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November 1, 2016

The Hon. Wayne Easter, PC, MP
Chair, Standing Committee on Finance
House of Commons,
Ottawa, Ontario K1A 0A6
Via email: wayne.easter@parl.gc.ca

To the Hon. Wayne Easter and members of the Standing Committee on Finance:

On behalf of [FEI Canada](#) (Financial Executives International Canada), we would like to thank you for your invitation to present our pre-budget recommendations to the committee last Friday, October 21st in Toronto.

We are pleased to respond to your invitation to provide more information on tax simplification, including our recommendations on group tax reporting, rationalization of CCA classes and small business tax reporting.

FEI Canada is a membership association of Chief Financial Officers and other senior financial executives, with 11 chapters across the country. Members typically hold titles such as CFO, VP Finance, Treasurer, Controller, VP Taxation, and audit committee chair. The recommendations attached to this letter were drafted by members of our Policy Forum, composed of experts in these areas.

Once again, we appreciate the opportunity to provide additional thoughts on our proposal to simplify the *Income Tax Act*.

Yours sincerely,

A handwritten signature in black ink that reads "Michael Conway".

Michael Conway, FCPA, FCA, ICD.D
President & Chief Executive Officer

A handwritten signature in black ink that reads "Norm Ferguson".

Norm Ferguson, CPA, CA
Chair, Policy Forum



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INTRODUCTION

The Supreme Court of Canada has indicated that taxpayers should have tax rules that are understandable, predictable and fair. Further, the Canada Revenue Agency has commented that clear and concise tax rules help to prevent aggressive tax planning. Since the *Income War Tax Act* received royal assent on September 20, 1917, tax legislation has grown from approximately 10 pages to more than 2000 pages.

An enormous amount of legislation has been amassed over the last 99 years, as provision after provision has been added by successive governments attempting to create a fair tax system that is responsive to the economic priorities of the day. However, while attempting to strive for fairness, the principles of clarity and predictability appear to have been given lesser consideration.

As we approach the centenary of the Income Tax Act, FEI Canada believes the time has come to consider a focused review of the tax act so it may become more understandable and predictable, with reduced administration, while maintaining revenue neutrality. The timing seems appropriate not only considering the government's initiatives to focus on the productive use of corporate and government resources, and also considering that much-needed corporate tax rate reductions over the past decade have lessened the significance of many legislative measures.

SIMPLIFICATION PRINCIPLES

Although this letter is by no means an attempt to cover all aspects of a simplification process, FEI Canada would like to offer some thoughts on the principles that would form the foundation of such an initiative.

1) Clarity

a) Consolidation

Consolidation refers to the combining of a number of provisions or reporting obligations. FEI Canada is in full support of a consolidated/group income tax return system. Additional measures of consolidation could include allowing consolidated GST return filings within a corporate group, rationalizing/reducing the number of capital cost allowance classes and permitting the consolidation of various multi-year deductions that require extensive tracking, such as financing costs which these should be deductible in the year the cost is incurred rather than over 5 years.

b) Elimination

Efficiencies can be gained by the elimination of those provisions or exceptions that are redundant, irrelevant or immaterial. For example, there is a growing international trend to reduce withholding tax on dividends to support the international flow of capital and encourage investment. The elimination of withholding taxes will enhance the benefits of investing in Canada while reducing this withholding and reporting obligation. Another example relates to how the 50% add back of meals and entertainment expenses operates. These general rules, as well as a number of other provisions, have a number of exceptions. Although exceptions have certain policy initiatives, exceptions add complexity to provisions and could be removed without a significant shift in revenues.

c) Reduction

Reducing administration is a key ingredient of a simplification review. One has to question the value of certain reporting required of taxpayers. For example, an inactive corporation which may be held for a future transaction should have a one page tax filing that declares that the company is inactive and has no revenue rather than having to file a comprehensive corporate tax return. Also, a major step to simplification would be to allow companies below a certain threshold of income and/or assets to file their taxes based on accounting income with only a few minor adjustments.

d) Organization

As the Income Tax Act has grown over the years, its general organization has greatly deteriorated. FEI Canada recommends that a general reorganization of the Income Tax Act be undertaken. A first priority should be to improve the indexing and cross-referencing on sections of the Income Tax Act. This initiative would make it easier to carry out key word searches on tax applications and would likely be more amenable to digital interrogation. The second measure in this regard might be to create separate tax acts for corporate and personal income taxes. The acts would then be more appropriately organized similar to other pieces of legislations with a definition section usually at the beginning of the legislation with charging provisions set out in the legislation and measures supporting the charging provisions set out in the regulations. These steps alone would make the Income Tax Act more user friendly and save an enormous amount of time for both tax practitioners and auditors alike.

2) Predictability

a) Intention

A significant, and important, measure to improve predictability of the tax outcome would be to set out the clear policy intention of each provision in the Income Tax Act. Clear

intention would improve both compliance by taxpayers and enforcement by the government.

b) Clarification

There are many sections in tax legislation that have words that lead to different interpretation and tax disputes. Interpretative legislation should be replaced, where practical, with bright line tests. For instance, the terms “all or substantially all” and “principally” have been interpreted by the courts to mean 90% and 50% respectively. These percentages could be introduced in the legislation to make clear the on-side test that is to be applied in the particular circumstance. Further, bright line tests should be codified for other terms that have been interpreted over the years in the courts, such as employee versus independent contractor. These types of measures will add to the accuracy of tax reporting, be more consistent, provide clearer audit guidelines and reduced audit disputes.

c) Completion

Over the years, both the private and public sector tax practitioners have identified various “holes” in the legislation. These are sometimes addressed by Finance Canada issuing a Comfort Letter stating the intended result, but are sometimes not addressed at all. These “holes” must not only be cleaned up with amending legislation, but also there needs to be a mechanism for the continuous improvement of the legislation on a timely basis which would mean no later than once per year.

3) Administration

In addition to the increase in complexity of tax legislation, FEI Canada members have also experienced an increase in the complexity and thus administration of the audit and dispute resolution process. To put this matter into context, the number of Notices of Objection increased 88% between the 2005-2006 and 2009-2010 fiscal years and 24% in 2010 alone.¹

The primary reason for these alarming statistics may be attributable to our understanding that the Canada Revenue Agency measures itself based on “tax earned by audit” (TEBA), which is calculated as the total tax reassessments divided by the number of audits. The problem with this statistic is that it does not take into account the ultimate dollar resolution of the dispute and therefore, the audit mandate is to reassess the greatest amount of tax dollars. This mandate results in unnecessary resources and costs to resolve audit disputes with the Tax

¹ **Tax Dispute Resolution: Is There a Better Way?** Presentation by Anne-Marie Lévesque, Assistant Commissioner, Appeals Branch, Canada Revenue Agency. Paul Lynch, CA and Carman R. McNary, QC, to the Canadian Tax Foundation’s 2010 Annual Tax Conference



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Appeals branch or with the Tax Court. The current process does not prompt continuous improvements, nor enhanced productivity of resources.

The resolution is clear. Rather than mandate tax auditors to reassess, mandate tax auditors to resolve or settle audits. In the United States, IRS auditors are directed to resolve disputes without litigation. Simply put, an organizational cultural change must be introduced within the Canada Revenue Agency with the utmost urgency to reduce the time and resources by both the government and taxpayers to resolve audit disputes.

CONCLUSION

FEI Canada requests that a task force be established to provide recommendations for the simplification of the Income Tax Act. FEI Canada members are ready to assist in this action plan.