-builders' Association have met with different members of the government. As well, the chief of staff to the finance minister met them on February 5. I assume those conversations are being held in private on the government side regarding the stress test, so to return to open banking here, I don't want this to be the last subject that we cover.

● (1255)

The Chair: It might be a good idea to return to open banking. We've only got about two minutes left.

Go ahead on open banking.

An hon. member: We need arbitration.

Mr. Tom Kmiec: Mr. McLeod, I agree: I need arbitration. That's what points of order are for.

I would hope that open banking will not be the last subject we cover. I have ideas for subamendments to the motion to strengthen it, including to have recommendations in the report. Then we'd have, if you'd be willing to have it again, a stress test study. Again, I have the motion.

This one needs to be strengthened, so we can have a comprehensive report. Then we can ask for it to be tabled and made public within 120 days after we report to the government through the House of Commons. We need a mandatory appearance by the advisory committee on open banking. For any major change to our banking system, such as the one that open banking could produce, I think it would be wise to have the minister appear as well. That was the experience in the United Kingdom—and that's what the European Union directives were indicating they would like to do. I think that such a large change to the banking system requires the minister to appear and explain his intent with that section of the budget that I read, from page 355, and exactly where he sees this going. I think that's the right thing to do.

If you'd be willing to amend the motion, then we could move on to other matters, such as scheduling witnesses for this. Beyond just the two I mentioned, I think the attendance of the advisory committee on open banking should be required in the motion—I mentioned the members of it—as well as the minister.

We should be offering specific legislative changes, if they're required and if we recommend open banking.

The Chair: I have to leave it there.

I'm just going to make one point. On those studies with Finance, we can require the government to report back in 120 days. We've done it before. We required it on money laundering. On the pre-budget consultations report, the budget is considered the government's response and then the estimates are tabled.

With that, we'll resume debate on the motion and proposed amendment by Francesco Sorbara at our next meeting.

The meeting is adjourned.